

The Fall of Glasnost: A Tale of Murder and Corruption in Russia | Bill Browder

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My grandfather had been the biggest communist in America, and...I decided to become the biggest capitalist in Eastern Europe. – William Browder

INTRODUCTION

William Browder (born 23 April 1964) was born in 1964 to an intellectual family with communist sympathies. His father, Felix, was an accomplished mathematician; his grandfather Earl Browder, was a labor union organizer from Kansas who became leader of the Communist Party of the United States and was invited to Moscow for an official visit in 1926. Bill was the founder and CEO of Hermitage Capital Management, once the largest foreign investor in Russia until 2005, with assets of \$4.5bn under management. Since 2009, when his lawyer, Sergei Magnitsky, was murdered in prison after uncovering a \$230 million fraud committed by Russian government officials, Browder has been leading a campaign to expose Russia's endemic corruption and human rights abuses. Before founding Hermitage, Browder was vice president at Salomon Brothers.

THE BACKSTORY

Browder initially raised \$25 million in 1996 from Edmund Safra, in order to start Hermitage Capital. His first big investment was in Sidanco (\$11mn stake), an oil company in western Siberia trading at a fraction of the price of its near identical competitor Lukoil (itself trading at a fraction of what comparable, Western oil companies were trading at). The trouble for Browder began in early 1997, when Vladimir Potanin, the Russian oligarch in control of Sidanco, announced that he would triple the total number of company shares and sell them at 95% market value, excluding Hermitage from the offering. Browder fought back this attempt at dilution by appealing to foreign investors. He got the decision reversed. However, the collapse of the Russian stock market in 1998 changed the terms of the peace. Russia became a financial pariah. Its turn inward meant it had less to lose from severing ties with the outside world. Eventually, hermitage lost \$900 million or 90% of its value during this period – wealth effectively stolen by the Oligarchs), setting Browder on the path to uncovering corruption in Russia as a way of recovering funds lost by his investors. This eventually led to Browder's ousting from the country in 2005. In 2007, the situation escalated when Hermitage's offices were raided by Moscow police, justified by the claim that Browder owed taxes. This formed part of a ruse to use Hermitage as a conduit for laundering \$230 million under the false claim that the company owned an equal amount in back-taxes. Browder, led partly by his lawyer Sergei Magnitsky, fought back. Magnitsky was eventually arrested on trumped up charges in 2008 (during the financial crisis), and died 12 months later in 2009, where he was handcuffed to a bed rail and beaten to death by eight guards in full riot gear. In his crusade for justice, and by putting his own life at risk, Browder persuaded Congress to pass – and the President to sign into law – the Magnitsky Act, which aimed to punish individuals responsible for the death of Russian tax accountant Sergei Magnitsky.



WHY DO I CARE?

I want listeners to appreciate the difference between open societies with robust legal systems like North America and Western Europe and increasingly closed societies with totalitarian leanings like Russia. The difference is not just theoretical. A similar descent into totalitarianism and corruption would make America unrecognizable to almost anyone. I also want the audience to come away with a deeper and more nuanced understanding of how the Russian political-economy operates and how clientelism features prominently therein. I would also like listeners to appreciate the source of the Russian public's anger and disillusionment – the way in which the nation's wealth was privatized remains an open scar, and we must reckon with it. Reckoning first requires that we acknowledge the injustice.

QUESTIONS:

THE CALL TO ADVENTURE

I didn't want to go back to Chicago, I wanted to get out and see the world—more than that, I wanted to work in the world. What I really wanted was to be Mel Gibson in "The Year of Living Dangerously." - Bill Browder

1. **Background/The Early Years** – You have had quite a full, interesting, and it would seem, meaningful life. Your grandfather Earl Browder, was for a brief time the leader of the Communist Party of the United States. Your father Felix, was some kind of math prodigy who got his undergraduate degree from MIT at the age of 18, but who had great difficulty finding work – it was the 1950s McCarthy Era and anti-communism ran rampant. Eventually though, he went on to a fine career, actually being awarded the National Medal of Science by President Bill Clinton in 1999. (renowned in the field of Nonlinear Functional Analysis). Yet, you have famously said that perhaps, *in spite* of your grandfather having been "the biggest communist in America," you would decide "to become the biggest capitalist in Eastern Europe." Which is a foreshadowing of the life calling that would really come to define most of your professional and indeed personal life, up until this very day. Do you reflect at all on what formative experiences in your early childhood and adolescence may be most responsible for making you the man you are today? How do you think these experience have informed some of the choices you have made in the most crucial periods of your life – periods that spans this book and that will form the basis for much of our conversation?
2. **Go East, Young Man** – What attracted you to finance? What pushed you towards eastern Europe and eventually Russia? Was there a romantic element? Tell me about your experience in Poland. What ultimately drove you to want to stay after your initial experience in that country? The most revealing line in the book that I think provides some answer is a reference to some investments you made in Poland while on mission from Boston Consulting Group: "After leaving Sanok, they [my stocks] rose steadily. With every percentage point increase I became more and more convinced that I had found my calling. What I really wanted to do was become an investor in the privatizations of Eastern Europe. As it turned out, I couldn't have been more right. Over the course of the following year my investments would



double, and then double again. Ultimately, they went up almost ten times. For those who don't know, the sensation of finding a "ten bagger" is the financial equivalent of smoking crack cocaine. Once you've done it, you want to repeat it over and over and over as many times as you can."

3. **Salomon and Bobby Ludwig** – You eventually found your way to Salomon Brothers in 1991. What was Salomon like during that time, after the crash of '87 and the S&L debacle? In enterprising fashion, you saw that, as everyone was fighting over deals in Eastern Europe, there was a gaping hole on the investment banking side for opportunities to invest in Russia. Your first deal was working on a trawler fleet (shipping operation) in Murmansk Russia, 200 miles north of the arctic circle. That eventually led you into the office of Bobby Ludwig, a guy with a reputation for making money hand over fist, year after year, who could pretty much do whatever he wanted. You gave him a presentation, and his response was to get up without saying anything, walk away, and return to say: "Browder, that story's the most amazing thing I've ever heard. I just went down to the risk committee and got twenty-five million for us to invest in Russia. Don't waste time doing anything else. You get back to Moscow and let's put this money to work before we miss out, you hear?"

That was not the first time you would get \$25 million to invest in Russia. In a short time, that \$25mn became \$125mn. What was that early success like? What did it *feel* like?

"Far from opening the way to emancipation, these changes led to beggary for most citizens, ushering in the most cataclysmic peacetime economic collapse of an industrial country in history. Under the banner of reform and the guidance of American-prescribed shock therapy, perestroika became catastroika." – The Guardian, 2001

HERMITAGE: THE OPPORTUNITY

4. **The Apex of Money & Power** – Eventually, you made the decision to strike out on your own, which led you to meeting Edmond Safra. Your description of Edmond and his home is rather magnificent. Generally speaking, we as readers of this book are being educated in "the game" of power and money, and where it resides. How inaccurate is the public's idea about wealth and power? Where are the centers of gravity in the world? How important is old money and dynastic wealth?
5. **Dissolution & Disillusionment** – Your first big deal in Russia seems like it was Sidanko. Why were opportunities like this so prevalent in Russia? What was it about the period between 1991 and 2000, that led to such deals? Can you describe the climate and the feeling of the time? Andrew Solomon has written eloquently about the art scene in Russia after the fall, and the trauma of having to put a price on one's art before learning to distinguish between monetary and intrinsic value.
6. **From Перестройка to Катастроика** – When you started hermitage in 1996, a lot of value was being transferred from the Russian government into the hands of a tiny group of well-connected, soon-to-be oligarchs. Who were the oligarchs before they became filthy rich? This period is dysphemistically referred to as katasroika (катастроика), a play-off-words (perestroika, the policy or practice of restructuring or reforming the economic and political system. First proposed by Leonid Brezhnev in 1979 and actively promoted by Mikhail Gorbachev.) Assets were privatized on the cheap. It was a fire sale of Soviet Russia.



Privatization Vouchers – You go into detail about how the post-Soviet economy was plundered, specifically, through the use of privatization vouchers. These vouchers were collectively exchangeable for 30% of the shares of all Russian companies with no restrictions on who could buy them. Russian citizens had no idea what to do with the vouchers and were often times happy to exchange them for “a \$7 bottle of vodka or a few labs of pork,” as you write. A network of enterprising individuals emerged to buy vouchers from individual Russians at the periphery of the country, moving them towards the center, where they were eventually sold in large blocks to wealthy investors like yourself. This was half the battle. The vouchers then had to be exchanged for shares. You write: “If only one person showed up with a single voucher, then the entire block of shares being auctioned would be exchanged for that one voucher. On the other hand, if the whole population of Moscow showed up with all of their vouchers, then that block of shares would be evenly divided among every single voucher that was submitted at that auction. The scenario was ripe for abuse, and many companies whose shares were being sold would do things to prevent people from attending the voucher auctions so that insiders could buy the shares cheaply.” Can you go over how this process worked, and how you managed to insert yourself as a foreign investor in this process?



Loans-For-Shares – You didn’t talk explicitly about the loans-for-shares program, but I’m curious if you can shed some light on how it worked for our audience? We covered the collapse of LTCM in one of our previous episodes with Jim Rickards, which was brought on by the Russian Sovereign Debt Default in 1998. As an amateur historian of this period, it would appear to me that this second phase of privatization, which contributed to the default in 1998, helped to isolate Russia and close it off from the West, allowing people like Vladimir Potanin to further consolidate their power (and, as a consequence, rid people like you from the country). Can you explain to us how the loans-for-shares worked and the role it played in the Russian debt default? What was the impact of Russia’s default on any hopes for liberalization and the continuation of glasnost?

Putin and the End of Glasnost – The privatization of the Russian economy and its eventual collapse in 1998 likely dashed any remaining hopes for reform. It also disincentivated Russia’s elite, who were now cut off from the international banking system, to “play by the rules,” at least, as Westerns understand them. Somewhere out of all of this emerged Vladimir Putin. There was internecine conflict among various factions – the elites, the government, the military, etc. – and somehow, Putin managed to consolidate power and institute something akin to order. How did this process come together? What was the Clinton administration’s role in all of this, and could we have managed our side of this better? Roughly, how long did this process take? I assume it is complete...



FROM BUSINESS MAN TO TOUGH GUY

7. **Rough & Tumble** – You eventually had your first major run-in with the rough and tumble world of Russian business in your confrontations with Vladimir Potanin, the person who controlled Sidanco. He planned to swindle you and your investors out of almost \$100 (\$87 million to be exact) million with the stroke of a pen (diluting you from 2.4% to .9%). Can you talk to us a bit about this confrontation, the run-in you had with Boris Jordan’s (Potanin’s financial adviser and head of Renaissance Capital) representative, Leonid Rozhetskin? What do you feel it captures about Russian business practices, at least, as they pertain to that world of high-finance and kleptocracy? (I can relate to experiencing the irrational behavior – to the ‘pissing contest’ – that does not allow for straight talk)
8. **Living Dangerously** – This began your first experience living on the edge, with surveillance and body guards. Eventually, you prevailed, by appealing to the international financial community, which people like Potanin still relied on for cheap financing. The real turn happened in 1998 with the Russian bond default. That pretty much eliminated the opportunity for Russian oligarchs to get capital from the West, and with that, the country was free to turn inward. This also coincided with the death of Edmond Safra in a bizarre arson at his home in Monaco. You did not allude to whether or not this was part of some business deal you were involved in. It’s been almost 20 years since then. Have you reflected on this incident over the years? Do you believe that Edmond’s death was connected, in any way to his business dealings? This was an experience that would repeat itself – living on the edge...
9. **From Friend to Foe** – Your investment in Gazprom was your most successful, and it was in no small part a result of your dedication to rooting out corruption in the businesses that you were invested in. It was also aided by Putin’s dedication to doing the same. “The enemy of my enemy is my friend...” But things changed, and it seems they changed after 2003, with the arrest of Mikhail Khodorkovsky, the CEO of Yukos and Russia’s richest man. This sent a message to the rest of the business world in Russia: “Stay out of politics, and you will be rich and happy. Meddle, and you will end up in a cage, no matter how powerful or rich you are.” You believe this is when Putin secured kick-backs in return for allowing the oligarchs to continue plundering the nation’s wealth. This seems indistinguishable from racketeering. You didn’t realize at the time that Putin had made this deal, so you continued to engage in anticorruption efforts, but now, you were eating into Putin’s territory. In 2005, you were detained at the Moscow airport, eventually being sent back, permanently, to London, never to return again. You were deemed a “threat to national security.” With the raiding of your offices in 2007, the nightmare kicked into full gear. What did it feel like to be detained at the airport, uncertain about the cause and unsure if you would end up back in London or in a Russian prison?
10. **Tax Fraud** – Was the tax fraud perpetrated against the Russian public by use of Hermitage’s companies as “zombie defendants” a rogue operation? Is this analogous to how mafia organizations run, by allowing people who are lower on the rung steal, as long as they kick profits up to the top? How do you think all the pieces came together to make something like this happen the way that it did?
11. **Slow and Steady Burn** – The way you write the story feels like a war. There is a sense in which you were fighting up against forces that would eventually crush you, yet you were



Sergei Magnitsky
April 8, 1972 – November 16, 2009

willing to exhaust every option in front of you. What drove you to do this? Was it ultimately an expression of your nature to not back down? Would walking away have been so incongruous with your sense of self that it was never a serious option?

12. **Magnitsky Act** – I want to talk about the Magnitsky Act, but first tell us about Sergei Magnitsky. Who was he, what did he do, and why has his particular sacrifice – his torture and execution in police detention – meant more to you than any other case? How has the Magnitsky Act been instrumental in undermining the modus operandi of the Putin regime? How has it effected Putin’s capacity to govern? How effective has it been? What’s the relevance to all this stuff we hear about banning the adoption of Russian children?
13. **Back to Vlad** – You have testified before congress and said that you believe the current president of Russia, Vladimir Putin, is personally worth over \$200 billion – money he received as kickbacks for overseeing an increasingly lawless post-soviet Russia. How did he amass this money, over what period of time, and how does this tie into the transformation of Russia since the fall of the Berlin wall?
14. **Living Under Threat** – What is your current living situation? Do you live under threat? What can you tell us about what it’s like to be an enemy of the Putin regime?
15. **US-Russian Relations** – What is the current state of Russian-US relations in your view? What will it take for things to change, and for Russia to begin to re-open? What is your biggest concern about relations between our two countries? What is your opinion of the shadow being cast over the current White House? Do you believe that this president has been compromised by Russian intelligence?

The **Magnitsky Act** is a bipartisan bill passed by the U.S. Congress and signed by President Obama in November–December 2012, intending to punish Russian officials responsible for the death of Russian tax accountant Sergei Magnitsky in a Moscow prison in 2009.

