

Criminal Liability for Fraud in the Field of Entrepreneurial Activity within the Context of the Resolution of the Constitutional Court of the Russian Federation dated December 11, 2014 № 32-П



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Abstract

The article discusses the situation surrounding the criminalization of fraud in the field of enterprise. The author notes the social significance of entrepreneurial activity and arising associated risks including those ensuing from failure to fulfil contractual obligations, the threat and acuteness of risks posed by fraudulent encroachments on property and its investment appeal; the author emphasizes the obligation of the state to implement measures aimed at minimizing entrepreneurial risks, stimulating good faith relations between property and enterprise, ensuring protection of property rights *inter alia* through the instrument of criminal law, the legal norms of which must preclude unjustified criminal prosecution and act as a powerful factor inhibiting encroachment on property and the legitimate interests of entrepreneurs, serve as one of the means of ensuring legal protection for conscientious entrepreneurs and investors, and not demonstrate loyalty to criminal business. The author bases his discourse on the legal positions of the Constitutional Court of the Russian Federation, expressed in its Resolution dated December 11, 2014 № 32-П "Apropos the Revision of the Constitutional Provisions of Article 159-4 of the Criminal Code of the Russian Federation pursuant to the inquiry of the Salekhard City Court of the Yamalo-Nenetsk Autonomous National District."



Keywords

criminal, fraud, liability, entrepreneurial activity, business, contract, property

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In accordance with article 2 of the Civil Code of the Russian Federation, entrepreneurial activity is aimed essentially at the systematic gain of profit from the use of property, sale of goods, performance of works or rendering of services, therefore this activity is based on legal relations arising from ownership of means for enterprise, the purpose of which being increase

of profit. In such relations, property is the essential condition for freedom of economic activity, presuming freedom of contract and equality of the parties in such activity, the legal situation of which is predetermined by the guarantee of such rights as enshrined in the Constitution of the Russian Federation and the criteria of their possible limitations. Pursuant to this, the Civil Code of the Russian Federation establishes the inviolability of property and freedom of contract, equality, autonomy of will and proprietary independence of parties in business, unimpeded realization of civil rights, proscription of random interference by any party in private matters, ensuring restitution and defence of violated rights (clause 1 article 1, clause 1 article 2) as fundamental bases of civil law.

By its nature, entrepreneurial activity is undertaken at parties' own risk, thus for the parties involved the gain of profit is neither permanent nor guaranteed, but dependent on contracting parties' imprudence in organization and performance, unfavourable state of the markets and failure to fulfil their obligations, which may cause not only financial losses, but also the entrepreneurs' loss of property as the subject of a transaction, investment, means for a commercial project, exercising a negative bearing on the situation of specific parties in economic relations and on the national economy as a whole. Consequently the federal legislator has not just the right to ensure the unity of the economic space necessary for economic activity, equal rights and obligations in the field of enterprise, performance of which is based on the equality of all before the law and the judiciary, inviolability of property, observance of balance in public and private interests in determination of the legal status of the parties in such relations, but is also obligated to take measures aimed at elimination of unfair competition, protection of property rights, minimization of entrepreneurial risks, stimulation of good faith relations regarding proprietorship and entrepreneurship and guaranteeing the restitution and protection of which is covered by a contract.

From the times of the Roman Empire, the civilized growth of economics has been based on the principle of *pacta sunt servanda*, whereby the fulfilment of a contract had a special, almost sacred significance. It was specifically trust in the binding nature of a contract and the expectation of conscientious conduct by the parties that has served as the foundation of contemporary economics, supported by law, for the transition from suspicion to trust¹. Trust arising from the reliability and solidity of a merchant's word gave rise to the development of enterprise in the Russian Empire. It is unlikely that a conscientious entrepreneur would be attracted to business in today's world in conditions of a crisis in trust between parties in entrepreneurial activity, aggravated by failure to fulfil contractual obligations, if lack of binding force in contracts becomes a "norm" of business conduct and the acquisition of a partner's property, ensuing from failure to fulfil contractual obligations, becomes a means of gaining profit.

The state is not empowered to interfere in private matters, yet it cannot remain aloof in matters pertaining to public interest and losses to business, citizens and the national economy. Pursuant to the Convention for the Protection of Human Rights and Fundamental Freedoms, every physical or legal entity has the right to expect respect for its property; no entity may be deprived of its property unless in the public interest and on conditions envisaged by law and the general principles of international law; the state has the right to ensure observance of such laws as are perceived to be essential to exercising control over the use of property in accordance with general interests (article 1 "Protection of Property" Protocol № 1).

The state must not place the conscientious party of a contract and participants of economic activity that could involve high risks into an obviously unprofitable and unequal situation *vis-*

¹ See: *Luman N. Social Systems: Note on General Theory*. Saint Petersburg, 2007.

a-vis their unscrupulous partners, moreover as this would cause not only loss of profit, but also loss of property, the protection of which is envisaged not only by civil law, but also guaranteed by the Constitution of the Russian Federation *per se* and the norms of international law. In any event, state policy in the economic sphere should not create “preferences” for unscrupulous entrepreneurs. Nor should there be any privileges for any entities committing crimes in the entrepreneurial field, as was noted by the Constitutional Court in its Resolution dated December 11, 2014 № 32-II.

Experts estimate that fraud remains one of the most serious threats to companies both in Russia and world-wide. In Russia, 60% of companies have reported that they have been victims of economic crimes in the past two years, a figure significantly higher than the analogous global indicator (37%)². The field of financial services remains the most attractive for fraudsters in view of the broad spectrum inherent in private funds, assets and confidential data on clients, enhanced the very nature of this sector³. In such circumstances, lack of action by the state may cost the Russian economy very dear by being detrimental to the attraction of investment, commercial development, encouragement of honest entrepreneurs and support of their trust in the law and the state with its ability to provide effective protection of their rights and legitimate interests.

Without doubt, criminal law is only marginally useful for resolving economic problems, nevertheless it can and must contain sanctions regarding illegal enterprise, encroachment on property, serve as an instrument for protection of honest investments and the rights and legitimate interests of entrepreneurs, guarantee fair liability commensurate and adequate regarding the nature and danger to encroachments on the relationship between property and enterprise, and the threat of criminalization of this field of activity.

The interests of protecting property rights and entrepreneurial activity has dictated the institution of criminal liability for acts encroaching on property that undermine the foundations of honest enterprise, expressed by theft — committed with the mercenary aim of illegal gratuitous expunging and (or) turnover of another entity’s property to the benefit of the guilty party or other parties, that inflict damages on the proprietor or other owner of the said property — in the form of fraud, caused by premeditated failure to observe contractual obligations in the field of enterprise (Article 159-4 of the Criminal Code of the Russian Federation).

Theft, in its essence, has nothing in common with entrepreneurship as such. Fraudulent acquisition of property through deliberate failure to fulfil contractual obligations, as encroachment with a complex composition with a dual object — the relationship between property and the established procedure of entrepreneurial activity — constitutes a high degree of social danger, and thus presumes a higher and adequate liability for such acts.

As was noted by Boris Titov, plenipotentiary for the defence of entrepreneurs’ rights under the President of the Russian Federation, in conditions of the fall in prices for energy resources a firm, uncompromising, federal and even nationwide support for business, in the first place protection of entrepreneurs and private property, is the key question in not just development, but simply the survival of the country. Unless we reach a rapid understanding of the situation and do not take immediate remedial measures, then I fear we shall see no entrepreneurs in the country. And this means we shall see no economy capable of sustaining competition, nor social wellbeing. The current criminal policy creates a basis for interference into the sphere of enterprise for unscrupulous representatives of law enforcement agencies and the courts. This is

² Russian Review of Economic Crimes for 2014. P. 4.

³ A/CONF.222/PM.1

the view held by experts such as lawyers, representatives of legal associations, executive power structures and entrepreneurs who have been subjected to criminal prosecution. This includes seizures by raiders, the creation of a regime of unfair competition, “roofing” of illegal business, all of which discourages entrepreneurs from setting up and developing businesses of any size⁴.

Without doubt, lawful invested means, honest business and enterprise should have adequate protection, including in criminal court procedure and by the instruments at the disposal of criminal law, ensuring that honest investors have the legal means to preserve and increase their funds. Such entrepreneurs and investors are not interested in seeking loopholes in the law for the purpose of evading liability for criminal business, they need genuine legal protection of their rights and interests, clear and predictable legislation, including legal enforcement. In connection with this, it is no idle question to which side the “center of gravity” should shift regarding liability for fraudulent encroachment on property in the field of enterprise — toward its intensification or liberalization, in other words, firm defence of property belonging to entrepreneurs with the aid of criminal law, or of entities illegally encroaching on such property. The actual accent in this sphere shall determine whether business in Russia will be honest and safe, or criminally-oriented and thereby pose a high risk for honest entrepreneurs, as crime-favorable activity, including the matter of liability, is to the benefit of criminally inclined entities and therefore dangerous and unacceptable to law-abiding citizens, honest proprietors and entrepreneurs.

Proceeding on the basis of data furnished by B. Titov, more than half of consulted experts (56%) consider the conduct of business in Russia to be unsafe. 53% consider that Russian legislation does not provide adequate guarantees to protect business from unfounded criminal prosecution. It may therefore be postulated that every second entrepreneur “takes measure” of its likelihood of being threatened by criminal prosecution. Moreover, allowing for the fact that 60% of Russian companies have reported that they have been victims of economic crimes⁵, it may also be assumed that more than every second entrepreneur does not fear criminal liability, but criminal encroachment on its property, business, rights and legitimate interests. Consequently, legal policy aimed at protecting property and enterprise must be sufficiently balanced and adequate, and legal norms should exclude both unfounded criminal prosecution, and serve as a powerful factor in protecting the property and legitimate interests of entrepreneurs from encroachment.

Otherwise, if one examines the concept of protection and encouragement of enterprise in the sphere of criminal policy through the prism of possible evasion of criminal liability, this may lead to a general presumption of the criminal nature of business, the development of which is naturally facilitated by a relaxation of liability, only until the moment when such encroachment occurs with regard to the encroacher’s property.

The introduction of Article 159-4 into the Criminal Code of the Russian Federation was aimed at separating criminally liable acts from genuine entrepreneurial activity, preclude the possibility of resolving civil legal disputes by means of criminal prosecution, create a mechanism of protection for honest entrepreneurs from unfounded criminal prosecution and at the same time ensure that guilty parties shall not escape liability under the cover of a civil legal transaction. To this end, in its Resolution dated December 11, 2014 № 32-II, the Constitutional Court of the Russian Federation noted those constructive signs of elements of fraud in the field of enterprise, which indicate the presence of specifically criminal law and not civil law tort: culpable use for theft of another entity’s property or acquisition of rights to the same by

⁴ “Business under the ‘article’”. *Vedomosti*. December 2, 2014.

⁵ *Russian Review of Economic Crimes for 2014*. P.4.

means of fraud or abuse of trust in contractual obligations that will not be fulfilled intentionally (moreover not due to circumstances that may govern failure to fulfil resulting from the risk-prone nature of entrepreneurial activity), which indicates that the subject of the crime had a direct intention to commit fraud.

At the same time, the Constitutional Court also noted the ambiguous wording of the article, the overlooking of qualifying signs that increase the social danger of fraud and the related substantial disproportion in sanctions, which leads to violation of the principle of equality and also creates unequal legal consequences regarding failure to fulfil contracts executed in similar circumstances.

Nonetheless the Constitutional Court of the Russian Federation, while acknowledging the provisions of article 159-4 of the Criminal Code of the Russian Federation as inconsistent with the Constitution of the Russian Federation, indicated directly that its provisions establish punishment in the form of deprivation of liberty that is disproportionate to the social danger of fraud linked with deliberate failure to fulfil contractual obligations in the area of entrepreneurial activity.

As noted by the Constitutional Court of the Russian Federation, in cases where the measures envisaged by criminal law cease to correspond to social realities, leading to a weakened protection for constitutionally significant values or, on the contrary, to excessive application of state enforcement, the legislator — acting on the basis of the indicated constitutional principles — is obligated to bring criminal law prescriptions in line with new social realities (Resolution dated April 20, 2006 № 4-II).

By its content, such regulation cannot exclude elements of constitutionally justified feasibility. Thus the legislator, in determining the elements of a crime and relegating them to different categories, has the right to take into account the factual state of social attitudes in concrete historical conditions and the related need to increase protection of one or another right and legitimate interests, while observing the balance between constitutionally significant aims and values, and the constitutional principles of justice and equality.

Resolution of the question of criminal liability for encroachment in the economic field is no exception. In its Resolution dated December 11, 2014 № 32-II The Constitutional Court of the Russian Federation indicated not so much in its declarative as in its reasoned part, the shortcomings of article 159-4 of the Criminal Code of the Russian Federation, regarding diversion from the principle of the equality of participants of economic activity, neglect of the rights of the proprietor, discrepancies with the purposes of the criminal law pertaining to protection of property from criminal encroachment and prevention of crimes, by factors stimulating illegal actions against proprietors or other owners and violation of property rights, which the legislator, by virtue of the provisions of article 6 of the Federal constitutional law “Apropos the Constitutional Court of the Russian Federation” is obligated to eliminate. Otherwise, upon the expiry of the six months’ period from the date of promulgation of this Resolution, article 159-4 of the indicated Code loses legal force, as ensues directly from clause 3 of its declarative part.



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