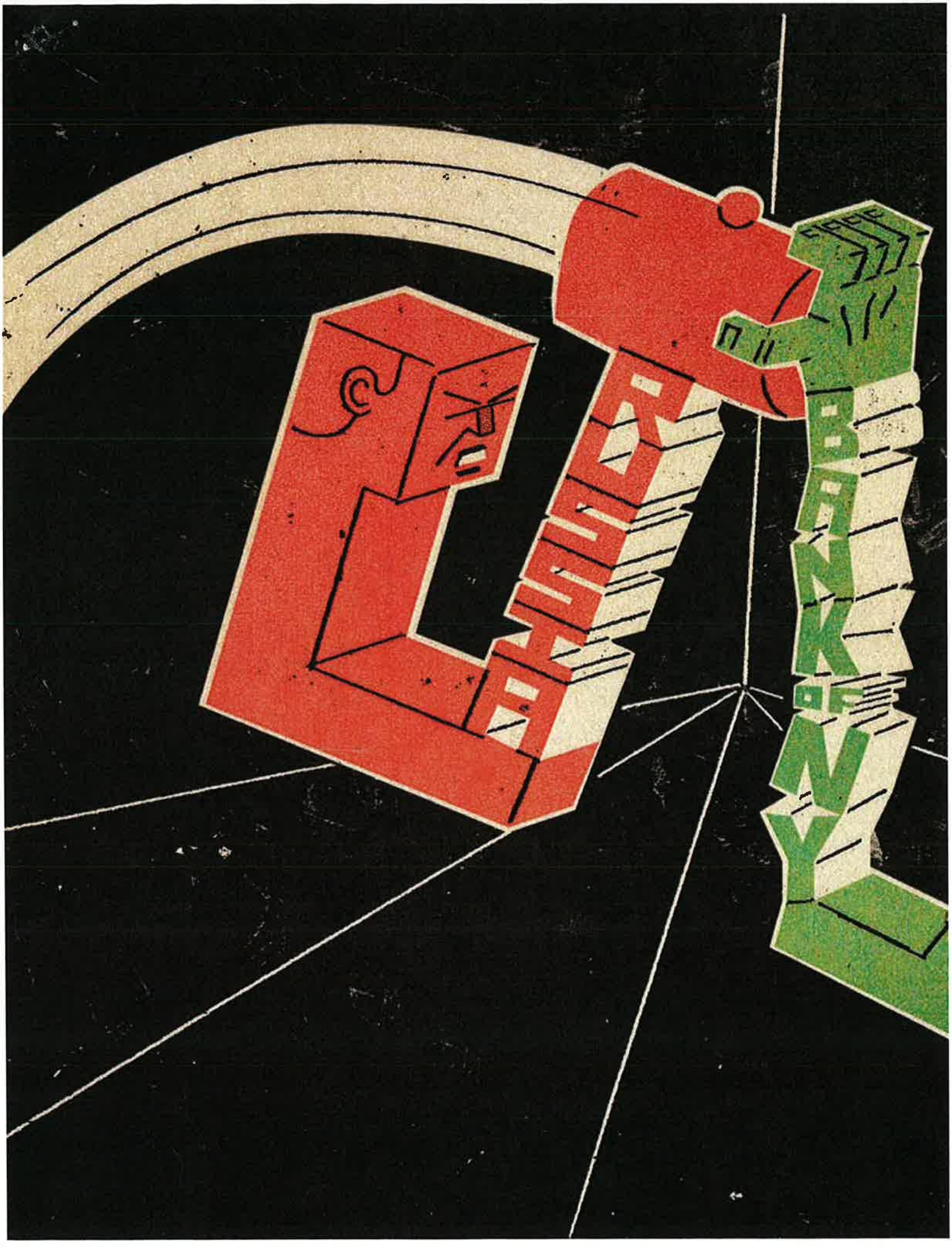
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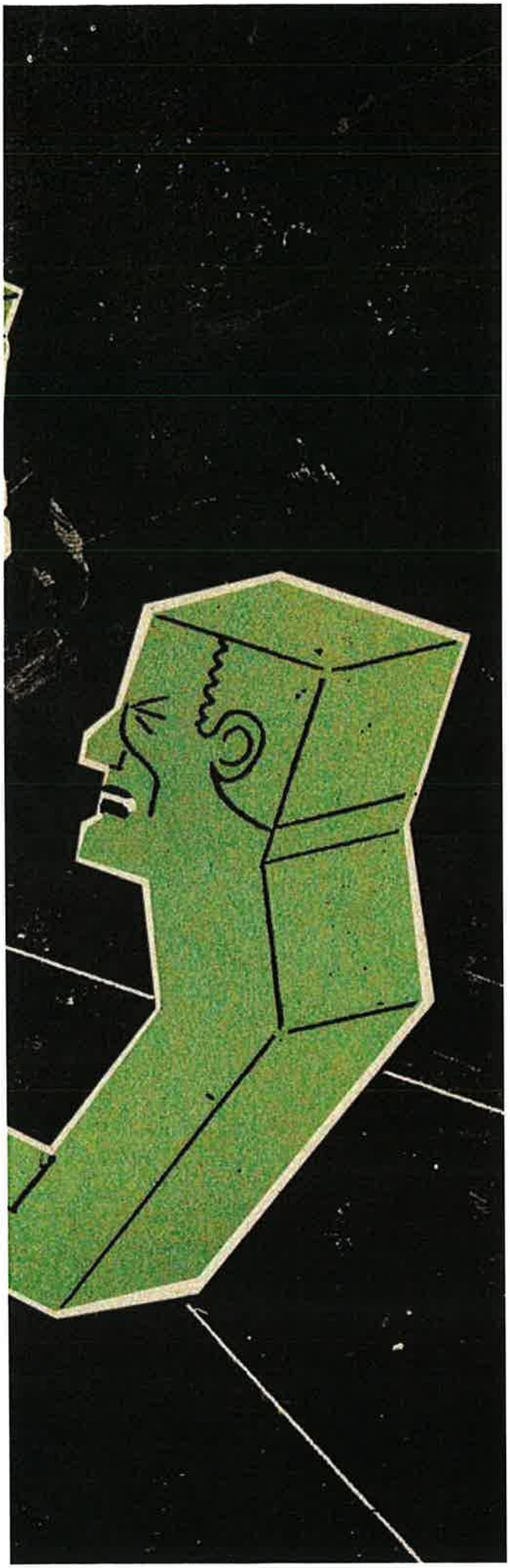


The Russian government is suing the Bank of New York for $22.5 billion for smuggling cash out of the country. Now the bank must make its case in a court experts say favors the Kremlin.

Can a U.S. bank get a fair trial in Moscow?

BY ROGER PARLOFF // *Illustration by David Plunkert*

INSIDE A RUNDOWN GOVERNMENT BUILDING on Novaya Basmannaya Street in Moscow, a bizarre lawsuit is playing out involving $7.5 billion in illicit money transfers and America's ninth-largest bank. The Russian government is suing the Bank of New York Mellon under the U.S. civil RICO statute—the Racketeer Influenced and Corrupt Organizations Act—seeking $22.5 billion. And what a cast of characters. Russia is represented by a Miami plaintiffs lawyer who specializes in airplane crash cases, whose experts include Harvard law professor Alan Dershowitz. The bank's defense is being led by Jonathan Schiller, a founding partner of super-lawyer David Boies's law firm, Boies Schiller & Flexner, and he has assembled his own phalanx of experts, led by former U.S. Attorney General Richard Thornburgh. In the suit the Russian Federal Customs Service seeks to recover taxes it says it should have collected on the $7.5 billion

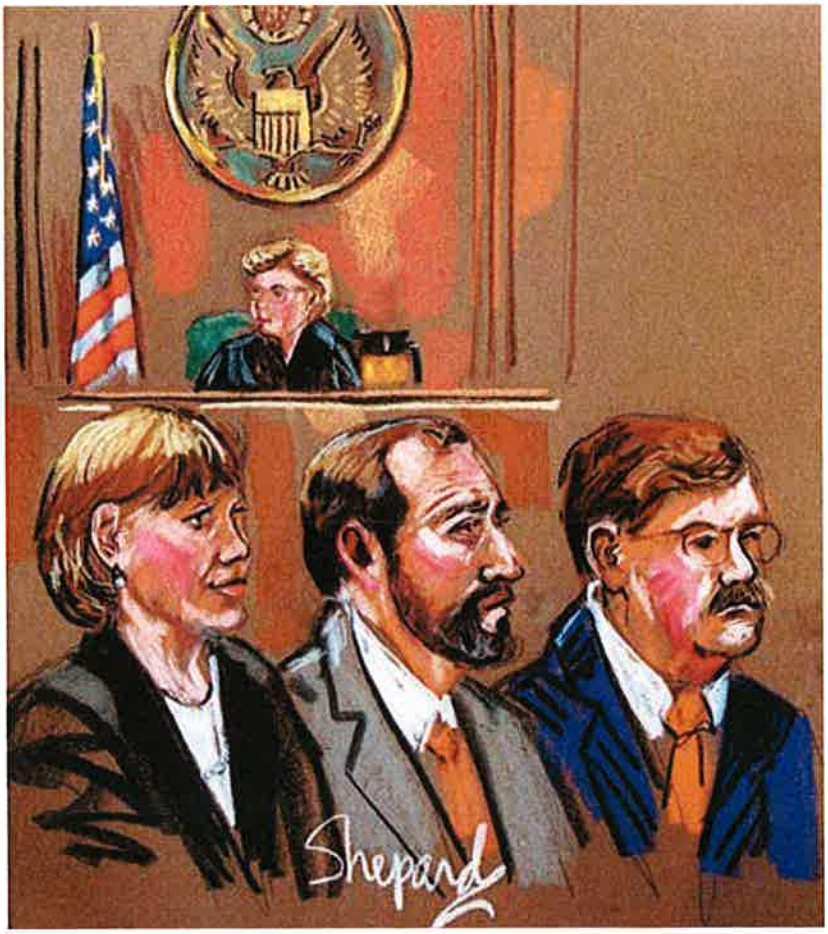
that one of the Bank of New York's employees helped smuggle out of the country about a decade ago. The bank maintains that the case has no merit.

What makes the dispute unique is that Russia has filed the suit not in "any appropriate United States district court," as the RICO statute contemplates, but in a Russian court. Moscow's commercial court is widely regarded as not only a place susceptible to corruption but one in which judges simply lack the judicial independence required to rule against important state interests. While a judgment in Moscow might well not be enforceable in the U.S., the Bank of New York does business in more than 100 countries, and the judgment would almost certainly be enforceable in some of them. Moreover, as a multinational operation, the Bank of New York does not relish the prospect of defying any country's judiciary. After an 80-year presence in Russia, it also dreads the prospect of having to pull out now, when Russia is the world's sixth-largest economy, its second-largest producer of oil, and a global superpower once again.

The case raises a larger issue: Can any Western company get a fair shake in the Russian court system when the adversary is the Russian government? In recent years Russia has often used the selective enforcement of its laws to advance policy objectives—most notably the nationalization of natural resources. From 2003 to 2006 it cited tax claims as the basis for seizing the assets of Yukos, then its largest oil company; in 2006 it alleged environmental violations in forcing Shell, Mitsui, and Mitsubishi to cough up half their stake in their Sakhalin Island oil franchise; and in recent months it has invoked transgressions of labor, migration, and tax laws to wring concessions from the Western half of the TNK-BP oil joint venture, including the ouster of its American CEO, Richard Dudley.

Yet the Bank of New York suit might also reflect a quirkier, narrower agenda. Russia's President, Dmitry Medvedev, has acknowledged that his nation's courts sometimes become the tool of powerful individuals. As the *Financial Times* reported in June—citing Moscow sources—"the Bank of New York case could not have got this far without support from a high-level 'sponsor' in government, the security services, or business—or one well connected in all three areas."

How high up in the Russian government hierarchy does one need to go to get approval to sue an American bank for $22.5 billion? Louise Shelley, an expert on the Russian legal system at the George Mason School of Public Policy in Arlington, Va., says, "The head of the customs service wouldn't have approval to do something like this on his own." Approval probably came, she says, from "somewhere in the Kremlin."



FORMER BANK OF NEW YORK VP *Lucy Edwards (left) and her husband, Peter Berlin (center), were convicted in 2000 of helping Russians illegally wire $7.5 billion from their country to the U.S.*

ANDREA SHEPARD—AFP/GETTY

THE DISPUTE STEMS FROM notorious events that exposed, at the very least, shocking regulatory failings at the Bank of New York, which is America's oldest financial institution, having been founded by Alexander Hamilton in 1784. In the early 1990s, after the Soviet Union fell, the Bank of New York launched a new Eastern European division made up largely of Russian émigrés. Among them was Lucy Edwards, one of about 1,700 vice presidents at the bank at that time.

In 1996, Edwards's husband, Peter Berlin, opened two accounts at a Bank of New York branch in Manhattan, ostensibly for an import-export business he claimed to be running. In reality, he and Edwards placed the accounts largely under the control of a Russian bank, which used them to perform illicit money transfers for its depositors, paying Edwards and Berlin about $1.8 million in commissions (which were not shared with the Bank of New York). Edwards bribed a subordinate and falsified records to conceal what she was doing from supervisors. She also supplied her husband with Bank of New York software he wasn't supposed to have, which enabled the wire transfers to receive less scrutiny from bank auditors than usual. The Edwards-Berlin

LEGAL HEAVYWEIGHTS *for the Bank of New York include lead counsel Jonathan Schiller (left) and, as expert witnesses, former U.S. Attorney General Richard Thornburgh (center) and former White House counsel and federal appeals judge Abner Mikva. They argue that Russia's case would go nowhere in a U.S. court.*

accounts were soon generating more wire-transfer fees for the bank than any other account in their branch.

Acting on a tip, Manhattan federal investigators raided the couple's apartment in August 1999. They pleaded guilty in February 2000 to having opened an unlicensed branch of a foreign bank and conspiracy. Though neither of those crimes can serve as a basis for a RICO case, the government alleged that the conspiracy had nine objectives, and that one of those was "laundering money" to promote a "wire-fraud scheme," which *can* serve as a basis for a RICO case. (Though the RICO law was originally aimed at organized crime, it has civil provisions as well as criminal provisions. It's not uncommon for plaintiffs suing major companies to include civil RICO allegations, because victors in such cases are entitled to recover three times their actual damages.)

In 1999, U.S. prosecutors asked Russian authorities to help them discover the motive behind the wire transmissions. One likely goal was evasion of Russian tax and customs duties, and another possibility was money laundering, which in this context refers to illicit transfers of funds that are themselves the proceeds of a crime. But contemporary press accounts suggest that the prosecutors' attempts to enlist Russian assistance were largely rebuffed at the time. (Mary Jo White, the U.S. attorney at the time, declined to be interviewed for this article.) Many powerful Russians were evading taxes during that period, and in 1998 President Boris Yeltsin had just vetoed a Russian parliamentary bill designed to crack down on illicit money transfers. In October 1999, the *Washington Post* reported that Russia's tax minister had announced that "an audit by his agency had determined that most money transfers made through the Bank of New York accounts by Russian commercial banks were legal."

Federal prosecutors ultimately concluded that tax evasion and money laundering had not been the crux of the operation after all. At Edwards's and Berlin's sentencing in July 2006 the prosecutor told the judge that the money transmitted "was used really for all sorts of purposes, many of them entirely innocuous." The couple, who had cooperated with the prosecutors, were sentenced to six months' house arrest and probation.

As for Edwards's supervisors and the bank itself, prosecutors leveled no charges. Instead, on Nov. 8, 2005, it dropped its inquiry on condition that the bank sign a nonprosecution agreement. In it, the Bank of New York acknowledged Keystone Kops–style incompetence, but no knowing, intentional misconduct. It admitted, for instance, that the personnel who'd developed their wire-transfer software "failed to appreciate ... the increased money-laundering risks associated with the ... product"; that the Bank of New York branch personnel "incorrectly believed ... that Berlin was in the 'import/export' business"; and so on. The bank has always maintained that none of those acknowledgments amounted to an admission of criminal conduct.

However, the Department of Justice press release that announced the agreement left a different impression. It stated near the top that the Bank of New York "has admitted its criminal conduct."

The press release and the nonprosecution agreement soon came to the attention of Florida attorney Marks, who had represented the Russian Federal Customs Service in unsuccessful litigation in U.S. courts against the major tobacco companies for allegedly smuggling cigarettes into Russia to circumvent taxes. As a plaintiffs lawyer for air-disaster victims, Marks was at home with cases that straddled the globe; he'd handled, for instance, successful litigation stemming from the crash of Silk Air Flight 185, which mysteriously went down between Jakarta and Singapore in 1997. Marks read the Justice Department announcement to mean that the bank had now admitted criminal conduct in the Edwards-Berlin prosecution. That created an opportunity for Russia to sue over the case, he reasoned, because such an admission of criminal behavior after years of denial could reset the statute-of-limitations clock.

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BY EARLY 2006, Russia had told Marks to go forward with a claim against the Bank of New York. Why did Marks choose to bring the case in Russia? The lawyer contends he was effectively required to do so, because of a Manhattan federal district judge's 2001 ruling in a case known as *Pavlov v. Bank of New York*. In that instance,

LEFT TO RIGHT: MARK MCQUEEN; KEN CEDENO—BLOOMBERG/LANDOV; NAM Y. HUH—AP

some depositors in an insolvent Russian bank sued the Bank of New York in Manhattan, claiming that their losses were ultimately traceable to the Edwards-Berlin scheme. Bank of New York lawyers argued that the depositors' case was mainly a Russian matter and should be heard in a Russian court, which could provide "an adequate, alternative forum." Though the depositors protested that Russian courts were corrupt, the Manhattan judge dismissed the case anyway, finding that "it is not the business of our courts to assume the responsibility for supervising the integrity of the judicial system of another sovereign nation."

Legal niceties aside, there's still an elephant in the room: Does anyone really think a U.S. bank running up against the Russian state can get a fair hearing in a Moscow court?

Marks argues, "The court said that that case didn't belong here and booted it to Russia. If I'd filed a new action in New York, the Bank of New York would've moved for sanctions!" Marks also contends that because the Bank of New York favored moving the Pavlov case to Russia, it is now legally barred from taking a contrary position in the current case.

The bank's counsel, Schiller, says that Marks' arguments are nonsense. "Pavlov was a case brought by private citizens of Russia regarding the failure of a Russian bank," he says. "The Bank of New York was not faced in that case with a government action in a court where U.S. and U.K. published court opinions have found that the [Russian] government has influence."

Schiller has a different theory for why Marks filed the case in Russia: "It would be summarily dismissed in the U.S. based on clear and controlling federal precedent."

Before filing suit, Marks met in the spring of 2006 with the Bank of New York's executive vice president and deputy general counsel, Matt Biben. Marks has acknowledged that on behalf of Russia he asked the bank to fork over $600 million if it wished to avoid litigation. Biben had joined the bank in 2004, after spending 12 years as a federal prosecutor—six in Manhattan—and having brought many criminal RICO suits himself. Biben had also personally negotiated the language of the Bank of New York's nonprosecution agreement in 2005. Biben says that Marks offered no documentation or written analysis for his demand, which Biben rejected. "It was certainly not the type of information that any corporation would make a serious decision based upon," he says.

Marks filed suit for $22.5 billion in the Arbitrazh Court for the City of Moscow in May 2007. There is no question that U.S. courts are sometimes called upon to apply the laws of foreign countries, and vice versa. While this is apparently the first time anyone has ever tried to bring a civil RICO case in a foreign court, the question of whether one can properly do so is ultimately a question of Russian law, not U.S. law. Still, legal niceties aside, there's an elephant in the room: Does anyone really think a U.S. bank running up against the Russian state can get a fair hearing in a Russian court?

According to three academics consulted by *Fortune*, the Moscow arbitrazh court's objectivity in any matter is likely to be inversely proportional to the state's interest in the case. In addition, three of the American legal experts who are currently serving as retained experts *for Russia* in the Bank of New York case, including Notre Dame law professor G. Robert Blakey, are listed as co-counsels on a brief submitted in a different case just two years ago that argued "Russian courts are highly susceptible to corruption, and a foreign [party] cannot expect to receive an impartial trial against major Russian interests." Blakey, who, as chief counsel to a Senate subcommittee in 1970, had been the principal draftsman of the RICO law, says his name appeared on the brief by mistake, since he was only working on other aspects of the case. He says his views then and now are the same: "I think the aspiration of the courts in Russia is for independence. I have no opinion whether they are, in fact. I haven't read enough of the literature, so I don't know." Marks says the Russian court is fair. "It defies common sense that the Russian judicial system would be honest in cases of little interest but would be dishonest in cases involving a great deal of public scrutiny," he writes in an e-mail. "You must be speaking to the ill-informed or persons with an agenda."

In accordance with Russian law, Marks appended to his complaint his retainer agreement, which shows that he has taken the case on a 29% contingency fee, even though Russia's highest constitutional court ruled in early 2007 that contingent fees are unethical and therefore unenforceable. (Marks won't confirm the fee arrangement, but says that his Russian co-counsel assures him that contingency fees are authorized under Russian law.)

TO A SIGNIFICANT EXTENT Marks has based his case on the language in that Nov. 8, 2005, press release from the U.S. Attorney's office that states that the Bank of New York has "admitted its criminal conduct." The bank's admission of criminal conduct is crucial to Marks' argument for resetting the statute-of-limitations clock, and it also helps get past a jurisdictional hurdle posed by Russian law: Arbitrazh courts, being commercial courts, aren't supposed to get involved in interpreting criminal laws (be they Russian or American). *Fortune*, however, has learned that that critical language in the release was apparently referring to a different investigation entirely. The nonprosecution agreement dealt not only with the Manhattan federal prosecutors' probe of the Edwards-Berlin affair but also with a simultaneous inquiry conducted by Brooklyn federal prosecutors. That probe was related to unconnected wrongdoing on Long Island at an Island Park branch of the Bank of New York that involved fraudulent loan applications.

Last month the U.S. Attorney's offices for both the Eastern and Southern Districts of New York (Brooklyn and Manhat-

EXPERT WITNESSES *for Russia in the case include Harvard law professor Alan Dershowitz (left) and Notre Dame law professor G. Robert Blakey, who was the principal draftsman of the RICO statute in 1970. Dershowitz says applying RICO internationally would help fight global terrorism.*

BRIAN SNYDER—REUTERS /LANDOV

tan, respectively) belatedly amended the confusing joint press release. It now states that the Bank of New York "admitted its criminal conduct with respect to the Eastern District of New York investigation"—i.e., the Island Park matter. A spokesman for the Southern District, which handled the Edwards-Berlin probe, tells *Fortune* that the changes were made "to correct inaccuracies." Biben, the Bank of New York's deputy general counsel, says, "We'd raised with the U.S. Attorney's office the fact that the press release was being used [by the plaintiffs] in a way that was inconsistent with the nonprosecution agreement."

Does the recent clarification of the press release wipe out Marks' argument that the bank has admitted criminal conduct? After *Fortune* informed Marks that the press release had been amended, he e-mailed back, "It is absolutely amazing that Justice would amend the release some three years later during pending civil litigation to potentially help the wrongdoer. ... This should be troubling to all of us that Justice is apparently subject to such influence and that the bank has so much power." He notes subsequently, however, that since the bank accepted "responsibility" for what had happened in the nonprosecution agreement—wording that has not been changed—the Bank of New York still unambiguously admitted criminal responsibility.

When asked why "responsibility" must mean "criminal responsibility," Marks wrote, "Please tell me that you are kidding. ... This was a criminal investigation, not a civil one, so what other responsibility could the U.S. Justice Department and law enforcement attorneys who prosecute criminal cases possibly mean?"

MARKS HAS SIGNED UP some marquee names to endorse the strength of Russia's RICO case. In addition to Blakey, this past June he nabbed the most famous criminal law professor in the country, Harvard's Alan Dershowitz. On June 25, Dershowitz submitted an 18-page affidavit (appended to a 70-page résumé) arguing, among other things, that "international application of civil RICO would be supportive of United States interests" in that it would help battle "global money-laundering" and "terrorism."

In the portion of his affidavit that lays out the facts of the case, however, *Fortune* noticed that some of the most dramatic allegations Dershowitz cited—for instance, that the Bank of New York "intentionally failed to ... report known evidence of suspected criminal wrongdoing ... even after that evidence came to the attention of senior Bank of New York executives"—are not quotations from the nonprosecution agreement, as his affidavit suggests, but rather quotations from the confusing, subsequently amended press release. And, yes, they are quotations relating to the wrong case—the Island Park case.

Repeatedly advised by *Fortune* of this apparent mistake, Dershowitz did not respond. Likewise apprised, Marks wrote that he (Marks) was "tied up" and wouldn't have time "to re-review all of the materials to fully respond" for a couple of days. Reminded nine days later that he still hadn't replied, Marks sent this cryptic response: "The nonprosecution agreement does involve admissions of liability in our case, and if there is still any doubt, we stand by Professor Dershowitz's statements in this regard."

PRETRIAL HEARINGS ARE SCHEDULED to resume next month in Moscow. The Bank of New York, of course, has hired its own roster of legal stars, including former Attorney General Thornburgh; former federal appellate judge Abner Mikva (a member of the House Judiciary Committee when RICO was enacted); the author of the leading treatise on RICO, Greg Joseph; and 17 experts on Russian law. Yet it's hard to believe that this suit will play itself out to the end. The bank continues to press its case to U.S. and Russian government officials, arguing that this sort of spectacle is not in Russia's long-term interest if it wishes to attract and maintain Western business investment. There are likely to be rifts within the Russian government itself over the wisdom of this kind of case.

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"We've done business in Russia for a very long time," says the Bank of New York's Biben. "We have clients who appreciate our services and want to continue to use us as partners."

If the case cannot be resolved through governmental channels, however, the bank may have no choice but to settle rather than risk litigating in a forum that appears to lack both the expertise and independence to render an impartial result.

Still, if it comes to that, a billion-dollar-plus settlement seems like a steep price to pay for a poorly worded Justice Department press release. ■

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