When Wild West Met Wild East?
Understanding the Special Place of the Bahamas in Russia's Offshore Network

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Introduction[1]

The embeddedness of the Russian economy in a complex network of offshore financial centres is well-documented in academic research and official statistics. For more than two decades, Cyprus has served as a *de facto* financial centre of Russia, having continually been the leading source of FDI into and out Russia, followed closely by other (often European) financial havens. This long-term historical pattern was interrupted in 2014/2015, when the Bahamas became the leading source of FDI inflows into Russia, accounting for more than 53% of FDI inflows in the country. Since then, top sources of capital flows into Russia have persistently included the 'wilder' financial havens such as Bermuda or the BVI, raising fresh concerns about illicit financial flows in and out of the country, including money laundering.

This paper analyses this trend in the context of the de-offshorisation initiatives of the Russian government undertaken since 2011. The basic question that is addressed here, is whether the rise of the Bahamas and 'wilder' fiscal havens is a temporary, transitory phenomenon, or whether it is part of a larger, structural change, and if so, why?

With the complex roots of Russia's tight relationship with offshore havens going back to Russia's pre-1991 history, the consensus emerging from the literature suggests that it is the protection of assets and identity of ownership, rather than taxation as such, that underpins Russia's reliance on offshore financial structures. It is also in this vein that Russian regulators tend to explain the rise of Bahamas as a source and destination of Russian capital flows.

[1]Part of research for this paper was carried out with the support of the EU-funded project, CORPLINK (grant agreement REP-694943-2)

Specifically, they refer to the desire of Western investors to bypass newly imposed US-led sanctions since 2014 in the search for Russian high yield. According to this theory, the new place of the Bahamas in Russia's capital structure was supposed to be transitory. Tighter regulations in the home markets of the advanced countries, as well as new international sanctions have increased, so it was argued, the political risks for foreign investors using Bahamas-based structures. But for the Russian economy, the Bahamas remain a central source for capital inflow and flight to this day. Analysing this trend, I find that the Russian demand for the haven is driven in large part by the desire of asset owners to protect their assets from the new scrutiny and penalties imposed by the Russian authorities, and partly by the secrecy regime provided by the Caribbean offshore.

The paper is structured as follows. Section One discusses the political economy of Russia's 'offshored economy.' It briefly situated the country's dependence on offshore FDI flows in the historical context of the post-1991 political economy, and analyses the dynamics of Russia's international financial and corporate integration during the past two decades. Section 2 dwells on change in the structure of FDI sources into Russia in 2014-15 and specifically, the rise of the Bahamas and other Caribbean havens as leading sources of capital inflows and outflows int the country. The Bahamas rose in importance as a leading source of capital in and out of Russia in 2015; in 2018 Cyprus, while still important, surrendered its position to the BVI. Compared with 2017, the share of Russian capital in the BVI in the first quarter of 2018 grew three-fold. During the past three years, Bahamas remained 4th or 5th investor in Russia recipient of Russian FDI.

The rest of the paper analyses the political economy of this shift. Initially, Russian authorities, as well as international observers, interpreted the change as a temporary shift in the structure of capital flows. Such temporary change, it was argued, is driven mainly by the change in the international financial context: (1) the decline of Cyprus as a leading investor in Russia since 2012 and (2) the imposition of anti-Russian financial sanctions by major powers in 2014 and the related desire of foreign investors to bypass the new restrictions in their dealings with Russia.

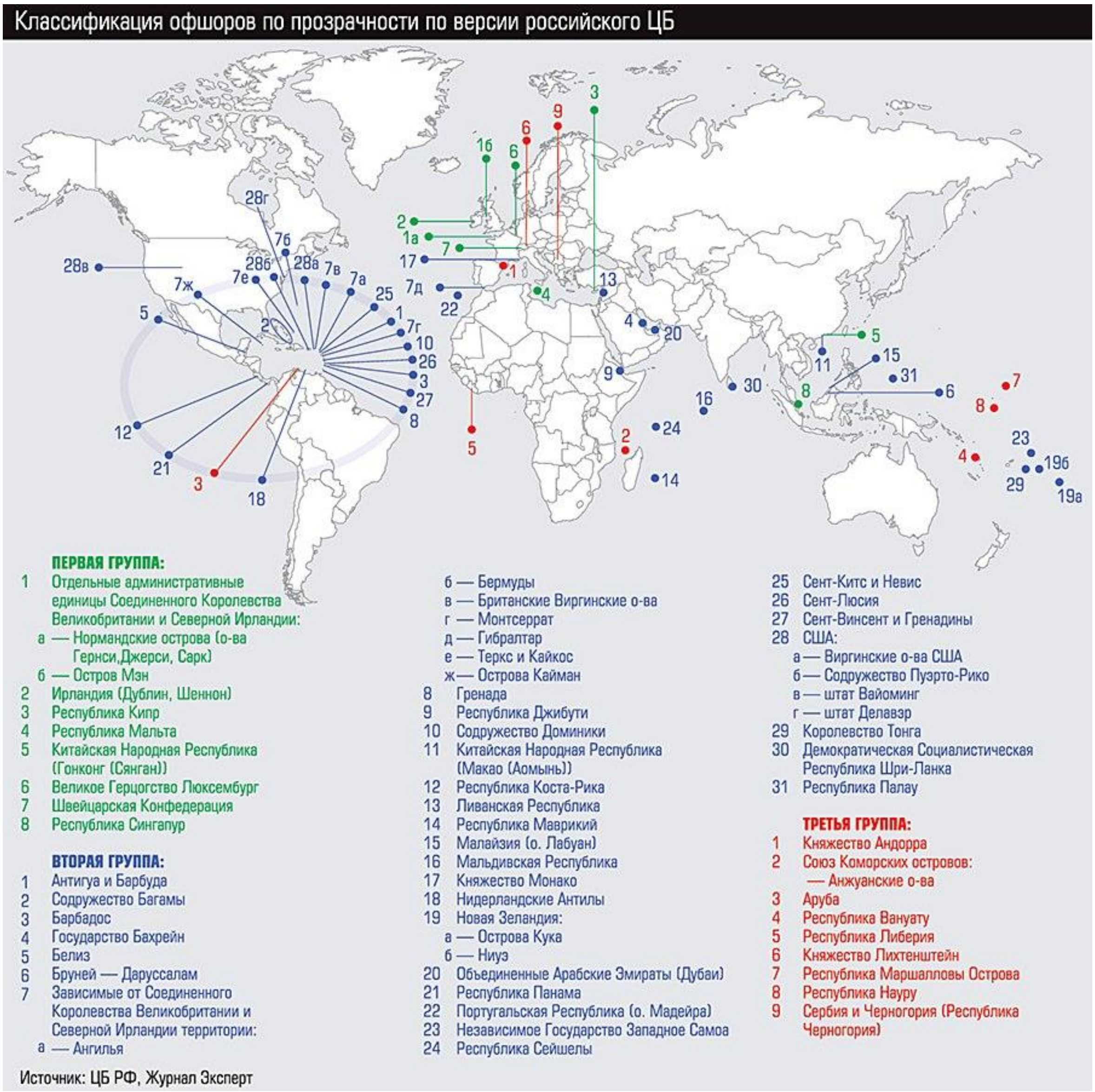
However, I find these prognoses to be short-sighted. Data and evidence suggests that the Bahamas and other Caribbean territories, as well as host of other offshore havens, are now firmly in the lead positions as capital sources in Russia. This has remained so even as Cyprus recovered its lead, and as other jurisdictions, such as Switzerland and the Netherlands, have gained importance. In the paper I explain this change by the effects of the deoffshorisation campaign launched by President Putin in 2011. The initiative, as I explain below, while still under-developed financially and institutionally, has prioritised criminal and legal mechanisms aimed at Russian businessmen and in particular, civil servants. As a result, their desire for secrecy havens in the search for asset protection has grown, fuelling the demand for the financial and legal services of fiscal havens such as the Bahamas.

1. Russia's Offshored Economy

Generally, it is difficult to overestimate the role of offshore fiscal havens in the globalisation of the economy (Palan 2003; Palan et. al. 2010). Offshore jurisdictions underpin the construction of most corporate and financial structures today, and are being used by individuals, corporations and states in their strategic planning and routine business operations. Offshore havens also play a very special role in the context of emerging and developing economies, effectively augmenting their role in the global structure of investments and capital flows. While it has been traditionally assumed that globally, capital travels from advanced economies into host countries – typically, undercapitalised emerging and developing markets - recently a different trend was noted by several key governing institutions. Globally, developing economies are becoming the leading players as both host and home of world FDI (Bulatov 2017 p.74).

Russia has a very special place in this global financial topography, having relied on offshore financial havens in its capital structure, ever since the collapse of the USSR. Whether one calls Russia's system of political economy oligarchic capitalism, crony capitalism or even a mafia state (Dawisha 2014), there is one aspect of the political economy of Russia that underlines all these theories. Since 1991, Russia's model of political economy has evolved around three main channels of global economic integration: 1) export of natural resources and a national system of redistribution of export revenues; 2) financialisation, acting as a boost for domestic consumption/demand; and 3) the offshored mode of the integration of Russian capital into global capital markets. The latter has become so prominent over time that the Central Bank of Russia (CBR) had to produce its own classification system of transparency of offshore financial centres, with world's fiscal havens divided into three main groups: advanced and transparent (green); semi-transparent (blue) and non-transparent (red).

Figure 1. Classifying Transparent and Non-transparent Offshore Havens, Russian Central Bank (2013)

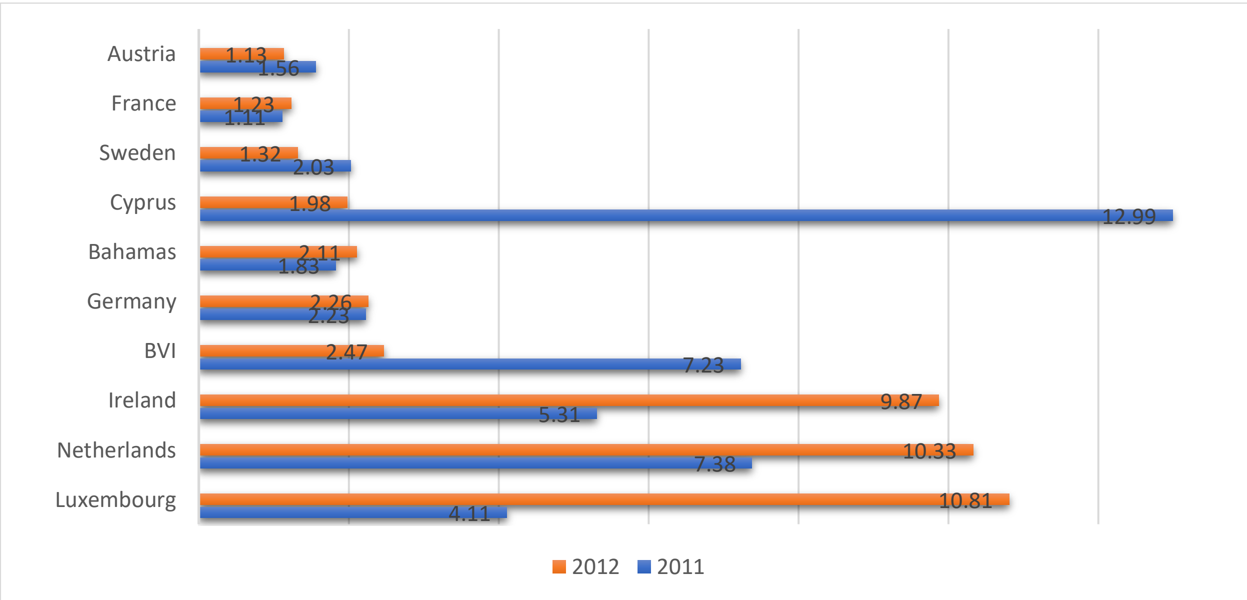


All three features have defined the traumatic period of the 1990s reforms and attendant crises, and persisted into the 21st century, notwithstanding the much-improved external economic context associated with windfall oil revenues since 2001-02. Indeed, Russia's economic growth during 2000-13, averaging 6.3 percent per year, helped sustain the efforts and appearance of a resurgent Russia on the global stage, as evidenced by the country's presence in global forums such as G8, G20, BRICs, etc. Domestically too, windfall gains from hydrocarbon exports, redistributed at federal and regional levels, enabled a consumer boom and a rise in living standards that sets Putin's Russia far apart from the crisis-ridden country governed by a 'stolen state' of the 1990s.

Although it was affected by the waves of the 2007-09 global financial crisis, with a deep drop in GDP, growth recovered relatively quickly. It was the 2014 drop in oil prices, which coincided with the introduction of anti-Russian sanctions by major powers, that slowed economic growth considerably and pushed Russia into an economic crisis. Between April 2014 and late 2015, the rouble has lost nearly half its value; net capital flight out of the country has doubled, reaching USD 151-160 billion in 2014; economic growth slowed down to 0.6 percent in late 2014, the lowest since the crisis of 2009. In 2015, Russia officially entered a recession. Between April and June 2015, Russia's GDP contracted by some 5 percent (and by 2.2 percent in January-March 2015).

The international sanctions and capital flight that escalated in 2014-15 laid bare the reality of Russia's appeal to international investors. While nominally part of the BRICs and deemed an emerging market with great potential for capital, Russia had never really become successful in attracting *foreign* investment.[2] It was only the brief period of 2006-07 that saw a net inflow of capital into Russia. Disaggregated data with respect to geographical origins of foreign investors in Russia reveals that the top foreign investors in Russia have consistently been Cyprus, the British Virgin Islands (BVI), Bermuda and the Netherlands.

Figure 2. FDI flows into Russia by country of origin, 2011-12 (billions of dollars)



[2] Ledyaeva *et al.*, *If Foreign Investment is Not Foreign*.

Source: Author's elaboration on Central Bank of Russia data. Central Bank of Russia (CBR), *Foreign Direct Investment in the Russian Federation: Flows Broken Down by Instrument and Country*, http://www.cbr.ru/eng/statistics/?Prtid=svs&ch=PAR_31141.

Table 1. **FDI inward and outward stocks of Russia, 2011 (millions of dollars)**

Inward 2011		Outward 2011	
Total	455,904	Total	361,738
Cyprus	128,816	Cyprus	121,596
Netherlands	59,745	Netherlands	57,291
BVI	56,442	BVI	46,137
Bermuda	32,545	Switzerland	12,679
Bahamas	27,089	Luxembourg	11,599
Luxembourg	20,316	UK	10,662
Germany	18,741	USA	9,501
Sweden	16,088	St.Kitts & Nevis	7,035
France	15,420	Jersey	6,692
Ireland	8,893	Germany	5,701

Source: Central Bank of Russia, *Foreign Direct Investment in the Russian Federation: Stocks Broken Down by Instrument and Country (directional principle)*, 2012.

The picture is mirrored in the structure of FDI out of Russia: the key destinations for Russian investment abroad in turn, have been Cyprus, the Netherlands, the BVI and Luxemburg.

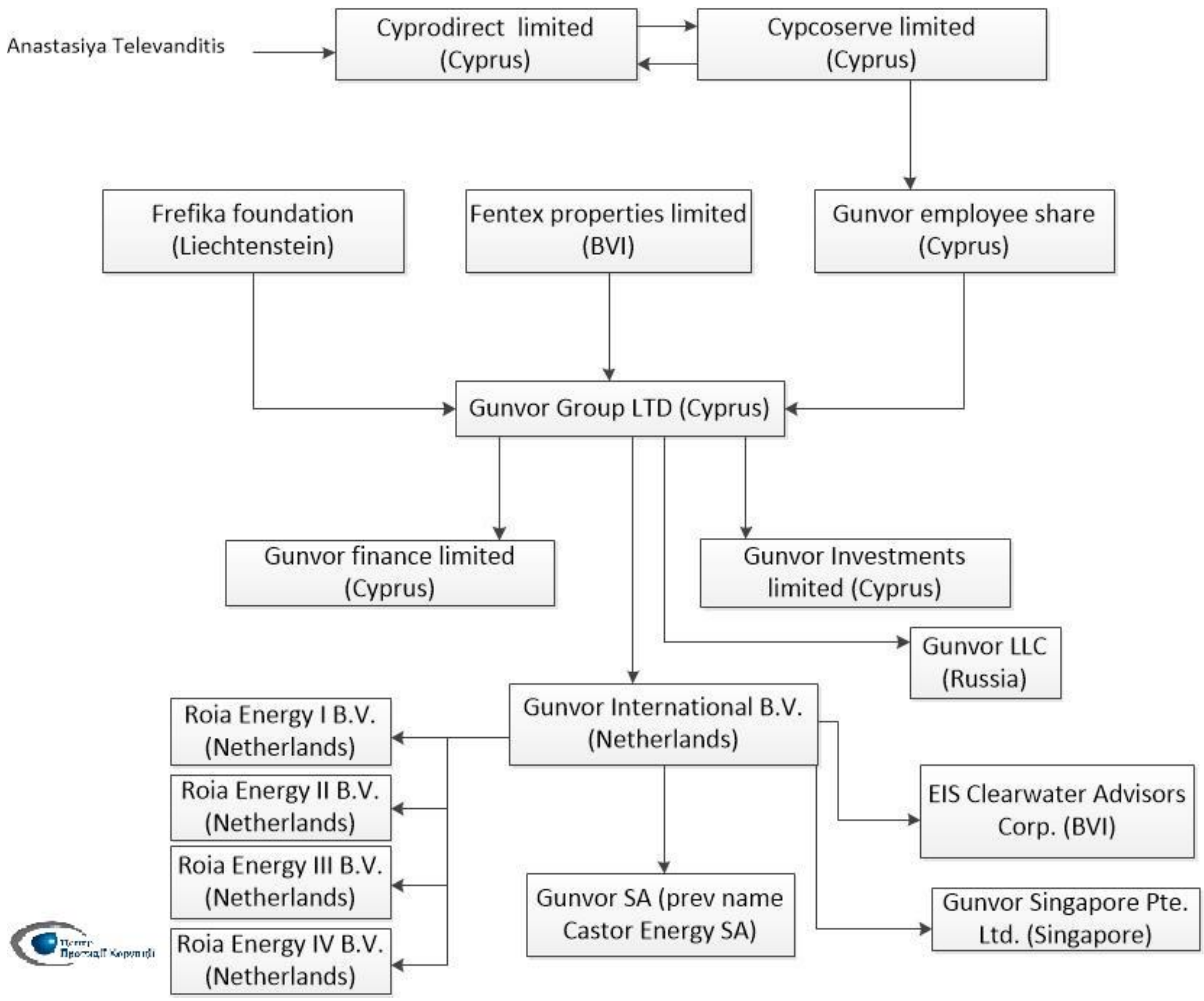
The data, as well as related research, suggest that it is the capital of Russian-owned structures, taken out of Russia through a chain of offshore-based intermediaries, that has been recycled back into Russia as FDI. As one indicator of the prevalence of offshore capital in the Russia economy, 14 out of 20 privately owned companies on Russia's Forbes list are owned by companies registered in offshore havens. Eight of such firms are from Cyprus, four from the Netherlands, and one each from Switzerland and the BVI.

To take one example, Yukos, the Russian oil giant owned by Michael Khodorskovky, was in fact a group of companies registered in offshore havens.[3] This is one of the reasons Yukos was able to bring a case against the Russian Federation in international arbitration courts. Another, more recent example is Gunvor, one of the world's largest oil trading firms allegedly having a close historical relationship with the Kremlin; since mid-2014, it has been under international sanctions. Officially, Gunvor employs a staff of 3,000 in 20 locations, with the majority in Europe.

According to an investigation by Ukrainian journalists, Gunvor is a complicated network of offshore shell companies. It is comprised of at least 27 offshore shells spread across 11 locations, with the majority in Cyprus and the Netherlands. Four anonymous companies are said to be conducting business in the UK, two in BVI.[4] (Figure 3)

Figure 3. **The Offshore Nexus of Gunvor**

[3] More specifically, Hulley Enterprises Limited ("Hulley" or "Claimant"), a company organised under the laws of Cyprus; Yukos Universal Limited (YUL), a company organised under the laws of the Isle of Man; and Veteran Petroleum Limited (VPL), a company organised under the laws of Cyprus.
[4] Kaleniuk and Peklun, "Hitting Putin's Pocket".



Source: Kaleniuk and Peklun, “Hitting Putin’s Pocket”.

Our own research into equity structure of Gunvor suggests yet a more complex picture. Gunvor is a global commodity business. But in the offshored corporate reality, it is a Lichtenstein-registered corporation with heaviest presence in Singapore and Cyprus (with most value being made in Singapore).

Figure 4. Gunvor: Equity Map (CORPLINK)

Figure 3. Map of Holdings of Frefika Foundation (Gunvor), all equity levels

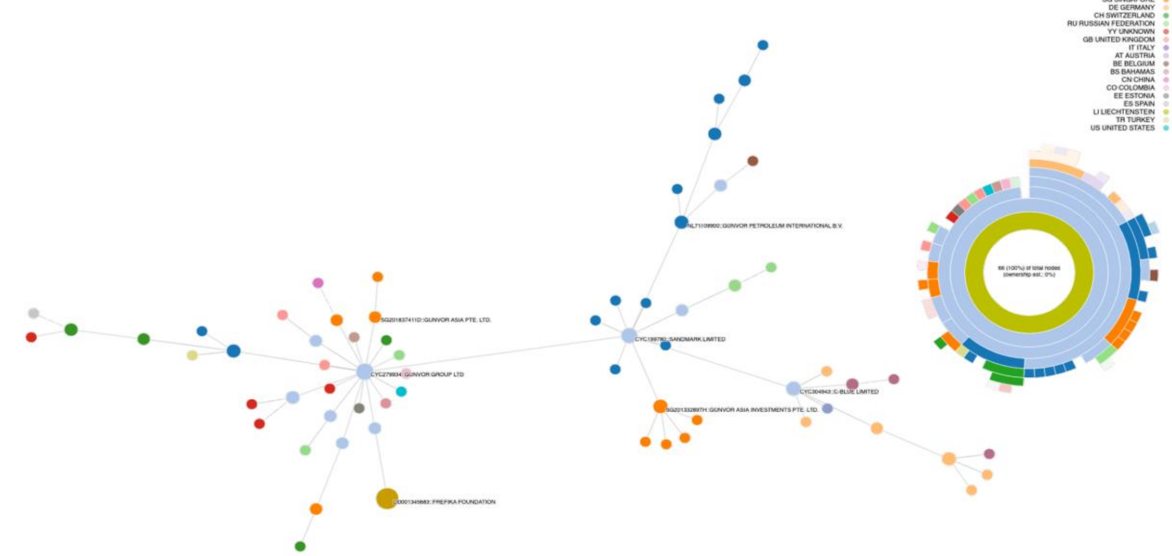


Figure 1. Number of Entities by Jurisdiction

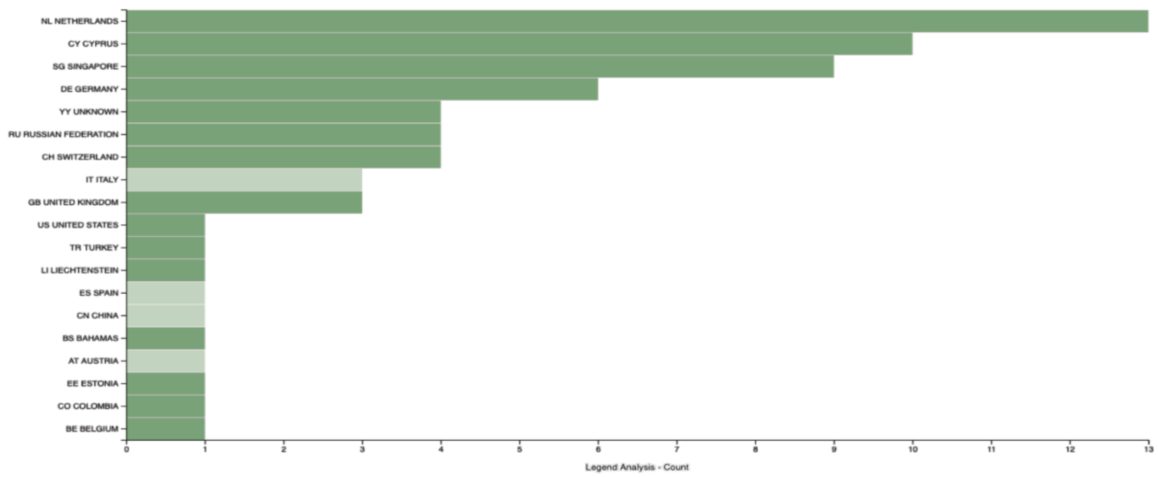
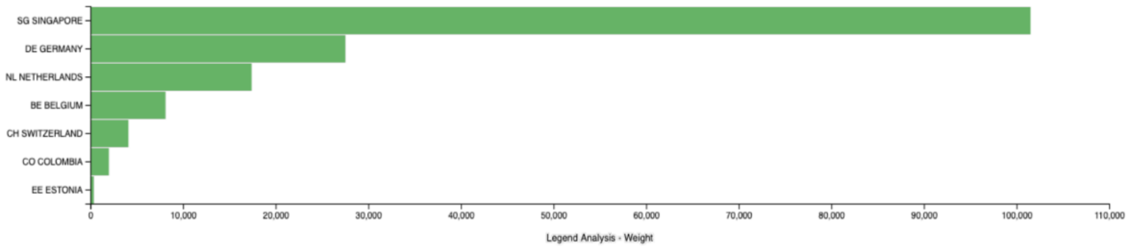


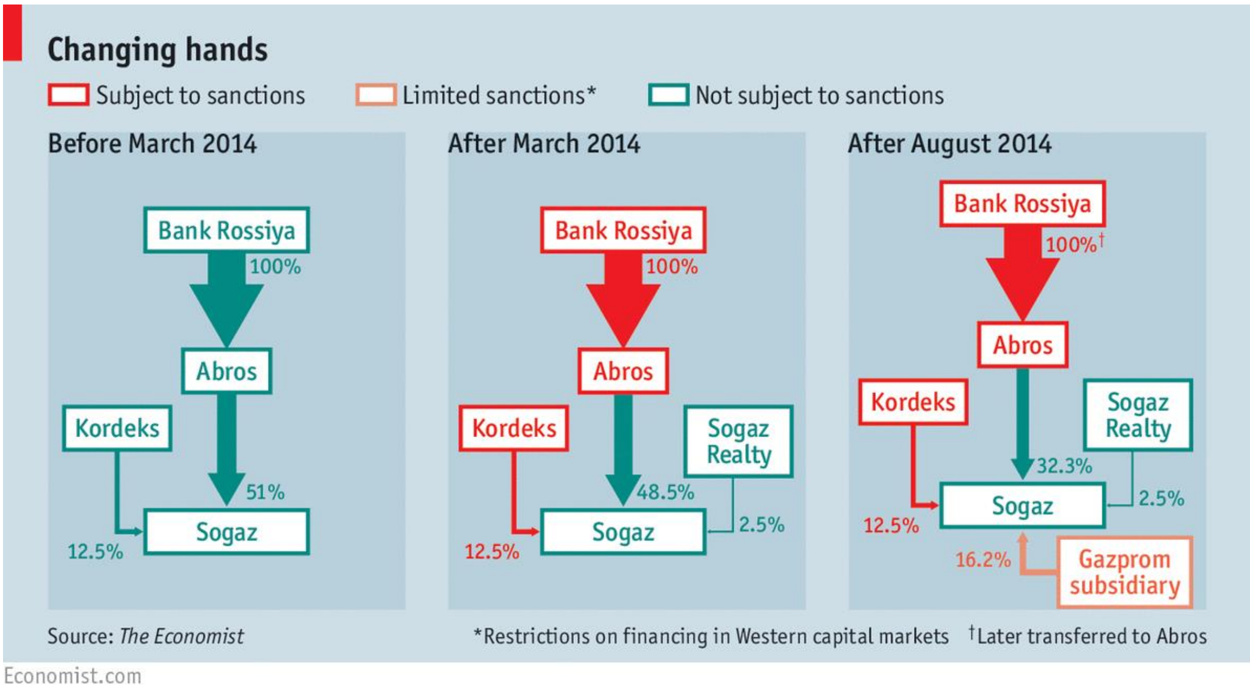
Figure 2. Mean Valid Accounting Value by Jurisdiction



Generally, it is hard to overestimate the role of the offshore network, a peculiar remnant of the British Empire,[5] both for the Russian owners of capital, as well as for international financial centres. Like elsewhere in the global economy, offshore facilities enable arbitrage and avoidance, as well as money laundering. Access to offshore ownership envelopes has enabled Russian owners to avoid the post-Crimea sanctions.[6] Offshore havens have also been benefiting the City of London and other financial centres in the post-2009 context, as money flowing out of Russia is not being recycled back into Russia but is invested in Western financial and property assets (with the exception of Crimea, where in 2014 there was an upsurge of foreign investments from Cyprus, the BVI and other offshore havens, led by inflows from Guernsey which accounted for 80 percent of all FDI into Crimea in 2014).[7]

Figure 5. How sanctioned Russian entities bust the sanctions

[5] Palan, "International Financial Centers".
[6] "Fancy footwork", *The Economist*, 52-3.
[7] "Kyda oseli $26,2 miliona inostrannyh investicii prednaznachennyh dlya ekonomiki Kryma?"(Where have $26.2 Million of Foreign Investments Intended for the Crimean Economy'Settled'?!), *RuInformer.com*.



Source: "Fancy footwork", *The Economist*

Foreign corporations too, use offshore jurisdictions (mainly to avoid sanctions), which makes discerning the origin of FDI difficult . For instance, 97.7% of FDI in Sakhalin originate in the Bahamas and Bermuda, with the region of Sakhalin accounting for 96.6% FDI into Russia as a whole.

Russia's deep-seated offshore-led mode of financial integration into the global economy brings out two issues. Formally, the country is considered a part of the BRICs, given its impressive growth rates generated by the expanding consumer market in 2000-14. As an investment opportunity, however, Russia has mostly been attracting Russian capital, with few non-Russian investors seizing the opportunities for capital grow (although there were several high-profile deals with foreign multinational corporations in the 2000s). Round-trip investors typically favour flows into the service sector, tend to establish manufacturing firms in resource-based industries and support the development of corruption in Russia by investing in corrupt Russian regions.[8] Throughout the post-1991 period, lack of diverse investment base, under-utilised internal market potential and an unfavourable external economic environment have always posed serious political-economic risks.

[8] Ledyaeva *et al*, *If Foreign Investment is Not Foreign*, 4.

2. Cyprus: Russia's Financial Centre

It is against this broader context that the ascent of the Caribbean tax havens in the list of Russia sources of capital, needs to be analysed. As it happens, there are two competing explanations for the rise of the Bahamas, the BVI and the like, on the list of Russia's main investors and FDI destinations. On the one hand, the relative decline of Cyprus as a Russian financial centre in 2012-13, suggests to many that the rise in the importance of Caribbean territories in Russia's capital structure is only a temporary phenomenon, replacing, in effect, Cyprus's lead at a time of Cyprus's internal financial crisis and international sanctions on Russia post-2014. On the other hand, however, the rise of the Bahamas, the BIVs and other exotic offshore zones on the list of Russian capital sources parallels another process - this time inside Russia itself - aimed at curbing the dependence on offshore capital and tighter control over foreign holdings of Russian assets. This process, I suggest, provides a much more long-term boost to the Bahama's role as a key destination for Russian FDI flows.

In order to evaluate these two (competing) theories, one specific issue needs to be flagged. Russia's extensive reliance on offshore havens has a peculiar function. While in the advanced economies, it is typically tax avoidance that is a common drive for the use of offshore schemes, in Russia, the use of overseas offshore havens has a distinct purpose. Around the world and specifically in the corporate economies of advanced countries, offshore structures are used in arbitrage schemes, typically to conceal profit flows or manage risks. In Russia, intricate chains of offshore-based entities are constructed with the aim of hiding the ultimate ownership of assets or to help launder funds. Historically, several former Soviet republics have functioned as central cogs in international money laundering chains (with the Baltic states and Moldova being the pioneers in the business, and Georgia, Abkhaziya and Armenia increasingly taking today over as offshore capital hubs and laundromats). But it is not only the EU periphery that is being used by businesses and criminal networks in their international financial dealings. Ireland, the Netherlands, and especially, Cyprus, are central elements in such schemes.

Since 1991, Cyprus has effectively served as the financial centre of the Russia Federation. According to CBR data, the country has been the leading origin of FDI in and out of Russia, throughout the post-1991 period. With a relatively close proximity to Russia itself and major European capitals, governed by common law and being part of the EU, Cyprus offers a set of advantages for corporate structuring and financial planning. In the long chains of Russian offshore 'envelopes' that may contain up to 20-30 corporate cells, Cyprus has historically been a popular node of initial offshore incorporation. The entity, in turn, would have financial and legal links to other financial havens in order to be able to tap into the onshore financial systems of Europe and North America. As of 2015, Cyprus accounted for 30% of all FDI flows into Russia, which is mirrored in the data for capital outflow throughout the period for which data is available.

Two typical models are used in Cyprus-anchored offshore chains:

1. A Russian company belongs to a Cyprus ‘mother’. The Cyprus company gives its Russian ‘daughter’ a loan (or the right to use the brand name, licence, etc.). The Russian company sells products in the Russian market and earns revenue. Most of this revenue goes to paying off the Cyrus mother (either as interest on the loan or as a fee for the title/right/royalty). As a result, the net profit of the Russian daughter is minimal, most of the sum goes to Cyprus.
2. A sub-type of the same model is based on exports: a Russian company sells products to a Cyprus firm at a low price. The Cyprus company in turn, sells products to the final consumer at a higher price. In reality, these are only recorded ‘paper’ transactions; the products go directly from Russian producer to (Russian) final consumer.

As elsewhere in the world, offshore havens also play a central role in real estate operations in Russia. In a typical scheme, a building in Russia would belong to a Russian company, but the Russian company itself would belong to a Cyprus company. What you buy in this case is not the piece of real estate, but the shares of the Cyprus company. This saves on VAT and defers profits. The leading locations of offshore jurisdictions for Russian firms are Cyprus, the Netherlands and the BVI. In 2014, the profits of Cyprus based Russian companies totalled 9.056 trillion RUR. This scheme was supposed to be banned in Russia by the end of 2015.[9] Overall, according to NBER, the share of Russian private capital in global offshore is about 8% of total offshore funds globally. Globally, the figure is $5.6 trillion, or 10% of the world’s GDP. In the context of Russia, the scale of Russian offshore assets is close to 60% of the country’s GDP, or apprx. $1 trillion. [10]

3. The Political Economy of Deoffshorisation

[9] Telegin, “Begyshie milliardery. Pochemy geroyam Forbes teper’ luchshe ne zhit v Rossii?” [Running Billionaires. Why Forbes Heroes Do Not Live in Russia?].
[10] Source: https://internationalwealth.info

It is partly due to this long-running structural dominance of offshore havens in Russian capital flows; partly (and perhaps in large part) due to the fact that offshore structures are used to conceal the identity of the owners of the assets, not only from the international regulators, but most crucially, from the Russian authorities too, that President Putin announced the launch of the national deoffshorisation campaign back in late 2011, long before the post-Crimea international sanctions hit Russia's exports and imports.

Over time, the campaign has evolved to centre three main sets of initiatives: *punitive and penalising* measures aimed at Russian officials and civil servants relying on offshore havens; *enabling* institutional reforms and financial mechanisms aimed at encouraging capital back into Russia; and a series of legal initiatives aimed at *adapting* the Russian tax code and financial regulation. The latter, it needs to be said, has generally been lagging behind the changing market context ever since the first reforms were introduced in 1991. As follows from below, deoffshorisation measures reached their height around 2014-15, when the country was hit by the double crisis of falling oil prices and the first wave of international post-Crimea sanctions. And while it is around this time that Russian authorities like to report that deoffshorisation measures yielded tangible results, some data suggests otherwise.

Russia: The Chronology of Deoffshorisation

2011-2013

23 December 2011. Putin makes the first statement about the abuse of offshore schemes. They key problem, according to him, is the fact that it is impossible to identify ultimate beneficial owners (UBOs) behind offshore schemes.

12 December 2012. "We need a whole set of measures that would build into a system of offshorisation of the economy", - the task set by V. Putin was delegated to the Senate.

February 2013. The government is instructed to prepare a set of deoffshorisation measures.

16 March 2013. The height of the financial crisis in Cyprus. The EU and Angela Merkel make financial aid conditional upon expropriation of bank deposits by imposing a one-off levy. 30% of deposits in Cyprus ($20bn) belong to Russian clients.

2014

30 April 2014. Sberbank, Russia's largest bank, folds its service to offshore firms. *Rocket Bermuda Ltd.*, controlled by Sberbank, informs its clients that they have to close their accounts serviced on Bermuda islands.

22 May 2014. Gennady Timchenko, one of the richest businessmen in Russia and a close friend of the President, promises he will transfer all his assets to Russia by the end of the year. His wealth is estimated at over $15bn.

23 June 2014. Putin introduces into the Duma the first draft of the Law prohibiting civil servants from having foreign bank accounts.

11 November 2014. CBR reports that illicit capital flight out of the country did not go above $9bn, which is almost three times smaller than $23bn for the same period of 2013.

18 November 2014. Duma passes the tough version of the Law on the Deoffshorisation of Business. One of the most significant changes: controlled foreign companies (CFCs) will now have to pay taxes into Russia's federal budget (rather than simply declaring the income and activities, as was the case before). The new anti-offshore law requires, first, that a Russian business owning 10 percent or more of a foreign company has to declare this ownership to Russian tax authorities. (In December 2014, Putin offered amnesty on all foreign asset ownership by civil servants, their relatives and former relatives). Also, if a Russian citizen owns, directly or indirectly, 50 percent or more of a foreign company, he/she will have to pay tax on its profits. (It remains debatable to what extent the new anti-offshore law will be successful, as opportunities to avoid new requirements exist. In the first half of 2015, Russia remained a net exporter of capital, albeit at a lower rate than in late 2014.)[11]
25 November 2014. Putin signs the law on deoffshorisation, obliging individuals and corporate entities to inform tax authorities about participation in ventures with foreign capital. The Russian Tax Code is also adapted to include mechanisms to tax profits of offshore companies.

12 December 2014. Duma bans anybody connected to Russia's national security systems, to have foreign accounts.
19 December 2014. Alisher Usmanov, one of the richest oligarchs, transfers his key assets (back) to Russia.

2015

[11] The CBR estimates that capital flight out of Russia will reach USD 111 billion in 2015.

20 January 2015. Russia ratifies the Joint Convention of EC and OECD on bilateral administrative assistance in taxation matters. Several offshore jurisdictions join the convention, which was a step forward as previous they could not exchange information due to the lack of bilateral taxation treaties.

23 March 2015. Central Bank of Russia (CBR) reports that due to the new measures, illicit capital flight has declined from $26.5bn to $9bn on a year to year basis.

20 April 2015. Rosfinmonitoring imposes banking (counter)-sanctions on 41 countries – banks are obliged to report all clients dealing with states that imposed anti-Russian sanctions, sponsors of terrorism and those not fighting corruption.

5 May 2015. The UK reportedly lost $356 bn of capital investment over 15 months, with the departure of Russian money constituting the bulk of the exodus (*The Times*).

8 June 2015. Putin signs the law on Amnesty of Capital – capital of whichever origin - is welcome back in Russia.

13 July 2015. Putin signs the law banning government purchases in offshore zones. Russian Tax code now has the new concept of CFC. Legal measures: amendments to the Tax Code, including the law on CFCs. Latest amendments include: the removal of criminal liability if CFCs pay back fully to the budget, compensating for any lost income related to unpaid or underpaid taxes by CFCs.

23 October 2015. Russia Duma MPs and civil servants at municipal levels can lose their mandate of they do not submit income declarations. On the 4th of November 2015 - the draft would become Law.

27 October 2015. Russian Parliament publishes the list of countries subject to new CFC rules. It includes 119 states, most of which are offshore jurisdictions (previously there were only 40). Included in the list are also the UK, Austria and Switzerland.

3 November 2015. Alexander Grigoriev is arrested. Grigoriev had been a leader of a large criminal network, which has laundered over $50bn. He was a co-owner of several credit institutions.

11 November 2015. CBR reports that illicit capital flight has shrunk twofold, compared with 2014.

29 December 2015: Capital amnesty on capital brought back into Russia is extended till 30 June 2016.

2016

18 January 2016. Net outflow of capital is down to $56.9bn, which is 2.7 times smaller than in 2014 ($153bn).

29 December 2016. Putin signs the law banning MPs and civil servants, as well as national security staff, from owning foreign assets. In 2016, CBR reported that about $12,664 bn of offshore funds, including from France and Germany, was repatriated back into Russia and that the inflow of capital into the economy is on the rise.

2017

20 April 2017. *Laundromat*. Cisinau. Vyacheslav Platon, a criminal gang leader, is sentenced to 18 years for taking $20 bn out of Russia into offshore havens.

21 December 2017. Putin instructs the authorities to decide on the parameters of Eurobond issue to attracted capital back into Russia and issue the bond in 2018. The bonds would be tax exempt, part of an ongoing amnesty on capital stashed abroad as the Kremlin looks for ways to help its allies insulate themselves against sanctions risks and return their wealth to Russia. Some ministers suggest extending capital amnesty. Putin proposes to exempt any money returned from the 13 percent national income tax.[12]

2018.

13 January 2018. *Gazprom Burenie* 'has finalised its deoffshorisation.'

[12] https://thediplomat.com/2018/01/the-fatal-offshore-deoffshorization-and-russias-infrastructure-crisis/

1 May 2018. The UK Parliament passes the Law obliging its overseas territories to declare UBOs. As far as Russia is concerned, the measure is aimed primarily, at Russian oligarchs.
3 May 2018. Putin signs a pack of measures aimed at creation of Russia's own offshore zones (Primorsksy Krai and the Oktjabrski island in the Kaliningrad oblast). One of the deoffshorisation measures as declared by Putin has been the creation of special economies zones (The Russian internal offshore). The expectation of the authorities is that these zones may attract up to $1bn into Russia.
2018. The UK has a new mechanism of unexplained wealth orders (UWOs).

2019.
9 July 2019. EN+ Group (owned by Oleg Derispaska) re-registered from Jersey to Russia.

4. "I'm going for the Bahamas": The Peculiar Result of the Deoffshorisation Campaign

According to Russian officials, the de-offshorisation campaign has brought fast and tangible results. Most of these were apparent, we are told, already by 2015-16. For instance, as of 2015, most of the companies in the leading RBK-500 list had Russian (rather than offshore) registration: 239 companies out of 500 were registered in Russia (47.8%). In 2016, CBR reported that about $12,664 bn of offshore funds, including from France and Germany, was repatriated back into Russia and that 'the inflow of capital into the economy was on the rise.'
Outside of the official proclamations however, the campaign has barely brought some success. There are, indeed, four high-profile companies that did bring their operations back into Russia:

1. December 2014. USM Holdings Ltd., owned by Alisher Usmanov, who finalised the transfer of control shares of two of the companies – Mellalloinvest and Megafon - which now will pay taxed into Russian budget.
2. RUSAL (Owner: Oleg Deripaska). Declared the intention to transfer residence from Jersey to Russia.
3. KAMAZ. Declared the intention to transfer the financial securities back into Russia.
4. RUSGIDRO liquidated its Cyprus-based companies.

On a larger scale however, the deoffshorisation campaign yielded feeble results; and so far, Russia has failed to become a sought-after investment opportunity.

As of 2016, Russia is one of the five leading investors into offshore (paralleled by the increased inflow of offshore capital into Russia).[13]

Overall, seven countries continue to account for 75.7% of FDI into Russia (Cyprus, Luxemburg, Bahamas, Bermuda, BVI). While these seven are traditional offshore havens, the status of the Netherlands and Ireland is more complex.

Table 3. FDI investors into Russia, January 2015

Counties and territories	$, million	Share in RF, %
Total	353444	100,0
Cyprus	100883	28,5
Netherlands	51377	14,5
Luxemburg	38749	11,0
Ireland	26493	7,5
Bahamas	21025	5,9
Bermuda	14569	4,1
BVI	14310	4,0
Germany	11623	3,3
Switzerland	10978	3,1
UK	10457	3,0
France	8818	2,5
USA	8701	2,5
Austria	7849	2,2
Jersey	4130	1,2
Finland	3143	0,9
China	2810	0,8
Sweden	1772	0,5
Belgium	1215	0,3

[13] Source: ruxpert.ru

Japan	1209	0,3
South Korea	1208	0,3

Data from CBR; Kuznetsova 2015: 55.

The much-publicised attempts by the Russian government to repatriate Russian offshore assets, yielded only a temporary victory. In reality, notwithstanding the new law on controlled foreign companies, the deoffshorisation campaign does not appear to have convinced businesses to return assets back into the country. Capital amnesty only worked for some 15% of capital, where owners of the assets uses the new law to declare their assets to the Russian authorities. The government opted to extend the amnesty into March 2019, opening the second wave of potential capital return.

The same, am afraid, applies to the aim of bringing corporations and their assets back into Russia. The devil, as they say, is in the detail. The RBK-500 list includes 87 state corporations which are *obligated t*o register in Russia. Thus only 152 private corporations out of 500 are actually registered in Russia, with 183 registered abroad, and a further 38 companies registered offshore via envelopes and shells. Some 40 corporations did not reveal their jurisdictions. Even with sanctions pressure on business, the share of companies carrying out large transactions under Russian legal jurisdiction has grown from 10% to 34%. But businessmen living more than six months abroad every year can still dodge most taxation and information disclosures, despite new laws that allow companies to remain registered abroad but require certain taxes on profits or personal incomes.[14]

Rich Russians, individuals as well as businessmen, also seem to doubt the bright prospects of the Russian economy, continuing to direct their funds offshore. The government insists that the federal budget is in surplus, saying that anti-Russian sanctions are pointless. Capital flight was estimated to reach $19bn (up from $16bn), a tendency that is often explained by the falling oil price. In 2018, capital flight accelerated ($17bn, up from $10bn in 2017). Thus in the first quarter of 2918, the federal budget was lacking 4.3% of the country's GDP.[15] It is these futures, along with the penalising measure and some high-profile arrests at the very top of the Russian power channels, that suggest to me that jurisdictions such as Bahamans, the BVI and Bermuda will continue to be an important source of capital into and out of Russia.

[14]https://thediplomat.com/2018/01/the-fatal-offshore-deoffshorization-and-russias-infrastructure-crisis/
[15] https://bosco-conference.com/ru/novosti/vyvod-rossijskogo-kapitala-iz-rossii-v-offshory-stremitelno-rastyot

There are several reasons for this. First, generally, despite the many officially declared successes of Russia's deoffshorisation, businesses continue to take capital offshore. Cyprus in particular, despite the blip in 2012-13, remains the financial centre for Russia. In the first quarter of 2018, about $9.6 bn left for Cyprus. Russian demand for real estate and commercial property was up 40% in 2018. There is always increased demand for Cyprus passports. There is also Russian demand for real estate in Malta. Capital flight from Cyprus is due to mainly, reduction of investment in Russian companies; it has reached $13.9 bn in the past year, a record for three years. As of 2018, there was $10.3 bn more of capital flight from Russian to Cyprus (rather than vice versa). The negative balance of FDI is thus highest in the past 12 years, among all the world's countries.
Cyprus was followed by the BVI ($1.9bn) and the Bahamas, were rich Russians poured some $1.8bn. Next were Ireland ($1.5bn), the Netherlands ($1.1bn) and Hong Kong ($1bn). $1bn left for Luxemburg and Bermuda.

Second, the main financial instrument designed to bring capital back in into Russia – the Eurobonds – also proved problematic. The proposed structure of the Eurobonds present Russia's capital owners with the reverse problem of squirreling money away from sanctions exposure: their money is in Russia where it can be raided by others. The latter include competitors in business, including, in particular, those who can utilise the administrative resource of the Russian state. Further, the specifics of the Eurobond structure remain unclear, deterring investor demand for the securities. (All that is known for certain is that up to $3 billion in Eurobonds would be issued and no special conditions would be entailed with their issuance). As these instruments are likely to be tax exempt, it is plausible that most of those who bought the bonds would want the money in cash and thus dodge capital gains taxes in Russia entirely. [16]

Third and perhaps more important in a long-term context, Russia's internal institutional reforms aimed at curbing the use of offshore capital have produced a paradoxical result. The measures may not have been too effective at the systemic level, but they did generate enough impact so as to scare the holders of the assets to use ever more intricate ways to hide their wealth. Here, changes to Russian legal code, as well as the criminalisation of foreign ownership, have been key. To date, the concept of the trust has been alien in the Russian law, if not Russian practice: Russians do set up trusts in tax havens. In the advanced markets, such arrangements are typically used as a first step of an investment in Europe or North America

[16] Ref.

markets. Russian settlors of these trusts often place Russian assets into the trusts as protection from Russia's internal oversight and potential raids, with Russian residents often being unknowing (or knowing) beneficiaries.

Against this context, it is interesting that the Russian authorities are (slowly) working towards a fuller development of the concept on trust in the national law. Although trusts are often used by businessmen for tax planning reasons, the Russian government believes that introduction of the concept of trust, in which legal ownership is separated from beneficial ownership, will not conflict with the general aims of the deoffshorisation initiative. Under the existing legal arrangements, many planning tools of the trust are not available under the Russian legal system. Among other things, Russian concept of *Doveritelnoe Upravlenie* does not make a distinction between legal and beneficial ownership, and the duration of the transfer is usually for a short period, much like an escrow prior to a sale or a period of administration during incompetency.

In addition to fears of competition and power struggles in the wider setting of national political economy, it is the lack of clear legal guidance and state guarantees that pushes many Russian asset owners to increasingly rely on the more exotic tax havens that offer secrecy and protection. Professional enablers advise their Russian clients to place a corporation or a holding company under the trust to hold all the assets. This creates additional protection in the event that the trust is not recognised by the Russian tax authorities.

Conclusion

Around 2014-15, Russian official records noted a peculiar ascent of the Bahamas and other exotic tax havens as leading sources of capital in and out Russia. The phenomenon was interpreted as a temporary change, mostly to do with the relative decline of Cyprus as Russia's *de facto* financial centre, and the newly imposed international sanctions on business dealings with Russia.

In this paper I disputed these projections. Such prognoses, I argued, turned out to be short-sighted. Data and evidence suggest that the Bahamas and other Caribbean territories, along with other offshore havens, are now firmly in the lead positions as capital sources in Russia. This has remained so even as Cyprus recovered its lead, and as other jurisdictions, such as Switzerland and the Netherlands, have gained importance. I have analysed this change by the effects of the deoffshorisation campaign launched by President Putin in 2011. The initiative, as I explained above, while still under-developed financially and institutionally, has prioritised criminal and legal measures aimed at Russian businessmen and civil servants. As a result, their desire for secrecy havens in the search for asset protection has grown, fuelling the demand for the financial and legal services of fiscal havens such as the Bahamas that, remain reluctant to fully follow the new international disclosure norms.

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