

English court gives guidance on when a person is “politically exposed” for AML purposes

In a much-anticipated decision, the High Court this week upheld the UK’s first Unexplained Wealth Order (“UWO”). The subject of the UWO, originally referred to as “Mrs A”, has now been identified as Zamira Hajiyeva, the wife of Jahangir Hajiyev, the former Chairman of the International Bank of Azerbaijan who was jailed in 2016 for embezzling tens of millions of pounds from the bank.

In the course of this decision, Mr Justice Supperstone shed some light on the definition of a “Politically Exposed Person” (a “PEP”) under the Fourth Money Laundering Directive (“MLD4”)¹ in respect of state-owned companies. This is relevant not only to UWOs, but also to the requirements for enhanced due diligence and monitoring for PEPs under the MLD4.

What is an Unexplained Wealth Order?

A UWO is a civil power and an investigation tool. It requires the respondent to provide information on certain matters (their lawful ownership of a property, and the means by which it was obtained). It is important to note that, as an investigation power, a UWO is not (by itself) a power to recover assets.

The power to obtain UWOs was inserted into the Proceeds of Crime Act 2002 (“POCA”) by the Criminal Finances Act 2017 and came into force on 31 January 2018. The ability to apply for a UWO is limited in England and Wales to:

- the National Crime Agency,
- HMRC,
- the Financial Conduct Authority,
- the Serious Fraud Office, and
- the Crown Prosecution Service.

The facts

The UWO in this case relates to a property in Knightsbridge, London purchased for £11,500,000 in December 2009 by a BVI company, against which a mortgage for nearly £7.5 million was secured and discharged five years later in December 2014. Mrs Hajiyeva is the beneficial owner of the BVI entity.

The judgment also notes that between September 2006 and June 2016, Mrs Hajiyeva spent more than £16 million in Harrods and used 35 credit cards issued to her by the International Bank of Azerbaijan.

Mr Hajiyev was the Chairman of the International Bank of Azerbaijan from March 2001 to March 2015. He was arrested in December 2015 and charged with offences including fraud and embezzlement for which he was convicted and sentenced to 15 years’ imprisonment. The state of Azerbaijan had a controlling stake in the bank.

In February 2018, less than a month after the UWO provisions came into force, the National Crime Agency successfully obtained a UWO against the Knightsbridge property at a “without notice” hearing. One of the requirements which the National Crime Agency had satisfied was to show that Mr Hajiyev (and so by extension his wife) was a PEP.

Mrs Hajiyeva applied to discharge the UWO on a number of grounds, including that her husband (and so she as well) had been incorrectly categorised as a PEP. The hearing took place from 24 to 26 July 2018.

1. Implemented in the UK by The Money Laundering, Terrorist Financing and Transfer of Funds (Information on the Payer) Regulations 2017

What is a PEP?

A “Politically Exposed Person” is defined in POCA as follows:

“an individual who is, or has been, entrusted with prominent public functions by an international organisation or by a State other than the United Kingdom or another EEA State”.

In addition, a PEP can be the family member of, close associate of or a person otherwise connected with an individual who falls within the above definition.

POCA further provides that Article 3(9) of the MLD⁴² applies in determining “*whether a person has been entrusted with prominent public functions.*” Article 3(9) of the MLD⁴ provides a non-exhaustive list of individuals who would be included within this definition:

- a) heads of State, heads of government, ministers and deputy or assistant ministers;
- b) members of parliament or of similar legislative bodies;
- c) members of the governing bodies of political parties;
- d) members of supreme courts of constitutional courts or of other high-level judicial bodies, the decisions of which are not subject to further appeal, except in exceptional circumstances;
- e) members of courts of auditors or of the boards of central banks;
- f) ambassadors, charges d’affaires and high-ranking officers in the armed forces;
- g) **members of the administrative, management or supervisory bodies of State-owned enterprises;**
- h) directors, deputy directors and members of the board or equivalent function of an international organisation.

The decision

Among her objections to the UWO, Mrs Hajiyeva objected to her husband’s classification as a PEP on two grounds: (i) that the bank of which he had been Chairman had not been a state-owned enterprise; and (ii) that he was not entrusted with prominent public functions “*by an international organisation or by a State...*”, as required under POCA to be classified a PEP.

State-owned Enterprise

Mrs Hajiyeva did not dispute that Azerbaijan’s Ministry of Finance had a majority shareholding in the bank during the relevant period, but contended that this was not sufficient by itself to establish “state ownership”. Mrs Hajiyeva relied on the evidence of one of her husband’s lawyers who explained that under Azerbaijani law the bank, which is an Open Joint Stock Company, is not a “state organisation” but a “normal commercial entity”.

Mr Justice Supperstone held against Mrs Hajiyeva, finding that the bank was a “state-owned enterprise” and ruling that the Ministry of Finance’s majority shareholding was sufficient to demonstrate this. It was not necessary for him to rule on whether a minority shareholding might have been sufficient, as argued in the alternative by the National Crime Agency.

Mr Justice Supperstone also dismissed evidence given by Mr Hajiyev’s lawyers as to the bank’s legal status under Azerbaijani law, finding that whether or not an enterprise was state-owned was not an issue of foreign law, and noting that neither POCA nor the MLD⁴ required consideration of foreign law. Mr Justice Supperstone emphasised that in order to determine whether an enterprise is state-owned, the appropriate test “*is one of ownership and control, not legal status or powers.*”

2. Money Laundering Regulations 2017 reg. 35(14)

Not entrusted with prominent public functions “by an international organisation or by a State” other than the UK or another EEA State

The wording of the POCA definition of PEP differs from that in the MLD4, by including the words: “*by an international organisation or by a State*”. Mrs Hajiyeva argued that this distinction meant that to be caught by the definition of PEP in POCA, an individual had to satisfy two steps:

1. the PEP definition in the MLD4, as used to interpret the phrase “*whether a person has been entrusted with prominent public functions.*”
2. If the individual met that MLD4 definition, then in order to be a PEP under POCA he or she also had to satisfy the additional wording: the prominent public position had to have been entrusted “*by an international organisation or a [non-EEA] State.*”

In short, Mrs A’s argument was that some of the categories in Article 3(9) of the MLD4 might not fall within the POCA definition of PEP, because, for example, members of the administrative, management or supervisory bodies of state-owned enterprises (Article 3(9)(g)) might not be said to have been entrusted with these positions “*by an international organisation or a [non-EEA] State.*”

Mr Justice Supperstone did not agree with this interpretation of the provisions. Holding that the operative component of the clause is not “by an international organisation or by a State” but “other than the United Kingdom or another EEA State”, the judge found that the intention of the additional wording in POCA was to exclude UK and EEA PEPs from the ambit of the UWO provisions. The judge agreed with the National Crime Agency that where a person is entrusted with prominent public functions, “*it necessarily follows that they will be entrusted to perform such functions “by” a State or international body.*”

Analysis and broader relevance

Mr Justice Supperstone’s determination on the wording difference between POCA and the MLD4 is relevant only to the definition of a PEP under POCA for the purposes of UWOs. By contrast, the decision as to what constitutes a “state-owned enterprise” is more significant, as it provides judicial interpretation of the PEP definition under the MLD4. Indeed, neither the National Crime Agency nor Mrs Hajiyeva had been able to find any legal precedent anywhere in the EU interpreting the term “state-owned enterprise” (as used in MLD4).

Being relevant to the definition of PEP under the MLD4, this decision is also relevant the requirements for enhanced due diligence and monitoring of PEPs laid down in the MLD4 (primarily under Article 20, but also Articles 21 and 22³). Businesses subject to these requirements should ensure that the procedures and systems they have in place to satisfy these requirements take account of all possible types of “state-owned enterprise” coming out of this judgment. Mr Justice Supperstone emphasised that the test to apply is one of ownership and control, not as to the local legal status of the enterprise. Moreover, although in this case the Ministry of Finance owned a majority stake in the bank, Mr Justice Supperstone specifically left open the possibility that it was not necessary for there to be a majority state-shareholding in order for an enterprise to qualify as “state-owned”; a minority shareholding might be sufficient.

National Crime Agency v Mrs A (Rev 1) [2018] EWHC 2534

If you have any questions or comments in relation to the above, please contact Susan Rosser or Jeremy Holden, or your usual Mayer Brown contact.

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3. All enacted in reg. 35 of the Money Laundering Regulations 2017.

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