Statement of Paul B. Stephan, University of Virginia School of Law, Before a Hearing of the Senate Judiciary Committee on KleptoCapture: Aiding Ukraine through Forfeiture of Russian Oligarchs' Illicit Assets, on July 19, 2022

Good morning. My name is Paul Stephan, and I am the John C. Jeffries, Jr., Distinguished Professor of Law and the David H. Ibbeken '71 Research Professor of Law at the University of Virginia. I have taught and written about the Soviet Union and Russia, as well as the foreign relations law of the United States, for all of my forty-three years on the Virginia faculty. I worked on behalf of the Department of Treasury to assist Russia in the creation of its tax system from 1993 to 1998. I served as Counselor for International Law to the Legal Adviser of the Department of State in 2006-2007, and as Special Counsel to the General Counsel of the Department of Defense in 2020-21. I also was coordinating reporter for the American Law Institute's Restatement (Fourth) of the Foreign Relations Law of the United States from 2012 to 2018. I appear here on my own behalf, and nothing I say should be taken as representing the views of the University of Virginia School of Law, the State Department, the Defense Department, or the American Law Institute. I have no clients with any interest in this proposed legislation. Rather, I am here in the role of a disinterested student of business activity involving Russia and of foreign relations law who hopes to help this body in its deliberations. It is a privilege and an honor to appear before you.

A. Why New Legislation is Needed – The Maintenance of Kleptocracy in Russia and the Use of Western Economies to Sustain Corrupt Regimes

First of all, this is the right time to broaden and strengthen U.S. law to fight the use of our economy to hide financial crimes and corruption. I have closely followed business engagement between the Soviet Union and Russia, on the one hand, and the United States and its allies, on the other hand, since Mikhail Gorbachev's reforms in the late 1980s. A disturbing consequence of the

freeing up of the Russia economy under Gorbachev and Yeltsin was the great outflow of flight capital, often in the form of commodities rather than cash, and the resulting large deposits and investments in the West. It was hard to believe that any of these assets had legitimate origins in Russia, but proof of their provenance was hard to come by. Initially some policymakers saw these flows as an understandable workaround in the face of irrational rules and policies and an obstructive state bureaucracy. Over time, however, it has become clear that the ongoing movement of dirty money out of Russia represents a threat to the law-based global economy that the United States and its allies have done so much to build. The present war in Ukraine shows what can go wrong when a government devolves into a kleptocracy. Accordingly, I welcome all efforts to strengthen our tools to detect and seize Russian assets sent to the rich world for the concealment of crimes.

I now turn to the specifics of the Biden administration's proposals and some alternative approaches I have considered. I first discuss those that seem clear and unobjectionable improvements over existing law. I then describe the handful of reservations I have about a few of the proposals.

B. Reinforcing the Existing Sanctions Regime

The administration's proposals include amendments to current law to strengthen enforcement of existing criminal sanctions. I endorse these steps and suggest clarifying changes to the proposal.

1. Tying the Racketeering Influenced and Corrupt Organization Act (RICO) to Violations of the International Emergency Economic Powers Act (IEEPA), the Export Control Reform Act (ECRA), and the Arms Export Control Act (AECA)

RICO (18 U.S.C. §§ 1961 to 1968) significantly enhances sanctions for specified criminal offenses. It both clarifies and extends the definition of complicity and provides stronger penalties. Under current law, this enhanced-enforcement regime does not apply to private actors seeking to undermine our national security through leveraging U.S. assets to support adversary regimes.

Closing this gap is straightforward and desirable. The administration proposal would add violations of IEEPA's freezing regime, ECRA, and AECA to the list of enumerated offenses that trigger RICO. This step will give prosecutors better tools to go after foreign actors who seek to leverage our economy to aid our adversaries. This amendment would not redefine primary offenses, but rather make it harder to draw third parties, such as potential business partners and financial institutions, into the plot while increasing penalties. It would increase deterrence and thus reduce the likelihood that bad actors will try to violate the sanction and export-control rules.

These proposals also do not raise any Due Process Clause problems. I discuss below how the Constitution might apply to some measures in the administration's legislative package. Adding IEEPA, ECRA, and AECA violations to the list of predicate offenses that trigger RICO only enhance enforcement of existing criminal prohibitions in a way that presents no constitutional difficulties. These changes will not only address the present crisis created by Russian aggression, but enhance our ability to deal with other adversaries in future international emergencies, including non-state actors such as terrorists and drug cartels.

This Committee can bring even greater clarity to sanctions enforcement by specifying that violations of other sanctions, such as those provided by the Sergei Magnitsky Rule of Law Accountability Act, the Global Magnitsky Human Rights Accountability Act, and the Countering America's Adversaries Through Sanctions Act (CAATSA), also are predicate offenses under RICO. An amendment to 18 U.S.C. § 1961 that refers expressly to these laws would remove any doubt whether sanctions pursuant to these laws implicitly incorporate IEEPA or instead rest on an independent sanctioning authority. It would remove an argument that, for example, CAATSA sanctions do not come under IEEPA and that their violation therefore would not implicate RICO.

2. Extending Money Laundering Penalties and Civil Forfeiture

An additional benefit from adding IEEPA, ECRA, AECA, Magnitsky, and CAATSA violations to the list of predicate offenses under RICO is clarity about money laundering jurisdiction. Section 1956(c)(7)(A), the provision that designates "specified unlawful activities" (SUA) for purposes of money-laundering liability, incorporates all RICO predicate offenses. Legislation that specified these crimes as RICO predicates would resolve any uncertainty over whether current Subsections (c)(7)(B)(v)(II) (referring to violations of Export Administration Regulations) and (D) (referring to 50 U.S.C. § 4905) already treat ECRA and IEEPA violations as SUAs.

Clarity about the applicability of Section 1956 to sanction and export-control violations also would put on a sounder basis the authority to use civil forfeiture to seize property traceable to these violations. The principal civil forfeiture authority, 18 U.S.C. § 981, designates as subject to forfeiture any property traceable to a violation of Section 1956. By confirming that Section 1956

extends to sanction and export-control violations, an amendment would ensure that the government also could invoke civil forfeiture in these cases.

C. Constitutional Issues Raised by Some of the Recommended Legislation

While I fully support the object and purpose of the administration's proposals, I am concerned about some of the details in the legislative package. Outrage at Russia's unprovoked and grossly illegal invasion of Ukraine and its annexations of Ukrainian territory is completely justified. I worked on behalf of Naftogaz of Ukraine, the national oil and gas company, as an expert witness to support its successful claim for compensation for Russia's lawless seizure of its assets in Crimea. I want the administration to have all the tools necessary to cut off Western support for Russian corruption and the resulting injuries to its neighbors. Ukraine's harms are the worst, but other former parts of the U.S.S.R. also face serious threats. What I fear, however, is that our righteous outrage might distract us from doing this the right way, based on strong legal foundations that represent our enduring commitment to the rule of law.

1. Due Process and Civil Forfeiture

I begin with the principle, well established in Supreme Court doctrine, that all property found in the United States, foreign-owned as much as that belonging to U.S. citizens, enjoys the protection of the Due Process Clause of the Constitution. Constitutional protection of foreign-owned property does not work exactly the same way as does that for domestically owned property. But core constitutional guarantees, in particular a right to notice of a legal challenge to one's liberty and property and a right to respond to such a challenge, do apply.

One component of the right to notice is the principle of legality, that is the idea that nothing can be an offense unless a law defining and prohibiting the conduct in question existed at the time of the activity constituting the offense. I recognize that the application of this principle, expressed as a rule of non-retroactivity of punishment, operates differently in the civil law context. But it is not irrelevant to civil forfeiture.

Accordingly, I have three basic concerns about the proposed legislation. The administration's legislative package includes retroactive use of civil forfeiture for conduct that violated no criminal law, greatly expands the jurisdictional scope of federal criminal law on the basis of unclear and potentially troublesome provisions, and does not clearly provide for adequate notice to people who might be affected by civil forfeiture.

2. Retroactive Application of New Criminal Law Through Civil Forfeiture

My first, and most substantial, concern involves proposed Section 4902(c). It provides for civil forfeiture of any property that would be covered retroactively by proposed 18 U.S.C. § 2324. That provision, if adopted, would greatly extend U.S. criminal jurisdiction beyond its current limits. It authorizes the government to undertake civil proceedings to seize and convert to its own use property that was not subject to any criminal provision of U.S. law at the time of its arrival in the United States or its freezing under 50 U.S.C. § 1702, that is to say IEEPA.

I do not understand the administration's proposal as seeking retroactive application of 18 U.S.C. § 2324 itself. Ex Post Facto Clause limitations on penal provisions almost certainly would bar that outcome. The issue instead is whether retroactive civil forfeiture provisions would violate the Due Process Clause of the Fifth Amendment. The Supreme Court's relevant precedents are far from clear. I would not say that it is absolutely certain that Section 4902(c) would be found unconstitutional. I would say that a concern about its constitutionality is reasonable.

On the one hand, the Supreme Court in *Landgraf v. USI Film Products*, 511 U.S. 244, 267 (1994), said this about retroactivity in civil cases: "The Constitution's restrictions, of course, are of limited scope. Absent a violation of one of those specific provisions, the potential unfairness of retroactive civil legislation is not a sufficient reason for a court to fail to give a statute its intended scope." In a footnote, however, the Court indicated that the use of punitive damages might produce a different outcome. *Id.* at note 20. Later cases indicate that the best reading of *Landgraf* is as follows: retroactivity in and of itself is not sufficient to invalidate retroactive civil legislation under the Due Process Clause, but a retroactive law imposing a sufficiently severe burden based on a sufficiently great departure from prior law may be unconstitutional. *E.g*, *Opati v. Republic of Sudan*, 140 S. Ct. 1601, 1607 (2020) ("The principle that legislation usually applies only prospectively 'is deeply rooted in our jurisprudence, and embodies a legal doctrine centuries older than our Republic.' . . . This principle protects vital due process interests, ensuring that 'individuals . . . have an opportunity to know what the law is' before they act, and may rest assured after they act that their lawful conduct cannot be second-guessed later.").

In short, *Landgraf* does not function as an open invitation for any retroactive application of a significant sanction. Given the severity of civil forfeiture as a penalty and the significant extension of existing criminal law that the administration proposes, the risk that a court would find Section 4902(c) unconstitutional is great.

Why risk violating the constitution? Retroactive application of civil forfeiture would solve one immediate problem, namely making additional funds available to support Ukrainian resistance to Russia's invasion. I agree that this support meets a vital national security interest of the United States. I question, however, whether raising money this way, rather than through the normal appropriation process, is so necessary as to justify the precedent that this act would create. Going forward, this measure would tell the world that any assets legally brought to the United States could be forfeited, if the United States deems the need sufficiently urgent. Existing law (the Trading With the Enemy Act and IEEPA) already authorizes such measures when the United States is in a declared war or engaged in an armed conflict. This Committee should think long and hard before going further, even if it believes that the proposal will survive constitutional scrutiny.

3. Abandoning Jurisdictional Limits on Federal Criminal Law

Two components of the administration's legislative packages would greatly extend the criminal jurisdiction of the United States. Section (b)(2) of proposed 18 U.S.C. § 2324 criminalizes conduct that contains all the elements of one of the offenses enumerated in Section (b)(1) except for its occurrence "within the jurisdiction of the United States." The administration also proposes to add to the list of enumerated offenses that trigger money-laundering sanctions under 18 U.S.C.

§ 1956 "any conduct in violation of foreign law that would constitute specified unlawful activity under this section if the conduct had occurred within the jurisdiction of the United States."

It is not clear whether the phrase "jurisdiction of the United States" refers to the constitutionally permitted jurisdiction of the United States, which arguably is worldwide, or instead to the jurisdictional prerequisites of the relevant enumerated offense. The distinction has potentially far reaching consequences. Consider as an example the Foreign Corrupt Practices Act. Currently it imposes criminal sanctions on conveying or offering to convey "something of value" to an official actor to influence an official decision-making process. The prohibition applies to U.S. persons (including foreign employees and agents of U.S. entities), any entity that seeks access to U.S. capital markets and thus qualifies as an "issuer" under U.S. securities laws, and any conduct in furtherance of a proscribed transaction that takes place on U.S. territory. Were the administration's proposals to be adopted, it would appear that any offer of something of value to a foreign official to obtain a desired outcome would become a U.S. crime as well as a predicate offense for money laundering, no matter who makes the offer or where the offer occurs. In other words, the United States would assert universal jurisdiction over bribery and related corruption, far in excess of what we do currently.

Making all violations of foreign laws that are equivalent to current money-laundering predicate offenses presents additional problems. First, it is harder than it might seem to specify what should count as a violation of foreign law. Second, determining what foreign law violations are equivalent to the specified U.S. offenses listed in Section 1956(c)(7) also can be very hard.

Consider, for example, evasion of Russian Central Bank regulations requiring a license before any Russian subject can open or own a foreign bank account. The rule exists, but noncompliance is widespread. Would noncompliance with a largely unenforced rule count as a law violation? Would noncompliance with this rule be equivalent to bank fraud, which is a specified offense under Section 1956(c)(7)(B)(iii)? If the answers to these questions are both "yes," then any unlicensed bank accounts (not only U.S.) held by any Russian national (or nationals of other countries with similar regulations) would be subject to civil forfeiture under U.S. law. Moreover, persons who engage in transactions involving these accounts, such as sellers of goods or services who accept payment from them, would face money laundering liability.

I am not sure whether this expansion of U.S. criminal jurisdiction would be a net good or not, but it certainly would be dramatic and possibly destabilizing. Such a step should not be taken lightly. Further study and hearing from a full range of stakeholders, including representatives of the financial industry and experienced legal practitioners in international business, are necessary to assess the impact of these proposals.

Proposed Sections 2324 and 1956(c)(7)(H) are not necessarily unconstitutional, aside from retroactive use in civil forfeitures under proposed 50 U.S.C. § 4902(c). There is a body of scholarship, and a handful of lower court cases, that question universal jurisdiction for federal criminal law, but the Supreme Court has not ruled on this point. These extensions of federal jurisdiction do represent significant breaks from current law. Once enacted, they will apply to all persons, not just those who are specially designated nationals under IEEPA. If the goal is to assert

worldwide U.S. criminal jurisdiction over financial crimes such as evasion of foreign taxes and other fiscal regulations, clearer language and greater deliberation are called for.

4. Adequate Notice in Civil Forfeiture

Finally, I am worried about the implementation of proposed 50 U.S.C. § 4903(e). This provision specifies who must receive notice at the commencement of a civil forfeiture proceeding under the new authority created by proposed § 4901. The proposal requires notice to "any person named in a relevant exercise of authority" under IEEPA or to any person "identified as appearing to have a protected legal interest in the property." Otherwise the provision relies on general notice to the public at large through an internet posting. Proposed 28 U.S.C. § 2467(c) supplements this provision by indicating that the existing rules governing forfeitures in admiralty and maritime disputes, which deal with notice to potential claimants when ownership disputes exist, may not apply.

People who bring into the United States assets with origins in corruption or related criminal behavior typically disguise their actual ownership. But people seeking to escape oppressive or predatory foreign practices also do this, even if they have behaved lawfully. When the United States asserts that a specially designated national has an interest in property subject to a freeze order, it may base that conclusion on a rejection of other formal claims of ownership. Many freeze orders thus trigger disputes about ownership, which forfeiture proceedings will only exacerbate. To satisfy the requisites of due process, the United States should provide adequate notice not only

to the persons whom it has determined to be the actual owner of property, but to all persons who may assert ownership of an interest in that property.

Perhaps the drafters of Section 4903(e) believe that publication of a claim on the internet will suffice to meet constitutional notice standards. I disagree. When the government has reasonable grounds to know that ownership of a frozen asset is contested and who the contestants are, it should provide specific and timely notice to all those persons. The government can do this without conceding in any way a belief that the claimed ownership is in fact valid.

To eliminate due process concerns, the legislation should use the established notice rules found in the Supplemental Rules of Admiralty or Maritime Claims and Asset Forfeiture Actions in all instances, and not just when "not inconsistent" with the proposed revision of 28 U.S.C. § 2467(c). Those Rules work in practice to resolve the problem of uncertain ownership of identified property subject to forfeiture. Some reasonable shortening of the deadline for responding to notice might be justified, but Rule G(4)(b)'s specification of who must receive personal notice should apply in any forfeiture proceeding with respect to assets frozen under IEEPA.

D. Other Legal Concerns

Constitutional issues aside, the administration's proposals raise other concerns. This Committee should not ignore the international-law background regarding asset seizures. It also should address ambiguities in the proposed legislative language that, as drafted, create unnecessary legal uncertainty.

1. Background Issues of International Law

The proposals raise a general point about the relationship between constitutional due process and the international legal obligations of the United States. For most of the last century as well the present one, the United States has been a strong proponent of the duty of states to respect the property rights of foreign nationals. In some cases, these rights are spelled out in specific bilateral treaties, although no such treaty exists with Russia. Still, it has been our position that these duties exist in general and independently of particular treaties.

It is clear that any laws of the United States that satisfy the requirements of constitutional due process also would meet all of our obligations under international law. In particular, international law would not regard a civil forfeiture of a foreign national's property as an expropriation, to which duties of compensation attach, where the forfeiture process complies with the requirements of the Due Process Clause.

A breach of constitutional due process does not necessarily mean a violation of international law. Rather, it is useful for this Committee to keep in mind that any law that pushes the limits of the Due Process Clause might also be problematic under international law. I recommend that the Committee, in its deliberations, take into consideration our country's long-term project of promoting respect for the property rights of foreign nationals. It is American who ultimately have the most to lose from a general erosion of these rights.

2. Expanding the Definition of Criminal Corruption in 18 U.S.C. § 2324

Lastly, I have a couple of technical questions about proposed 18 U.S.C. § 2324(b). First, it defines as "corrupt dealing" subject to U.S. criminal penalties benefits or advantages obtained "from or through" the Russian government or any of its officials. Would an "benefit" include an official not carrying out a threat to enforce the law arbitrarily? If so, would a private person's cooperation with government demands obtained by extortion poison all of that person's assets? After the Yukos affair, the Putin administration induced other oligarchs to take over the delivery of social benefits in designated regions as the price of staying out of jail. Does that mean that all of their assets are picked up by § 2324(b) and thus made subject to civil forfeiture?

These questions point to a larger problem in applying civil forfeiture to Russian kleptocrat assets. A pervasive practice among super-wealthy Russians (and not only Russians) is separating legal interests from actual power and control. The "real" owners never enter into transactions that give them a legally enforceable entitlement, but rather rely on trust and coercion to ensure that nominal stakeholders do their bidding. To compound the problem, at least for the legacy oligarchs (those who became wealthy in the 1990s), most of their nefarious activity lies in the past. Their corruption today consists mostly of doing what it necessary to hold off the current regime from confiscating their property and throwing them in prison, as happened in Yukos. For both these reasons, laying down an evidentiary base to link assets to past crimes is going to be challenging.

This does not mean that we should not adopt the best tools possible. Rather, we should do so knowing that difficulties will remain. What we do not need are overbroad criminal provisions that would not do much in Russia but will have unintended consequences elsewhere in the world.

3. Redundancy and Confusion in Proposed 18 U.S.C. § 2324(b)(1)

In addition, subsection (b)(1) defines as corrupt dealing:

> A federal offense was committed involving foreign official corruption, ***and*** associated money laundering, fraud, or other related conduct; violations of sanctions imposed under the International Emergency Economic Powers Act (50 U.S.C. § 1701, et seq.) and other relevant sanctions and related laws; violations of export controls under the Export Control Reform Act (ECRA) (50 U.S.C. §§ 4801-4852); war crimes (18 U.S.C. § 2441); cybercrimes (18 U.S.C. §§ 1028, 1028A, 1029, 1030); ***and*** violations by a foreign public official, or an associate of such a person, of the Foreign Agents Registration Act (22 U.S.C. § 611, et seq.), of an offense constituting bank fraud, or of the Prohibition on Concealment of the Source of Assets in Monetary Transactions (31 U.S.C. § 5335), . . . (bold italics added).

What is the work of the two "ands" in this subsection? Is the first "and" meant to conjoin only violations of the Foreign Corrupt Practices Act and "associated money laundering"? If so, what work does the second "and" do? Are we to understand that a federal offense will exist only if the elements of all the clauses are present? I cannot believe that is the drafters' intent. Also, why is the money laundering reference in the first clause necessary? Shouldn't we apply civil forfeiture to all proceeds with a substantial connection to proscribed activity, whether laundered or not? In any event, civil forfeiture already applies to money laundering as defined by Section 1956.

E. Conclusion

In conclusion, I applaud the administration for exploring steps to make it harder to exploit the U.S. economy to cover up corrupt and predatory activity around the world. There are ways to do this that still maintain the principles of legality and due process that, at the end of the day, distinguish us and our allies from the current regime in Russia. Most of the proposals before this Committee do this, although a few provisions do not.