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Happy Holidays from the staff of the U.S.-Russia Business Council!
Seated (L-R): Ursula King, Jo Bottalico, Iwona Skrzypek. Standing (L-R): Keith Bush, Karen Montagne, Sarah Manaker, Blake Marshall, Anna Kokourina, Eugene Lawson, Jeff Jones, Svetlana Minjack. **Not pictured:** Joe Yancik

RUSSIA BUSINESS WATCH

The quarterly report of the U.S.-Russia Business Council

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W I N T E R 2 0 0 1 - 2 0 0 2

PRESIDENT'S MESSAGE



By any definition, 2001 has been a remarkable year for U.S.-Russian relations and for our member companies' activity in the Russian market. The trade and investment climate has dramatically improved, and it feels good to have the wind to our backs!

We are particularly impressed with the amount of legislation moving through the Russian Parliament, including judicial reform, a money-laundering bill, pension reform, licensing measures, currency controls, and the draft of Russia's new Corporate Governance Code.

Perhaps most important, the Putin Administration has overhauled the corporate profits tax to stimulate business activity and recapture firms from the shadow economy. It has produced two major accomplishments that will have a far-reaching impact on bottom-line performance when enacted on January 1: a considerable rate reduction from 35 to 24 percent and full deductibility of legitimate business expenses. When the income tax set at 13 percent combines with a corporate profits tax of 24 percent beginning next year, Russia will suddenly have one of the lowest marginal tax rates in the world.

The business community's optimism about the Russian market is supported by impressive macroeconomic trend-lines. After posting growth rates of 5.4 percent in 1999 and 8.3 percent last year (with even higher jumps in industrial productivity), the 2001 figure is expected to be somewhere in the 5-6 percent range. This marks the first time that post-Soviet Russia has registered three consecutive annual expansions.

Furthermore, Russia is running budget and trade surpluses and finds itself in a good position to manage its debt service in 2002 and 2003, when roughly \$30 billion comes due — indeed, Russia made some of its

2001 IMF payments ahead of schedule.

The top ratings agencies agree that Russia has become an increasingly attractive place to invest. Fitch, S&P and Moody's have raised their ratings and upgraded the outlook on Russia from stable to positive, with Fitch citing "exceptional macroeconomic performance and acceleration in structural reform," that makes Russia "well placed to weather even a severe global downturn."

The Council's member companies are capitalizing on this momentum and pressing forward with their business development plans. Announced earlier this year, the \$330 million General Motors deal with AvtoVAZ is a tremendous example of successful international investment in Russia. The Caspian Pipeline Consortium (CPC) is another manifestation of the optimism surrounding the investment climate. The total cost of the 1,000 mile pipeline project will be \$2.6 billion, of which \$2.2 billion is being invested in Russia. And most recently, Exxon Mobil announced a \$5-6 billion commitment to the next phase of Sakhalin-I development, which could total \$12 billion upon completion.

At the Council, we too are capitalizing on this momentum and creating some of our own. With a new U.S. administration taking office this year, we have accomplished what we set out to do in the "transition paper" we distributed in the first quarter. Throughout the key U.S. government agencies, we made the case persuasively for engagement with Russia and are pleased to have provided input for four presidential summits in six months. We specifically focused our message on the importance of commercial engagement and supported efforts by Commerce Secretary Evans and Treasury Secretary O'Neill to build working relationships with their Russian counterparts. We worked closely with the White House to

make our vision of private-sector engagement a reality with the launch of the Russian-American Business Dialogue. And we have helped lay the groundwork for a range of policy initiatives outlined in the transition paper, including graduating Russia from the Jackson-Vanik regime.

This issue of *Russia Business Watch* includes coverage of our most well-attended Annual Meeting in the Council's history, where National Security Adviser Condoleezza Rice articulated the fundamental changes that have taken place in the U.S.-Russian relationship. The impact of those changes was reinforced by President Putin at a dinner we co-hosted for him during the Washington-Crawford Summit last month. You will find the transcript of President Putin's remarks, as well as summaries from our Annual Meeting, in this issue.

We will continue to work with all our members to foster a vibrant, prosperous Russian marketplace and to help shape the U.S.-Russian relationship in the early part of this century. We look forward to your active participation in the year ahead!

As always, we welcome your thoughts, particularly in areas where we can be more responsive to your needs and help you meet your goals in Russia.

With high hopes for the year ahead,

Eugene K. Lawson
Eugene K. Lawson

KEYNOTE ADDRESS BY DR. CONDOLEEZZA RICE

Assistant to the President for National Security Affairs, The White House

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Obviously, this is an extraordinary time for the United States, and an extraordinary time for the world. We are, of course, all still trying to recover from the shock of the September 11th events, events that I think changed fundamentally the way that we think about the threats and the concerns of Americans. But perhaps more importantly, it changed the way that we as a civilized world think about the threats that we all face together.

While September 11th was a horrible day, it is a day that has also refocused us as a people, as people of civilization, on the things that unite us.

I can tell you that in many ways, there was no more dramatic example of that than what happened with the Russian Federation and the Russian president immediately in the aftermath of those events of September 11th. I was there in the secure facility, as we call it, in the White House, when a phone call came in from President Putin, who was asking to speak with President Bush. And he had two messages for him.

One was that they had watched what had happened and that they too saw the horror, and wanted to send both their sympathy and their desire to help if they possibly could. But also, in really a kind of crystallizing moment for the end of the Cold War, they knew that the United States would undoubtedly have to put its forces on alert because there was now a threat to the homeland of the United States. And President Putin called to say that not only had Russia not put its forces on alert in response to that, but it had indeed decided to cancel several exercises that were going on so that there would not be any confusion.

I do not think there could have been a more crystallizing moment for the end of the Cold War. If you think back 25 or 30 years ago, there would have been a spiral of alerts between two heavily armed, ideologically opposed camps. And here we were now with the first phone call being from the Russian president to say, we understand, we are standing down, we want to help.

Indeed, that feeling, that spirit of the possibilities of a new U.S.-Russian relationship had already been foreshadowed at Ljubljana and at Genoa, when the two presidents talked about looking beyond the Cold War to see if there was not a

more common agenda that they could pursue. And they have been pursuing that agenda since those meetings. But since September 11th, it has been given new impetus.

There will undoubtedly be new cooperation on counterterrorism, a threat that we all face. And indeed, the way to think about the coalition that is being built against counterterrorism is that it is a broad coalition for a war that will be fought on many fronts. And countries will bring different contributions to that war on terrorism. While many will continue to focus on what can we do militarily, it may well be that some of the most important things that we will do is to share information, share intelligence, to cut off financial networks for terrorists – these are things that we expect to cooperate on broadly with the Russians. They have been among the first and most active in that coalition in dealing with the terrorist threat.

We are also, of course, seeking to look for other areas of common security policy with Russia, how to deal with the emerging threat of ballistic missile technology, of potential proliferation of weapons of mass destruction. I think there will be new impetus to that.

“ I THINK THAT IN MANY WAYS ECONOMIC RELATIONS, BUSINESS RELATIONS, AND INVESTMENT CAN BE THE LEAD PHALANX OF THIS FUNDAMENTALLY DIFFERENT RELATIONSHIP WITH RUSSIA. ”

But perhaps most important, we want to see this relationship broaden beyond the security and strategic relationship to one that looks at those things that we can do together to make better the lives of our people, to make us more prosperous, to open Russia to the world and the world to Russia in economic terms, and that is

the business that you have been engaged in so effectively for a very long time. I think that in many ways economic relations, business relations, and investment can be the lead phalanx of this fundamentally different relationship with Russia.

Russia, of course, is a country of enormous potential, and we have all known that and said that for many, many years. There are only three things that we all need to do together in order to make certain that the potential is reached.

“ RUSSIA IS NOT JUST A RAW MATERIALS SUPPLIER. ITS PEOPLE MAY WELL BE ITS BEST AND GREATEST RESOURCE. ”

One of the more impressive elements of the conversations that we have had with President Putin and his government has been the acceptance that the first of those is, first and foremost, the responsibility of Russia, and that is to create conditions domestically that will attract private investment and private capital. This is not a government that talks so much any longer about financial assistance or talks about aid from the world, but rather talks about trying to create the conditions into which private investment will flow.

You know as well as I do — perhaps better than I do — that capital will flow to those places where it is secure; capital will flow to those places where it is welcome; capital will flow to those places where it can get a return on its investment. For Russia, that means laws, rule of law. It means a safe and secure environment. It means conditions in which capital can prosper. Indeed, the tax policies of the Russian government, which have been moving in exactly the right direction, are perhaps just one symptom of the fact that the Russian government now accepts responsibility for building that environment.

There is much that we can continue to do in helping Russia to build that environment, but it is really up to Russia itself to make certain that capital will flow to Russia just as it would flow to any place that creates the conditions to make it worth its while.

A second condition is one with which we can certainly help, and that is that we tend to think of Russia as a country with vast and enormous resources. Of course, it is a country with vast and enormous resources. The investment of the West in those resources and the development of those resources is an important step. But I want to submit to you that Russia is not just a tremendous place for energy and resources, but rather it is a place, a country that should have a place in the more advanced economy as well. Russia is not just a raw materials supplier.

That should not be its aspiration. That should not be our aspiration for Russia. Russia is a country with an enormously educated population. Its people may well be its best and greatest resource.

I was in Moscow in October 1999. I have been there a couple of times since, but as a government official, I do not have quite as much fun anymore. I was wandering in a bookstore in downtown Moscow, an enormous bookstore at one o'clock on a Saturday afternoon. And the bookstore was just full of people — young people — old people, all there in the bookstore. Ladies and gentlemen, you can shoot a cannonball through a bookstore in the United States at one o'clock on a Saturday afternoon and not hit anybody. (Laughter.) This is a very literate population — great brainpower in Russia.

Given that the currency of economic development and well-being these days at the upper end is the knowledge economy, there is no reason that Russia should not be a major player in the knowledge economy, in software engineering, in the development of ideas. So, we as partners with Russia should encourage that development, and of course encourage the development of Russia's resources,

but also encourage the development of Russia's greatest resource, its people.



National Security Adviser Condoleezza Rice takes questions from Council members.

Now, the third, again, comes back to what Russia must do, because we know that the kind of people that we are talking about — creative and talented people — only flourish in a free society. And therefore, issues of freedom, issues of democracy, issues of a free media are inextricably linked to how well Russia will do in joining this great international economic movement forward. You cannot ask people to think at work and not at home.

Fortunately, Russia is making strides in democratic development. There is still much more to do. There is more to do in pushing the development of democratic institutions out of Moscow and into the provinces outside the cities. Russia is, after all, an enormous country that cannot be governed just from the center. There is more to do in the stimulation of media and debate. There is more to do in the stimulation of the Russian people to involve themselves individually in the political life of their country. But I do believe that the Russian government understands that you cannot disconnect creativity and freedom.

“ ...ISSUES OF FREEDOM, ISSUES OF DEMOCRACY, ISSUES OF A FREE MEDIA ARE INEXTRICABLY LINKED TO HOW WELL RUSSIA WILL DO IN JOINING THIS GREAT INTERNATIONAL ECONOMIC MOVEMENT FORWARD. ”



Council Chairman Bob Strauss with Condoleezza Rice.

but Russian business development — this is going to be an economic powerhouse one day.

You are at the lead edge of helping with a Russian partner to create those conditions, and there is a lot that is at stake. I started by saying that the United States and Russia may be well on their way to a fundamentally different relationship, certainly than we had with the Soviet Union, but even than we have had over the last several years.

If Russia is able to take on these three tasks, to improve the climate of laws, the investment climate, to make it possible for capital to flow; if Russia is able to develop not only its natural resources, but its people; and if it is able to create conditions in which entrepreneurship and creativity can flow — small business, not just large business, not just outside investment,

That fundamentally different relationship, as it becomes based more and more on common values, will serve not only Russia and the United States well, but the entire world. Imagine, if you will, for just a moment, a Russia fully integrated into Europe. Imagine, if you will, for just a moment, a country with the potential of Russia as an engine of economic growth for the world —

not a drag on the international economy, but an engine of growth for the international economy. Imagine that when we talk about the American economy or the Japanese economy or the European economy, that we talk also about Russia's role in international economic growth. This could be an extraordinary story. Russia has around her many neighbors who are also looking to see if this can be the kind of development in which Russia finds its rightful place in the world — not by 19th century means, but by 21st century means, based on its economic power and its economic strength.

I know that several years ago that might not have seemed possible. I think it is possible. It is why it is so important that there be gatherings like this. It is why it is so important that we explore with Russia what we all can do, not just because it is good for Russia, but because it is good for the world. Thank you very much. ■

because it allows all men and women to pursue their own destinies, regardless of their backgrounds or their religious beliefs. That is both a foundation for greatness, and it is a foundation for goodness. It is the foundation for all that is right and just. And it is central to the kind of world that we all strive for, a world of peace and prosperity.



Secretary of Commerce Donald Evans speaks at the USRBC Annual Meeting.

to become a reality. Their actions were no doubt calculated to add instability to our economic structure. Well, we can not let that happen, and we will not let that happen. We must focus on strategies that are centered on growth, strategies that do create wealth for all people around the world. And the surest route, the absolute surest route to a more stable economic environment for all nations is greater openness in the world economic markets, which brings me to why we are here today, why we are all here this morning.

The U.S. relationship with the Russian Federation is, and will be, an ongoing priority for this administration. It is our hope that the trade and commercial relationship we are building between our two nations will be a cornerstone of an ever-stronger partnership between our countries. I have tremendous faith in the future of the U.S.-Russia partnership. I know President Bush is committed to building an enduring, mutually beneficial relationship between our countries. And in July, on my first trip to Russia, I experienced first-hand the commitment of President Putin and other Russian government and business leaders to building a strong partnership. And it was clear that the commitment to stronger ties between the U.S. and Russia goes beyond Russia's leaders. Indeed, it is widespread throughout the business community in Russia.

While I was in Russia, a businessman gave me a plaque. I brought it with me today. It is a plaque that I have hung in my office here in Washington. It lists 12 principles of business ethics, which were adopted by the Russian Chamber of Commerce in the late 1990s. The first principle on this plaque says, "Profit is important, but honor is more valuable than profit." Russia's commitment to the kind of principles that we cherish like this is a sure sign of its sincerity in forging a solid relationship with U.S. business.

The U.S.-Russia Business Council has

played a vital role in strengthening ties between our countries, and you have indeed the sincere appreciation of the Bush Administration for your contributions. We thank you for helping to organize the new Russian-American Business Dialogue, which I understand has its first meeting tomorrow, and we look forward to the progress of that dialogue being a constructive force in building our relationships.

And I must give credit where credit is due, and that is to this Council and the successful work you have carried out over many years, which has helped make my first overseas official business development mission a reality. When I travel to Russia next week with leaders of 14 businesses, it will be the first business development mission to Russia led by a U.S. Commerce Secretary in over seven years. I want to thank this Council, as well as the American Chamber of Commerce in Russia and the Russian-American Business Council — they all helped make this happen.

"THE U.S.-RUSSIA BUSINESS COUNCIL HAS PLAYED A VITAL ROLE IN STRENGTHENING TIES BETWEEN OUR COUNTRIES, AND YOU HAVE INDEED THE SINCERE APPRECIATION OF THE BUSH ADMINISTRATION FOR YOUR CONTRIBUTIONS."

When we first posted the news about our trip, the response was immediate and broad-based indeed. And the enthusiasm for this trip has not wavered since the September 11th attack. By focusing on our business, we are showing the world what we are made of. We are saying our confidence remains high. We are refusing to be intimidated by a pack of cowards. In fact, many more companies applied to go on this trip than we could possibly accommodate. Seventy-five companies — companies that ran the gamut in terms of size and sector — wanted to join us. After careful review, 14 businesses will be going. They include a small entrepreneurial company that employs less than 20 people, and also corporations that are among the largest in the world.

ANNUAL MEETING 2001 Washington, DC ■ October 4-5, 2001

KEYNOTE ADDRESS BY DONALD L. EVANS

U.S. Secretary of Commerce

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If anybody out there has ever been introduced by a giant of a man, I just was. Bob Strauss made a comment about he's been called on seems like numerous times during difficult times and to handle difficult tasks. And he is so right. As all of you know — I do not need to tell you — his guided hand of good judgment, discernment, wisdom, has touched American administrations for a long, long, long time. And I put great emphasis on American administrations, because Bob first and foremost is an American. I have known that ever since I have known this outstanding man, and I am, I can tell you standing here before you at this moment, humbled that he would introduce me with such kind words. Thank you, Bob, very, very much.

I am pleased to be here today with all of

you. I do thank Bob, and Gene Lawson, thank you for being so instrumental in bringing this group together and for your support in pushing forward U.S.-Russian business relations. I would also like to acknowledge a number of distinguished guests we have here: First Deputy Prime Minister and Minister of Finance Aleksei Kudrin — Mr. Kudrin, thank you for being here; Deputy Head of the Presidential Administration Dmitry Kozak; Russian Ambassador to the U.S. Yuri Ushakov; and former Russian Ambassador to the U.S. and President of the Russian-American Business Council Yuli Vorontsov. So, I thank all of you distinguished gentlemen for being here.

A lot has happened in the last several weeks. I do not need to tell you. The last few weeks are unprecedented. Our

hearts are all very heavy. We mourn the tragic loss of life, and struggle with uncertainties about what the attack on the United States of September 11th really means. But life must go on — life will go on. Business must go on, and it will go on. We will move forward. This country, this world will persevere. We will not concede our freedoms, we will not give up our dreams. We will find our souls. We will all be strengthened, and we all will focus on the values that all of us around share and have in common.

"THE U.S. RELATIONSHIP WITH THE RUSSIAN FEDERATION IS, AND WILL BE, AN ONGOING PRIORITY FOR THIS ADMINISTRATION."

We are committed to freedom — and we are committed to freedom precisely

The enthusiasm of the businesses springs from the optimism about what is happening in Russia. They know the Russian market is opening, and they are eager to establish contacts for bilateral trade and investment. There is a window of opportunity right now, both for the U.S. and Russia, and we want to make sure the benefits of this window of opportunity are realized. There is no doubt in my mind that Russia wants a more open, transparent and investment-driven economy. Their goal is an economy governed by laws and rules that make it more attractive to foreign investors, as well as to domestic investors.

Russia also has signaled its intent to actively seek membership in the World Trade Organization (WTO). Just last week, Ambassador Zoellick was in Russia to help move this process along. WTO membership should give businesses greater confidence, as the rule of law continues to take hold in Russia. And I believe that other actions of the Putin Administration — including things like pushing for major tax reforms, maintaining tight fiscal discipline — also emphasize that Russia is ready, willing and able to take the necessary steps to join the global economy as a full economic partner.

The Russian government has also demonstrated willingness to reform in other areas. They passed a new Land Code that allows for the sale of commercial and residential property. And they are working on important judicial and labor reforms. These are all positive signs for the Russian business environment. They help to build business confidence and business trust. Finalization of the multibillion-dollar Caspian Pipeline Consortium is another important symbol to foreign investors of Russia's movement in this direction.

But barriers do remain. Barriers do remain in Russia for full participation in the global economy, and further reforms are necessary to tear down these barriers. Russia's banking system needs to be restructured. International accounting standards need to be adopted. Intellectual property rights must be recognized and protected. Court judgments

and awards from arbitrations must be enforced. And Russia's production-sharing agreement regime must be finalized. These reforms are critical to building successful commercial relationships with industry partners and with business partners around the world.

Russia's economy is moving in the right direction, poised for the growth that will follow as reforms are pursued and take hold. Despite concerns for the worldwide economy, Russia's economic growth is likely to continue this year. Inflation is in check. And real foreign investment in Russia continues to expand. While Russia is not a large market right now, with a GDP of about \$300 billion, we are confident that it can be as it continues to grow its economy.

As we pursue opportunities in Russia, we must keep our eye on the ball and stay focused on the end result. It goes far beyond free trade and economic growth. Our goal is nothing less than a world that lives in peace and prosperity. The recent attack on America is a defining moment for this world. It showed more clearly than ever the relationship between open trade, prosperity, peace, and freedom. Free trade offers the opportunity for a higher quality of life, not just in the United States, but around the world. It creates better jobs. It creates economic growth. It raises standards of living. It lifts people out of poverty. And it is a fuel, thirst and demand for greater political and social freedoms.

And political and social freedoms are critical weapons in the fight that we have against those who use victims of poverty and unfortunate circumstances as their fodder for war and power. There are six billion people that live on the planet today. Three billion of those people live on less than two dollars a day. In Afghanistan, people living there live on about one dollar a day. This poverty, this extreme poverty, breeds instability in the world, and creates an environment where extremists for their own evil end can exploit people who have no hope. The status quo is unacceptable.

Our nation must fulfill its responsibility as a world leader. Part of our responsibility is to lead the world in trade, which is critical to the quest for economic, political and social freedom. It is with this responsibility in mind that President Bush has



Council Chairman Bob Strauss welcomes Secretary of Commerce Donald Evans to the USRBC Annual Meeting.

asked Congress to grant him Trade Promotion Authority (TPA). Trade Promotion Authority is critical to the United States in order to maintain its leadership in the global economy. It signals that the administration and the Congress have reached a consensus on our negotiating objectives, that we are united, and those negotiators will speak with authority. It also signals a strong understanding of just how important trade is to our economy and the global economy.

Last Friday I traveled to Kansas City with former Secretary Bill Daley to promote TPA and trade — so you have some idea how the relationship has continued. All along the highway, we saw signs that said, "Each Kansan farmer feeds 101 Americans." What I would love to see along the sides of the road is, "12 million Americans owe their jobs to exports and to trade" — jobs that pay 18 percent more than the average American job.

Before September 11th, the economic case for TPA was strong. Today, I believe the case is even stronger. We need to demonstrate leadership to help a slowing global economy. We need to do what is right for our country — and for the world. TPA promotes an open international economy,

which in turn provides for greater choices and freedom, and the greater understanding among cultures that can help lead to a peaceful, prosperous world.

As we move forward in the wake of the September 11th attacks, we must ask ourselves — will the United States sit on the sidelines, and allow others to write the rules that govern trade? Or will we lead? I think we all know the answer to that question. As citizens who enjoy the richness of life made possible by our democracy, it is our responsibility to lead. As President Bush has said many times, freedom is our greatest export. It is our responsibility to export freedom to the rest of this world. It is our responsi-

bility to lead a world toward peace.

Every one of us in this room has the freedom to use our talents — we have the freedom to succeed, we have the freedom to fail. The point is, we have the freedom. Free trade is a platform for launching and protecting freedom for people all around the world. Trade is ultimately about freedom. This is an opportunity to succeed and create new American jobs, and it is about opening opportunities in other nations for people to pursue better lives for themselves and for their loved ones. It is about inculcating the values of freedom and democracy around the world. It is about letting people go where their

ingenuity and their innovation will take them.

Let me close with this. There is a Russian proverb that says, "Pray to the Lord, but keep rowing to the shore." In these challenging times, when our hearts are heavy and our losses are great, our oars are in the water in this world in ways they have never been in our history. Our goals remain clearly in focus. We have not stopped, nor will we. We are all strengthened. We are committed to carrying the banner of freedom and opportunity forward — for our nation and all mankind — with the help and support of people all around the world, and our friends in Russia. Thank you very much. Spasibo. ■

ANNUAL MEETING 2001 *Washington, DC ■ October 4-5, 2001*

KEYNOTE ADDRESS BY JOHN B. TAYLOR

Treasury Undersecretary for International Affairs

The following are excerpts from John Taylor's keynote presentation at the Russian Embassy Gala Dinner (subheadings have been inserted editorially).

...As the Ambassador indicated, and President Bush has mentioned many times, President Putin was the first foreign leader to call him after the events on September 11th. This new relationship has three components, and I stress all three — they are interwoven and interrelated. There's the military side or security, there's the political side, and there's the economic side. In many respects we focus on the first two, but I want to stress the third, not just because of this audience but because I do not think we pay enough attention to that third item.

...President Bush has emphasized how both of our countries can benefit as Russia begins to fulfill its great economic potential. This summer I visited Russia twice, and on one of those trips I joined Secretary O'Neill in visiting a young entrepreneurial family that started a printing factory in Nizhny Novgorod. The factory started with

just two brothers and a sister. Now there are 120 people printing almost all of the Coca-Cola labels in Russia. I again saw this potential, on that same trip, also in Nizhny Novgorod, when we visited an old ship-building factory that is now being converted by a smart, aggressive businessperson. He is thinking of ways to make that factory do things it had not done before. For instance, he is changing the way that barges on the Volga River operate. They are now carrying a little less grain and a little more oil. All sorts of things can be done if you have that entrepreneurial spirit.

Recent Reforms

...Since 1998 there has been a lot of progress in Russia, and talking with the Russian economic leaders, you can sense this. There is a powerful team working under President Putin's leadership. I always like to talk about the tax reform. The 13 percent flat tax has generated more revenue than the old tax system — not a bad idea to

apply in some other countries. I was also told about the remarkable cut in the corporate tax rate to 24 percent, or even 20 percent if the regions choose to lower it. ...President Putin has emphasized that he would like per capita income in Russia to rise to the level of Portugal, which would require 6 percent growth for the next 10 or 15 years. To do that, many more of these same kinds of changes will be needed.

One of the things that I look at is the formation of new enterprises. More new enterprises are needed. In the United States, approximately 50 percent of employment is created by new, start-up firms or small businesses. Actually, the same numbers are true in Poland and Hungary. The number is much smaller in Russia, close to 20 percent at this point. So there is a lot of room for encouraging entrepreneurship.

"THE UNITED STATES AND RUSSIA CAN WORK TOGETHER TO ASSIST RUSSIA IN JOINING THE WTO AND GETTING ALL OF THE BENEFITS ASSOCIATED WITH THAT MEMBERSHIP."

One of the other things I worry about is the financial intermediation system. It is not easy to get a loan if you are starting up a new business. That makes a big difference, as many of you know. Most of the financing of firms now is through retained earnings, rather than through new loans. Only three percent of new

investment is financed through new loans. If you would like to compare things in terms of GDP, only about 12 percent of GDP is in the form of credit for businesses and consumers in Russia, and it is close to 16 percent in other market economies. So, there is quite a lot that can be done.

Role of the United States

What role can the United States play as we interact with Russia in this new economic, strategic and political package? I think there are a number of principles to keep in mind, and then a number of specifics. We must recognize that the need for big packages of financing from international monetary institutions and international financial institutions has diminished. In fact, those days are probably over. The focus on microeconomic assistance and advice from these institutions is a more attractive alternative.

We must also emphasize private invest-

ment. Foreign direct investment in Russia would benefit the Russian economy, and the United States can play a role in that in many ways, the least of which is to communicate to the foreign business community how things are changing in Russia.

I also think that our engagement in the United States with Russians should be measured and thought about in terms of concrete objectives. What we did in the second trip I made to Russia this summer, in which I accompanied Secretary O'Neill and Secretary Evans, was to establish with President Putin the idea of making a list of 15 or 20 things that our two governments could work on in the economic and business area. Then we will go through that list and accomplish the tasks, and check them off.

There are also some details that we should be thinking about. The United States and Russia can work together to assist Russia in joining the WTO and getting all of the benefits associated with that membership. It is very important for the Russian economy to engage internationally, and I think WTO accession is a very important step. There was actually much more trade in the former Soviet Union between Russia and the former republics than there is now between Russia and those same countries. Formerly it was roughly 70 percent, and now it is down to 15 percent. So there is room for more international trade. We can also work on other international trade issues together — for example, steel. There is a huge effort to reduce global capacity in steel so that we can end the protectionist pressures that exist, and Paul O'Neill has worked on that heavily, and has engaged the Russians on it as well.

The second thing is to resist the pressure to think only about the center, and not about the regions. We must remember that this is a very diverse country with many different regions. In a way, maybe the United States has more to offer here in an exchange than people realize. After all, the United States is a federal government and we have states. In fact, I have always liked the term "states-as-laborato-

ries". In the United States, we can implement different policies in different states and learn the benefits of that. For instance, some states can attract more business from the policies they implement. I think that we have had a good experience, and when working together with the Russian regions we can share how that federal system can work better for the economy.

"WE HAVE SEEN GREAT IMPROVEMENT ON THE MACROECONOMIC SIDE IN RUSSIA, AND A GREATER FOCUS ON THE SMALL BUSINESSES IN THE PRIVATE SECTOR WOULD BE FRUITFUL."

The third point I would mention in terms of more direct engagement, is to have the international financial institutions focus more on the businesses in the microeconomic aspects, rather than the macro side. We have seen great improvement on the macroeconomic side in Russia, and a greater focus on the small businesses in the private sector would be fruitful. One thing that I have been very impressed by in terms of the international financial institutions is the work of the EBRD in Russia: finding ways to encourage financial intermediation — that is, to find ways for businesses to get loans and in fact, to encourage change in the banking sector.

A fourth thing that we could be thinking about is ways to improve the banking sector. Ensuring that businesses are able to get loans and expand into new areas at a better rate is very important. There are ways to help. I know that there are efforts underway to reform banking, to encourage more loans — mortgage loans, consumer loans, etc. The private sector can play a big role. Western — American and European — banking institutions, if they had more opportunity within Russia, could share a lot of the skills and techniques of banking. This may be something that the private sector could do much better than the public sector, and I would like there to be some encouragement from the public sector.

...A very important event that occurred this summer is the passing of a money-

laundering bill in Russia. ...In the last few days, I have spent a lot of my time thinking of ways to deal with the financial aspects of terrorism. For example, President Bush issued an executive order blocking the accounts of any terrorist or person associated with a terrorist, associated with al Qaeda. That applies to U.S. banking institutions. But to make that work, it has to also apply to banking institutions in other countries. Russia is now in a position, through these new laws, to take actions that they would not have been able to before. Finance Minister Kudrin is going to participate in discussions with the G-7 finance ministers on Saturday on this very topic. This will be the first time that there has been a dialogue on these issues among these

ministers. This is an aspect of the economic relationship that we are benefiting from in a way that we may not have anticipated earlier.

And the final thing, and this is something that President Bush and President Putin emphasized in their meetings this summer, is that we need to find more ways for the business community to interact in our countries. President Bush asked Secretary Evans to lead a delegation to Russia. He wants to develop this relationship more. Your organization and the organization in Russia are essential for this. Government-to-government interaction is very important, but business-to-business interaction is even more important.

"...WE NEED TO FIND MORE WAYS FOR THE BUSINESS COMMUNITY TO INTERACT IN OUR COUNTRIES. GOVERNMENT-TO-GOVERNMENT INTERACTION IS VERY IMPORTANT, BUT BUSINESS-TO-BUSINESS INTERACTION IS EVEN MORE IMPORTANT."

...The attacks of September 11th illustrate how cooperation between the United States and Russia can be so useful. Our agenda must be very broad, though, and look for new ways to interact. We must always stress the importance of democracy and the importance of free markets, and if we do that we will be prepared for any future events. Thank you very much. ■

ANNUAL MEETING 2001 *Washington, DC ■ October 4-5, 2001*

KEYNOTE ADDRESS BY ALEKSEI L. KUDRIN

First Deputy Prime Minister of the Russian Federation

I am impressed by the presentation by Secretary Evans, and I am inspired by the unity of the American people during these difficult days. The Russian people share your feelings and are ready to participate in all aspects of the international fight against terrorism. The latest initiatives of our president also addressed this issue, and it will also be discussed tomorrow at the meeting of the ministers of finance of the G-8 countries. I am also very grateful to Mr. Evans for the support that he and the U.S. administration have provided recently in the area of Russia's accession to the WTO. After the meeting of our presidents in Genoa, we prepared an agreement on business cooperation, which will become the initial point of cooperation between the business elite of our countries.

Russia has been experiencing political and economic stability for the second year in a row. This is just a very short period, and the main task of the Russian government is to provide stability for the coming years and to add assurance and predictability in the actions of our gov-

ernment to continue to work on developing our economy. The next two years are going to be test years for us to maintain a stable economy and to maintain positive trends in our economy, which may be very difficult due to Russia's high debt obligations and continuing debt payments. I believe we can overcome these difficulties and maintain stability. This will be the main proof that it is possible to work in Russia, and that investments made in Russia will yield a good return.

I will report a few numbers, very briefly. This year we expect GDP growth of 5 to 5.5 percent. And while other countries are lowering their economic forecasts for this year, we might increase this forecast by the end of 2001. Industrial growth for the first nine months of this year was 5.3 percent, and in such industries as metallurgy, machine building, chemical, petrochemicals, and food production, the growth was more than 8 percent. Total investments

increased 7.5 percent in the first nine months of 2001, and foreign investments in Russia during this period were \$6.7 billion. These are obviously positive developments, which support our economic growth. It is also very important that consumption started to also influence economic growth in Russia, and consumption has grown by 12 percent. In analyzing the economic growth in Russia, the internal factors have become dominant, and we are less dependent on the external climate and the external conditions. That is just further proof that the stability of economic growth is increasing.

"WE DO NOT COUNT ON ANY DEBT RESTRUCTURING BUT INSTEAD ARE PREPARING THE MEASURES THAT WILL ALLOW OUR GOVERNMENT TO OVERCOME THE DIFFICULTIES WE WILL BE FACING IN THE NEXT TWO YEARS."

I would also like to note that the budgetary process in Russia is being implemented positively, and in the first eight months of 2001, the budget surplus reached three percent of GDP. We hope



John Taylor, Undersecretary of the Treasury, speaks at the Gala Dinner at the Russian Embassy.



First Deputy Prime Minister of Russia Aleksei Kudrin addresses Council members.

that it is not going to decrease significantly by the end of this year, and that the budget surplus for 2001 will be approximately two percent of GDP. For next year, the Russian government has already submitted a reduced budget, which will have a surplus of no less than 1.6 percent of GDP. This is the first time we have proposed a budgetary reduction to the Duma, and in September the Duma approved in the first reading the main parameters of the budget for next year. This shows that the parliament and the government have reached consensus on the main parameters of budgetary policy and how it influences the main macro-economic processes.

We have also planned to create a financial reserve, which is going to contain approximately \$3.5 billion by the end of next year. The reserve will provide a strong protection against worsening of external economic factors, including a decrease in oil prices. Our calculations were based on an assumption that oil prices next year for Russia will be approximately \$23.50 a barrel. But the protective mechanisms included in the budget, such as the financial reserve, will allow us to withstand the lowering of oil prices up to \$18.50 a barrel. This creates a sufficient foundation to implement the budget. I would like to refer

to the latest reports of the ratings companies Fitch and Standard & Poor's, issued on October 4, 2001, after the parliament approved the budget draft in the first reading. According to these rating companies, this forecast is realistic, and the Fitch company has assessed the possibility of creating such reserves even this year, which will then be transferred to the next year in the amount of \$3.5 billion of the federal budget. By the end of next year, an additional \$3.6 billion will be added to the financial reserve, which will provide sufficient protection against negative effects of external factors or lowering of prices. This will allow us to meet all of Russia's debt obligations, including external ones, completely in 2002. It also creates a good foundation for meeting our debt

obligations in 2003, which will be a difficult year for us due to the increase in payments by approximately \$5 billion.

I would like to repeat once again that, if oil prices drop, and if our budgetary income drops, our financial reserves will decrease as well. To solve "the problems of 2003," we will need to introduce additional measures, including cooperative programs with the IMF. Currently, we are not receiving any additional credits from the IMF, but we have an agreement on post-program monitoring that could be converted at any moment into a loan program. Of course, our gold reserves have grown significantly in recent years, and today they consist of more than \$37 billion. This year the gold reserves of the Central Bank have grown by more than \$9.5 billion, and this is also a very strong foundation for stability in 2002 and 2003. To that extent, we understand that raising the issue of debt restructuring would adversely impact these positive expectations. Therefore, we do not count on any debt restructuring but instead are preparing the measures that will allow our government to overcome the difficulties we will be facing in the next two years. By doing this, we will be able to lower the risks, which will allow our economy to develop at a normal pace, and support investors' hopes for the

continuation of the positive trends into 2002 and 2003. We expect that, by the end of 2002, the total state debt (internal and external) will comprise no more than 50 percent of GDP, which is within normal standards even for the European Union. We also hope to lower the debt to 40 percent of GDP by the end of 2004. All these measures that I just talked about are part of our policy, which was announced in the president's address to the parliament this year. Our goal is to lower the country's dependency on external factors and to increase stability and continue positive trends in the Russian economy. I hope that we will be able to achieve this goal.

"...BANKING SECTOR REFORM IS ONE OF OUR NEAR-TERM GOALS ALONG WITH OTHER STRUCTURAL REFORMS."

We continue to work on implementing structural reforms. First of all, we are conducting reforms in the area of taxes — we are trying to simplify the taxation system and lower the tax rate. The tax reform is called the Velvet Tax Revolution in Russia [*RBW: peaceful reform, as analogy to the Velvet Revolution in Czechoslovakia in 1989*]. We are lowering taxes gradually, while maintaining all government social programs and reducing any possibility of serious social risks in our country. This year, the real income of the population has grown by more than five percent, and we expect that by the end of the year the increase will be approximately six percent. The standard of living is rising, and this is one of our main goals as well.

I would like to add that banking sector reform is one of our near-term goals along with other structural reforms. I noticed that this reform was mentioned in several presentations as the most important initiative. Indeed, the banking sector should provide investment guarantees. Two weeks ago, the Russian government and the Central Bank of the Russian Federation adopted a joint strategy on reforming the banking sector. I would like to name some of the most important components of this strategy. In July, the parliament passed a law that talks about banks' responsibilities to shareholders and clients, and introduces

new indices including a capital sufficiency index. We have not had this in Russia before. We also expect that banks will improve their performance indicators significantly. Beginning January 1, 2004, we plan to adopt International Accounting Standards (IAS) within our banking system, which will increase the requirements on banks even more. According to the Central Bank, nearly half of Russian banks will need to be restructured by the beginning of 2004 so that they can work with these higher standards. Moreover, we have introduced a five million Euro minimum capital requirement for new banks. This capital requirement has to be met in order to obtain licenses for foreign currency operations, precious stone operations, and others. We are also taking measures to privatize state banks gradually and to separate the Central Bank from the capital of the banks it owns today. We will be monitoring the activities of Sberbank more thoroughly. Currently, we are preparing a major inspection of Sberbank, which will make the banking-services market more competitive. This is going to be achieved by using a set of measures that are outlined in the strategy.

Among other major reforms is the reform of accounting systems. This would cover accounting procedures in different industries, as well as the switch to IAS in 2004. International accounting standards are being introduced in a gradual manner. This is an evolutionary process because it will take time for accounting services to learn and get accustomed to the new system.

"WE VIEW PARTICIPATION IN THE WTO AS A MAJOR GOAL FOR RUSSIA."

Among other challenges is land reform, resulting from adoption of the Land Code, as well as reform of foreign economic relations. Also, in the near future, we are planning to introduce a new Customs Code that will be in conformity with our goal of WTO accession. A draft of the Customs Code has been prepared and soon will be introduced to parliament. There is also draft legislation for deregulation of the economy — debureaucratiza-

tion, as we call it. The number of licenses one has to obtain in order to work in Russia was decreased to about 70. Many other license requirements will be removed. Some permissions will still need to be obtained, but they will be transformed into specific permission documents and certification. We will also limit the amount of interference of the state in the work of economic entities.

Among the most important tasks we foresee for the next couple of years is entry into the WTO. Therefore, we are working very closely with other members of the WTO Working Party on Russia. A dramatic positive change in this area took place last summer. The U.S. administration has had a lot to do with this. Secretary of Commerce Evans played a key role, as did U.S. Trade Representative Zoellick, and Treasury Secretary O'Neill, who visited Russia two months ago and gave serious impetus to our negotiation process. The positions of Russia and the United States on very sensitive trade issues, including tariff agreements, became closer. During the recent visit of President Putin to Brussels, all the agreements that we are now in the process of achieving with the United States were reconfirmed at the European Union level. The United States and EU are the biggest supporters of Russia's accession to the WTO, which is a serious precondition for Russia joining the WTO in the next two years. Our proposal to discuss a report on Russia's accession to the WTO at the Working Party meeting this fall or early next year has also been accepted. We need to talk about the conditions for Russia's entry into the WTO in relation to tariffs, as well as the agriculture and service sectors. I believe that major agreements are likely to be reached next year and in the following year as well.

We view participation in the WTO as a major goal for Russia. It will require synchronization of our legislation and certain reforms,

and bringing them into conformity with international standards. A month ago, the government approved a plan of legislative work, according to which in the next 18 months, all the necessary drafts of legislation will be introduced in the Duma. And hopefully they will be adopted. It will enable us to successfully complete the negotiation process and see Russia as a member of the WTO. What we expect from the process is not only the opening up of the Russian market, but also the appearance of Russian goods and services in markets abroad. Currently, Russia is facing serious restrictions in foreign markets, with 80 percent of Russia's exports to the United States falling under various restrictions that have been enforced for a long time, including anti-dumping sanctions. Some progress has been made in this area. In July 2001, Russian companies submitted a memorandum to the U.S. Department of Commerce in support of U.S. recognition of Russia as a market economy. The petition was accepted for consideration. We will continue to work with the Department of Commerce, and hopefully as a result of objective consideration of this petition, Russia will be able to obtain status as a market economy. This will open up new prospects for business relations between Russia and the United States.



First Deputy Prime Minister of Russia Aleksei Kudrin (left) with Council Chairman Bob Strauss.

Having participated in a number of international forums devoted to free-

dom of trade, I learned that the newly accepted members of the WTO often have the status of the younger brother. It is very difficult to achieve agreement on the key issues that are sensitive for these new member countries. We [potential members] are always on the defensive. I believe that more equitable trade is on the agenda throughout the world, and it is an important issue not only for Russia, but also for all countries that are serious about the liberalization of their economies. We are prepared to engage in this discussion and expect reciprocal measures that will result in the establishment of equitable trade relations.

"THE POLICY PURSUED BY THE RUSSIAN GOVERNMENT IS QUITE CLEAR – ITS GOAL IS TO IMPROVE TRANSPARENCY OF THE RUSSIAN ECONOMY AND DEVELOP DEMOCRATIC INSTITUTIONS."

Russia and the United States have tremendous potential for joint work. U.S. investments in Russia hold leading positions in the total value of accumulated investments. At the same time, in the last year other countries have begun to catch up. I think this is only temporary, and the United States, with its tremendous potential, will be able to maintain its position of the leading investor in Russia. We know well the companies that have been successfully operating in Russia for many years. I see a lot of familiar faces, a lot of friends with whom I have been working in the past 10 years. I am sure that we are talking the same language. The policy pursued by the Russian government is quite clear — its goal is to improve transparency of the Russian economy and develop democratic institutions. I believe, and it was confirmed by presentations of the representatives of the U.S. government, that there will be a better understanding at the political level that we are building one world. The most recent events

that called for even greater unification in our struggle against terrorism show that the world is changing, and only if we stand together shall we be able to overpower this threat. This task requires a common language in every area. Russia, as I said, is prepared to engage in full-scale measures aimed against terrorism. The ministers of finance are developing plans and measures to cut all funds and financing of terrorism. This is a very serious issue, and Russia has its own mechanisms that will enable it to identify and freeze assets of organizations that might be culprits in terrorist activities. We support the proposals and suggestions made by the U.S. administration. We are prepared to make our contribution in fighting against the financing of terrorist organizations. I am going to discuss these issues today with Secretary O'Neill, and tomorrow I will also have further meetings in the Treasury Department. I believe that together we will be able to defeat this evil or create conditions that minimize its dangers. ■

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ANNUAL MEETING 2001 Washington, DC ■■ October 4-5, 2001

COMMITTEE MEETING AGRIBUSINESS COMMITTEE

MODERATOR	David Lyons <i>Vice President, Government Relations, Louis Dreyfus Corporation</i>
SPEAKERS	Christian Foster <i>Chief of the Trade and Investment Branch of the USDA's Foreign Agricultural Service</i>
	Vadim Solovyov <i>Agribusiness Investment Officer, International Finance Corporation (IFC)</i>

Mr. Foster provided an analysis of the current situation in the agribusiness sector in Russia and discussed the results of the Spring 2001 Agribusiness Mission to the Russian regions.

More foreign investment is going into Russian agribusiness today than into any other sector of the economy. While beverage production, the confectionery industry, tobacco processing, catering, and packaging have received the majority of investment in recent years, FDI has recently increased in dairy, vegetable oil and meat processing. The food processing industry is now performing better than any other sector of the Russian economy.

Mr. Foster presented a detailed look at the Russian agribusiness sector based on the latest data. The year 2000 was the best year for the food-processing sector in Russia since reforms began more than 10 years ago. Overall, the agricultural data for 2000 demonstrated the following improvements:

- increase in gross agricultural output of seven percent
- grain output up 11 million tons, or 20 percent
- meat output increase of three percent (first increase in a decade)
- food-processing sector output up 14 percent, mainly as a result of the ruble devaluation in 1998
- production of tractors up 25 percent

- production of grain combines doubled.

The forecast for 2001 is even more optimistic for the agribusiness sector in Russia (projections as of September 2001):

- total agricultural output up 10 percent
- grain output up 15 percent
- meat output unchanged
- food-processing industry production up 10 percent.

This positive trend will continue to create opportunities for American companies. Nevertheless, the Russian market remains one of the world's riskiest for investment. According to the recent country risk ratings published in *The Economist*, Russia was ranked just behind Iraq, Kenya and Pakistan. Mr. Foster named the absence of land reform in the rural sector of Russia and inadequate rule of law practices as the major stumbling blocks for investment in Russia. The new Land Code (signed into law by President Putin in October 2001) does not extend to agricultural land and affects only about four percent of all land in the country. In the private sector, many enterprises are still in great debt to the state and have to carry the burden of social taxes. And finally, great tensions remain between the federal government and the regions. These issues, he cautioned, should be

considered when making investment decisions in the Russian market.

Mr. Foster stressed that almost all of the sectors in Russia's food-processing industry (except for the sugar, bread/baked goods, and flour/vegetable oil sectors) are performing well this year and are going to demonstrate good annual results due to increasing domestic demand and competition with imported goods. The following sectors are expected to increase their production in 2001 more than 10 percent: beer, margarine, cheese, meat, and sausage.

According to Russian State Statistics Committee data, total FDI in Russia from 1989 to date is approximately \$30 billion. This volume is comparable to the level of FDI in Poland (\$35 billion), but extremely low compared to the total FDI in Brazil (\$170 billion) and China (\$325 billion). In 2001, it is expected that Russia will have attracted up to \$7 billion in FDI.

There is currently over \$6 billion of FDI in the Russian food industry. The majority of FDI in the food sector has gone into beverage production (soft drinks, beer and water), the confectionery industry, tobacco processing, catering, and packaging. FDI in dairy processing, vegetable oil processing, and meat processing has recently increased.

Mr. Foster then turned to the subject of U.S. agricultural exports to Russia. In 2001, the total volume of U.S. agribusiness exports is expected to exceed \$800 million. This number is still lower than

the pre-August 1998 crisis volume of more than \$1.2 billion, but U.S. exports to Russia are beginning to pick up. In terms of export composition, consumer-oriented goods account for a major share, with poultry products holding the leading position

The USDA covered about 40 percent of mission expenses, and USAID in Moscow covered most of the research expenses. The mission was oversubscribed and turned out to be very successful. Almost every American company that visited Russia on this mission

What are the most attractive sectors in Russian agribusiness for an investor? One observation might be useful for a potential investor: an increase in real income in Russia has changed consumer tastes from cheaper goods like noodles and potatoes to more expensive and nutritious products like meats and oils.

What is the current status of the poultry industry? The demand for poultry will continue to increase in Russia. Russian fresh poultry production can not compete with American frozen poultry exports due to much higher cost of domestic production. Demand in Russia still outpaces its domestic production, and Mr. Foster suspects this will be the case for at least four more years.

What do you think about agricultural reforms in Ukraine and Russia? The last two years has not seen any agricultural policy reform in Russia. Ukraine, which has always lagged behind its neighbor in terms of agricultural reform policy, is now making progress relative to Russia. For example, land reform in rural areas is proceeding somewhat faster. On the other hand, the restructuring of management of former state and collective farms in both countries has not changed in the aggregate, but is certainly changing throughout the regions. Subsidy cuts in the sector have forced such changes. Mr. Foster said that until the state stops writing off debt and allows for the development of bankruptcy laws, there will not be any significant reform of either the management of the enterprises or changes in labor and employment.

Mr. Solovyov spoke about the IFC's experience in the Russian agribusiness sector. The IFC, a member of the World Bank Group, is the largest multilateral source of loan and equity financing for private-sector projects in developing countries. It promotes sustainable private-sector development primarily by:

- Financing private-sector projects located in the developing world.

- Helping private companies in the developing world mobilize financing in international financial markets.
- Providing advice and technical assistance to businesses and governments.

The IFC invests jointly with the private sector. To ensure the participation of investors and lenders from the private sector, IFC limits the total amount of own-account debt and equity financing it will provide for any single project. For new projects the maximum is 25 percent of the total estimated project costs, or, on an exceptional basis, up 35 percent for small projects. For expansion projects IFC may provide up to 50 percent of the project cost, provided its investments do not exceed 25 percent of the total capitalization of the project. On average, for every dollar of IFC financing, other investors and lenders provide over five dollars. IFC investment typically ranges from \$1 million to \$100 million. Its funds may be used for permanent working capital or for foreign or local expenditures in any World Bank member country to acquire fixed assets.

IFC's History in Russia

The IFC started working in Russia in 1992, with privatization projects in the agricultural, retail, and trucking sectors and privatization of large enterprises. Through its Land Privatization and Farm Reorganization Project, funded by the British Government, the IFC reorganized over 650 farms in 19 regions, privatizing over four million acres of land. It created five Russian institutions that continue to carry out farm reorganization at an average rate of 160 farms per year. In other sectors, the IFC assisted in privatizing over 140,000 small businesses and 1,100 large enterprises through open and transparent auctions across Russia. Similar privatization programs were implemented in Belarus and Ukraine.

The IFC also assisted in the preparation of over 100 pieces of legislation throughout the former Soviet Union

in areas such as land and property ownership, small business regulation, corporate governance, and leasing legislation.

The IFC's company-level work during these early privatization initiatives has enabled it to gain a first-hand understanding of the way business is done in the regions and foster relations with regional authorities. Mr. Solovyov spent eight months in the Oryol region assisting local farms with reorganization and working with local authorities to help them promote land reform and reorganize agricultural enterprises in the region.

In 1993, Russia became a member of the World Bank, and the IFC began to invest in the country. In the agricultural sector, all the investments have been in foreign food processors. IFC investments in the agricultural sector include: Depsona — a juice maker in Tula with Fiat, DreVo — a cash crop production in Voronezh with Louis Dreyfus, and Campina Melkunie — a Dutch cooperative dairy processor that established a yogurt factory in Moscow. No investment has been made in a fully owned local company for a number of reasons including a lack of transparency, poor corporate governance, and a lack of qualified management.

Lessons Learned from IFC's Work in Russia's Agricultural Sector

- 1 Due to the decline and deterioration of Russian agriculture in the 1990s, the problem of low quality and insufficient raw material supply to food and agribusiness (F&A) companies will continue to be a difficult one. While the demand of F&A companies for raw materials in different agribusiness sectors has increased, the lack of technology, know-how, experience and financing in the primary sectors means that supply — both in terms of quantity and quality — will continue to be limited.
- 2 Many processors have been at least partially unsuccessful in setting up local raw material supply on their own. They fall into three categories with

respect to how they have handled their raw material problem:

- a. Some have had no alternative but to invest in their supplier-farms on their own and have found that this is a time-consuming and expensive option;
- b. Others have relied on imports of raw materials, especially where quality issues are paramount. This is obviously an even more expensive option, which partially negates the positive effects of investing in local production in Russia;
- c. A third group has decided to delay its local processing plans in Russia, until Russian agriculture improves to acceptable quality and quantity levels.

To address these issues and to facilitate FDI in agriculture, IFC is working to build local supply chains of raw materials through its technical assistance program in the former Soviet Union called Private Enterprise Partnership. For example, it recently completed a project for Campina, a Dutch dairy company, which led to a \$50 million Campina/IFC investment in a yoghurt production plant outside of Moscow. The IFC, with funding from the Dutch government and Campina, surveyed Russian farms to select the strongest as potential suppliers of milk to Campina — conducted thorough technical and legal review (including property rights) of the selected farms — and introduced modern technical and management know-how to improve the quality and increase the quantity of produced milk to meet European standards. The IFC also served as an honest broker in negotiating long-term supply contracts between the farms and Campina and helped Campina structure \$1 million of investment to purchase modern agricultural equipment and rent it to supplier farms. Given the farms' lack of capital, the cost of equipment was calculated in milk, and the farms make rent payments in milk with a term of one to four years.

This experience demonstrated a shift in the way Russian farms operate.



(L-R) Agribusiness Committee Chairman David Lyons, Vice President of Government Relations, Louis Dreyfus Corporation; Vadim Solovyov, Agribusiness Investment Officer, International Finance Corporation (IFC); and Christian Foster, Chief of the Trade and Investment Branch of the USDA's Foreign Agricultural Service.

Mr. Foster spoke of last spring's Agribusiness Mission to the Russian regions organized by the U.S. Department of Agriculture (USDA) and the U.S. Agency for International Development, with the cooperation of the U.S. Department of Commerce and the Russian Ministry of Agriculture. Representatives of 12 American agribusiness companies visited the Moscow, Rostov, Samara, and Lipetsk regions. In order to be included in the USDA program, the targeted regions' business leaders were encouraged to work closely with their policy makers and regulators in order to improve the investment climate.

The USDA worked closely with USAID, the U.S. Department of Commerce, and Russian federal and local Ministries of Agriculture to organize the mission. In addition, several Russian agribusiness experts working in these regions were enlisted to identify and qualify potential investment opportunities. Information about 20 companies in each region was compiled and offered to American investors and trading companies.

concluded some investment or sales agreements with Russian partners.

Funding is available for conducting another agribusiness mission to Russia next spring, and initial planning is underway. Mr. Foster encouraged all those interested in participating in the next trade mission to contact the USDA. He also announced that the training program and trade show in the Russian Far East that was to be conducted in Vladivostok in October 2001 was cancelled. This program will be rescheduled in early 2002.

Question and Answer Session

Do you think Russia is going to introduce quotas in the poultry industry? The development of Russia's WTO accession process will definitely influence the decision to impose quotas. Mr. Foster said that the USDA is fighting to prevent the introduction of poultry quotas in Russia. There were a series of meetings with representatives of the Russian Ministry of Agriculture, where the negative results of these restrictive trade measures were discussed.

Specifically, Russian farms are keen to enter into long-term supply relationships with reliable F&A partners. They fully realize the importance and benefits of long-term supply relationships and are willing to radically change the way they work in order to reach quality levels acceptable to major F&A companies.

Given that the supply relationship with farms can be set up as a tight link between farm and processor, the investment scheme whereby the farm pays for investment through its raw material (commodity) supply has proven to be very effective. In the case of the Campina investments, over the past two years there has not been a single disruption of payments and/or supply.

External financing options for the agricultural sector are very limited. The major (and in some cases the only) source of financing has been processing companies and, in minor cases, government subsidies. The latter almost always require that the financing be used to procure Russian-made equipment.

IFC's partnership is looking into developing a pilot farm credit company. This financial institution may finance the purchase of modern equipment and rent it to farms who are suppliers to strong agro processors. The processors will make direct payments to the company, while the supplier farms will make in-kind rent payments with their product to the processor.

The provision of financing alone, without technical assistance and proper monitoring, is extremely risky in the farming sector. Thus the partnership plans to train local farms in financial management and continues to provide technical assistance in agricultural management to help the farms make informed investment decisions.

In addition to building local supply chains, IFC's technical assistance programs in the agricultural sector can be designed to facilitate investment into

existing local processors. In this case they will survey local processors to identify those that are best positioned to modernize their production and management, and match them with prospective investors to create joint ventures and to introduce foreign ownership in local businesses. They further support and strengthen such joint ventures by assessing and advising them on corporate governance practices, financial management, obtaining financing, improving production, and building supply and distribution chains.

New initiatives to improve distribution are also under consideration. The IFC is considering creating a wholesale distribution company, which would assist large supermarkets with establishing a reliable supply of fresh produce. On the investment side, the IFC is looking to participate in the second Agribusiness Fund, which will invest in agribusiness and logistics companies in Russia.

Investment Areas

In his experience, Mr. Solovyov has seen significant increases in investment activity in several sectors. These are poultry, beer, market infrastructure, and packaging. The IFC is looking at opportunities with a couple of multinational corporations to develop malting facilities in the former Soviet Union in response to the growing market demand for beer.

Question and Answer Session

Although the IFC seems concerned with marketing contracts and credit for farmers, what is being done on the input side? The IFC's experience in financing inputs in the Russian Federation is limited. IFC has provided financing to Drevo, which provides inputs to Russian farms, with the farmers and Drevo then sharing the crop. To become self-sustainable, however, the project needs to be expanded to achieve economies of scale.

What was unique in the yogurt project that made it so much more successful? The project was successful due to a surge in demand for yogurt in Russia and very

thoughtful project execution by Campina.

While the World Bank is winding down many of their technical assistance programs, the IFC seems to be taking more on. Is this a trend or a coincidence?

The IFC started with technical assistance and at one time had 700 people on the ground working in five regions in Russia. Technical assistance programs were always a major focus, but after the 1998 crisis the IFC felt that technical assistance could play even a bigger role in promoting investment and encourage private enterprise development. With the creation of the Private Enterprise Partnership, IFC is expanding its technical assistance in the former Soviet Union and is further integrating technical assistance into its investment programs. The interest from the donor governments in continued technical assistance also remains very high.

How are the technical assistance programs funded? Technical assistance initiatives are mostly funded by donor governments. In cases when technical assistance is directly linked to an investment project, usually the main sponsor is the government of the investor's country. In the agricultural sector, the Dutch Government is the largest donors. The IFC's contribution to technical assistance covers the management costs, new project development, and project assessment — it comes to about 22 percent of the cost of any single project. In addition, IFC contributes time and expertise of its investment staff in designing and implementing technical assistance programs. ■

¹ IFC's Private Enterprise Partnership is the technical assistance arm of IFC's Central and Eastern Europe Department with five permanent country offices in Armenia, Belarus, Georgia, Russia, and Ukraine, staffed with over 200 local professionals. The partnership is funded by donor governments and IFC. Its focus: (1) promoting private sector investment with emphasis on foreign direct investment by resolving enterprise-level constraints to investment; (2) supporting the growth of SMEs, particularly through developing financial markets and building viable financial institutions, such as leasing companies, venture capital funds, micro-finance, and commercial banks; (3) improving the business-enabling environment with an emphasis on corporate governance.

ANNUAL MEETING 2001 *Washington, DC ■ October 4-5, 2001*

COMMITTEE MEETING ENERGY COMMITTEE

MODERATOR Terri L. Otzmann
Director-Russia, Texaco Inc.

SPEAKERS Howard Chase
Director, International Affairs, BP

Ambassador Stephen R. Mann
Special Advisor to the President and the Secretary of State for Caspian Basin Energy Diplomacy

Mr. Chase began his remarks by noting that a new phase in U.S.-Russian relations and, indeed, Russian-European relations began even before September 11. The terrorist attacks have shown that new opportunities are possible due to the importance of the geographic link between the location of oil and gas resources and their natural markets.

The vast majority of Russian energy fuel resources are distant from the markets, landlocked and isolated. Furthermore, supply far exceeds domestic demand and will remain this way for a long time. Therefore, export infrastructure is critical to Russia and the global economy. Russia inherited from the Soviet Union overwhelming monopolies in oil and gas transportation that are critically important sources of state revenue. Many Russian government officials consider them politically and economically indispensable. Yet, large resources remain undeveloped because there is no access to markets. New oil fields are hostage to limited export pipeline infrastructure, thus shifting the investment opportunities from production to transportation networks.

Perhaps more than anywhere in the FSU, the Caspian region is a good example of the interaction between investment, infrastructure and politics. The Caspian Pipeline Consortium (CPC) represents a major achievement in that it has unlocked the oil of the north Caspian and allows it to flow reliably to the market. It demonstrates

that international investment can provide the necessary infrastructure and proves that there are alternatives to national pipeline monopolies. The south Caspian region will also soon see significant progress with the Baku-Tbilisi-Ceyhan (BTC) pipeline. It will divert the daily loading of one million barrels of oil into the Novorossiysk

Marine terminal on the Black Sea and reduce tanker traffic through the Bosphorus Straits. Mr. Chase pointed out that a number of oil producers in Kazakhstan as well as in Russia are now looking into using the BTC pipeline, which could easily be expanded to become the Aktau-Baku-Tbilisi-Ceyhan (ABTC) pipeline.

Mr. Chase also discussed the East-West gas pipeline, which will deliver Azeri gas to Turkey. The Sakhalin projects and BP's Kovyktinskoye (Kovykta) are also good examples of the critical role infrastructure plays and demonstrate that progress being made as the export outlets are defined.

Mr. Chase noted that three years of

high oil prices have allowed Russian companies to improve their balance sheets and make significant progress toward more stable corporate structures. Improving financial performance has taken precedence over developing reserves and production output. This change suggests that Russian companies are developing a better understanding



Vice Chair of the Energy Committee, Terri L. Otzmann, Director-Russia, Texaco Inc., introduces speaker Howard Chase, Director of International Affairs at BP.

of the role of competition in attracting new customers and increasing market share and shareholder value. Competition will accelerate the much-anticipated leveling of the playing field.

However, a lot has to be done in the area of corporate governance to encourage further progress in the sector. Also, analysts must distinguish between those companies that practice asset stripping and those that are merely seeking to grow their business on behalf of their shareholders.

Mr. Chase stated that BP remains the largest single international investor in Russia, and he mentioned that BP's asset-stripping problem with Sidanco is very close to a final resolution. BP's major investment in CPC demonstrates that BP is a major player in Russia, and Mr. Chase expects continuing expansion of their involvement in Russia.

Regarding the signposts of change in Russia in a low oil price environment, Mr. Chase feels that one positive signal would be legislation that establishes an effective production-sharing regime. It would unlock pent-up investment in the energy sector, especially in technologically and geographically difficult areas.

As to whether Russia could be the big spoiler of U.S.-OPEC reliance, Mr. Chase does not believe Russia could or would want to be a spoiler. Higher prices have allowed Russian companies to strengthen their balance sheets, and while international oil companies are operating under conservative estimates of oil prices, no one wants to force oil prices sharply upward or downward.

On the topics of the production of associated gas in Russia, its market access and Gazprom's role in maintaining the monopoly over gas pipelines, Mr. Chase said Gazprom remains an enigma. Market access for associated gas is dependent upon infrastructure (now non-existent) to deliver the gas to the consumer. BP is not expecting an imminent unbundling of Gazprom's production and transportation systems.

Ambassador Steven R. Mann gave committee members a status report on U.S. interests in Caspian Basin energy developments. Despite a number of problems plaguing Caspian region energy-sector development including central control, economic cynicism, corruption, a lack of legal structures, and under-investment, the progress is being made and billions of dollars are flowing into the region. Moreover, brilliant new generations of energy professionals are arising throughout Eurasia.

The U.S. government's policy has been

to support modernization of the Caspian energy sector, in conjunction with development of the region's economies. Multiple export routes are a vital goal for sustainable regional economic development and stability. It is not an anti-Russian policy; rather, it is anti-monopoly. The Soviet Union pursued the construction of a Caspian Basin energy sector with monopoly power designed to put other states at a disadvantage. In fact, this monopoly structure also did a great disservice to Russia: competition will force Russia to become more efficient and compel them to adopt global standards.

Ambassador Mann cited CPC as a success story for international cooperation. He also believes that the Baku-Tbilisi-Ceyhan pipeline could become an Aktau-Baku-Tbilisi-Ceyhan pipeline, which will provide tremendous opportunities for U.S.-Russian cooperation. Already underway is a \$150 million engineering design study, and the BTC

construction could start next summer.

Ambassador Mann also praised Deputy Foreign Minister Kaluzhnyi for encouraging a Caspian Sea delimitation scheme. The U.S. does not consider delimitation a prerequisite for cross-Caspian transportation infrastructure. An agreement by participating countries for the transport of Caspian energy is sufficient, but delimitation will allow the resources to be extracted with greater confidence.

Ambassador Mann closed his remarks by saying that new pipelines are not an economic cure-all for either an exporting or transit country. Pipelines must be only part of a plan for national development.

In her closing remarks, Ms. Otmann emphasized the need for a greater focus on the knowledge economy. In addition, a focus on value over simple dollar injections is worthwhile. ■

ANNUAL MEETING 2001 *Washington, DC ■ October 4-5, 2001*

COMMITTEE MEETING LEGAL COMMITTEE

MODERATORS Sarah C. Carey
Partner, Squire, Sanders & Dempsey, L.L.P.

Richard N. Dean
Partner, Coudert Brothers

SPEAKER Dmitry N. Kozak
Deputy Head of the Russian Presidential Administration

Dmitry Kozak began his presentation by describing far-reaching reforms that have been instituted in Russia. The reforms permeate literally all aspects of life – politically, economically, socially – and a whole range of legislative reforms were begun this year on everything from land laws to civil services. These reforms will demand substantial efforts including financial infusions. Their overall goal (those currently being implemented and those being planned) is the creation of a democratic state based on the rule of law and a developed market economy. The Constitution of the Russian Federation declares that individual rights and freedoms are of supreme value, a principle that defines the state's functions. Unfortunately, due to a variety of factors, both subjective and objective, this overarching principle remains merely declarative in nature. Therefore, the first priority is the creation of objective juridical and political mechanisms that will allow the proper functioning of all state and public institutions, and thus speed the implementation of important constitutional principles in everyday life.

The key components of creating a state mechanism to protect individual citizens' rights and freedoms are the justice system and law enforcement. This is why President Putin made judicial reform initiatives a legislative priority for 2001.

Judicial reform began in Russia in the early 1990s. In 1991, a judicial reform

doctrine was adopted, and in 1994-96 (in accordance with this doctrine) the main judicial reform legislation was passed. At the time there were two principal objectives. The first objective was to make judges independent from any kind of external influences and dependencies. In Soviet times, influence on judges was known as the so-called "telephone judgement," as judges were highly susceptible to the interests of influential members of the Communist Party apparatus. The second objective was to form a court system that would be capable of adjudicating not just divorce cases or alimony settlements, but also property disputes and obligations emanating from new market-based business agreements. The courts also needed to be capable of annulling unconstitutional laws.

For the most part, these objectives were met. But it became evident toward the end of the past decade that these issues were resolved in a hurry, resulting in faulty laws. As a consequence, the court proceedings became too long, and accessibility to the justice system started to decrease in proportion to its development. Quite often courts were being used as instruments of unfair competition, and the citizenry's trust in judicial authority began to diminish rapidly. It became apparent that without a number of improvements, neither economic nor political development in Russia would be feasible.

The main goal of judicial reform is to create objective, efficient and reliable

mechanisms for defending citizens' rights. At the same time, judicial reform in Russia is considered one of the key aspects of economic reform. The difficulty of this task is compounded by the fact that over the past decade, exaggerations were embedded in the laws of the early 1990s, and have taken deep roots in the practices of courts, law enforcement agencies, and even more so, in the mindsets of civil servants who work for these institutions. The new package of reform laws has been criticized by many interest groups, especially by employees of the judicial system, prosecutors, and representatives of law enforcement agencies. Thus, for instance, in regard to the law on the status of judges, the issue is the ratio of judges' independence to the objectivity in administering court rulings. The presidential package of judicial reform legislation differentiates between the notions of judicial independence and objectivity. The legislative initiatives brought to the Parliament intend to create procedural orders for appointment and dismissal of judges. In combination with the measures increasing compensation for judges, this would guarantee, facilitate and strengthen the independence of courts and judges (from the other branches of state authority).

Mr. Kozak stressed that the independence of judges is one of the most important factors of judicial reform, but certainly not the only one. Judicial independence itself does not necessarily guarantee the objectivity

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and impartiality of court proceedings or rulings on any given case. It only provides a higher degree of freedom for a judge, both in the areas of performing judicial duties and beyond. However, the vital interests of citizens, the state and society are vested in the impartiality and objectivity of judges and courts. The independence of judges represents simply one of the most important instruments of achieving objectivity and impartiality.

Mr. Kozak emphasized the importance of strengthening financial support for judges. He also stressed that judges have to be held accountable for their decisions. Today, in Russia, every judge possesses judicial immunity from criminal and administrative (civil) prosecution. In accordance with current legislation, a judge's immunity from criminal prosecution can only be repealed by special bodies of the judicial community, such as qualified peer review boards comprised exclusively of judges. When it comes to administrative crimes, the prosecution of judges is not possible at all (in Russia, public misconduct and traffic violations are categorized as administrative crimes). In fact, there exists a law that prohibits prosecution of judges, irrespective of the gravity of the particular administrative crime committed. The presidential package of judicial reform legislation contains proposals that would: 1) revoke absolute immunity for judges from administrative prosecution (because if judges commit even minor administrative crimes, by doing so, they cast a shadow over all judicial authority and undermine public confidence in judicial power); 2) transfer responsibilities related to annulment of judicial immunity from the peer review boards to a higher-level court; 3) establish additional procedural guarantees for judges (much different from the ones applied to ordinary citizens), regarding immunity from criminal charges. These procedural guarantees will protect the judges from mistrial for judicial decisions. It is suggested that questions of disciplinary responsibility of judges remain the prerogative of

qualified judicial review boards. Hence, the resolution of all questions related to the control and responsibility of judges for administering their judicial duties, for maintaining public confidence in the justice system, and for upholding their judicial reputation, are within or the judicial branch of the government in the form of a higher-level competent court. No additional responsibilities related to the oversight of the judicial decision-making process will be given to other bodies or select officials of the executive or legislative branch.

The presidential administration believes that the proposed package of legislative initiatives will equip the Russian justice system with true independence, impartiality, transparency, and accountability to the society at large.

Another significant component of judicial reform is the development and implementation of new procedural legislation to adequately address the realities of contemporary Russia. Despite the eight-year span since the adoption



(L-R) Dmitry N. Kozak, Deputy Head of the Russian Presidential Administration; Richard N. Dean, Partner, Coudert Brothers; Sarah C. Carey, Partner, Squire, Sanders & Dempsey, L.L.P.; and Council President Gene Lawson.

of a new Constitution, several fundamental principles of justice have yet to be enacted. For instance, the principle of equality and competitiveness of court proceedings implies that either side of the process (whether representing government or an individual) possesses equal procedural rights. However, another principle deeply engrained in the Civil, Criminal and Arbitration Codes grants special privi-

leges to the prosecutor and chairman of the court, which in turn directly contradicts this constitutional requirement.

In addition, the 1993 Constitution affirms that a citizen's personal freedom and the inviolability of a citizen's residence can only be limited on the basis of a court decision. However, similar decisions regarding citizens have been made personally by the Prosecutor General. This summer the Duma approved the new drafts of the Arbitration, Civil and Criminal Procedure Codes. These drafts contained presidential proposals suggesting the resolution of these significant problems.

Another problem for the judicial system is that economic transformations in Russia have revived commercial arbitration. According to unofficial estimates, 3,000 commercial arbitration firms operate in Russia. Part of them function under the aegis of the Russian Chamber of Commerce and Industry, and others are organized around the stock markets. Still others are located

in major industrial centers. Nonetheless, there is no clear legal basis for their existence. Moreover, there is no agreed-upon procedure for recognition or enforcement of their decisions, so there is no legal mechanism that gives these decisions judicial power through the courts. The "Federal Law on Arbitration Courts" is designed to finally regulate the status of these non-governmental institutions. This law is

currently under consideration by the State Duma.

The most acute problem in Russia is the issue of implementation and enforcement of court decisions passed by both state and non-state courts. The present legislation on enforcement of court decisions is far from adequate. In his recommendations on procedural laws, President Putin proposed concrete mechanisms for improving the enforcement of court rulings. Unfortunately, this has been undermined by the gradual erosion of legal system's integrity, which endured for a decade or so (until 1999) and had a negative impact on the resolutions of the Constitutional Court. Many of

the decisions of this supreme judicial body have not been enforced. For the past year, President Putin has undertaken political measures to abolish unlawful and unconstitutional legislation enacted by both the federal and regional governments.

The presidential package of legislative initiatives also contains proposals for creating a reliable legal framework for the activities of attorneys. As of today, the functions of attorneys (as well as the entire legal framework for their practices) are determined in accordance with the Soviet law of 1980. The presidential administration realizes that without strong public defender provision justice is impossi-

ble. The presidential draft law on attorney practice determines the legal status of lawyers and the entire community of legal service firms. More important, it will formulate federal organizational principles for Russian attorney practices. This law also provides procedural guidelines for the provision of free legal service in criminal cases, which is also guaranteed by the Constitution, but cannot be implemented because no relevant legislation has been enacted.

In conclusion, Mr. Kozak stated that the implementation of this legislative reform package would result in positive, qualitative changes in the Russian justice system. ■

ANNUAL MEETING 2001 *Washington, DC ■ October 4-5, 2001*

COMMITTEE MEETING | IT/E-COMMERCE WORKING GROUP

MODERATOR Pawel Stelmaszczyk
Director of Emerging Market Government Policy, Intel Corporation

SPEAKERS Konstantin Vetrov
Chairman, Committee on Information Policy, State Duma of the Russian Federation

Esther Dyson
CEO, EDventure Holdings Inc.

Ivan Kurnosov
Deputy Head of IT Department, Russian Ministry of Communications

Konstantin Vetrov, the Chairman of the Committee on Information Policy in the Russian State Duma, led off the discussion with an update on the status of two important pieces of legislation before the State Duma: the draft law "On Electronic Signatures" and the draft law "On E-Commerce". He identified the following key components of the draft digital electronic signature law:

- A digital electronic signature is the legal equivalent of a handwritten signature if it is verified by the "public key," and the certificate at the

moment of signing is valid and has not been altered.

- All copies of the file endorsed by the digital electronic signature are legally equal to originals and are admissible as evidence in the courts.

- The owner of the electronic "private key" has the right to possess, use and sell an unlimited number of "private keys."

- Individuals who unlawfully use the digital electronic signature and the "private key" of another person are subject to prosecution in accordance

with the Criminal, Civil and Administrative codes.

- Files endorsed by the digital electronic signature can be presented in the courts as forensic evidence along with papers and other official hard-copy documents.

Mr. Vetrov then turned to the draft law "On E-Commerce", a bill that he and seven of his Duma colleagues drafted in close consultation with the Ministry of Communications. He believes that the most important elements of the bill are the following:

- The bill defines "legal persons" as any individual who is registered as an entrepreneur. When legal persons exchange electronic files that are endorsed by the unaltered signatures of the parties to the transactions, this process satisfies all requirements that exist for the written format of any business transaction as established in the Civil Code.
- Electronic transactions should not be regarded as invalid only on the basis of the fact that they were concluded by electronic means.
- Business transactions which, by law, must be notarized or are subject to special state registration cannot be concluded by electronic means.
- Electronic documents endorsed by electronic digital signature belong to the category of "written evidence."
- People engaged in electronic commerce must present to both their clients and relevant government agencies information on their legal status and the scope of their activities.

Ms. Dyson explained that she believes the overriding goal of the Council's work in the IT field should be to support the creation of an economy in Russia that uses information technology effectively. Getting IT in the hands of users so that the Russian marketplace as a whole is more productive is a key part of that process. She suggested three ideas on how this might be achieved.

- *Organize a "field trip" using marketplace incentives.* Russian systems integrators and U.S. suppliers would identify Russian customers and potential customers that are most in need of IT products. The IT managers and systems managers from those companies would then be invited to visit their counterparts in the U.S. for a demonstration of how American companies apply IT to their business models to solve problems and improve efficiency and profitability.
- *Compare and contrast the IT industry in Russia with the IT industry in India.* Much has been written about the Indian "economic miracle" and

value of that outsourcing domestically. Ms. Dyson pointed out that in India much of the value associated with outsourcing revenue leaves the country. This is a problem that the Russian IT sector, although significantly smaller, must continue to avoid.

- *Emphasize the importance of American business "know-how" in the Russian IT sector.* This includes both old-style management skills and project development skills, both of which are lacking in Russia. Since such skills are best acquired through experience, the outsourcing business is a tremendously important "school" for Russian programmers. The simplest and best way to invest in the education of Russian programmers is to send them orders for IT projects.

Ivan Kurnosov was the last speaker to address the group. He spoke about recent trends in the IT sector and barriers to its continued and accelerated growth. He also outlined key elements of the "E-Russia" program.

Mr. Kurnosov identified three major developments in the past year that have had a profound impact on the IT sector in Russia: the launch of the E-Russia program; progress towards creating a legal and regulatory environment that encourages the development of the IT sector; and the creation of an "IT dialogue" between industry executives and the Russian government.

The establishment of the IT dialogue, he explained, ensures that government decision-makers understand how their policy decisions impact the IT community. In April, President Putin himself met with a group of Russian IT entrepreneurs to discuss how the Russian government can play a constructive role in the growth of the IT sector. Additional meetings with industry leaders and Ministry representatives regularly occur.

Mr. Kurnosov then recognized the ability
continued on page 31...

9th ANNUAL MEMBERS AND DIRECTORS MEETING



National Security Adviser Condoleezza Rice arrives to deliver the opening keynote address, escorted by Council President Gene Lawson.



(L-R) Russian Ambassador Yuri Ushakov, Joseph Samora of CaseNewHolland Inc. and Richard Conn of Latham & Watkins.



IT/E-Commerce Committee panelists: (L-R) Esther Dyson, CEO, EDventure Holdings Inc., Konstantin Vetrov, Chairman, State Duma Committee on Information Policy, Ivan Kurnosov, Deputy Head of IT Department, Russian Ministry of Communications, and Pawel Stelmaszczyk, Director of Emerging Market Government Policy, Intel Corporation.

Esther Dyson began her remarks by emphasizing the enormous intellectual capital of the Russian people, a resource, she explained, that must be fully explored in order for the country to realize its enormous economic potential.

India's \$4-5 billion in outsourcing revenues. A comparison of the Russian and Indian IT sectors would provide valuable information on what Russia can do to increase its outsourcing revenue in the IT sector, while at the same time capturing the



Richard Matzke of Chevron Corporation (left) and Allen Daniels Midland at the Gala Dinner.



9TH ANNUAL MEMBERS AND DIRECTORS MEETING



*First Deputy Prime Minister of Russia
Aleksei Kudrin with
Council members.*



*Secretary of Commerce Donald
Evans kicks off the second day
of the USRBC Annual Meeting.*



*Richard N. Dean,
Partner, Coudert
Brothers, introduces
the discussion on the
new Corporate
Governance Code.*



*Council President
Gene Lawson
opens the 9th
Annual Meeting.*



9TH ANNUAL MEMBERS AND DIRECTORS MEETING



Richard H. Matzke, Vice Chairman of Chevron Corporation, gives a historical perspective on the Tengizchevroil/Caspian Pipeline Consortium, beginning in the late 1980s.



Ernie Stern of J.P. Morgan Chase (right) talks with Paul Rodzianko of Access Industries.



Dmitry Kozak, Deputy Head of the Russian Presidential Administration, speaks about judicial reforms in Russia.



Igor V. Kostikov, Securities Commission Chairman, speaking on Russia's new Corporate Governance Code.



Commenting on Russia's new Corporate Governance Code, Howard Chase, Director of International Affairs at BP Amoco (left), and William Jarosz, Managing Director of American International Group, Inc.

PRESIDENT PUTIN COMES TO WASHINGTON



Jack Smith, Chairman of General Motors (left), speaks with President Putin.



(L-R) Mark Zilberquist, President of CEBM Inc., Paul Rodzianko, Senior Vice President of Access Industries, and Council Executive Vice President Blake Marshall.



President Putin discusses positive changes in U.S.-Russian relations at the Embassy dinner.



(L-R) Alexander Vershbow, U.S. Ambassador to Russia, Council President Gene Lawson and Benno Hoogendoorn, President and Joint CEO of Mars Incorporated, share a laugh.



Donald Kendall, former Chairman and CEO of PepsiCo, chats with President Putin.



(L-R) Jack Smith, Chairman of General Motors, and Council President Gene Lawson talk with Igor Ivanov, Minister of Foreign Affairs of Russia.

...continued from page 22

conducive to the growth of the IT sector. Like Mr. Vetrov, he pointed to two key pieces of legislation, the draft law "On Electronic Digital Signature" and the draft law "On E-Commerce," as positive steps forward. Both are high on the priority list of IT leaders, and he is hopeful and optimistic that both will be passed into law.

Before outlining the E-Russia program, Mr. Kurnosov laid out some of the specific challenges the program was designed to overcome. First is Internet accessibility – increasing the level of Internet and PC penetration throughout Russia. Other priority challenges include improving government regulation of the IT sector, implementing the concept of "e-government," and

reforming technological education.

The E-Russia program addresses each of these issues. Connecting state-run organizations to modern information and communication networks is essential to the program's success. According to Mr. Kurnosov, more than 50,000 villages and towns in Russia still do not have regular phone connections. Attracting the necessary investment to modernize communication infrastructure in these areas and connecting them to modern communication networks, including the Internet, is a priority issue for the government and an important goal of the E-Russia program.

E-government is an equally important part of the program. This means using IT to facilitate increased transparency

and accountability in government operations. Mr. Kurnosov explained that an important first step in this area is requiring ministries and executive branch agencies to provide information to citizens online and requiring electronic communication between government offices.

Mr. Kurnosov also spoke about the programs aim to create "interagency centers on information technology." Such centers will be created in partnership with the Russian Academy of Sciences and various agencies of the Russian government. These centers will serve as sources of information and training for IT companies. They may also serve as centers for registering Internet domain names and communicating regulatory concerns to the Russian government. ■



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ANNUAL MEETING 2001 Washington, DC ■ October 4-5, 2001

PANEL POLITICS UNDER PUTIN

- MODERATOR** G. Allen Andreas
Chairman & Chief Executive Officer, Archer Daniels Midland Company
- SPEAKERS** Michael McFaul
Senior Associate, Carnegie Endowment for International Peace
- Valery P. Goreglyad
Deputy Chairman, Budget and Tax Committee, Federation Council
- Masha Lipman
Deputy Editor, Ezhenedelny Zhurnal
- Mikhail V. Margelov
Chairman, International Affairs Committee, Federation Council

Michael McFaul discussed the new levels of support and cooperation between the U.S. and Russia, and cited some of the domestic constraints on President Putin in expanding our bilateral relations. He also shared his views on what needs to be done in order to solidify the high level of good will and emotion that currently exists between the two nations.

U.S.-Russian relations. Mr. McFaul does not see Russian cooperation as an attempt to achieve short-term gains and believes that President Putin's statement of support for America was sincere. However, he cautioned the audience that support for the President's cooperation with the U.S. is not unanimous among the Russian elite, or even throughout Russian society. Therefore, he considers Putin's recent statements as profound, against the grain, and politically risky.

Putin's popularity has led to public pronouncements of support from Russian government officials and military. Underlying these public statements, however, are some issues of concern. First of all, the Russian military (especially Mr. Kvashnin) is not pleased with having NATO troops in Central Asia. If the NATO operation is not short and successful, Defense Minister Ivanov, who is loyal to Putin now, might become a source of opposition within the government. The military-industrial complex, and Duma deputies who support this industry, did not like President Putin's statements about Iraq, Syria and Iran. The communists, and Mr. Zhirinovskiy, will publicly attempt to undermine the support for the Putin government should things begin to go badly (fortunately, they do not matter much now). Even Russia's foreign poli-

cy leaders split on the issue of how involved Russia should be in cooperating with NATO and the United States. Many liberals are also worried that getting involved in the fight against terrorism might cause erosion of human rights and democracy within Russia itself. Finally, the society at-large might oppose President Putin's support of U.S. actions in the region. Even though recent polls in Russia show that Russians are generally Western leaning and strongly believe not only in the norms but also in practice of democracy [see "Can Russians be Democrats and Capitalists at the Same Time?" by Michael McFaul in the Summer 2001 issue of RBW], they remain ambivalent about the role of the U.S. in the world, and about the war against terrorism. Therefore, it would be a mistake to assume that Russian society will continue to fully support President Putin on this issue.

Mr. McFaul offered his suggestions on what should be done by the American side to turn President Putin's statements into actual policy, and provide tangible rewards for his politically risky cooperation with the United States. First, if the arms controllers believe that treaties binding Russia and the United States should be different from those that existed with the Soviet Union, why doesn't the United States take a

similar position about trade? Second, the United States should push for Russia's further integration with the West, including Russia's accession to the WTO and Russian cooperation with NATO. Third, there should be an allowance for NATO to buy Russian weapons. Fourth, NATO allies should buy Russian weapons to ship to the Northern Alliance like the U.S. did with Czechoslovakia when it purchased weapons to ship to the mujahideen. Fifth, cooperation with Russia on fighting terrorism based in Georgia is a way to prevent a unilateral intervention, which could have very dangerous consequences. Now is a time for breakthroughs in Chechnya, not further deterioration. Finally, continued support for democratization in Russia is vital. Russia will only be a fully integrated partner with the West when Russia is a consolidated democracy. Ultimately, this is an opportunity for Russia to become a long-term, close ally of the United States.



Valery P. Goreglyad, Deputy Chairman of the Federation Council Budget and Tax Committee, addresses Council members on federalism in Russia.

Mr. McFaul said the fastest democratizers among post-communist countries also happen to be those that grow the fastest economically. There is a point of view among some American businessmen that dictatorship is needed in Russia to get things accomplished. Mr. McFaul cited Tajikistan, Egypt, Pakistan, Congo, and Afghanistan as good examples of why these views are misguided. There are lots of examples

of weak states with oilfields that have severe corruption and no opportunities to do business normally. The free press and the opposition party are the best watchdogs for the crooks in any government, and both of them are under siege in Russia today. Transparency and democracy are Russia's allies during this time of developing new long-term relationships.

The panel's next speaker, Valery Goreglyad, discussed federalism in Russia. Nationalism and separatism will be the biggest challenges in the 21st century, and Russia is classified as one of the most vulnerable countries in these terms. Enormous pressures will be put on Russia as a multinational federative state. The establishment of strong federative and economic ties will help to shield Russia from these challenges and threats. The Russian model of federalism needs to be renewed, which involves the reconstruction of an effectively functioning vertical state authority that is democratic in its nature. For centuries, the statehood of Russia was characterized by unlimited power from the center, and the public processes were not based on the principles of free choice.

The government sometimes makes policy based on ethnic factors, and this will only lead to further deterioration. It would be naïve to think that the relationships between the center and citizens could have changed dramatically during the past hundred years. The development of a legal framework slowed down after the adoption of the Constitution in 1993, and none of the important proposed amendments went through the Federation Council. For a while, the practice of bilateral negotiations between the regions and the federal center was chosen as the main channel for settling disputes. This became a source of significant tension between the subjects of the federation. Despite a wide usage of the word "federalization" in Russia, there is no system of developed federative relations in Russia. A profound social crisis and total corruption in the initial stage of



Masha Lipman, Deputy Editor of Ezhenedelny Zhurnal, speaks about human rights concerns.

democratization gave rise to nostalgia for a "strong hand," which some believed could return order to the country. The growing independence of the regions was interpreted not as a natural democratic process, but rather as concessions on the part of the central government to certain regions. Such concessions led to significant economic losses.

After the election of President Putin, it became possible to reverse the course of Russia's transformation into a confederation. The Russians are facing a serious dilemma today. The government should either declare the orientation toward federal relations a mistake and begin building a unitary state, or begin creating the basis for true federalism. Mr. Goreglyad believes that the country is ready for the latter model.

Only an economically and politically mature system of federalism will guarantee the integrity of Russia as a multi-ethnic state and generate incentives for long-term socioeconomic progress. Federalism should become the most important constitutional-legal safeguard of entrepreneurial freedom, competitiveness, the rights of investors and property owners, and support for Russian manufacturers in world markets.

Making a choice of a system that has functional federal relations, the Russian government needs to take into consideration the following factors:

- The development of federalism is a long-term process that consists of multiple stages. This is why contemporary Russia cannot adopt models implemented in other countries that have centuries of experience in developing federalism and markets.



Deputy Chairman of the Federation Council International Affairs Committee Mikhail V. Margelov speaks about U.S.-Russian cooperation after September 11th.

- It is important to determine the criteria that will make clear which regions have the right to contend for the status of federation.
- The federation can be considered stable only if it is based on the principle of economic and not ethno-political formation.
- The success of a democratic, federal Russia depends directly on the success of market reforms.
- It is necessary to construct a two-tiered state system of territorial administration with clearly defined functions of federal and regional authorities.

Mr. Goreglyad then spoke about the shortcomings of the Russian federal system today and their origins. The formation of the territorial structure of Russia took place while political life in the country was mostly determined by the ruling classes to enforce and enhance the independence of the regions. Also, there was a very weak connection between the economic and social challenges of the regions. Today, despite good precondi-

tions for implementing strategic and economic goals in the social sphere, the imperfections of Russia's statehood becomes a serious obstacle to further reforms. The establishment of President Putin's special representatives in the regions and seven federal administrative districts (which initially caused a great deal of debate and criticism) enabled Russia to bring regional legislation in compliance with federal legislation and, consequently, made the organs of federal power more effective.

The creation of seven administrative zones in Russia supervised by a presidential representative was the first step in building an effective system of statehood, which depends on many factors. Russia needs to improve relations between the center and the regions and find ways to make the Russian regions economically independent. The subjects of the federation are formal legal entities; yet, many of them depend heavily on subsidies from the federal budget. For example, Tuva receives 18 times more funds from the federal budget than the amount of taxes collected in the region. Less than one-third of the regions are economically independent. Economic stimuli are necessary to help them gain independence. The Russian government understands the urgency and importance of the establishment of a sound and truly balanced federal system, and the examples of its actions include the adoption of a federal development program to the year 2005, and the reshaping of the budgetary principles and the tax system.

Masha Lipman raised concerns about the effects of the September 11th events on human rights. The tragic events offer President Putin a unique chance to integrate with what he referred to as "civilized humankind." President Putin has demonstrated that he realized this opportunity and was not going to lose it. This was not an easy decision, however. Underneath the seeming consensus, the Russian political elite has been conflicted

between pro- and anti-Western forces. Along with protecting itself from terrorists, joining the coalition against terrorism will also be economically beneficial to Russia through potential debt relief, WTO accession and closer economic cooperation with the world's most prosperous and developed countries. Closer cooperation with the West might encourage Russia to become a more solid democracy and give a push to liberal freedoms, and freedom of the press in particular. However, the horror of terrorist attacks has created an unfavorable context for the promotion of rights and freedoms in Russia. She said people seem to be more willing now to sacrifice civil liberties for security.

Ms. Lipman expressed her concern about the violation of human rights in Chechnya. Despite having occupied a greater portion of Chechnya and losing over 3,000 Russian soldiers, Russia feels no more secure. Western criticism of Russia's actions in Chechnya has been muted since the recognition that Chechen terrorists are linked to Osama bin Laden.

Likewise, there is reason for concern about freedom of the press in Russia. The Russian media is neither fully controlled by the state, nor fully free of it. Soviet-style censorship no longer exists, but there is still a desire on the part of the Russian government to control the coverage of sensitive subjects. The Russian government enjoys a high degree of cooperation with most media, which is confined to such subjects as Kremlin decision making, the military, state security matters, and the president himself. While there is no direct censorship or harassment of journalists, the majority of the Russian media demonstrate extreme loyalty to the government when it comes to matters of a sensitive nature. The public's indifference and passivity only support the media's self-imposed policy of not questioning the government's actions. For the government this means there is no power to hold it accountable, and for the media — no need to dig deep.

The accountability of the Russian government is emphasized by the closed matter of Kremlin performance. While President Putin appears often on television, he has only given one press conference since taking office. Furthermore, Kremlin events have become semi-closed events for an inner circle of reporters. If reporters are not cooperative, they risk losing access to valuable sources of information.

The Russian government may consider itself lucky to have a passive society and a loyal press. However, its unchallenged performance is likely to cause Russia more harm than good.



"Politics Under Putin" panel members (L-R) Michael McFaul, Valery Goreglyad, Masha Lipman and Mikhail Margelov.

Mikhail Margelov began his presentation by saying that not only was America attacked in September, but also all of humanity as well. Civilized humanity has demonstrated a tremendous potential for cohesion in the face of a common danger. The universal instinct of self-preservation has had its say.

Mr. Margelov said we have to admit that the existing international security system, as well as national security systems, has proved inefficient in the face of the horrifying ingenuity of terrorists. The events of September 11 made it clear that there is no longer only internal policy, but all policy has international aspects and consequences. The proposals for the global

monitoring of terrorist activities and a coordinated hunt for terrorist hotbeds have turned into an absolute priority of international policy. The body of antiterrorist law must be reviewed without delay.

The fundamental national interests of the United States and Russia are not contradictory. This does not rule out competition, which is a driving force of all development. We should acknowledge that the transnational extremism that challenges mankind today has been generated, to a certain extent, by the era of head-on military, political and

ideological confrontation between the United States and the Soviet Union. The forces that used to be pawns in the global chess game of the two superpowers are trying hard to make their way to the last row of the chess board. Remoteness from hotspots no longer guarantees security. The world has become too small.

Mr. Margelov stressed that the Jackson-Vanik Amendment remains a part of this Cold War vision and represents an obstacle in the further development of business relations between the two countries.

Mr. Margelov concluded by mentioning the creation of a new working

group formed by the Federation Council and the U.S. Senate, which will compare the legislation of both countries and identify the obstacles for cooperation and root out the remains of the Cold War in the legislative area.

Question and Answer Session

How do you define the term independent media? How can the business community help Russian journalists and small media outlets? Ms. Lipman responded that she would not focus too heavily on the term "independent media." Press depends on public opinion, values, and many other things. More important is the diversity and what percentage of the press is not owned or controlled by the government. In Russia today, it is easier for the print press to be more critical and diverse than it is for television. This is because television has a much larger audience than the press, and thus is more relevant.

Mr. McFaul noted that 72 percent of Russians use television as their main source of news. He expressed concern over the way the government looks at TV-6's accounting books, because any time the rule of law is enforced arbitrarily, it affects everyone.

Mr. Goreglyad said that consistent reform in civil society and the establishment of democratic institutions, including media, need further development in Russia. Sometimes the media is responsible for the purposeful distortion of facts, and this problem can not be properly addressed without a functioning court system in place.

Mr. Margelov emphasized that freedom of press has to be discussed not only in terms of its independence from the federal government; special attention should also be paid to the influence of some local administrations and governors on the regional media. ■

ANNUAL MEETING 2001 *Washington, DC ■ October 4-5, 2001*

PANEL INVESTOR FRAMEWORK

- MODERATOR** Brian McDonald
General Director, International Paper (Svetogorsk)
- SPEAKERS** Oleg Vyugin
Executive Vice President and Chief Economist, Troika Dialog
- Laza Kekic
Director for Central and Eastern Europe, Economist Intelligence Unit
- Arthur L. George
Partner, Baker & McKenzie
- Michael Leathes
Head of Intellectual Property, British American Tobacco
- Dmitry V. Vasiliev
Executive Director, Institute for Corporate Law and Corporate Governance

As moderator of the panel, **Brian McDonald** outlined how International Paper has been a tremendous success in Russia. It began operations in Russia in 1998 with a pulp and paper factory, and took a business that never made money and turned a profit in the first year. International Paper is now the market leader in office paper and liquid packaging boards in Russia and is a significant supplier to the European market.

progress. However, Mr. Vyugin believes this reduced risk has not been priced to the valuation of Russian assets. Dependent on the outcome of current global events, risk in Russia will continue to decline. He thinks perception will catch up with reality in 2002.

Russia's equity market has outperformed expectations and looks like a stable, emerging market. The same decline in risks is reflected in the debt market. We now see economic predictability, as the economy has recovered well from the 1998 crisis. President Putin is more active in managing politics and the economy. He has been supportive of Minister Gref's new reform plan. Further, he reacted quickly to the tragedy in the United States. His moves have shown that he would like the two countries to be closer economically and politically. Economic policies are now more consistent and have little political opposition.

Oleg Vyugin reported that Russia is an economy with declining risks. Improvements in the market environment and substantial political changes, including improvement in the overall management of the country and of corporations, have brought about this

Mr. Vyugin discussed several tables that reflected the recovery since the 1998 crisis, including data on GDP growth, the trade balance, fiscal balance, inflation, unemployment, and consumer confidence indices. He stressed that the outlook for 2002-03 is quite posi-

tive with sustainable economic growth on the horizon, assuming that oil prices will remain above \$20 per barrel.

However, investors in Russia still face general political risk. Russia still lacks an established civil society, forcing economic and political progress to depend on the motivations and behavior of its rulers, including incentives provided by President Putin. Fortunately, current management in the country is very proactive and is refraining from political games.

While oil, gas and the devaluation of the ruble saved the Russian economy, we now see that the Russian economy is capable of growing with lower oil prices and a stronger ruble. The 1998 crisis was followed by three stages of economic development: import substitution, an oil investment boom, the recent growth in household consumption and investment demand in all industries. This is the first year of widespread sectoral growth, due largely to strong motivation on the part of businesses. Their main goals include increasing the value of assets, volume of sales, and market share and consolidation. Current growth in industrial output and the future of the "new economy" are positive signs. Mr. Vyugin pointed to

further indices, including investment in fixed assets, disposable income, and retail and trade consumption as signs of the stable growth trend.



Troika Dialog Executive Vice President and Chief Economist Oleg Vyugin expounds on risk in the Russian economy.

He said, however, that the oil risk is real. Some attempt was made to simulate the sensitivity of the balance of payments and the budget to a drop in oil prices from \$23 to \$15 per barrel for two years. His conclusion is that the balance of payment problems would be evident, but not dramatic. The Central Bank would be obliged to finance the deficit or reduce international reserves. The Russian budget situation looks better because the government was able to collect \$7 billion in excess revenues. This could be used to finance a fiscal deficit in the future. The accumulated budget surplus will be equivalent to 2.7 percent of GDP or \$10 billion. All commitments of the budget, including debt commitments, will be covered without any problem. If oil prices remain at their current levels, Russia will have the ability to manage both macroeconomic stability and exchange-rate stability and still continue the policy of exchange-rate appreciation in real terms. All macroeconomic anchors will be in place. Therefore, he does not foresee any big problem for macroeconomic stability and economic growth.

Laza Kekic discussed FDI in Russia coming from European and U.S. companies. The background for FDI in Russia has been quite bleak. He concurs with the success story of Russia over the last two years as characterized by Mr. Vyugin. However, FDI is a notable absentee from this success story. Last year was a record year for

world FDI, measured at \$1.3 trillion. Russia only received about \$3 billion, or 0.2 percent, of world FDI. This is about five times less than Russia's share of world GDP.

Furthermore, there was negative net FDI in Russia in 2000, and a paltry \$1 billion went into Russia in the first half of 2001. The problems have been in both supply and demand. In regard to supply, investors are still taking a wait and see attitude. The demand side problems are due to the government's lack of commitment toward FDI, both nationally and regionally. The rate of FDI does not match Russia's aspirations. Output is still 30 percent below its value in 1989 — Russia needs much faster and more dynamic growth than 3 or 4 percent per year.

Most sources show that the United States is the main investor in Russia, with approximately \$5 billion in FDI stock. However, OECD data claim it is only \$1 billion. The mid-1990s saw U.S. investors buying into the Russian transition much more than the Europeans. Heavy support for Yeltsin and the reformers also bolstered U.S. investment. The reaction and backlash of 1998-99 disappointed expectations, especially in the United States. The relationship with Russia also extended further than the financial factors, with the NATO bombing of Yugoslavia serving as a prime example. Convincing head offices to establish a presence or expand in Russia became very difficult. Mr. Kekic said there has been a recovery in 2000-01, but it has not been broad.

Mr. Kekic said there is not any empirical evidence that U.S. investors respond differently than others to such problems as corruption and transparency. However, if it is true that U.S. companies are more sensitive to the overall political environment that surrounds relationships between countries, then the outlook is positive. If September 11 serves to redefine Russian ties with the West, then companies will feel more comfortable engaging in Russia. Furthermore, Russia may also improve its business environment and adopt policies more

favorable to direct investors. The EIU forecasts a doubling of FDI flows over the next few years.

Arthur George presented his views on the Russian tax system in relation to the investment climate. He said there are two primary tax-related costs to investing in Russia: the tax rates and the cost of administration and compliance with the system, which is a bigger unknown in the overall cost in terms of the overhead to hire people to administer the tax returns and records. Uncertainty and unpredictability make it difficult for businesses to plan.

However, there have been some significant developments this year. The costs have decreased compared to this time last year. Since January, the income tax dropped to 13 percent, which turned Russia into a low tax jurisdiction. Payroll taxes or social taxes, which stood at 38 percent of salary, have been combined into what is called a unified social tax, which now stands at 5 percent and is due to drop to 2 percent next year. There are now fewer turnover taxes and they decreased from 4 percent to 1 percent and will be completely eliminated in two years. Furthermore, capital construction expenses are allowed to offset VAT, whereas previously, companies had to amortize them.

In August, the profits tax part of the new tax code was passed, which reduced the basic tax rate to 24 percent. This now applies to all enterprises, eliminating prior distinctions. Furthermore, the problems with deductibility of expenses are diminishing. For example, advertising, recruiting, legal auditing, consulting,



Laza Kekic, Director for Central and Eastern Europe, Economist Intelligence Unit, discusses FDI in Russia coming from European and U.S. companies.



Arthur George, a partner at Baker & McKenzie, explains the Russian tax system in relation to the investment climate.

and business travel expenses are largely resolved. However, in order to deduct a training expense, the organization that conducts the training must now hold a government license. Further, the training must be related directly to the business at hand, which will create substantial administrative costs for the government. The profit tax reform also gives companies the option to apply straight-line depreciation or accelerated depreciation. This will go into effect on January 1, 2002.

With regard to predictability of the tax climate, there are a number of positive developments. First, the tax officials are more experienced. Second, the courts are more familiar with tax law, despite Russia's lack of a specialized tax court. Further, the courts are not afraid to rule against the government. Corruption in the Russian courts, Mr. George said, does not apply to cases involving the Russian government. Third, the burden of proof has shifted from the taxpayer to the tax authorities. There is some concern that the Ministry of Finance is reconsidering this development, after having a difficult time in the courts. Tax penalties were reduced from 100 percent of the undisclosed sum to just 20 percent. Property tax, state duties, sales tax, customs, technical corrections legislation, and transfer pricing rules are all matters that will soon be addressed by the Russian government.

Michael Leathes opened his discussion by explaining that intellectual property affects investment, not just in Russia, but in any country. Intellectual property regulations especially affect companies that

are research-based and rely on patents, as well as fast-moving consumer goods reliant on trademarks. All companies in the software business, for example, rely on copyright. Poor IP protection results in very low levels of investment because corporate assets are the sum of intellectual property. The challenge is to improve the IP norms and framework in order to improve investment opportunities.

British American Tobacco (BAT) is not just a foreign corporation, but also a local one. Its total investment exceeds \$300 million, and it owns three major plants in Russia. BAT is currently one of the largest trademark owners in Russia and the second-largest in the world behind Unilever. Yava, the brand leader in Russia, has suffered severely from counterfeiting. Even the tax stamps on the forged products are false. For every \$1 of profit made by BAT in the world, \$15 is contributed in taxes. Counterfeiting, therefore, is also costing the government in tax revenue.

BAT's goals are the four D's—detect, desist, destroy, and deter. BAT would like to see laws to detect who is responsible for the counterfeits, including the financiers. Laws also need to stop the process and allow the companies to destroy the infringing articles, thus hopefully deterring others from engaging in counterfeiting.

The Russian legal framework does help. However, the "detection" laws are lacking, and while the "desist" laws do exist, there are major obstacles in terms of process. There are no laws permitting the destruction of infringing articles, and proper punishments are also lagging. Mr. Leathes said there has been a major improvement in the attitudes of the authorities towards intellectual property, partly because major Russian brands have been counterfeited, and also because many in Russia have explained to the government that it is a major hindrance to inward FDI. Mr. Leathes complimented the work of the Coalition of Intellectual Property Rights, a multi-industry body supported by many firms. He said laws are in the Duma

right now that move in the direction of WTO/TRIPS standards.

Mr. Leathes suggested several legal improvements that could be made. First, companies should be given access to the document trail. Second, fast judgments are needed and must be properly enforceable. Third, the litigation process needs to be made less laborious. Fourth, infringing goods need to be destroyed, with only reference samples retained.

BAT has worked extensively with the authorities, shared intelligence with competitors and lobbied for new and better laws. The U.S. government has also been of major assistance in cracking down on foreign suppliers. Negotiations with Russian infringers have also been held. However, a credible environment for negotiations needs to be arranged with mediators present, and a greater understanding in Russia of the mediation process is also necessary. The CPR Institute for Dispute Resolution is conducting a major feasibility study on this subject in November. The help of the investment community abroad, Russian businesses and the judiciary will be a great aid. Real progress has been made, but much remains to be done. Significant value can be added to Russia's investment climate as the process of change unfolds.



Michael Leathes, Head of Intellectual Property at British American Tobacco, speaks about the effects of intellectual property infringements on investment.

Dmitry Vasiliev spoke of corporate governance and the questionable advice of investment analysts in Russia. For example, he said Troika Dialog did not find corporate governance risk in four companies that are strongly recommended by brokers.

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ANNUAL MEETING 2001 *Washington, DC ■ October 4-5, 2001*

PANEL RUSSIA IN THE GLOBAL ECONOMY

MODERATOR Roger Munnings
Managing Director, KPMG Russia and CIS

SPEAKERS Harry G. Broadman
Lead Economist, Russia, Europe and Central Asia Operations, The World Bank

Alexander Kiselev
Deputy Minister, Russian Ministry of Communications

Konstantin V. Vetrov
Chairman, Information Policy Committee, State Duma of the Russian Federation

Pawel Stelmaszczyk
Manager, Emerging Markets Government Policy, Intel Corporation

Gerson S. Sher
President and Executive Director, U.S. Civilian Research & Development Foundation



Roger Munnings, Managing Director, KPMG Russia and CIS, opens the panel discussion on "Russia in the Global Economy."

Roger Munnings, the panel moderator, opened the discussion by outlining KPMG's operations in Russia. The amount of the company's business in Russia in 2001 has surpassed even the peak it had reached in 1998.

The Putin Administration has been working with stamina and commitment on the economic infrastructure for the last year and a half. Russia, in turn, is becoming a more attractive place to invest. Mr. Munnings, however, added the normal caution to American businessmen. He empha-

sized the process of establishing the extent to which there is a unity of interest with investment partners.

Harry Broadman examined the issues surrounding Russia's WTO accession. He noted that all economies in transition consider membership in the WTO an important step toward integrating their economies into the international economic system. Although Russia has clearly come a long way in implementing various trade-related reforms, much more needs to be done.

The benefits of Russia's accession to the WTO are enormous both for Russia and its trading partners. For Russia, joining the global economy is crucial to its efforts to build an efficient market and to raise the country's long-term standard of living. WTO accession would also foster greater competition among enterprises, increase transparency, attract foreign investment, and reduce corruption. Another key benefit is guaranteed access to export markets. Conversely, a prosperous Russia within the WTO would be a major market for exporters worldwide.

Russian authorities have accomplished much with regard to Russia's WTO prospects. Tariffs and quotas have been lowered and offers on market access, services and further tariff reduction have been tabled with the Working Party in Geneva. Bilateral consultations, a major part of the WTO process, are in full swing and involve more than 50 countries. Furthermore, the Ministry of Economic Development and Trade has put together a program for the more than 50 laws that must be amended in order to make the legal and regulatory regime consistent with the WTO.

The scale of the structural reform agenda in Russia has also made the accession process more difficult. Some of this difficulty stems from an insufficient number of government officials who are trained in the technicalities of WTO processes. There is also interagency fighting and frequent conflict between central and regional government authorities when devising the various documents and offers that must be put on the table for accession. Other interest groups throughout the economy believe that they in fact have much to lose with WTO accession, particularly in the short term.

Mr. Broadman emphasizes that the support of the international community is essential for Russia's rapid accession to the WTO. Providing clear signals and strong support for Russia's reform efforts is necessary to ensure that the current momentum for structural reform in Russia is maintained. More important, it will help the Russian government resist the protectionist lobby that is beginning to form.

Asked what could be done by domestic organizations to overcome some of the entrenched interests, Mr. Broadman said he thinks they can facilitate the educational process, especially in cities outside Moscow and St. Petersburg. When many large economies begin to think about liberalization, people in the regions are not attuned to both the costs and benefits of such policy changes. This is why organizations such as the Eurasia Foundation that have tremendous networks throughout the regions of Russia can work further with NGOs and universities to get the message out that liberalization is positive.

Russian government had not yet formally approved the banking reform initiative. The question for Russia will be how much competition in the banking sector is beneficial to Russia. Mr. Broadman's advice to the government is to make the reforms consistent with the WTO standards now, rather than having to reform again later.

Alexander Kiselev discussed development trends in the communications sector and government support for its continued growth. Mr. Kiselev noted that the volume of telecommunications services grew by 34 percent during the first six months of 2001, and the volume of postal services and information services increased by 33 percent during the same period. Significant growth also occurred in Internet access services and mobile communications, signifying the development of the "new economy." In 1999, the number of Internet users increased 2.6 times and now amounts to 3.1 million people.

Looking ahead, Mr. Kiselev reported that the volumes in the IT and software markets are expected to nearly triple by 2005 and increase about six times by 2010. The information and communications sector will make up no less than seven percent of the economy by 2010. By 2005, the number of personal computers used in

business will increase six times and the number of Internet users in Russia will grow more than eight times. This expansion will allow a 40 percent reduction in access costs by 2005.

Information and telecommunications technologies fuel economic progress. They ensure significant growth in labor productivity, create new commodity and services markets, create stable demand, and drastically change

the functioning mechanisms of many institutions. In the majority of developed countries, the state of info-communications is an indicator of the quality of economic growth. In the United States, the contribution of this sector to the economy amounts to 4.4 percent of GDP. In Japan and Europe, it is 2.7 and 2.5 percent respectively, while the contribution of Russia's info-communications sector to its economy is less than 2 percent.

International documents, such as the Okinawa Charter on Global Information Society, recognize the important role of the state in promoting the development of info-communications. As a result of this and other developments, Mr. Kiselev explained that there has emerged in Russia an understanding of the need to develop a single program able to coordinate the activities of all levels of government. That program is called "E-Russia."

In July 2001, the Russian Parliament approved the legislation adopting "E-Russia." That bill identified the Ministry of Communications and Information as the program's coordinator, tasked with the following: to increase the efficiency and economic performance of the federal and regional governments; to develop civil society by securing the rights to free access to information; and to expand training in information technologies. Mr. Kiselev said the program would help in the following areas:

- improvement of regulatory activity in communications and information technologies;
- assurance of information transparency and effective interaction between the government and citizens;
- improvements in the activities of state power and local self-governance bodies;
- interaction of government bodies with the business community;
- education and human-resources development;

- supporting the development of independent mass media; and
- development of e-commerce.

Mr. Kiselev also outlined a draft law relating to licensing in the telecommunications sector, explaining that it significantly reduces the number of activities subject to licensing. Under the new law, licensing will only be necessary when chargeable services are provided. The areas still requiring licensing include:

- radio frequency spectrum usage;
- cable, wireline, radio, and TV broadcasting;
- transmitting voice information via data transmission networks;
- building and operating communications channels;
- crossing the borders of a subject of the Russian Federation;
- use by licensee or third party for providing free communication services; and
- carrying out the activities of the postal service.

In closing, Mr. Kiselev noted that both the Ministry of Economic Development and Trade and the Ministry of Anti-Monopoly Policy in Russia are working to reform state regulation of tariffs for telecommunications services.

Konstantin Vetrov talked about his committee's work in preparing the Russian environment for e-business. He explained that as the world becomes interdependent, information technologies become more important.

Mr. Vetrov believes that the top priority for Russia today is to expedite economic development while providing a certain level of economic and cultural conditions. These conditions include Russia's accession to the WTO and the adoption of new legislation bringing Russian law into compliance with international legislation.

The State Duma has many draft laws under consideration. One set of laws deals with business activities in Russia, which includes laws pertaining to mortgages, consumer loans, cooperatives, municipal companies, and humanitarian companies. Another package of laws deals with the protection of consumers' rights, and yet another focuses on the protection of individual entrepreneurs. Laws dealing with IT and e-commerce, including electronic signatures, electronic services and Internet payment networks will be finalized before the end of 2001.

Among the most important laws to the IT community are laws "On Electronic Signature" and "On E-Commerce." Both passed the first reading in the Duma this summer. Most important, he pointed out, these bills will assure that electronic signatures have the same legal force as paper signatures. In preparing these bills for the second reading, 140 amendments have been brought forward.

Preparation of the first reading of the federal law "On Personal Information" is now underway. Although the growing use of personal computers and the Internet in gathering personal data will make public life much more transparent, the government is sensitive to privacy and security concerns. Mr. Vetrov emphasized that as they proceed, the government will protect privacy based on generally accepted international principles and in conformity with the Constitution of the Russian Federation.

After briefly discussing e-government initiatives and legislative attempts to guarantee citizens access to public information, Mr. Vetrov discussed Russian efforts to join the WTO. When President Putin notified the Federal Assembly that he considers accession to the WTO a priority, the Ministry of Economic Development and Trade prepared a package of legislation to harmonize Russian laws with WTO requirements. The total number



Konstantin V. Vetrov, Chairman of the State Duma Information Policy Committee, addresses Council members.

of these laws is 55. Twenty-eight of them are related to the foundations of economic activities and operations. Nine bills deal with trade in commodities, and strive to protect Russian interests in foreign trade. Fourteen bills are legal acts regarding the exchange of services and the protection of the securities market. Three bills amend the current system of intellectual property protection, and the final one is aimed at improving regulation relating to government subsidies.

Pawel Stelmaszczyk offered a look at e-business from the perspective of the private sector, stressing that the global economy Russia is aspiring to join is digital and has no borders.

He then explained that Russia, like other emerging markets, could accelerate its integration into the global digital economy by focusing on five key areas. The first is connectivity. Are networks easy and affordable to access and use for the population-at-large? The second area is e-leadership. This simply asks whether e-readiness is a national priority. Third, information security depends on proper processing and storage of networked information and relies on a solid regulatory and legislative framework firmly in place. This includes the protection of intellectual property. Fourth is digital skills or the development of human capital. Are the right people available to support e-business and to build a knowledge-based society?



Harry Broadman, Lead Economist, Russia, Europe and Central Asia Operations, The World Bank, examines issues surrounding Russia's accession to the WTO, while (L-R) Alexander Kiselev and Konstantin Vetrov listen.

When asked what he considered to be the most important and challenging areas where legal reform is needed in order for Russia to get through this process, Mr. Broadman said the services sector would be particularly tricky, including telecommunications, legal services, accounting, and the natural-monopoly sectors.

Asked about the banking reform initiatives in relation to the WTO accession process, Mr. Broadman said that the

The fifth area is transferability. Are other sectors in place to make use of e-business? Focusing on these five areas is essential to attract investment, because investment dollars increasingly flow to markets with skilled labor, modern infrastructure, flexible labor regulations, and a predictable and enforceable regulatory framework.

would most assuredly speed integration into the global economy.

Gerson Sher talked about industrial research and development in Russia. The U.S. Civilian Research and Development Foundation (CRDF) was created in 1995 by the National Science Foundation pursuant to an act of Congress. CRDF is a private, nonprofit organization that helps sustain Russia's internal science capability by fostering scientific cooperation with the United States. It provides productive alternatives to emigration for Russian scientists. Second, it promotes U.S. policies on non-proliferation of weapons and technologies related to mass destruction. The program helps transfer scientists from the production of chemical, biological and nuclear weapons into civilian scientific research. Third, CRDF promotes industrial

cooperation in applied and pre-commercial research between U.S. companies and scientists and engineers in the former Soviet Union.

Mr. Sher echoed earlier remarks that Russia's greatest resource is its people, not what is in the ground or what grows on the ground. Russia was the greatest scientific community in the world until 1991. The people are still there, and the educational system remains strong. However, the infrastructure needs development. How to adequately address this community and collaborate with it continues to be a challenge. The primary instrument

CRDF uses is research grants on a fairly small scale (\$50,000-\$100,000) for pre-commercial research projects. These grants are made available for both pure and applied research.

A program called "Next Steps to the Market" uses cooperative research to pair industrial companies in the United States with scientists and engineers in the former Soviet Union. Once the partners come together, they must write a proposal that is scientifically competitive and has a good business plan. Trust is a primary element — this was a major issue in the early 1990s when businesses entered the former Soviet Union to tap cheap labor. A perception arose that U.S. companies were trying to steal Russian technology. As a result, part of the problem of developing an intellectual property regime is overcoming the paternalism and protectionism the Russian government has adopted.

Cooperation starts at an individual level. In technology cooperation, there are two models: "technology push" and "market pull." Technology cooperation is not accomplished by putting a database out and hoping people will find it. You must take skills and go directly to a company. CRDF has developed a number of different techniques to accomplish this. Sending talent to conferences and forums where company representatives are present is an effective way to market skills. A focus on skills over technologies is necessary — disembodied technology rarely takes precedence over skilled people, and Russia is full of skilled people. ■



Gerson S. Sher, President and Executive Director of the U.S. Civilian Research & Development Foundation, explains programs for fostering cooperation between Russian scientists and U.S. companies.

Mr. Stelmaszczyk also spoke about the "four pillars" of integration as defined by the European Commission to integrate EU countries into the "pan-European information society." First, if countries want to be integrated with the EU, they must implement the basic building block of the information society: affordable communications services. Second, Internet access must be cheap, fast and secure. Third, countries must invest in people and skills. And finally, they must stimulate the general use of the Internet. Mr. Stelmaszczyk said that Russian acceptance of these principles

ANNUAL MEETING 2001 *Washington, DC ■ October 4-5, 2001*

PANEL BUSINESS ROUNDTABLE DISCUSSION

MODERATOR	Margaret M. Richardson <i>Partner, Ernst & Young L.L.P.</i>	
SPEAKERS	David J. Herman <i>Vice President, General Motors RNS</i>	Anatoly Karachinsky <i>President, IBS Group of Companies</i>
	Vladimir Kadannikov <i>Chairman, AvtoVAZ</i>	Michel Tchesnakoff <i>President and CEO, ABB Russia Ltd.</i>
	Scott Nicol <i>President and CEO, ClearWater</i>	

Margaret Richardson: *On June 27, General Motors signed an agreement with Russia's largest automobile manufacturer, AvtoVAZ, and the European Bank for Reconstruction and Development (EBRD) to create a joint venture that will produce sport-utility vehicles in Russia. How did GM choose AvtoVAZ as its Russian partner? How and why did the EBRD get involved? What were the main obstacles to this project?*



(L-R) Roundtable moderator Peggy Richardson, Partner, Ernst & Young L.L.P.; Vladimir Kadannikov, Chairman, AvtoVAZ; and David J. Herman, Vice President, General Motors RNS.

David Herman: The Russian automobile market is one of the few markets in the world that is actually going to grow faster than the total world market. Obviously, anybody who wants to be a leader in the automotive market has to establish a significant presence in Russia. Today, there are virtually no foreign automotive ventures in Russia, and those that do exist produce so few

vehicles that they are in trouble — GM was among them. The new venture will produce 75,000 vehicles annually — such volume allows us to get a reasonable cost structure. And the most important, this vehicle will be exportable.

The participation of the EBRD is very important. This is the largest EBRD project in the region if one includes the \$100 million of loans they provide in addition to the \$40 million in equity.

Having EBRD as a partner helped us to address some country risk problems. The EBRD is equally delighted to participate in the project, especially because the supplier industry that has to follow will also require funding in the future. Their most important reason for participating was the complex nature of the contacts that will be created

between AvtoVAZ and GM with its European subsidiaries.

In terms of the difficulties, we faced some problems associated with country risk. The EBRD has had two large investments in Russia that have been unsuccessful — Kamariver Truck Company and GAZ — and these experiences made them very cautious

about another project in Russia. On our side, we spent a lot of time preparing for the investment and insuring it against any potential third party that might not like to see us succeed.

I believe that we will succeed. We have started building a plant, and next September you will be able to buy a new Chevro-Niva in Moscow.

Ms. Richardson: *Mr. Kadannikov, how has this joint venture changed the culture of AvtoVAZ?*

Vladimir Kadannikov: AvtoVAZ is an open joint-stock company with a state share of only two percent. More than 30 percent of our shares are owned by individuals. We produce 750,000 passenger cars annually, which represents approximately 80 percent of the Russian market. We utilize 100 percent of our production capacity, compared to the current average level of 83 percent for the leading U.S. automobile manufacturers.

In preparation for the joint venture with GM, we went through a long transformation from a state company with production limits and controlled distribution of cars to a joint-stock company that operates according to market-based principles.

Ms. Richardson: *Mr. Karachinsky, tell us about the information technology*

(IT) business in Russia and what the future holds. If there is someone in the audience who wants to get into the IT business, what advice would you offer?

Another important thing that helped the IT industry in Russia was the appearance of a political leader who was thinking about strategic priorities



Roundtable participants (L-R) Scott Nicol, President and CEO of ClearWater; Margaret M. Richardson, Partner, Ernst & Young L.L.P.; Vladimir Kadannikov, Chairman of AvtoVAZ; David J. Herman, Vice President of General Motors RNS; Anatoly Karachinsky, President of IBS Group of Companies; and Michel Tchesnakoff, President and CEO of ABB Russia Ltd.

Anatoly Karachinsky: Major changes are happening in the IT market in Russia. First of all, this is related to the fact that the market model in Russia is changing. Until recently, the market model was based on the power of some players to control monetary flows. Within this model, information technologies were not needed, because IT instruments are only useful for managing transparent businesses.

There was a significant breakthrough after 1997, related partially to the development of the securities market in Russia. Here is one instructive example. Surgutneftegas company is a Russian oil company with older oil fields and relatively high costs of production. By 1999, the company cost approximately \$13 billion, while a huge company like Gazprom cost \$3 billion, and other oil companies cost even less.

This example was a signal to Russian managers that the old model of management through the control of monetary flows no longer worked. Moreover, many Russian companies realized that transparency and usage of the latest information technologies would bring them tens of billions of dollars in market capitalization. This was a tremendous push for our industry. Now the Russian IT industry is experiencing very strong growth — up to 100 percent in some segments.

for the country and the importance of information technologies. This person was Minister of Economic Development and Trade German Gref.

New people in political power realized that Russia has two strategic resources. First, as everyone knows, are natural resources. Russian natural resources have been developing for many years. And today, Russia is very dependent on oil and gas prices. The cyclical nature of oil and gas markets forces constant revisions to the nation's budget and requires the creation of a scenario for when oil prices decrease.

Our second strategic resource, sometimes forgotten, is a highly educated population. However, Russia does not know how to make money from this second strategic resource because we have never tried it before. When Russia began its transition to a market economy, this unique resource was forgotten. We are trying to persuade our government that we can use this resource. Examples of other countries' success with information technology supports our point. For example, in 10 years, India went from zero to eight billion dollars in software exports.

Currently, Russia's export of oil is only \$36 billion. Seventy-five cents of each dollar that Russia earns on oil trading goes toward the maintenance of oil wells and pipelines, while our people live in unlivable conditions. At the same time,

80 cents of each dollar earned on software development goes back to those who write the software — i.e., directly into the economy. It has become apparent that it is much more strategically important to develop the second resource in Russia. Therefore, it is a very good time for the IT industry in Russia. The country is changing, and the understanding of the future is changing.

Ms. Richardson: *Mr. Nicol, tell us about your experiences with establishing small business operations in Russia. How would you characterize the difficulties faced by SMEs today in Russia? Are licensing/regulations or financing the main obstacles to growth?*

Scott Nicol: We started off in 1993, and the markets have changed considerably since then. Over the last two days, I think everyone has heard a lot about the human resources and human capital in Russia. In our business, we take that to heart. If you are going to start a business today in Russia, look at the people first and work to train them. At ClearWater, we actively do that. We have training programs for our staff weekly and regularly send Russian employees abroad for training. In my opinion, such an approach is the recipe for establishing a successful business in Russia from the ground up.



David Herman (left) listens to Anatoly Karachinsky.

Complying with numerous and complicated licenses and regulations in Russia has always been a very big challenge, but just like everybody else we have to comply and deal with this issue. That being said, financing is a different issue. In my opinion, the biggest obstacle for businesses in Russia

is access to reasonably priced capital.

When ClearWater entered the Russian market, we had very good margins and favorable cash flows, which allowed us to sustain growth. Today, newcomers need some initial financial resources to get started. A small business in Russia has very few avenues to access capital, and the available capital is very expensive. Russia needs something similar to the Small Business Administration (SBA) to address this problem.



Scott Nicol gets a laugh from Peggy Richardson.

Ms. Richardson: *Mr. Tchesnakoff has spent a number of years in the banking sector. Could you tell us how the banking business is doing in Russia, and about ABB's experience with financing?*

Michel Tchesnakoff: Today the main problems of the banking sector in Russia are related to the lack of confidence from customers and poor quality of provided services. Today, businesses can be serviced easily by foreign banks in Moscow, less so in St. Petersburg, but are left with local, poorly capitalized banks outside of these two cities. Sberbank, a big machine, exists for those outside the major cities, with service that needs to be improved, to say the least.

As far as financing is concerned, I think a lot has already been said this morning about the difficulty of obtaining credit. Even ABB's biggest customers — large exporting companies — finance their operations with their own resources. Fortunately, they have been profitable in 1999 and even more so in 2000. However, if they continue to finance their development from their own resources, we will not see the kind

of growth in the economy that we have seen the past few years.

Ms. Richardson: *Do you have any advice about what it takes to be a successful direct foreign investor in Russia?*

Mr. Tchesnakoff: It is very important for a newcomer to identify its customer or determine whom they want to have as a customer in future. ABB went into Russia on a major scale in 1992. Obviously, our customers in 1992 were different from our customers now, and they will also be very different in 2005. Then we decided that because we sell electrical equipment, our customers would be 89 Russian utilities. We expected that their needs for transformers would be fantastic because any kind of utility uses transformers. However, we have never been able to sell a single transformer in Russia. There are plenty of

old malfunctioning transformers in Russia, but most of the utilities have their own huge service organizations that repair old transformers. This is very inefficient, but such practices are still taking place, because shuttering service centers would result in a significant increase in unemployment.

Due to the absence of any demand for transformers in Russia, ABB redirected its sales efforts to other clients. As consumption of electricity in Russia was growing, protection of transformers with bushings has become very important. Today, the company's market share of bushings is over 70 percent. About 15 utilities are buying ABB bushings exclusively. This is a good example of why you should get to know your customer in a new market and understand how businesses operate there. Otherwise, you could miss opportunities by targeting the wrong customers.

Ms. Richardson: *To all — what government measures, both administrative and legislative, have been implemented in the last year that have directly benefited your company? How do you expect the new Profits Tax will impact your company?*

Mr. Nicol: For us, the most important measure was the introduction of a flat income tax on individuals, as well as changes in social taxes. Additionally, some simplification of local licensing procedures made our life easier.

Mr. Kadannikov: I was trying to pick my brain to try and remember what the state did for us, but unfortunately, despite my efforts, I am not able to recall anything that was done to our benefit.

Mr. Herman: I have to talk about the future implications because we are not in business yet. The Profits Tax reduction to 24 percent will help us to conduct business. Tax reform, in general, has been very beneficial for us.

In terms of licensing and registration procedures, there has not been much improvement, and there is a long way to go before a normal regime will be in place. So, I would say Vladimir is right in his wisdom. But let us hope for better results in the future.



(L-R) Anatoly Karachinsky and Michel Tchesnakoff.

Mr. Karachinsky: I would like to join Scott. In our business, 70 percent of our costs account for salaries, so we are very sensitive to all changes in taxes related to employee compensation. That is why, to us, the introduction of a flat 13 percent income tax was a great step forward. This is a first step in reorganizing the Russian system of individual taxation that used to be meaningless and unreasoned. The remaining significant burden for Russian businesses is a social tax, which has to be paid by the company and represents indirect taxation of employees. This burden makes many companies look for all possible ways to avoid paying the social tax.



Vladimir Kadannikov, Chairman of AvtoVAZ, (second from right) amuses his fellow roundtable participants (L-R) Scott Nicol, Peggy Richardson and David Herman.

They simply cannot afford to pay it.

What prevents Russia from having a 40 percent growth rate annually? In my opinion, — which is also affirmed by a 1998 McKinsey report — the main reason is an absence of equal standing among businesses in Russia. If your company is paying all the taxes, while your competitor is hiding its revenues and successfully avoiding taxes, you simply are losing your competitive edge. And the Russian government is finally looking at the ways to resolve this important problem. Of course, this will take some time, but the intention is very inspiring.

Mr. Tchesnakoff: I can only agree with my colleagues. The steps that have been taken in developing an equal playing field for businesses are encouraging. Although this is a long-term process, it will require a lot of work during the next few years. The next step is the implementation of the new laws — because everybody knows that there are a lot of good laws in Russia that are not being implemented.

The next challenge, which was addressed this morning by Russian executives, is de-bureaucratization of Russia and reduction of the number of licensing requirements. When Mr. Kudrin said today that the number of licenses one has to obtain in order to work in Russia was decreased to 70, I saw people in the audience smiling. However, one must keep in mind that such a reduction is big progress in comparison with 300 licenses that were required before. Of course, 70 is still

a lot. This is certainly a challenge for the next few years, but at least we can say that the Russian government is going in the right direction.

Audience: *I have a question for Mr. Herman and Mr. Kadannikov about the state of consumer loans for automobiles in Russia. What are some of the main obstacles that prevent it from being a mass market?*

Mr. Kadannikov: Today in Russia, it is still practically impossible for an automotive company to take out a loan. The refinancing rate for long-term loans is about 25 percent annually. No single automobile industry in the world can be so profitable. The maximum profitability that we can achieve on new projects is 12 percent annually, which is relatively high for the auto industry. Short-term loans are cheaper — approximately 18 percent annually — but even this price is too high for our industry. AvtoVAZ uses short-term financing occasionally, but only if we have to pay wages or purchase certain products that we need immediately.

The same situation exists in the consumer car loan market in Russia. AvtoVAZ is making its very first steps in providing car loans to its customers. In St. Petersburg, we are launching a car loan program through our dealers, who were able to attract a few commercial banks interested in working with us. These banks will offer car loans with terms that are not great, but acceptable. I am hopeful that this program will grow and the terms will improve, since more and

more banks in Russia have become interested in providing consumer loans.

Mr. Herman: I would like to add that the inflation rate is a very important factor in the development of the auto industry. For example, in Central Europe in the mid-1990s when inflation got down to 15 percent, a big business “explosion” happened — OpelCredit Bank, Ford Motor Credit and others were establishing operations.

There are some legal issues that have to be addressed — for example, enforceability of chattel mortgages. Can you imagine going out and repossessing cars in Russia? Having said that, I believe the inflation rate is the main issue.

Audience: *Can you describe the status and the role of unions and labor relations at AvtoVAZ?*

Mr. Kadannikov: At AvtoVAZ, we have not one, but two labor unions. Every year, the management concludes a labor contract with each of them and then strictly observes it.

Our company’s expenditures for social needs are tremendous. As you may know, AvtoVAZ was built 30 years ago in an empty field, and the city of Togliatti was created around our plant. AvtoVAZ built all the infrastructure in the city, and we can not just abandon it. About 110,000 AvtoVAZ employees live in Togliatti. Can you imagine this number of people without social support? Therefore, our expenses for social needs and implementation of the labor contracts remain very high.

In addition to our two unions, we have a “production board,” which was once required by Russian law, but some time ago such mandates were declared null and void. However, we decided to keep our production board because we believe that the participation of workers in managing the company is very important.

Mr. Herman: I would like to add that I would be happy if GM’s labor relations were as good as AvtoVAZ’s. ■

PRESIDENT PUTIN COMES TO WASHINGTON ■ November 13, 2001

On November 13th, during the Bush-Putin Summit in Washington, the Council co-hosted a dinner in President Putin’s honor at the Russian Embassy for several hundred U.S. and Russian officials, business executives, media representatives, and prominent members of the broader policy community. Following is the text of the President Putin’s remarks. (Full coverage of the Washington-Crawford Summit, including all joint statements and other background documents, can be found on the Council’s website, www.usrbc.org.)

Good afternoon, ladies and gentlemen, dear friends. It gives me great pleasure to see and welcome all of you on Russian soil. The Ambassador proudly told me just now that this ballroom is the pride of our embassy. No other embassy in Washington can boast such a room. This ballroom has never hosted such a dignified audience, and we are very proud to see you here. I would like to thank you all for coming here, for having abandoned your important business in order to meet with us.

“...TODAY WE HAVE A FAVORABLE MOMENT TO FULLY CAPITALIZE ON THE ENORMOUS POTENTIAL FOR COOPERATION BETWEEN RUSSIA AND THE UNITED STATES IN THE SETTLEMENT OF REGIONAL CONFLICTS.”

I remember very well our first meeting with President Bush in Ljubljana. We were nervous, and that was quite natural. But most importantly, we were ready for a dialogue, and that dialogue did materialize. An important discussion materialized both for us personally and for our countries. We said that the Cold War had been left in the past and our countries were no longer enemies. We said that the very nature of our relations was changing and that they rest upon common interests, common values and mutual respect for each other.

But let us be frank. In Ljubljana, there were just intentions. We thought we had a lot of time to deliberate and to make decisions. We did not know at that time what the United States would have to endure, what we all would have to endure.

Two months have passed since the appalling terrorist acts in New York and Washington, but all of us, including myself, still have in our mind’s eye the footage of that tragedy. Terrible acts of evil have been committed against each of us and all mankind. And as it always has been in the history of humankind, the greater the scope of a tragedy, the stronger the human solidarity and readiness to help, the greater the heroism and courage of the people who happened to be at the very center of the tragic events.

I am proud that among those heroes were Russian citizens and our former fellow countrymen. I am proud of Evgeny Knyazev, an engineer of Russian descent who rescued almost 70 people from the building and died later in the debris. Words of special gratitude go to the Russian journalist Yuri Kirilchenko, who helped rescue people from the World Trade Center. And he did so until he collapsed from a massive heart attack. We will not forget the victims of these terrorist acts, and we should protect the ones whose lives are still threatened by terrorism.

Today we know that no country or nation in the world is secure against this threat. Russia was one of the first countries to experience the onslaught of modern terrorism. We have fought against it on our own. And today a wide coalition of countries has formed, ready to counter this threat.

Terrorists hoped to intimidate us, to take advantage of differences between the countries, and eventually split the world community. But what they achieved instead was the consolidation of world opinion; I would say a solidari-

ty unheard of in recent history. Their hopes that our desire for revenge would make us use the same brutal methods did not come to pass.



President Putin addressing the diverse audience at the Russian Embassy.

For us, there are no enemies except terrorists themselves. They tried to force a wedge between the Christian and the Muslim communities and to instigate a clash between civilizations. But they failed again, and today all countries of the Islamic world condemn terrorism. Our common enemy has no nationality, no religion and no civilization. For Russia, this is evident from the unique experience in our history of centuries of harmony and coexistence of Christian and Islamic cultures. In light of that experience, we can say that there is no more urgent task than to unite in the fight against terrorism. First of all, we will need common efforts of the law enforcement and customs authorities, financial institutions and special forces, as well as coordination of information policies. To this end, an entirely new level of interaction between leading powers is necessary. What we need is a fully-fledged, constantly functioning alliance.

Ladies and gentlemen, the key role in strengthening the unity of the world community today belongs to the United Nations. This organization is and will remain what we, members of this organization, want it to be. First of all, it is important to ensure strict adherence by all countries to the U.N. Security Council's resolutions, especially those posing a detriment to the material resources and infrastructure of terrorism. We propose to elaborate and adopt a comprehensive convention for fighting terrorism and an international convention for fighting nuclear terrorism. And finally, all countries should accede to the already-existing international treaties on the fight against terrorism and bring their national legislation in compliance with those agreements.

I am confident we will be able to create a worldwide atmosphere of total rejection of terrorism. However, we will only be able to succeed if the international network of terrorism is countered by an international community of law and justice.

vast financial flows. That is why we welcome and support the current efforts within the United Nations, within the G-8 and other fora, with the purpose of combating poverty, the poverty that often drives people to crime.

Dear friends, it is of primary importance to ensure that our countries' interaction in the fight against terrorism does not remain just an episode in the history of the Russian-American relations, but that it marks the beginning of long-term partnership and cooperation. Today we should take another look at the history of our relations. History, as our famous Russian thinker and historian Vladimir Klyuchevskiy once said, is not so much a teacher as a disciplinarian. It does not teach you anything, but only punishes you for not knowing the lessons.

After the Second World War, the relations between our two countries have gone through different stages.

Nevertheless, we have eventually achieved the main goal: our countries have stopped being afraid of each other. This has opened up an opportunity to jointly free ourselves from what has been horrifying the people of the entire world for decades – the arsenals of nuclear and other weapons of mass destruction. Their present quantitative level is absolutely inconsistent with either the current situation in the world or the nature of the

current threats. I had no doubt that we would reach an understanding in the United States on this issue, and today's statement by President Bush is a confirmation of this.

That is why Russia declares and reiterates its readiness to make considerable reductions in strategic arms. That is why today we propose a radical program of further reductions of strategic

offensive arms by at least three times, to a minimal level necessary for maintaining strategic balance in the world. We no longer have to intimidate each other to reach agreements. Security is not created by weapons – it is created by the political will of people, nations and their leaders.

Today unfortunately, the world is far from having international relations be based solely on trust. That is why it is so important to rely on the existing foundation of treaties and agreements in the arms control and disarmament areas.

"... AT DRAMATIC TURNING POINTS IN HISTORY, IN THE MOMENTS OF TRUTH, WHEN THE VERY EXISTENCE OF OUR NATIONS WAS AT STAKE, RUSSIA AND THE UNITED STATES HAVE ALWAYS STOOD TOGETHER."

I also believe that today we have a favorable moment to fully capitalize on the enormous potential for cooperation between Russia and the United States in the settlement of regional conflicts. One of the manifestations of this potential is the joint participation of Russia and the United States in the efforts to find solutions to the Middle East crisis. Now, such cooperation is critically important for reaching a just and lasting intra-Afghan settlement. I am convinced, in the face of common threats and challenges, co-sponsorship in regional issues must become the predominant formula of Russian-American relations.

We must also understand what model of security is the most productive for the European continent. Here we need to work hard together with our European partners. There is a need for a new level of cooperation that would allow us to jointly make decisions.

As regards the relationship between Russia and NATO, we intend to move toward the development of an equal partnership with this organization, to go as far — and I would like to stress this — as far as the Atlantic alliance itself is ready to go, and to the extent

that it is capable of taking into account the national interests of Russia.

Ladies and gentlemen, today Russia is a rapidly changing country that has made its irreversible historic choice. The problems we are now solving in finding pathways to form a mature democratic state with a modern economy are testimony to this. Russia today is a country whose integration in the commonwealth of free democratic nations is irreversible.

The fortunes of our nations are different. For many years they had been moving along different paths. But if we look back at more than two centuries of our relations, one thing would strike you: at dramatic turning points in history, in the moments of truth, when the

very existence of our nations was at stake, Russia and the United States have always stood together.

They were together at the dawn of American independence. Let us remember when the Russian Empress Catherine II politely but resolutely denied the request of King George III to send Russian soldiers to participate in the suppression of the uprisings in the American colonies.

Our nations were together during the time of liberation reforms in both countries in the middle of 19th century — this period coincided with the Civil War in the United States. It is symbolic that the two great statesmen, Emperor Alexander II and President Abraham Lincoln, abolished slavery in their

countries at approximately the same time. And both fell victims at the hands of terrorists.

It is also symbolic that Russia made its own financial contribution to the creation of the Statue of Liberty, which now rises above New York and is a symbol of freedom for the entire world. Finally, our peoples were together during the Second World War.

I am sure that now, when our destiny meets history again, we will be not only partners, but also friends. We must act vigorously — just like one famous Jack London character said that time does not wait for men. Thank you very much for your attention. ■

...continued from page 38

Mr. Vasiliev found these same companies participating in asset stripping, transfer pricing and illegal charter provisions, with no monitoring by independent directors or minority shareholders. He said there is a serious lack of in-depth, legal analysis by brokerage firms. The Institute for Corporate Law and Corporate Governance measures these risks.



Dmitry V. Vasiliev, Executive Director, Institute for Corporate Law and Corporate Governance, speaks about corporate governance and the status of top Russian companies.

Mr. Vasiliev discussed the updated ratings by his organization, with 25 companies accounting for 90 percent of market capitalization were shown in a table. There are huge gaps between the best-governed companies and the worst, and the differences are growing.

He then discussed changes in corporate behavior. The good news is that there is real improvement in information disclosure and transparency. The bad news is that there are more companies with unequal treatment of shareholders in their charters. Second, there are more companies with unlawful rights of managers. Again, he believes that this is owing to the lack of attention by brokerage firms and investors to the legal problems of companies.

Sibneft and UES have seen significant improvements in corporate governance. Sibneft has voided the authorized but unissued shares in their charter, which

posed a significant risk of dilution. Another positive development is that minority shareholders are also present. UES has launched a restructuring program including minority shareholder representatives and now has more control over their Board in the charter. Another positive development is that Gazprom has voided the provision disallowing the replacement of its General Director by the Board.

Irkutskenergo and Uralsvyazinform have significantly fallen in their corporate governance ratings. There are very low levels of transparency within these companies. In addition, there are no minority shareholders represented on the Board. Third, their charters evidence more risk of capital dilution.

Overall, Mr. Vasiliev said the main risk for investors in Russia has been and still is related to the issues of corporate governance, a risk that can be reduced through due diligence. ■



Council President Gene Lawson exchanges a few words with President Putin.

Moreover, we need to pay special attention to the socioeconomic roots of these new challenges including the gap between rich and poor, both domestically and globally. After all, if an Afghan peasant has nothing to live on but the pennies he gets from the opium dealer, this means that terrorists and criminals of all kinds will continue to manipulate

NEW MEMBER PROFILES



The American-Russian Chamber of Commerce & Industry (ARCCI), a nonprofit membership organization, was established in 1992 in Chicago. In 1995, the ARCCI founded its sister organization, the American-Eurasian Chamber of Commerce. In 2001, to facilitate networking with the U.S. Administration and Congress, the ARCCI opened a satellite office in Washington, DC.

Through its activities and services, the ARCCI provides essential information and practical assistance to members interested in trade and investment in Russia and the New Independent States of the former Soviet Union. By organizing high-level conferences, briefings, seminars and delegation exchanges, the ARCCI brings together leading figures from government, the business community and the media.



Argus Limited, a member of the International Pipe Line and Offshore Contractors Association (IPLOCA) and the American Welding Society, was founded in 1981 by executives with extensive working experience in the oil and gas industry in the former Soviet Union. Argus Limited is headquartered in Rockville, Maryland. The company also has offices in Russia, Kazakhstan, Uzbekistan, and Great Britain, and maintains warehouse facilities with a partner company in Baku.

As an engineering and marketing company, Argus offers an all-in-one solution to organizations involved in building, maintaining and rehabilitating pipelines and various reservoirs. The company's highly qualified staff provide technical advice, help select equipment and materials, prepare commercial proposals, organize training in the use of new technologies, and provide warranty and post-warranty service of equipment supplied under contract.



The Center for Russian Leadership at the Library of Congress operates the Open World Program (formerly known as the Russian Leadership Program), an exchange created in 1999 that brings young Russian civic and political leaders to communities across the United States on short-term working visits.

The purpose of the Open World Program is to expose Russian decision-makers to the people, institutions, and practices that make American-style democracy and free enterprise work. The program's nearly 4,000 alumni have come from 87 of Russia's 89 regions, including nearly 150 members of the Russian Federal Assembly who have taken part in Open World's special parliamentary program, and 169 judges who have participated in its rule of law programming.

First proposed by Librarian of Congress James H. Billington, a noted Russia scholar, Open World receives financial and programmatic support from the U.S. Congress.



Founded in 1998, **Eurasia Group** is a research and consulting firm with offices in New York, Washington and London. Building on a unique network of more than 450 experts, Eurasia Group prepares custom-tailored research as well as multi-client studies and regular flagship publications that address current political developments and their bearing on business in the Eurasian region.

Eurasia Group also features a full line of U.S.- and London-based seminars and briefings, as well as frequent executive visits to countries in the region. These programs are designed to allow clients to conduct a direct dialogue with top government officials and business leaders and receive in-depth analysis from Eurasia Group experts.

In 2000, Eurasia Group joined forces with Lehman Brothers to create the first qualitative comparative political and economic index designed specifically to measure stability in emerging markets. Developed over a two-year period by experts in transitional politics and economics, the joint venture produces a monthly Lehman Eurasia Group Stability Index (LESGI) and accompanying country reports. The LEGSI provides an "early warning" system that helps anticipate critical trends and provides a measure for country capacity to withstand political, economic, security, and social shocks.



KPMG Advisers, Ltd. is a global network of professional service firms that provide assurance, tax and legal, financial advisory and consulting services. In Russia and CIS countries, more than 1,000 professionals collaborate across industry sectors and national boundaries to deliver services designed to meet specific complex needs of clients.

Marks & Sokolov is an international law firm with offices in Philadelphia and Moscow. The company focuses on commercial litigation and corporate matters, handling litigation and arbitrations in the United States, Russia, Sweden, Switzerland, Cyprus, and other countries throughout the world. The firm's clients range from large global organizations to individual businesspersons. Litigation services provided include contract, commercial fraud, securities fraud, bankruptcy, maritime, RICO, lender liability, real estate, construction, civil rights, and professional malpractice. Corporate services include general corporate matters, banking and finance, construction, real estate, and intellectual property.

The firm has a special focus on representing Western companies doing business in Russia and Russian companies doing business internationally. It also provides expert legal opinions on Russian and American law for law firms throughout the world. Marks & Sokolov's attorneys are qualified to practice in both the United States and Russia. Many of the firm's attorneys and paralegals are fluent in English and Russian, as well as other languages.

The experience of its leading attorneys in the U.S. and Russia allows the firm to offer clients premier services that adhere to the highest ethical standards.

Created in 1993, **MDM Bank** has gradually developed into one of Russia's leading financial institutions, offering customers a broad range of commercial and investment banking services. At the end of 2000, MDM was one of the five largest banks in Russia as measured by IAS Capital. Corporate banking is MDM's largest business, accounting for approximately two-thirds of revenues. MDM's customers include approximately 40 of Russia's top 100 companies.

MDM is one of Russia's leading clearing institutions, with daily international settlements of approximately \$60 million. It has total credit facilities of over \$100 million from more than 30 foreign banks, and has been accredited or accepted for individual transactions by several leading European and North American export credit agencies (ECAs). The bank is focusing on developing its international trade finance, ECA and multilateral-backed financing, as well as loan syndication services.



M.E.C. Technology, Inc., formed in 1987, specializes in product design with such clients as American Red Cross (blood transfer equipment), Ford Motor Company and New York Telephone Company. M.E.C.'s primary concentration is the semiconductor business.

M.E.C. plans to establish a joint venture that will transfer Russian technology to a viable worldwide marketplace using its technology, manufacturing talent and resources. It also hopes to modernize Russian semiconductor manufacturing facilities, enabling them to become competitive entities within the current marketplace, and removing their current dependency upon foreign integrated circuit suppliers.



Founded in 1975, **Microsoft Corporation** is the worldwide leader in software, services and Internet technologies for personal and business computing. The company offers a wide range of products and services designed to empower and enrich people in the workplace, at school and at home. Microsoft® products, available in more than 30 languages (including Russian), are sold in more than 50 countries.

In November 1992, Microsoft Corporation opened up its CIS subsidiary (located in Moscow). The goal of the CIS subsidiary is market development in the territory of the former Soviet Union, and localization and deployment of the leading products and technologies.



The Nuclear Threat Initiative (NTI) is a charitable organization working to reduce the risk of use and prevent the spread of nuclear, biological and chemical weapons. Co-chaired by Ted Turner and Senator Sam Nunn, NTI has brought together international experts with different views and experience who share a common goal of taking immediate action to close the gap between the global threat from weapons of mass destruction and the response. NTI seeks to increase public awareness, serve as a catalyst for new thinking and take direct action to reduce these threats. NTI is strengthening global security through model programs to inspire private and governmental efforts toward threat reduction.

NTI is funded by Mr. Turner's pledge of at least \$250 million over five years. In addition to Mr. Turner and Senator Nunn, NTI is guided by an international board of directors that includes Russian Duma Member Andrei Kokoshin.



The Russian American Nuclear Security Advisory Council

(RANSAC) was founded in 1997 for the purpose of developing new U.S.-Russian cooperative nuclear security initiatives, and ensuring the timely and effective implementation of existing programs. The council consists of members drawn from both Russian and American institutions who possess significant experience in policy and technical fields, and who have first-hand knowledge of the substance and implementation of cooperative nuclear security programs.

RANSAC works with government officials in the United States, Russia, and Europe, produces and disseminates reports, and interacts with academic institutes, nongovernmental organizations, and the media around the world.



Renova, Inc. is the U.S.-based representative office of ZAO Renova, a major Russian corporation engaged in the metallurgical and natural resource sectors in Russia and other CIS countries. In addition to its representative functions, Renova, Inc. is involved in consulting and other business support activities. Improving the level of understanding and cooperation between American and Russian business partners is a priority for the company's operations.



Sun Microsystems, Inc. is a leading provider of hardware, software, service, and support solutions that power enterprises and network computing environments. Sun provides unparalleled support for its global customer base by delivering innovative technologies, open-standard based products, and services for enterprise, commercial, and technical computing.

Continually raising the bar for innovation, Sun boasts several groundbreaking technologies and platforms including the Java™ and Jini™ platforms, Jiro™ technology, Solaris™ operating environment, and Sun™ Open Net Environment (Sun ONE).

Sun began working with high-tech groups in the former Soviet Union in 1989, and opened its Moscow office in 1993. Today, it is one of the 10 most well-known foreign computer companies in the NIS.



Suvar-Kazan Company, Ltd. is one of the leading oil and oil-product exporters in Tatarstan. The company also provides trans-

port and logistical services to its clients. In addition, Suvar-Kazan is involved in the production of petrochemical products and raw materials for the glass and construction industries.



United Financial Group (UFG) is one of the leading investment banks in Russia.

UFG trades actively, both in local shares and in ADRs and GDRs listed overseas. Its clients primarily comprise institutional investors, hedge funds and Russia-dedicated funds from Europe and North America, with local Russian funds forming a small but growing part of the business.

Founded in 1994, UFG has built a solid reputation based on its integrity, solid trade execution and high-quality research. UFG has consistently been ranked in the top three for research coverage in Russia.

UFG has an experienced management team that offers a blend of extensive local knowledge and international investment banking experience. UFG currently employs more than 130 people in its main office in Moscow and additional offices in London and Cyprus.



USEC Inc., a global energy company, is the world's leading supplier of enriched uranium fuel for commercial nuclear power plants. In 2001, the company's revenues totaled nearly \$1.2 billion.

Through its subsidiary, the United States Enrichment Corporation, USEC Inc. operates the only uranium enrichment facility in the United States, a gaseous diffusion plant in Paducah, Kentucky. USEC Inc. also operates sampling, transfer and shipping facilities near Portsmouth, Ohio. Company headquarters are located in Bethesda, Maryland. The company, formerly a government corporation, was privatized in July 1998.

USEC Inc. is also the U.S. government's executive agent for the Megatons to Megawatts program, the historic U.S.-Russian non-proliferation agreement to dilute highly enriched uranium taken

from dismantled Russian nuclear warheads into low-enriched uranium fuel used by USEC Inc.'s customers to generate electricity. This national security program has been entirely funded by the private sector. To date, USEC Inc.'s nuclear weapons-derived fuel purchases from Russia exceed \$2 billion.



VimpelCom is a leading wireless telecommunications service company in Russia, operating under the "Bee Line" family of brand names. VimpelCom's license portfolio covers approximately 70 percent of Russia's population.

From its inception, VimpelCom has played a key role in the development of the Russian cellular telecommunications industry. VimpelCom introduced two digital cellular communications standards to Russia and built the first dual band GSM-900/1800 cellular network in Russia.

VimpelCom benefits from the strengths and expertise of its two strategic partners, Telenor and Alfa Group. VimpelCom was the first Russian company to list its shares on the New York Stock Exchange in November 1996.



Volcano Partners LLC is a Miami-based company recently formed to license and market a proprietary patented thermochemical technology, known as Ecomelt®, for the decontamination and treatment of municipal and industrial waste and contaminated soil.

The Ecomelt® technology, which was developed by the prominent Gas Technology Institute, does not produce secondary waste streams and does not discharge pollutants into the atmosphere. It is fully compliant with the U.S. Clean Air Act and the U.S. Environmental Protection Agency.

William T. Robinson PLLC is an international law firm serving clients in the United States, Asia, Russia, and other countries of the former Soviet Union. The firm specializes in international business law, trade and investment in Russia, privatization, international dispute resolution, government relations, energy, and technology protection. Representative clients are in finance, manufacturing, fishing, shipping, agribusiness, computer services, energy, trade, port development, transportation, engineering, and construction.

The firm regularly advises clients of various nationalities how to structure and manage Russian business operations, including participation of affiliated companies in other jurisdictions. The firm's international law practice is equally divided between representing Russian-owned companies and Western or Asian companies doing business in Russia and other countries.