

The Analysis of the Criminal Case: The Prosecution of Nika Gvaramia

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Key Findings

Transparency International Georgia studied the criminal case #074200719801. The review of the indictment against Nika Gvaramia and the evidence provided in the case has made it clear that the accusation involves key theoretical issues of the corporate law as well as the criminal law.

Taking into consideration the Georgian legislation, norms of international law, court practice, legal doctrine and the facts of the case, the embezzlement of property rights, commercial bribery, creation and use of false official document by Nika Gvaramia cannot be proved.

Furthermore, the charge of legalization of illegal income levelled against Nika Gvaramia neither contains signs of money laundering crime defined in Article 194 of the Criminal Code nor conforms to its conventional content.

The majority of charges brought against Nika Gvaramia are related to managerial decisions taken by him in 2015. According to the reasoning set out in this document, only in exceptional cases may the taking of risks and certain managerial decisions in the interest of the company by a director become a ground for corporate liability, let alone criminal liability.

Holding a director liable because of a managerial decision, taken when running a company, that did not bring the enterprise as much income as in the previous year contravenes the business judgment rule. A director may take risky decisions in the best interests of the company. He must not be held liable only because his decision has not proved successful or profitable for the company. A director's decision may fail to earn profit for a company, but be justified for carrying on the company's efficient operation.

I. Factual Circumstances of the Case

On 9 August 2019, Nika Gvaramia was charged under the investigation launched on 20 July of the same year. On 1 November 2019, the initial indictment was extended to include new charges. Nika Gvaramia was accused of embezzling property rights in aggravating circumstances, commercial bribery, creating and using a false official document, legalizing illegal income, and abusing power.¹

Over the period between September 2014 and July 2019, Nika Gvaramia served as General Director of Rustavi 2 Broadcasting Company Ltd (hereinafter, Rustavi 2 or Company). To sell commercial airtime, the Company had a contract with sales houses. In 2013 and 2014, the contractor, in addition to fixed payments, received approximately 5% of all proceeds from commercial airtime as a bonus at the end of each year.

The above-described payment arrangement was amended under a master agreement with Inter Media Plus Ltd (hereinafter, the Sales House) which was signed on 16 January 2015. According to the agreement, the parties were to agree on a particular amount of payment every month. During the last four months in 2015, the revenues of the Company declined as compared to the previous year. Decisions taken during that very period became the ground for bringing changes against Nika Gvaramia.

Episode of Embezzlement of Property Rights

According to the prosecution, Nika Gvaramia, while serving as General Director of Rustavi 2, abused official duties, failed to act in good faith and in the interests of the Company. In particular, over the period from September through December 2015, he demanded from Inter Media Plus Ltd that it agree, in exchange for ceding the right to place commercial advertisements to it, to a smaller remuneration than it received under the agreement on a similar service concluded in 2014. As a result, Gvaramia, jointly with the financial director of the Company, embezzled the property rights of Rustavi 2, defined in the master agreement, and caused a material damage of GEL 6 763 509 to the Company. The amount of the damage was calculated by the prosecution as a difference between the revenues from commercial ads (GEL 43 230 509 in 2014 and GEL 36 467 000 in 2014). The prosecution reckoned that since the advertising market had not shrunk, the Company must have received the revenues in the similar amount to the previous year.

¹ The offences provided in Subparagraphs “a” and “d” of Paragraph 2 of Article 182, Subparagraph “b” of Paragraph 3 of the same article, Paragraph 3 of Article 221, Subparagraph “b” of Paragraph 2 of Article 362, and Subparagraph “c” of Paragraph 3 of Article 194 of the Criminal Code of Georgia (hereinafter, GCC).

This document assesses the accusation provided in the first part of the indictment.

Episode of Commercial Bribe, Creation and Use of a False Official Document

According to the prosecution, as benefit in exchange for embezzling the property rights of Rustavi 2, Nika Gvaramia obtained immovable property (two apartments) from Inter Media Plus Ltd. through a sale and purchase agreement of 21 March 2017. To ensure the receipt of the immovable property, false (fictional) loan agreements were executed on 5 and 25 July 2016. Based on the aforesaid, the director of Inter Media Plus Ltd., pretendedly in exchange for the repayment of loan liabilities, transferred the abovementioned immovable property to Nika Gvaramia on the basis of the sale and purchase agreement.

Episode of Money Laundering

According to the indictment, after receiving the property, Nika Gvaramia decided to legalize illegal income. To make a criminally obtained property appear lawful, to conceal its true nature and disguise a source of origin and the property, Nika Gvaramia sold the property for GEL 602 521.80 on 7 July and 26 September 2017 and as a result, got an especially large amount of income.

Nika Gvaramia's Position

At the stage of investigation, on 2 August 2019, Nika Gvaramia was interrogated as a witness before a magistrate judge. According to him, the aim of agreeing a fixed rate under the master agreement of 16 January 2015 was to insure the Company against risks and if the advertising market deteriorated, to guarantee the inflow of revenues necessary for the operation of Rustavi 2. That decision was endorsed by the partners of the Company. In the first eight months of the year, the Company received an income similar to the previous year. However, with a lawsuit filed by Kibar Khalvashi against Rustavi 2 in August 2015, Rustavi-2 assets and partners' shares frozen and related court hearings underway, also, changed advertising market regulations, the risks of the market deteriorating and accordingly, revenues declining became real. Therefore, based on the master agreement, Nika Gvaramia requested from the Sales House a guaranteed amount that would be necessary for the Company to carry on operations. After the above risks did not materialize, from 2016, the Company reverted to the previous payment arrangement.

II. Charge of Embezzlement of Property Rights and Commercial Bribery

According to the indictment, Nika Gvaramia violated his obligations assumed under the charter of the Company and the legislation, and did not act in good faith and in the interest of Rustavi 2. Consequently, the lawfulness of managerial decisions taken by Nika Gvaramia and soundness of the criminal charge against him must be assessed in the light of a status of company manager and his rights and responsibilities under the corporate law.

Company Management and Control

The Law of Georgia on Entrepreneurs defines an obligation of a director to conduct the company's business in good faith; in particular, to take care as an ordinary person of sound mind in a similar capacity and under similar circumstances and to act in the faith that his/her action is in the best interest of the company.² A director may be held liable for the breach of these very obligations.

Despite the absence of a universal principle of good corporate governance, it is acknowledged that the management of a company must rest on the principles of independence, accountability, transparency and good faith.³ It is important that a director selects qualified employees, establishes a competent management structure, leads the activity of company in good faith and undertakes actions towards the increase of company's efficiency.⁴

Efficient management of a company is the key responsibility of a director. Efficiency implies not only generation of profits, but also a sustainable development of the company to maximize profits. To increase a company's efficiency, a director has to take decisions on a daily basis. In a changing business environment, however, it is impossible to plan all nuances in advance. Therefore, in order to act for the success and in the best interests of the company, a director has discretion to exercise flexibility in decision making. To make a business successful and avoid potential losses, a director may take risky decisions. A conscientious director must not be held liable only because his/her decision did not prove successful or profitable for a company.⁵

Advantage of a limited liability company mainly lies in its flexibility, in a limited liability of partners and the directorate. Protection of leadership from liabilities facilitates risk-taking, encourages innovations, fosters entrepreneurship and supports economic development.⁶ Naturally, a director may be held liable under the conditions of limited liabilities too.⁷

² The Law of Georgia on Entrepreneurs, Paragraph 6 of Article 9.

³ Du Plessis and et al., *Principles of Contemporary Corporate Governance*, Cambridge University Press (2018).

Also, National Association of Corporate Directors, *Key Agreed Principles to Strengthen Corporate Governance for U.S. Publicly Traded Companies* (2011) <https://www.nacdonline.org/files/PDF/KEY%20AGREED%20PRINCIPLES%202011.pdf> [Last visited: 10.03.2021].

⁴ *Ibid.*

⁵ Bakakuri, Gelter, Tsrtsvadze, Jugheli, *Corporate Law – Textbook for Lawyers* (October, 2019) 79.

⁶ McPherson and Raja, *Corporate Justice: An Empirical Study of Piercing Rates and Factors Courts Consider when Piercing the Corporate Veil*, 45(3) *Wake Forest Law Review* (2010) 931.

⁷ Freedman, *Harpooning the Corporate Whale: A Federal Maritime Treatise on Veil-Piercing*, 43 (1) *Transportation Law Journal* (2016).

Piercing Liability of Director

A doctrine of piercing the corporate veil originated because of its corporate context. Directors or partners may be held personally liable for creditors' loss. In case of fraud, inadequate capitalization, neglect of corporate requirements or abuse of power, managers or partners may be subject to personal liability. For piercing the corporate veil, it is necessary that several fundamental elements occur cumulatively:⁸

- Instrumentalization of a company or the case of so-called alter ego
- Wrongful use of the corporate form
- A causal relationship to the loss

Determining a piercing liability is an exceptional case of individual liability. The application of the doctrine may “like lightning” bring rare and severe results.⁹ Failure of company managers to fulfill corporate requirements alone cannot constitute a ground for veil piercing.¹⁰ It may be applied in case of breaching fiduciary duties or committing a crime.

While leading a company, duties of a director are divided into two groups: the duty of care and the duty of loyalty.¹¹ Duty of loyalty means primacy of interests of a company. It is unacceptable for a director to take decisions to the detriment of company for personal gains.

According to fiduciary (care) duty, managers and board of directors of a company shall conduct company business in good faith, in the honest belief that the action they take are most conducive to goals and interests of the company. It also requires the demonstration of diligence of an ordinary person.¹² **Liability of directors arises not when decisions taken by them has not brought profit to a company but when the failure of directors to fulfill their obligations has caused damage to a company.**¹³

⁸ Blumberg, *The Transformation of Modern Corporation Law: The Law of Corporate Groups*, 37(3) *Connecticut Law Review* (2005) 605.

⁹ McPherson and Raja, *Corporate Justice: An Empirical Study of Piercing Rates and Factors Courts Consider when Piercing the Corporate Veil*, 45(3) *Wake Forest Law Review* (2010) 931.

¹⁰ Bell, *Veil Piercing and LLCs: Supporting the Case for a Meaningful, Legislated Standard*, 52(4) *South Texas Law Review* (2011) 615.

¹¹ Jugheli, *Protection of the Capital in Joint Stock Company*, German Agency for Technical Cooperation (GTZ) 2010.

¹² Chanturia, *Corporate Governance and Liability of Directors in the Corporate Law*, Tbilisi, 2006.

Model Business Corporation Act (2016 Revision) (December 9, 2016), §8.30.

https://www.americanbar.org/content/dam/aba/administrative/business_law/corplaws/2016_mbca.pdf [Last visited: 10.03.2021].

¹³ Cahn and Donald, *Comparative Company Law: Text and Cases on the Laws Governing Corporations in Germany, the UK and the USA* (2nd ed.), Cambridge University Press (2018).

The Business Judgment Rule

The business judgment rule is a rule providing directors with guarantees of freedom in making business and non-interference with business.¹⁴ However, it is applied only when a director has been impartial and independent in decision making. It must be based on the informed decision, taken in good faith and with due care and in the honest belief that the actions are in the best interests of the company.¹⁵ If the aforementioned requirements are met, a court does not assess the reasonability of business decisions taken by directors even when the result has not proved beneficial or desirable for a company.¹⁶

In the case *Kamin v. American Exp.*, the court explained that unless there had been a fraud or evidence of other dishonest act committed by a director, it was beyond court's remit to determine reasonability of director's decision.¹⁷ **A court is not the body that has a capacity to determine reasonability of business decisions. This is one of the reasons why a judge has to assess a director's decision post factum, according to a result that occurred.** Furthermore, since a judge lacks the experience in managing and conducting business as well as a specific knowledge of a particular business activity, assessment of director's decision retrospectively is a difficult task.¹⁸

Plaintiff bears the burden of proof to rebut presumption of business decision's righteousness by proving that the director, when taking a decision, breached any one of the triads of fiduciary duty: duty of good faith, loyalty or due care.¹⁹ In such case, the burden shifts to the director to prove the entire fairness of the action. Based on this rule it must be determined whether the transaction was the product of both fair dealing and fair price.²⁰ **Thus, a decision is assessed as to whether it was taken in good faith, with due care and as a result of rational process. The determination of lawfulness and reasonability of a business decision, however, lies outside the control of a court.**

¹⁴ Poindexter, *Criminal and Civil Liability for Corporations, Officers, and Directors*, Thomson Reuters (2016).

¹⁵ Supreme Court of Delaware, *Gantler v. Stephens*, 965 A.2d 695 (2009) <https://casetext.com/case/gantler-v-stephens-2> [Last visited: 10.03.2021]. With regard to duties and responsibilities of directors, the court practice of the State of Delaware is significant as it influenced the corporate law of a number of countries.

¹⁶ Bakakuri, Gelter, Tsrtsvadze, Jugheli, *Corporate Law – Textbook for Lawyers* (October, 2019) 79.

¹⁷ Supreme Court, New York County, *Kamin v. American Express*, 86 Misc. 2d 809, 383 N.Y.S.2d 807 (1976) <https://casetext.com/case/kamin-v-american-express> [Last visited: 10.03.2021].

¹⁸ Cahn and Donald, *Comparative Company Law: Text and Cases on the Laws Governing Corporations in Germany, the UK and the USA* (2nd ed.), Cambridge University Press (2018).

¹⁹ Avergun, et al, *Corporations, Directors, and Officers: Potential Criminal and Civil Liability*, *Cadwalader, Wickersham & Taft LLP* (2018).

District Court for the District of Delaware, *In Re Hechinger Inv. Co. of Del.*, 327 B.R. 537 (D. Del. 2005) <https://www.courtlistener.com/opinion/1853185/in-re-hechinger-inv-co-of-del/> [Last visited: 10.03.2021].

²⁰ Supreme Court of Delaware, *Cede & Co. v. Technicolor, Inc.*, 634 A.2d 345 (1993) <https://www.law.upenn.edu/live/files/6825-a> [Last visited: 10.03.2021].

According to the indictment, the execution of master agreement was an element of the crime, which was later used to embezzle the property rights. Consequently, it is important to assess the interrelation of legal issues concerning the master agreement and the fiduciary duties.

Master Agreement and Additional Agreements

Articles 10 and 319 of the Civil Code of Georgia (hereinafter, the Civil Code) sets forth principles of private autonomy and freedom of contract. Subjects of private law are free to enter into a contract, to choose the form and type of a contract, and to determine its content. It is one of crucial principles of private law, which is based on the equality of persons, allowing the parties to arrive at any agreement that is not prohibited by the law. It represents the main foundation of the free market economy.²¹

As operating licensed broadcaster, Rustavi 2 had the right to obtain economic benefit by placing commercial ads.²² Rustavi 2 was entitled to concede this right to Inter Media Plus Ltd in exchange for a relevant payment. Furthermore, it has been established that the master agreement between Rustavi 2 and Inter Media Plus as well as the subject of this agreement did not contravene the civil legislation of Georgia.²³

Under the master agreement, the payment for the concession of the right to place commercial ads was to be determined monthly, according to a pre-agreed amount.²⁴ Hence, the agreement between the parties did not depend on the amount of advertising airtime used by the Sales House. In the assessment of experts, this rule of calculating payments was a commercial condition which did not contravene the Georgian legislation.²⁵

Reasonableness of Criminal Charge

At the investigative stage, the prosecution was to obtain evidence that would become a precondition for proving beyond a reasonable doubt that Nika Gvaramia violated the fiduciary duty. It is important the attention be focus on the circumstances that led to the entry into the master agreement and additional agreements as well as the change in the rule of payment.

²¹ Sergi Jorbenadze, *Freedom of Contract in Civil Law*, publishing house of the Davit Batonishvili Institute of Law, Tbilisi, 2017.

²² Expert Opinion published by EY Ltd. on 6 February 2020, §37.

²³ *Ibid.*

²⁴ Master Agreement of January 16, 2015, §4.1-4.2.

²⁵ Expert Opinion published by EY Ltd. on 6 February 2020, §45.

According to the defense, legislative changes to the advertising market regulation,²⁶ ongoing dispute over Rustavi 2, freezing of Rustavi 2 assets and a potential decline in the rating of the broadcaster, all formed the ground for the decision to insure the Company against expected risks by getting necessary amount for the operation of the Company from the Sales House.²⁷

Holding a director liable because of a managerial decision, taken when running a company, that did not bring the enterprise as much income as in the previous year contravenes the business judgment rule. A director's decision may fail to earn profit for a company, but be justified for carrying on the company's efficient operation. When taking a decision, a director shall have comprehensive information and a capacity to exercise a critical judgment in evaluating that information.²⁸ If a director's decision meets subjective and objective criteria of the business judgment rule, it is unjustifiable to hold the director personally liable. A criminal liability of a director may arise only in case when actions undertaken by the director constitute a crime.²⁹

To hold a director criminally liable, it is necessary to establish a deliberate disregard of the interests of the company. A person on a managerial position will be held liable, if he/she is directly involved in an

²⁶ In December 2014, a draft law on amendments to the Law of Georgia on Broadcasting was submitted to the Parliament of Georgia (<https://info.parliament.ge/#law-drafting/7768>). On 19 February 2015, the draft law was adopted, while 1 April 2015 was set as the date of its entry into force. Article 64 provides for a different regulation of advertising time. In particular, according to Paragraph 2 of the mentioned article, ads aired during commercial intervals shall not exceed **20% per hour** (compare with Paragraph 11 of Article 64, effective before the amendment, whereby the entire time of advertisement and teleshopping **in 24-hour period** shall not exceed 20% of **total broadcasting time**).

Harmonization of the legislation to the Audiovisual Media Services Directive 2010/13/EU was cited as a reason for the adoption of the draft law (see the explanatory note <https://info.parliament.ge/file/1/BillReviewContent/54691>) [Last visited: 10.03.2021].

However, it should be noted that the timetable for the entry into force of Directive 2010/13/EU was set at 1 July 2016. Provisions of this Directive were to be implemented within three years of the entry into force of the Association Agreement, except for Article 23 of this Directive (regulating the issues of commercials and teleshopping) which was to be implemented within five years.

See, **Annex XXXIII** - Association Agreement between the European Union and the European Atomic Energy Community and their Member States, of the one part, and Georgia, of the other part.

<https://matsne.gov.ge/ka/document/view/2496959?publication=0> [Last visited: 10.03.2021]

Article 23 – Audiovisual Media Services Directive 2010/13/EU <https://eur-lex.europa.eu/legal-content/EN/TXT/PDF/?uri=CELEX:32010L0013&from=EN> [Last visited: 10.03.2021]

See additionally https://idfi.ge/ge/tv-ads-limitations?fbclid=IwAR1UHF8m7ZP0RljGWxr1Xinv3UAlG5o4ppRMkToHA_lz6ptt9ehjnNHF3A8 [Last visited: 10.03.2021].

²⁷ Among others, see the protocol of Nika Gvaramia's interrogation of 2 August 2019.

²⁸ Bakakuri, Gelter, Tsrtsvadze, Jugheli, *Corporate Law – Textbook for Lawyers* (October, 2019) 79.

²⁹ Fisse, Fraud and the Liability of Company Directors, *Canberra: Australian Institute of Criminology* (1992) 13.

illegal activity.³⁰ It is important to establish a fact of dishonest act and an intention of acting for personal gains.³¹

According to the principle of legality, any action that the state considers a crime shall be defined as a criminal offence by the criminal law.³² It is impermissible to construe the law extensively to the detriment of an accused.³³ Article 182 of the Criminal Code of Georgia defines the embezzlement of another person's property rights is a criminal offence.

Given that the evidence provided in the case does not prove the breach of fiduciary duty by Nika Gvaramia during 2015, an objective element of embezzlement of the Company's property rights is excluded. Furthermore, for an action to be qualified as the offence under Article 182 of the Criminal Code, there must be mental and volitional elements.³⁴ In parallel to objective elements of a crime, a person must, on the one hand, have the knowledge of the elements of act and a desire to commit it (will/volition), and on the other hand, there must be a specific motive (personal gains).

As the breach of fiduciary duty by Nika Gvaramia during 2015 is not determined, signs of the element of commercial bribery are excluded outright. A necessary element of the offence defined in the abovementioned article is such action of a director that violates his official duties.³⁵

III. Charge of Creation and Use of a False Official Document

The act specified in Article 362 of Criminal Code is the offence against the rule of governance. A direct object of the crime is the rule of creation and use of an official document. According to legal literature, a document is deemed official if it grants a right to a person or releases a person from a duty.³⁶ A false document may be a fictional document as well as a document where content or details are altered and falsified (altering data, adding data, forging someone else's signature, erasing data, etc.).³⁷

³⁰ Poindexter, *Criminal and Civil Liability for Corporations, Officers, and Directors*, Thomson Reuters (2016).

³¹ Fisse, *Fraud and the Liability of Company Directors*, *Canberra: Australian Institute of Criminology* (1992) 13.

A manager may also be held responsible for negligence. For example, the Supreme Court of the United States established the Responsible Corporate Officer doctrine which allows for criminal prosecution of a manager who was not personally aware of corporate misconduct but his official duties included the control and prevention of it, or was aware of misconduct but failed to undertake effective steps to identify and prevent it.

³² Hall, *Nulla Poena Sine Lege*, 47(2) *The Yale Law Journal* (1937) 165.

³³ *Vasiliauskas v. Lithuania [GC]*, no. 35343/05, ECHR 2015, §154.

³⁴ Turava, *Criminal Law, General Part Book I, Concept of Crime*, publishing house Meridiani, 2011.

³⁵ Elements of crime in Article 221 of the Criminal Code of Georgia are set out alike offering and accepting a bribe construct. The difference between them is determined according to the interest protected by law and a doer of crime.

³⁶ Lekveishvili, Todua, Gvenetadze, Mamulashvili, *Private Part of Criminal Law (Book II)*, third edition (2009) 243-244.

³⁷ *Ibid.*, 146.

If the court determines, in accordance with the standard of proof set in the Constitution of Georgia and the Criminal Procedure Code, that the loan agreements of 5 and 25 July 2016 have not reflected the reality and have been created to disguise certain circumstances, it is necessary to assess whether signs of the elements of the action specified in Article 362 of Criminal Code are present.

The prosecution refers to a fictional nature of the agreements as a proof of falsehood. It should be noted that neither the criminal law nor the civil law defines a notion of fictional transaction. It might be assumed that the indictment implies a sham or fraudulent transaction defined in Article 56 of the Civil Code of Georgia.

Article 56 of the Civil Code regulates two instances of making transactions based on the lack of will - sham and fraudulent transactions. Both of them involve simulation and different methods of simulation.³⁸

A **sham transaction** is a transaction when the parties intend to achieve the aim that does not correspond to a legal implication that follows from the content of the transaction. In a **fraudulent transaction**, the will of subjects who have expressed the will is agreed and they intend to achieve a particular legal implication, although the inner will and expressed will do not coincide with each other.³⁹

According to court practice, target of sham transactions is mainly the relationship with third parties (for example, one of the motives of making a sham transaction is to deceive the third party, to avoid responsibility, etc.).⁴⁰ However, a transaction does not necessarily target the relationship with the third parties.⁴¹ In a fraudulent transaction, however, the inner will and expressed will of the parties do not coincide with each other – they conceal other transaction which they are actually willing to make.⁴²

A fact of making a sham or fraudulent transaction must not automatically become a ground for criminal liability. It must be assessed in conjunction with other circumstances. Such transactions may be regarded as criminal acts only if it is established that they have been used to deceive third parties or to facilitate a crime. Even in such case, according to opinions expressed in the legal literature, the need of additional qualification may not arise. For example, if a false official document was used in committing a fraud, it may be regarded as a method of crime and the need of additional qualification may be excluded by cumulative crimes.⁴³

³⁸ Chanturia, Comment on Civil Code, gccg.ge, 01.11.2015, Article 56. <http://www.gccc.ge/wp-content/uploads/2015/11/Artikel-56.pdf> [Last visited: 10.03.2021].

³⁹ *Ibid.*

⁴⁰ Decision #AS-571-879-2009 of the Supreme Court of Georgia of 30 April 2010. <http://prg.supremecourt.ge/DetailViewCivil.aspx> [Last visited: 10.03.2021].

⁴¹ Chanturia, Comment on Civil Code, gccg.ge, 01.11.2015, Article 56. <http://www.gccc.ge/wp-content/uploads/2015/11/Artikel-56.pdf> [Last visited: 10.03.2021].

⁴² Decision #2b/4900-14 of the Tbilisi Court of Appeals of 5 May 2015. <http://library.court.ge/judgements/71842015-12-01.pdf> [Last visited: 10.03.2021].

⁴³ Lekveishvili, Todua, Gvenetadze, Mamulashvili, *Private Part of Criminal Law (Book I)*, second edition (2011) 383.

Thus, if it is established, in accordance with a relevant standard of proof, that the entry into a loan agreement was not a true will of the parties, the elements of the crime defined in Article 362 of the Criminal Code will be excluded, but the need to use the rules of sham and fraudulent transactions defined in Article 56 of the Civil Code will arise. When a sham or fraudulent transaction has not been used to facilitate a crime or has not caused damage to a third party, it is irrelevant to assess such action from the perspective of criminal law.

IV. Charge of Legalizing Illegal Income

As universally defined, legalization of illegal income, or money laundering, means making illegally gained property appear legal.⁴⁴ The first country that criminalized money laundering was the United States of America (Money Laundering Control Act of 1986).⁴⁵

Important steps in combatting money laundering were the adoption of Vienna Convention in 1988 and the Strasbourg Convention in 1990.⁴⁶ Parties to the conventions expressed their readiness to define fight against money laundering, signs of elements of money laundering and other important aspects. It is worth noting that the Strasbourg convention extensively construes the definition of money laundering. The aim of aforementioned is to encompass the legislation of states parties and enhance efficiency of fight against organized crime.⁴⁷

⁴⁴ Achim and Borlea, Economic and Financial Crime Corruption - Shadow Economy, and Money Laundering, *Studies of Organized Crime*, Springer (2020).

OECD, Shining Light on the Shadow Economy: Opportunities and Threats (2017) <https://www.oecd.org/tax/crime/shining-light-on-the-shadow-economy-opportunities-and-threats.pdf> [Last visited: 10.03.2021].

⁴⁵ Sharman, Power and Discourse in Policy Diffusion: Anti-Money Laundering in Developing States, 52(3) *International Studies Quarterly* (2008) 635.

Money laundering was criminalized for the aim of enhancing the efficiency of fight against organized crime.

⁴⁶ Vienna Convention against Illicit Traffic in Narcotic Drugs and Psychotropic Substances, Subparagraph b) of Paragraph 1 of Article 3.

https://www.unodc.org/documents/commissions/CND/Int_Drug_Control_Conventions/Ebook/The_International_Drug_Control_Conventions_E.pdf [Last visited: 10.03.2021]

Strasbourg Convention on Laundering, Search, Seizure and Confiscation of the Proceeds from Crime, Article 6. <http://www.supremecourt.ge/files/upload-file/pdf/act28.pdf> [Last visited: 10.03.2021].

⁴⁷ Zoppei, *Anti-money Laundering Law: Socio-legal Perspectives on the Effectiveness of German Practices (International Criminal Justice Series, Volume 12)*, The Hague: T.M.C. Asser Press (2017).

It should be noted that Article 194 of the Criminal Code of Georgia is formulated according to signs of the crime of money laundering, determined by Strasbourg Convention, which, naturally, allows for a broad interpretation.

Article 194 of the Criminal Code of Georgia:

Legalization of illegal income, i.e., giving legal form to illicit and/or undocumented property (use, purchase, possession, conversion, transfer or other actions in connection with property) in order to conceal its illegal and/or undocumented origin or/and to assist another person in evading liability, as well as concealment or disguising of its genuine nature, source of origin, location, dislocation, movement, its title and/or of other rights related to it.

An important tool in combatting money laundering is the Financial Action Task Force on Money Laundering (FATF).⁴⁸ The aim of FATF is to set international standards and combat this type of crime.⁴⁹ Much like the FATF, the European Committee of Experts on the Evaluation of Anti-Money Laundering Measures and the Financing of Terrorism (MONEYVAL) aim to enhance efficiency of the fight against money laundering.⁵⁰

Essence of Money Laundering

The essence of money laundering lies in processing criminal proceeds through various transactions so that to make it impossible to identify their illegal origin and to create the ground for the use and access of these proceeds. Thus, money laundering is the process when criminal proceeds are given a legal appearance by using lawful means, the source of illicit funds is disguised and these funds are reinvested in legal activities.⁵¹

Necessary elements of money laundering are:⁵²

- Predicate offence
- Illegal income gained as a consequence of crime
- Process of legalizing illicit funds
- Intention to conceal the source of illegal income

As a rule, a source of illegal income is a transnational or organized crime. Furthermore, illegal income may result from tax evasion, corruption or bank fraud.⁵³

A process of money laundering represents a combination of complex transactions which may manifest in various forms. Money can be laundered by breaking up a large amount into smaller ones, so-called smurfing, and performing multiple banking transactions, using offshore companies, formal and informal money transfer systems and parallel banking services (Hundi, Black Market Peso Exchange

⁴⁸ <http://www.fatf-gafi.org/home/> [Last visited: 10.03.2021].

⁴⁹ Kern, The International Anti-Money-Laundering Regime: The Role of the Financial Action Task Force, 4(3) *Journal of Money Laundering Control* (2001) 231.

Doyle, Cleaning up Anti-money Laundering Strategies: Current FATF Tactics Needlessly Violate International Law, 24(2) *Houston Journal of International Law* (2002), 279.

⁵⁰ <https://www.coe.int/en/web/moneyval> [Last visited: 10.03.2021].

⁵¹ Ardizzi, et al., Money Laundering as a Crime in the Financial Sector: A New Approach to Quantitative Assessment, with an Application to Italy, 46(8) *Journal of Money, Credit and Banking* (2014) 1555.

What is Money Laundering? <http://www.fatf-gafi.org/faq/moneylaundering/> [Last visited: 10.03.2021].

⁵² Madinger, Money Laundering - A Guide for Criminal Investigators, Third Edition, *CRC Press, Taylor & Francis Group* (2012).

⁵³ Levi, Money Laundering and Its Regulation, 583(2) *The Annals of the American Academy of Political and Social Science* (2002) 181.

System, Hawala Banking), making transactions on stock exchanges, investing, using gaming and casinos.⁵⁴

Money laundering consists of several phases:⁵⁵

Placement – income from illegal activities is placed into circulation and enters the financial system. This may be done by breaking up large amounts of cash into less conspicuous smaller sums which are then deposited into bank accounts, or by purchasing monetary instruments (cheques, securities, money orders, etc.) that are then cashed and deposited into other accounts.⁵⁶

Layering – to conceal the true nature of the funds, transactions of certain type are made (layering), that make it difficult to identify the source of funds. In this phase, small amounts of cash are transferred multiple times. Countries with weak mechanisms of combatting money laundering often make this phase easy to fulfill. Money laundering may be disguised by using fictional transactions, services, and acts of delivery and acceptance, thereby giving the money transfers the appearance of payments for goods or services.⁵⁷

Integration – in this final phase of money laundering, illicit funds are legalized, they are returned to its owner and enter the legitimate economy. This may be done by investing the funds, purchasing real estate, luxury assets, antiques, starting a new business, thereby “cleaning” the money and making it appear as legitimate business profits.⁵⁸

It should be underlined that a specific aim of money laundering is not to gain profits but to have an illegal income enter the legitimate economy and prevent law enforcement authorities from learning about its origin and true nature.⁵⁹ Thus, for an action to be qualified as money laundering there must be the aim of a person to conceal the source of funds through various transactions.

⁵⁴ Passas, *Informal Value Transfer Systems, Terrorism and Money Laundering, Report to the National Institute of Justice*, Boston: Northeastern University (2003).

He Ping, A Typological Study on Money Laundering, 13(1) *Journal of Money Laundering Control* (2010) 15.

Alldrige, Money Laundering and Globalization, 35(4) *Journal of Law and Society* (2008) 437.

Jost and Sandhu, *The Hawala Alternative Remittance System and its Role in Money Laundering*, Prepared by the Financial Crimes Enforcement Network in cooperation with INTERPOL/FOPAC.

⁵⁵ Achim and Borlea, *Economic and Financial Crime Corruption - Shadow Economy, and Money Laundering, Studies of Organized Crime*, Springer (2020).

Schneider and Windischbauer, Money Laundering: Some Facts, 26(3) *European Journal of Law and Economics* (2008) 387.

How is money laundered? <http://www.fatf-gafi.org/faq/moneylaundering/> [Last visited: 10.03.2021].

⁵⁶ Teichmann, et al., Money Laundering – the Gold Method, *Journal of Money Laundering Control* (2020).

⁵⁷ Madinger, Money Laundering - A Guide for Criminal Investigators, Third Edition, *CRC Press, Taylor & Francis Group* (2012).

⁵⁸ Schneider and Windischbauer, Money Laundering: Some Facts, 26(3) *European Journal of Law and Economics* (2008) 387.

⁵⁹ Alldrige, *Money Laundering Law: Forfeiture, Confiscation, Civil Recovery, Criminal Laundering and Taxation of the Proceeds of Crime*, Hart Publishing (2003).

Reasonableness of the Money Laundering Charge

Disposition of Article 194 of the Criminal Code provides an ample room for qualifying an action as a legalization of illegal income. However, its interpretation must be guided by aims of Convention and objectives of the fight against money laundering. When assessing the soundness of a money laundering charge, it is necessary to establish whether there are the elements of this crime – predicated crime, illegal income and a process of legalization of illegal income (including its phases), as well as a specific aim.

Interpreting otherwise and reading the disposition of Article 194 literally will result in automatic qualification of the use of item unlawfully obtained as a consequence of crime against property committed for personal gains as money laundering. This assumption conflicts with the principles of criminal law, including the principle of prohibition of double jeopardy (*ne bis in idem*). Thus, ordinary actions undertaken with regard to property obtained as a result of crime, including the use, sale or disposal of unlawfully obtained item, cannot be considered money laundering.

If a person uses unlawfully obtained funds, this cannot be qualified as money laundering because the aim of this action is not to conceal the origin of illegal income, but to use it. Such action may only be considered money laundering if a person deposits the amount into bank accounts in the form of smaller sums, performs multiple transfers or undertakes other actions with the aim to disguise the source of funds and at the end of the day, make it appear to be a legitimate income.

Such approach is adopted by a number of countries combatting money laundering. For example, according to a recommendation provided in the guiding principles of criminal proceedings of the United Kingdom Crown Prosecutor Service, a money laundering charge ought to be considered when an accused person has done more than simply consume proceeds of crime. In other circumstances, it will suffice to confiscate the benefit of the crime without the need to level additional charge.⁶⁰

A similar conclusion can be made from the analysis of court practice. In the case *U.S. v Millender* which concerned a fraudulent scheme of investment, the court held that to sustain a conviction for money laundering, the prosecution must prove “a specific intent to structure a transaction so as to conceal the true nature of the proceeds.”⁶¹ Although the court found defendants guilty of fraudulently obtaining USD 600 000, it held that “none of the relied upon transactions as to either Defendant was sufficiently structured such that a jury could infer the required *mens rea* for concealment money laundering. None

⁶⁰ Proceeds of Crime Act 2002 Part 7 – Money Laundering Offences, Legal Guidance, Proceeds of Crime <https://www.cps.gov.uk/legal-guidance/proceeds-crime-act-2002-part-7-money-laundering-offences> [Last visited: 10.03.2021]

⁶¹ *United States v. Millender*, 1:16-cr-239-1 (AJT) (E.D. Va. Sep. 21, 2018)

<https://casetext.com/case/united-states-v-millender-11>

<https://www.moneylaunderingnews.com/2018/09/money-laundering-and-specific-intent-can-be-difficult-to-prove/>

also, *United States v. Gilliam*, 975 F.2d 1050 (1992) <https://casetext.com/case/us-v-gilliam-6#p1056> [Last visited: 10.03.2021]

concealed the source of the money and the payments were not otherwise structured to raise an inference of an intent or purpose to conceal.”⁶²

Since it cannot be established that Nika Gvaramia committed embezzlement or commercial bribery, which is regarded as a predicate crime, it is impossible to claim that Nika Gvaramia committed the crime of money laundering. Furthermore, circumstances described by the prosecution as the process of money laundering cannot be qualified as legalization of illegal income.

In particular, the indictment against Nika Gvaramia reads:

Having illegally obtained a large amount of real estate from Inter Media Plus Ltd., Nika Gvaramia pursued an intention to give a criminal property the appearance of legal property in order to disguise its true nature, origin and the property. To fulfill the intention, within several months of registering the real estate in his name, on 7 July 2017 and 26 September 2017, he sold both apartments to various persons on the basis of sale and purchase agreements and as a result, received a particularly large amount of income – GEL 602 521.8.

According to the prosecution, Nika Gvaramia developed the intention to launder money after receiving the real estate, while the elements of money laundering are the sale of two apartments and the receipt of proceeds from that sale.

In the absence of manipulations characteristic of money laundering, the circumstances indicated in the indictment relate to the use of obtained property, not money laundering. According to an opinion dominating legal literature, bringing additional charge of money laundering because of the use of criminal proceeds is unjustified.⁶³ The sale of apartments can only be qualified as the use of obtained property, not an action that may constitute an element of money laundering.

In addition to abovementioned circumstances, the indictment is not substantiated in terms of special aim either. The analysis of Nika Gvaramia’s actions does not provide the ground to conclude that his purpose was to conceal the illegal origin of the property, to disguise true nature, source and property. The defendant sold the property without undertaking any attempt to disguise the source.

⁶² *Ibid.*

⁶³ Bell, Discretion and Decision Making in Money Laundering Prosecutions, 5(1) *Journal of Money Laundering Control* (2001) 42.