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# TREATMENT OF U.S. BUSINESS IN EASTERN AND CENTRAL EUROPE

## HEARING

BEFORE THE

SUBCOMMITTEE ON EUROPEAN AFFAIRS

OF THE

COMMITTEE ON FOREIGN RELATIONS
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# TREATMENT OF U.S. BUSINESS IN EASTERN AND CENTRAL EUROPE

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**WEDNESDAY, JUNE 28, 2000**

U.S. SENATE,
SUBCOMMITTEE ON EUROPEAN AFFAIRS,
COMMITTEE ON FOREIGN RELATIONS,
*Washington, DC.*

The subcommittee met, pursuant to notice, at 2:15 p.m. in room SD–419, Dirksen Senate Office Building, Hon. Gordon H. Smith (chairman of the subcommittee) presiding.

Present: Senator Smith.

Senator SMITH. Good afternoon, ladies and gentlemen. I will call to order this hearing of the Subcommittee on European Affairs of the Foreign Relations Committee. The topic is the treatment of U.S. business in Central and Eastern Europe.

I would like to welcome our witnesses today who are here to discuss this topic. In the decade that has passed since the fall of communism American businesses have been in the forefront of the emerging markets of the countries of Central and Eastern Europe. The U.S. Government has matched the business community in its support of these emerging markets with resources to teach these new democracies such important topics as the rule of law, trade promotion, market access, and intellectual property rights.

I sought to hold this hearing to find out how successful our endeavors have been in trying to help these former Communist countries to join the global economy. As the owner of a small business myself, I have actively sold products abroad and know the importance of a favorable business climate.

This hearing will attempt to answer two questions: the first, has our Government attempted to create a promising business climate for interested Americans, the second, have these emerging countries created a climate that allows a market economy to work?

We hear horror stories all the time of capitalist systems that are really not capitalist but are masquerading in some form of cronyism. We do have a number of witnesses today both from the Department of State and the private sector who will comment on the business climate in Central and Eastern Europe.

I am a little concerned that the Department of Commerce has chosen not to participate today with even an Under Secretary or Assistant Secretary, or even Deputy Assistant Secretary to talk about what they have done to support emerging democracies. I assume something is being done, but no one from the Commerce Department has decided it was important enough to come here today.

I would like to invite the next Secretary of Commerce, whoever he or she is, to come before this committee on another occasion so that we can revisit this issue.

There are problems for some American businesses abroad. The Greenbrier Companies from my State is one of the largest manufacturers of railroad cars and is located in Lake Oswego, Oregon. Greenbrier is actively involved in a joint venture in Poland, and Peter Nevitt, chairman of Greenbrier Europe, is here to give their view regarding doing business in Poland.

I am also happy to welcome former U.S. Ambassador Ron Lauder, a pioneer in the emerging markets of Eastern Europe. Mr. Lauder is here to testify on the ups and downs of his company, Central European Media Enterprises Limited, and what he has had in terms of experience in these countries.

I am also pleased to welcome Mr. Kempton Jenkins, president of the Ukraine-United States Business Council. I look forward to your thoughts on the business in the Ukraine.

I would also like to note for the record the testimony submitted by Mr. Paul Singer on behalf of Elliott Associates. For the record, I would like to state I am especially troubled by reports of inappropriate pressure by the European Union on countries in Central and Eastern Europe who aspire to become EU members themselves.

It is well-known that EU has said quite clearly to candidate countries that by choosing American companies over European firms they place their EU membership in jeopardy. It is critical to ensure that U.S. companies are competing on a level playing field, and I certainly hope this administration is making this point clearly and consistently to our friends in the European Union.

It is now our pleasure to hear from the administration Assistant Secretary, Tony Wayne, and we welcome you, sir, and would turn the mike to you. Thank you for being here.

**STATEMENT OF HON. EARL ANTHONY WAYNE, ASSISTANT SECRETARY OF STATE FOR ECONOMIC, BUSINESS, AND AGRICULTURAL AFFAIRS, DEPARTMENT OF STATE, WASHINGTON, DC**

Mr. WAYNE. Thank you, Mr. Chairman. It is my pleasure to be here, and I want to commend you on taking the initiative to have a hearing on this important topic. The transformation going on in Central and Eastern Europe, as you know, is vital to the national security of the United States. The role that U.S. business has played and is playing in that is vital to our prosperity and to the prosperity of the countries of that region, and so again thank you very much for providing this opportunity to talk.

I might just start off by reassuring you on your last point that whenever we become aware of an EU member State making that inappropriate argument we take it up directly with the member State and with the country to which the argument may have been made.

We do not accept that argumentation, as you can understand, at all and in fact there should be no linkage between choosing the best commercial partner for your country and the prospect of EU membership, which we do support, but you can be assured that I personally have many times made that argument, and I know the Secretary of State has, and our ambassadors do also.

Senator SMITH. Unfortunately you have to make it too often, do you not?

Mr. WAYNE. Well, people try to use any leverage they think they might be able to use. That is a fact of what happens out there, and so we remain vigilant, and we will continue to do so.

Let me make a few introductory remarks, and I will try and keep them to a few and I might cut back a little bit on some of my oral remarks here if I go on too long, but clearly attracting trade and investment to Central and Eastern Europe is vital if that region is going to complete its transition to free market prosperity and democracy.

It is equally vital and a similarly high priority for us to support American business in identifying the opportunities that are out there and overcoming the challenges, of which there are many, that still fall in their path, and to assure that there is, indeed, a level playing field for our businessmen and businesswomen as they work to expand into these areas.

I think that Americans, from your State of Oregon all the way here to Washington, DC, know how important trade has become in today's world for our prosperity. Between 1994 and 1998 we created 1.4 million jobs related directly to trade, and American jobs which are involved in trade, I think as you probably know, Senator, average a higher pay of 13 to 16 percent above the norm, so trade is very important, and I would argue it has become more important as we move into what has been called the new economy.

We are linked even more closely together than we were before, so this is increasingly important, and we at the State Department certainly place a very high priority in supporting our firms in Central and Eastern Europe.

Now, where we are today in Central and Eastern Europe may need just a little bit of setting the scene. Ten years after the fall of the Berlin Wall many of these countries are still seeking the prosperity that comes with free markets. The transition has been a difficult one. Some places it has progressed more quickly than others, but there have been problems everywhere, and there are clearly lingering problems throughout the region.

One of the key issues that we think about as we look at this broadly is transparency. Justice Holmes once talked about "sunshine being the greatest of all disinfectants." Well, that certainly is true. In decisionmaking throughout the region we very much want to encourage transparency in government decisionmaking.

When an official makes a decision about a contract, about a new regulation, about a business opportunity, we would like to have it be clear why he made that decision, and we would like to have the opportunity to be there to comment on it to make sure that there is a level playing field. That is not often the case in some of these countries.

Lack of transparency also relates to another problem that you know is prevalent throughout the whole region, and this is corruption and bribery. Worldwide bribery results in the loss of tens of billions of dollars in lost American exports and lost opportunities to invest. This is a very high priority for us, as I mentioned in a number of our programs and in a number of individual interventions that we make to try to support American communities, or companies.

Related to that, of course, is criminal activity, which in some of these societies is still a very serious problem, so we are working, of course, not only with the economic authorities but with law enforcement authorities in the region to try to get a hold of this serious problem of illicit activities.

Physical infrastructure is a big problem throughout the region, the ability to deliver goods. Roads, ports, telecommunications systems are still below the standards in Western Europe, let alone in the United States.

Institutional infrastructure, what relates to good governance, remains a serious problem. In a number of the banking systems there are still debts left over from the previous Communist rule. There are out-of-date operating procedures. There are supervisory structures that are woefully lacking, often to ensure the right kind of regulation, the regulation that we have come to expect in our own system.

Just recently I think you might have noticed there was a bank that collapsed in the Czech Republic. A few weeks earlier there was a serious banking crisis in Romania, and so these remain problems that the countries have to deal with.

Finally, there is a problem of continued privatization. Privatization has not gone forward completely in the great majority of these countries, and that is part of the ongoing structural reform that is required.

Not surprisingly, the countries that have made the most progress toward free market institutions have attracted the most American and other direct investment, and so getting the right framework is very much important, and that is part of what we have tried to do.

As well as addressing specific business concerns when they have come up, and opportunities, we have tried to get the countries of the region to adopt the right economic policy and regulatory framework that will attract investment.

Now, there are some impressive results to date on the trade front. In 1991, U.S. companies exported about $1.6 billion worth of goods to the 15 countries of the region. By the end of 1999, U.S. exports had doubled to about $3.2 billion.

We have been working broadly through on the anti-bribery and corruption front through the OECD. I think, Senator, you know there is an OECD Anti-Bribery Convention which we have gotten many of the countries of Western Europe to adhere to, some of whom we have had to persuade to move in that direction. That is dealing with one part of the problem.

We have also been working in Central and Eastern Europe in a number of specific areas in the intellectual property, working with the American Bar Association Central and Eastern European law initiative to help these countries develop stronger legal systems. We have been working also in some cases with NGO's such as Transparency International and, as I mentioned, we have been working on some specific anticorruption programs in southeast Europe.

Our ambassadors in Central and Eastern Europe and all of our embassy officers for the variety of economic agencies, including the Commerce Department, of course, have been on the front lines of this effort and the effort of supporting American businesses. This has really been where we are often alerted first to problems that come up, and then we can support them both through higher level demarches from back here and in visiting officials to those countries.

The opportunities are clearly substantial. American firms have invested more than $7 billion in Hungary, for example, $5.1 billion in Poland, $1.5 billion in the Czech Republic, as reported by those countries. That is a substantial amount of investment.

We have taken some specific approaches to certain regions. In southeast Europe, following the fighting in Kosovo, we developed with our European partners something that is called the Stability Pact for Southeast Europe.

As a key part of that, we knew as a part of that that what we have to do is create the right structure of where private capital can come in and investment can flourish because, Senator, as you know, it is not government capital these days that really makes the difference. It is the flow of private investment and capital, and that can move overnight, or quicker than overnight from one corner of the world to another. There are many choices out there, so you have to have the right environment that will have people make the decisions to invest.

So we have really tried in the stability pact to lay out a bargain to the countries of the region. We will support you in attracting investment, we will provide seed money for you to get investment going, we will provide risk insurance, but in turn you need to undertake the reforms that are needed to create a good business climate, to create good free markets with good governance, with transparency that will invite private investors to come in.

In that connection, we have established an anticorruption initiative to which the countries of the region have signed up, and an investment pact to which countries of the region have signed up, and we have begun to put in place, country by country, monitoring programs to see how these countries are now going to carry out the commitments they have made, and we are pulling together all of the donors, that is, the international financial institutions as well as the donors, the representatives of the local government, and also in liaison with the private sector.

In this approach OPIC has been involved and has made available several hundred million dollars of investment guarantees to help mobilize private equity financing. We are going to be working with the European Bank for Reconstruction and Development in the same vein of making over $100 million available to support small and medium enterprises.

On the trade side of this, there is an important initiative that we were hoping we can get the support of the Senate for. This is the Southeast Europe Trade Preferences Act, which one of your colleagues, Senator, has introduced, that would extend duty-free treatment for 5 years on a number of items for Southeast Europe. We think this is a very important initiative. It would help strengthen the economies of the region. It would promote a robust private sector development in the region, and encourage further the integration of the region.

It is also, I think, an important part of a lever that we are working on with the European Union, because we, as part of our initiative, have encouraged them to move forward with their own unilateral one-way lowering of tariffs so goods from Southeast Europe can move into the European Union without any tariffs.

So I very much hope that you and your colleagues will consider supporting and passing this legislation.

In the Baltic region, we have also taken a specific effort to work with the Governments of Lithuania, Latvia, and Estonia to remove specific investment barriers and to promote U.S. investment in exports, and again there have been very good results. Overall trade between the United States and the three Baltic States has nearly doubled since 1996.

The United States has also undertaken strenuous efforts to foster investment in other business ties with Russia. Russia's new president, Vladimir Putin, has stated clearly that foreign investment will be essential to improving the economic outlook for Russia, and that significant progress on economic reform will be necessary to attract investment.

The United States, I think as you know, Mr. Chairman, is the leader in foreign direct investment in Russia, with over $2 billion invested in 1999 alone. During his meetings with President Putin in Moscow recently President Clinton emphasized that major new flows of foreign investment to Russia are possible, but only if action on the necessary structural and policy reforms is forthcoming.

Perhaps no other country in the region has experienced such a large gap between economic performance and potential as Ukraine, endowed with good natural resources, superb agricultural land, and well-educated population, as well as a strategic location, Ukraine is positioned to be one of the most successful of the former Soviet States in attracting foreign investment needed to restructure its economy, yet at $55 per capita, Ukraine has one of the lowest rates of direct foreign investments in the region.

The United States, with some $570 million out of $3 billion total of foreign investment is the single largest source of foreign investment in Ukraine. The United States, the IMF, the World Bank and other donors have delivered the same message to Ukraine for the past 5 years: market economics can only be successful in Ukraine when the government reduces its role in the economy and creates an environment conducive to investment, foreign as well as domestic, deals with serious problems of corruption, and gives freer reins to private enterprise.

These initiatives in Central and Eastern Europe benefit Americans. They encourage peace and stability in that part of the world, the part of the world that not long ago was an alliance threatening the United States. These initiatives also translate into economic opportunities for American workers, farmers, and business people.

In 1998, for example, aggressive advocacy by our Ambassador to Croatia and our Under Secretary of State for Economic and Business Affairs resolved a number of obstacles with the Croatian Government which resulted in Bechtel Corporation signing a $600 million highway construction contract with the Government of Croatia.

In Bulgaria over the past several years we aggressively and successfully tackled severe levels of piracy of compact disks and CD-ROM software. The joint efforts by Commerce, State, and USTR, and our embassy in Bulgaria, resulted in stringent Bulgarian enforcement programs, the closure of all factories producing unauthorized CD's, and the protection of important American intellectual property rights.

In all candor, Senator, I also would like to add that our budget and our personnel are stretched very thin as we try to undertake these activities both in Central and Eastern Europe and around the world. In today's global economy, as I mentioned, our capacity to defend our national security interests and our capacity to defend our economic interests are more closely linked than ever.

We work very hard to defend these interests, to be good advocates for American commercial and economic interests, yet, as you know, only 1 penny out of every $1 that the Federal Government spends right now is on international affairs and, as you well know, we are not talking about foreign aid here.

We are talking about the 44,000 export licenses that we at State work to approve each year, worth $25 billion. We are working for the 120,000 American jobs in the defense industry and in the dual use industries that are tied to that, the many more thousands or millions of jobs tied to other kinds of exports.

When we negotiate in the State Department with our colleagues our U.S. intellectual property rights that save American film, music, and software industries from piracy, we are talking about a total of maybe $200 billion a year that we are working to save, so I think we are working hard to defend America's national security and economic security interests, and we appreciate your support in this effort.

It has been my pleasure to make this initial statement, and I look forward to your questions, sir.

Senator SMITH. Thank you, Mr. Secretary. I assure you we are concerned about the budget for this 150 account. It should be more if we are serious about protecting American business interests as well as national security interests and waging peace and spreading prosperity. It is not a budget I will defend, and have tried to change.

I am going to include for the record a statement for the Entergy Corporation. It is a statement of Patricia Schwab, who is their vice president for Government and Regulatory Affairs. It is testimony about their company's experience in Bulgaria, which is a positive one, which is nice, so I am going to include that in the record, and also a letter from Chairman Jesse Helms to the Prime Minister of Poland.

[The Entergy Corporation statement can be found on page 71.]

[The letter from Chairman Helms follows:]

U.S. SENATE,
COMMITTEE ON FOREIGN RELATIONS,
*Washington, DC, May 9, 2000.*

The Honorable JERZY BUZEK
*Prime Minister*
*The Republic of Poland*

DEAR MR. PRIME MINISTER:

I have just learned that the government of Poland has taken steps that may significantly undercut the ability of the Polish economy to attract foreign investment, particularly American investment.

Poland's Ministry of Treasury has filed an action in a Polish court to prevent one of the National Investment Funds (NIF's), Octava, from exercising its full rights to amend its charter to permit share redemptions. I understand that the Ministry has continued to pursue this anti-market activity, even though Poland's Securities and Stock Exchange Committee has expressly held that the proposed action by the NIF is lawful.

Most disturbing of all, however, has been public statements by a Deputy Minister of the Treasurer that Poland does not want to give large shareholders, "e.g. American investment funds, the possibility to withdraw their money from the NIF's at a profit." This is profoundly disappointing to those of us who have watched and supported the market reforms that have been the foundation of Poland's great economic growth over the last decade.

Mr. Prime Minister, our confidence in this progress, and the partnership between the United States and Poland, will certainly be shaken if your government chooses to disregard private rights and to treat American investors unfairly. Unfair treatment, including the use of state power to bring about dilatory lawsuits, betrays the promise of privatization and will undercut Poland's standing in the international marketplace.

I request your assistance to resolve an apparently dilatory lawsuit against Octava and to allow it and other NIFs the freedom necessary to exercise their full rights, including share redemptions. I would be grateful if you would inform me of the steps the government of Poland is taking to bring this matter to a fair and just close.

Sincerely,

JESSE HELMS, *Chairman.*

Senator SMITH. And in connection with his letter, Mr. Secretary, I have this question that is directly related to the letter. Are you aware of problems investors have had withdrawing from the Polish national investment funds that were originally created to back the transition of about 500 State-owned business to privatize companies.

Are you aware of that? And it is my understanding that one American investment corporation, Elliott Associates, is now unable to withdraw its funds from these funds.

Mr. WAYNE. Mr. Chairman, I will honestly admit I am not aware of that, but I would be happy to get the information and look into it and get back to you.

[A reply to Senator Smith's question and to additional questions for the record can be found on page 54.]

Senator SMITH. We will supply you with a copy of this letter from the chairman. The European Union has repeatedly stated that the Czech Republic is far behind the West in dealing with corruption and crony capitalism. Do you agree with their assessment of that?

Mr. WAYNE. Well, Senator, I think there is a problem, I think throughout the region in dealing with corruption and crony capitalism.

Senator SMITH. It is not unique to the Czech Republic?

Mr. WAYNE. It is not unique. There are a few other countries that might even have a more serious problem.

Senator SMITH. My only other question is, are you helping the Greenbrier Company, one of those that will be testifying today who have run into a number of problems with the Transportation Ministry? Are you aware of their circumstance, and have you made any effort to be helpful to them?

Mr. WAYNE. Yes; Senator, I am aware of it, and I can happily say that we have been working very closely with the Greenbrier Companies and have raised their difficulties repeatedly with the Government of Poland at the very highest levels. Not only has our Ambassador in place raised this a number of times, but Deputy Secretary Eizenstat particularly raised it with Deputy Prime Minister Vosorovek and with Foreign Minister Gremek.

We have underscored that there needed to be in this case, and in this case there needs to be all the time an open end transparent public procurement procedure in Poland which, as I understand, was part of the problem which the Greenbrier Company faced.

I believe that in response to a number of these arguments and other arguments the Government of Poland has, indeed, issued a new tender recognizing that there was not an open process here, that there has been progress made, and I know you will get to hearing more detail probably from representatives of the Greenbrier Companies in dealing with their concerns. We hope that now these problems will be dealt with with a second tender.

We also note that there is a process going on of privatizing the Polish Railway System, of providing budgetary sustenance to the railway system to buy some of the materials, Greenbrier cars and other things Greenbrier makes, so this is an ongoing process, but we certainly intend to stay active in this process and to be as supportive as we can.

Senator SMITH. Well, Mr. Secretary, I thank you for coming and participating and answering questions. We appreciate very much the work that you do, and those in the State Department, to help our businesses in this country to reach markets abroad. It is one of the best ways we can spread peace and prosperity, so thank you, sir.

Mr. WAYNE. Thank you very much.

[The prepared statement of Secretary Wayne follows:]

PREPARED STATEMENT OF HON. E. ANTHONY WAYNE

INTRODUCTION

Thank you, Senator for inviting the Department of State to join you in your probe of challenges and opportunities for the American business community in Central and Eastern Europe. I am pleased to be here, and would personally like to thank you for your leadership on this vital topic. The Department shares your deep concern about the frequent incidences of corruption and weak rule of law which impede free trade in many of these emerging economies.

On behalf of Under Secretary Larson who, as you know, is in Japan today, I would also like to thank you for your dedicated service as a judge for the Ambassador Charles E. Cobb Awards—warm appreciation to you and to your Chief of Staff for helping the Department select the Ambassador and Economic Officer who exhibit the most dedication, innovation and success in promoting U.S. exports and trade overseas.

Senator, I am pleased to have this opportunity to discuss the current environment for business in Central and Eastern Europe. The region's ability to attract private sector involvement, including trade as well as investment, is critical to its ability to complete its transition to free market prosperity and democracy. We have long stated that as important as the assistance we give these countries is, private sector involvement in their economies is essential.

The region provides opportunities to a wide variety of American enterprises—small- and medium-sized enterprises as well as large corporations, farmers as well as business people. At the same time, supporting American business, identifying economic opportunities, and leveling the playing field for American exporters and investors are top priorities for the State Department and for our embassies in this region and around the world.

Americans from Oregon to Washington, D.C. are increasingly aware of the role trade is playing in our current economic prosperity and overall growth. Data show that open markets helped make the United States the fastest growing economy in the G–7 with an annual growth rate of 3.9% from 1994-1997. Jobs supported by American exports grew by 1.4 million between 1994 and 1998 and statistics show these American jobs supported by goods exports pay about 13% to 16% above the U.S. national average.

We in the State Department play a central role in working with American companies and with the firms, governments, and other institutions in Central and Eastern Europe to create open markets and rule of law. This has been a challenging process and one that will continue to require our attention. The numbers show we will be successful: Those countries that have made the most progress towards open markets and democratic rule of law are the ones that have been most successful in attracting private sector U.S. investment.

SITUATION IN THE REGION

Ten years after the fall of the Berlin Wall and the demise of Communism, the countries of Central and Eastern Europe are continuing their work to realize free market prosperity. The transition has been difficult and has moved at different speeds in the different countries. Although the situation varies from country to country, certain problems remain all too common in the region.

One is the lack of transparency. "Sunshine," as Justice Holmes once remarked, "is the greatest of all disinfectants." We find, however, that governments and other institutions in the region are not always open in their decision-making. Too often it is not apparent, either to Americans or even to the citizens of that particular country, why an official does what he does or what the reasons are behind the government instituting a particular regulation or procedure. In some cases, the governments do not publicize laws or regulations.

The lack of transparency feeds directly into another barrier to trade and investment: bribery and corruption. Worldwide, bribery results in tens of billions of dollars in lost exports for American companies and, others that play by the rules. However, bribery and corruption also impede governments from delivering the services their citizens need and expect and undermine their confidence in their governments and in democracy.

An additional problem in a number of countries in the region is the high level of criminal activity. Domestic and transnational criminal activity is a powerful deterrent to domestic, let alone international investment in certain of the countries of Central and Eastern Europe. Such criminal activity includes intellectual property rights piracy in sectors including pharmaceuticals, audio recordings, and the optical media.

Problems with infrastructure, physical as well as institutional are further concerns. Roads, ports, telecommunications systems, and other physical infrastructure are often not up to the standards we take for granted in Western Europe or the U.S. The people of Central and Eastern Europe and their present governments have inherited the results of decades of mismanagement by Communist governments. Albania is perhaps the most extreme example where the public still lives in decrepit apartments and there is no rail link to the rest of Europe because of the Hoxha paranoia. Estimates are that the imported Swedish concrete used to build the more than 700,000 bunkers could have been used instead to build as many two-bedroom apartments.

Institutional infrastructure also varies from country to country in the region, but again in many cases its weakness constitutes yet another challenge for investors, domestic as well as foreign. For example, the banking systems in a number of these countries are saddled with bad debts left over from the period of Communist rule or continue to suffer from out-of-date, uncompetitive operating procedures. Financial and regulatory supervision authorities in a number of these countries also need to be strengthened. The banking system of the Czech Republic was recently shaken by the collapse of the country's third largest bank. A similar situation also occurred recently in Romania.

The failure of a number of countries in the region to complete the process of privatizing state-owned entities not only perpetuates the inefficiencies and economy-damaging distortions of the Communist era, but raises questions in the minds of some as to how serious those governments are about making the needed reforms. Again, the figures show those countries that have made the most progress toward free market institutions and good governance have attracted the most American and other foreign direct investment.

The amounts of investment can be substantial. To date, American firms have invested more than $7 billion in Hungary, $5.1 billion in Poland, and $1.5 billion in the Czech Republic, according to data published by the recipient countries.

WHAT THE UNITED STATES IS DOING

In partnership with the governments of the region, as well as with our own private sector and with interested nongovernmental organizations, the State Department and we in the Department's Bureau of Economic and Business Affairs are working to address these concerns and to help foster a framework that opens these countries further to American business and investment. We remain convinced that such a partnership will yield real benefits to both sides.

There are a number of overarching efforts, for example, our efforts to battle corruption through encouraging countries in the region that have signed the OECD Anti-Bribery Convention to ratify and fully implement it. The Czech Republic and Hungary, both of which are members of the OECD, have ratified and implemented the Convention, as have Bulgaria and the Slovak Republic. Poland has signed, but has not yet ratified or implemented. We are pressing governments in Central and Eastern Europe, as we do elsewhere in the world, to take action to protect intellectual property rights. We are working with the American Bar Association's Central and Eastern European Law Initiative (CEELI) to help these countries develop stronger legal systems.

We have worked with the governments of the region to strengthen their IPR regimes. Bulgaria has been a particularly good example where, working with us, the Bulgarian government authorities have taken effective action to combat a serious problem with piracy of intellectual property in that country.

We have pursued bilateral investment treaties (BITs) with many of the countries in the region. The basic aims of the BIT program are to protect U.S. investment abroad and, in particular, to guarantee national treatment for U.S. investments; the free transfer of all funds related to investment; access to international arbitration to settle investment disputes with host country governments; freedom from performance requirements, such as local content or export quotas; the right to engage top managerial personnel of the investor's choice; and expropriation only under internationally recognized standards and with prompt, adequate and effective compensation. The BITs also encourage adoption of market-oriented domestic policies that treat private investment fairly and support the development of international legal standards consistent with all these objectives. We currently have signed BITs with 15 countries in the region, though not with Russia. Twelve of these are now in force.

In addition, I must point out the State Department and our embassies and consulates in the region constantly work hard on behalf of American commercial interests. In Central and Eastern Europe—from the Baltics to the Balkans—U.S. Ambassadors and our embassy officers are the eyes, ears and in-country negotiators for U.S. commercial and economic interests—from trade and investment to anti-corruption, environmental safeguards, and cultural, people-to-people exchanges. Furthermore, as experts on host-country markets and business practices, these officials can and do identify opportunities for American firms and advocate on their behalf, companies that range from small and medium enterprises like bagel bakeries to major firms such as Enron and Ford.

Exemplary business practices overseas and good corporate citizenship are among the best exports that the United States can offer. To emphasize this, the State Department initiated an annual Award for Corporate Excellence, an award recognizing outstanding corporate citizenship, innovation and exemplary business practices overseas. America business leaders are frequently Ambassadors in transition economies. They lead by their conduct: strict adherence to the Foreign Corrupt Practices Act, high labor, environmental and human rights standards; shared technology, training and professional, exchanges with local firms; and, their own democratic values. In many Central and Eastern European countries, business executives are close and effective partners with our Ambassadors and Embassy teams.

I should point out that the European Union, as it pursues enlargement to include most of the countries of the region, shares many of our goals, and seeks many of the same reforms. We are consulting closely with the EU on how our efforts can be coordinated to achieve the best results. Still, from time to time, some in the EU try to influence commercial decisions by saying that choosing a U.S. firm or partner over a EU firm could harm the EU accession prospects of a country. We rebut such assertions quickly and firmly to the EU and to the recipient country.

In addition to these general policies and programs, there are a number of specific initiatives geared to particular parts of the region designed to improve the investment and business climate.

*Southeast Europe*

One such international partnership is the Stability Pact for Southeast Europe. The Pact was announced at the July 30, 1999 Sarajevo Summit with President Clinton and other leaders—both Western European and from the region. The Pact is a straightforward bargain in which the international community will work to integrate Southeast Europe into the broader European and Transatlantic mainstream and the countries of the region will implement the reforms that are necessary for such integration to take place.Part of the Stability Pact is the Investment Compact under which the region's countries take steps to improve the investment climate. In return, the other Stability Pact members, including the U.S. committed to help the region in this effort and to work together with the international financial institutions to develop appropriate vehicles to mobilize private finance and mitigate risk.

On the investment side, OPIC is using its investment guarantees to mobilize up to $150 million in private equity financing by creating one or more private sector investment funds which will provide a $200 million credit line for companies or commercial partnerships with significant U.S. participation; and establish an OPIC on-the-ground presence in the region to serve as a resource for the U.S. investment community.

We are working with the European Bank for Reconstruction and Development (EBRD) to develop an initiative for providing up to $130 million to support small- and medium-sized enterprises (SMEs) in this region. A U.S. contribution of $10 million this year towards a total U.S. contribution of $50 million is expected to leverage an additional $80 million from the EBRD in debt financing for SMEs from other European donors. Part of the U.S. contribution will provide technical assistance to accelerate the transition of these countries to more market-oriented economies. Specifically, EBRD teams will identify legal and regulatory constraints for private sector development and provide technical assistance to promote sound business practices and good governance.

On the trade side, Stability Pact Partners underscored the importance of Southeast Europe's integration into and access to the European Union's more developed markets and the global trading system.

Connected with this is the proposed Southeast Europe Trade Preferences Act (SETPA). President Clinton discussed SEPTA during the July 1999 Sarajevo summit as an important mechanism to stimulate economic growth in the region and to integrate countries of the region into the broader European and Transatlantic mainstream. We note Senator Moynihan has introduced legislation to create a preference system for Southeast Europe.

The SETPA would demonstrate American commitment to the economic development of Southeast Europe by extending duty-free treatment for five years to a number of products that are currently ineligible under the GSP program: iron and steel products, agricultural products, footwear, glassware, ceramics, automobiles, bicycles, clocks and watches. The only product area not to receive additional coverage under SEPTA is textiles and apparel.

Through SETPA, the United States aims to strengthen the economies of the region, promote the robust development of the private sector and encourage further integration of countries of the region into international trade regimes such as the WTO. The announcement of SETPA also prompted the European Union to propose expanding its existing autonomous trade preference package for western Balkan countries, further boosting the region's economies and commitment to reform.

At the urging of the United States, the Stability Pact also includes an anti-corruption initiative that brings together the United States, the European Union, and regional countries in a common effort to promote good governance and to combat official corruption. The initiative will thereby help improve the environment for trade and investment in the region.

Let me note as well that while we support Southeast Europe's integration into the European Union's markets, we strongly believe this should be done in a way that avoids commercial problems with the U.S. Enlargement is not a zero-sum game, but rather should serve to strengthen the transatlantic relationship through stronger linkages between candidates for accession to the EU and the United States as well as to the European Union. Enlargement Commissioner Verheugen agrees and has argued strongly there is no contradiction between our growing transatlantic partnership and enlargement.

*Central Europe*

Results on the trade front are already impressive. In 1991, U.S. companies exported $1.6 million worth of goods to the fifteen countries of Central and Eastern Europe. By the end of 1999, U.S. exports had doubled, to $3.2 million.

We have a good and very active dialogue with Hungary, which, as one of the most advanced of the EU accession candidate countries, is progressing in its negotiations with the EU. At the same time, the Hungarians are working very constructively with us on trade problems associated with accession, including the issue of tariff differentials. Hungary also ratified early the OECD Bribery Convention, and is now working on its implementation.

Poland too is a leading candidate for EU accession, and we have been successfully engaging the Poles in a number of economic areas important to the U.S. On IPR, Poland is in the process of updating its antiquated copyright law to bring it into compliance with its WTO obligations. The Polish Government is also in the process of enacting legislation to restructure and privatize the Polish Railways. We expect this to result in a number of business opportunities for U.S. railroad companies. In this connection, I note that Paul Nevitt, Chairman of Greenbrier-Europe, will be testifying on the next panel. I would like to point out that our embassy in Warsaw as well as senior officials here in Washington have convinced Polish officials to take steps to meet the concerns that Greenbrier had regarding the sale of rail cars to Polish Railways.

United States investment in Poland continues to grow. Citibank, for example, is in the process of becoming a major participant in the Polish banking sector, with its acquisition of Bank Handlowy. Like Hungary, Poland has ratified the OECD Bribery Convention; it still is in the process of passing implementing legislation.

American firms are also active in the Czech Republic. Boeing is a 35% owner in a Czech fighter trainer manufacturer (called Aero Vodochody) with Czech Airlines (CSA). Boeing will also be competing for a number of civilian aircraft tenders by CSA. One problem we are discussing with the Czech Government is eliminating the current 4.8 percent tariff on large civil aircraft so that Boeing can compete fairly with Airbus which pays zero duty. The Poles and Bulgarians have done so and the Hungarians have agreed to a waiver. We expect the Czech Republic to do the same.

I note that Ronald Lauder, Chairman of Central European Media Enterprises (CME) will be speaking on the next panel about the problems his company encountered in the Czech Republic. American shareholders have a significant investment in the Czech broadcasting sector through CME. We have been very active in support of CME, and there is a process underway in the context of our Bilateral Investment Treaty (BIT) to resolve CME's BIT dispute through international arbitration.

*Northern Europe Initiative*

The U.S. is looking at trade and business development in the Baltic Sea region as well, a key component of our Northern Europe Initiative (NEI). NEI is a U.S. Government strategy to promote stability, strengthen free market and democratic institutions and security structures, and bolster U.S. trade and investment in the Baltic Sea region. Two of the six priority areas for NEI activity are business promotion and law enforcement. For FY 2000, we have allocated $1 million in regional Support for East European Democracy (SEED) Act funds for NEI activities.

Working closely with American businesses, we established, a business/government dialogue with the governments of Lithuania, Latvia, and Estonia to remove specific investment barriers and to promote U.S. investment and exports.

The NEI law enforcement programs have also targeted problems such as IPR protection and contract enforcement. Among the results are NRG's $500 million investment in Estonia's energy sector, which Estonia's cabinet approved June 27. Overall trade between the U.S. and the three Baltic states has nearly doubled since 1996.

*Russia*

The United States' efforts to foster investment and other business ties with Russia deserve particular attention. Russia's new President, Vladimir Putin, has stated that foreign investment will be essential to improving the economic outlook for Russia, and that significant progress on economic reform will be necessary to attract that investment. However, Russia still lacks a genuine competitive environment for investment, both domestic and foreign, and it lags far behind Central Europe in attracting foreign investment. In the ten years from 1988 to 1998, Russia received only $61 per-capita in foreign investment, compared to $389 for Poland and $967 for the Czech Republic.

The United States is the leader in foreign direct investment in Russia, with over $2 billion invested in 1999 alone. Many household names in the United States are now household names in Russia. However, Russia has yet to realize the potential offered by its abundant natural resources and educated workforce. The financial crisis of 1998 dealt all investors in Russia a setback. During his meetings with President Putin in Moscow this month, President Clinton emphasized that major new flows of foreign investment to Russia are possible, but only if action on the necessary structural reforms is forthcoming.

The United States Government has consistently urged the Russian Government to institute reforms to improve the climate for doing business in Russia, while continuously supporting U.S. investors who have undertaken the risks of establishing businesses there and encouraging the development of domestic Russian entrepreneurship. We have used the U.S.-Russia Joint Commission and its Business Development Committee to keep investment-oriented reform issues at the forefront of our bilateral agenda. The U.S. has also supported the activities of the international financial institutions in Russia, while insisting that their assistance be additional to private sector resources and be conditioned on structural reforms that benefit foreign and domestic investors alike.

Reflecting the importance of Russia's vast reserves of oil and gas, U.S. and other Western oil companies have been among the pioneers of investment in Russia. The USG has long encouraged the development of the legislative and regulatory framework for Production Sharing Agreements (PSAs) in Russia, with the goal of establishing a stable and transparent legal, financial and regulatory environment for investments in the oil and gas sector. In Moscow, President Putin assured President Clinton of his commitment to completing the framework for PSA's.

The election of many new Duma members last December opened an opportunity, which we are pursuing, for the Duma's ratification of our 1992 Bilateral Investment Treaty with Russia. This treaty would ensure treatment for U.S. investors no less favorable than that accorded to Russian investors in many areas of the economy, provide protections against expropriation, and set rules for adjudicating investment disputes. Another avenue for reform is Russia's accession to the World Trade Organization, a process that involves bringing Russia's regime for trade and investment into line with internationally accepted standards. We have actively encouraged and supported that process. We are also encouraging the Organization of Economic Cooperation and Development to deepen its dialogue with Russia on policy reforms to improve its investment climate.

We are, moreover, committed to enhancing the rule of law and protection of shareholder rights in Russia and have acted on this commitment in a very tangible way. Late last year, Secretary Albright made a difficult decision to delay $500 million in Ex-Im Bank guarantees to the Russian oil company TNK, in order to give time for a review of that company's business practices before the transaction was completed. Also, advocacy by USG officials in Washington and our Embassy in Moscow helped to convince Russian officials to terminate an attempt to re-privatize the Lomonosov Porcelain factory near St. Petersburg. It also blunted efforts to reduce the scope of foreign investment in the Russian insurance industry. We have repeatedly raised, at both the local and federal levels, the difficulties U.S. investors have had in securing enforcement of favorable judgments made by Russian courts.

The focus of our bilateral assistance in the economic area has turned to the regions of Russia, where we support: the implementation of international accounting standards; development of small- and medium-sized enterprises; and improvement of legislation affecting business. The U.S.-Russia Investment Fund makes equity investments in Russian enterprises and Russian-American joint ventures, as well as providing capital to business through Russian banks. We have funded thousands of exchanges that give Russian citizens an opportunity to develop their skills and establish valuable contacts with U.S. counterparts.

Admittedly, progress toward a welcoming climate for investment in Russia has been slow and the environment for doing business in Russia remains extremely difficult. However, as President Clinton noted in his speech before the Duma earlier this month, with a new President, a new government and a new Duma, Russia has a new chance to build prosperity and strength, while safeguarding democratic freedoms and the rule of law. The President emphasized to both President Putin and the Russian people that the United States welcomes a strong Russia that uses its strength to promote economic development, reinforce the rule of law, fight crime and corruption, defend democratic freedoms and build good relations with its neighbors and the world. We will continue our efforts to promote a better climate for investment in Russia as a means to that end.

*Ukraine*

Perhaps no other country in the region has experienced such a large gap between economic performance and potential as Ukraine. Endowed with good natural resources, superb agricultural land, a well-educated population, ethnic peace, and a strategic location in Europe, Ukraine was positioned to be one of the most successful of the former Soviet states in attracting the foreign investment needed to restructure its economy.

Yet at $55 per capita, Ukraine has one of the lowest rates of direct foreign investment in the region. The U.S., with some $570 million out of $3 billion total, is the single largest source of foreign investment in Ukraine. These figures have both remained static for several years and are very small for a country of 50 million people with the resource base and economic potential of Ukraine. In contrast, the figures for Poland, a country of 40 million which aggressively embraced reform, are $5.1 billion and $30 billion.

The United States, together with the IMF, the World Bank, and other donors, has consistently delivered the same message to Ukraine for the past five years: market economics can only be successful in Ukraine when the government reduces its role in the economy and gives freer reign to private enterprise. When this happens, we will begin to see investment rise again, and with rising investment will come sustained growth.

Much of U.S. assistance, $200 million last year and, $2 billion since independence, has been focused on helping Ukraine reform its economy and its governing institutions. We remain committed to making Ukraine's future a success and improving the climate for investment and opening up Ukrainian markets is crucial to a positive outcome.

We are also seeking ways to support the reform efforts of Prime Minister Viktor Yushchenko's government—leveraging resources and cooperating with other international donors whenever possible. USAID and other agencies continue to target economic reforms, privatization efforts, private sector development (small and medium enterprises) and civil society for crucial assistance.

As I have said, U.S. investors are the single largest source of foreign investment in Ukraine. Their problems, both specific and general, are a regular agenda item in all high-level bilateral meetings, most recently during President Clinton's trip to Kiev on June 5. We have been pleased with the more business-friendly policies of the Yushchenko government. Investors report they have encountered a more cooperative, businesslike attitude when dealing with officials under the new government.

We remain concerned, however, about U.S. investor problems that remain unresolved, and more generally about Ukraine's poor investment climate and slow pace of economic reform. In addition to resolving the investment disputes, we have urged Ukraine's government to take specific steps to improve its investment climate, including instituting more transparent procurement and licensing requirements, implementing regulatory reform, improving protection of shareholder rights, improving enforcement of judicial decisions, and enforcing a strong code of ethics.

Ukraine has a reputation as a difficult place to do business. In its Corruption Perceptions survey of 85 countries, Transparency International ranked Ukraine 69th. Corruption is a major obstacle to genuine reform and long-term economic recovery in Ukraine, Russia, and indeed throughout the former Soviet Union. Again, we have and will continue to provide assistance, in this area. However, it is the responsibility of Ukraine's government to tackle this problem, through deregulation, legal reform, and greater transparency.

## CONCLUSION

In closing, let me reiterate that these initiatives in Central and Eastern Europe yield benefits to Americans in terms of peace and stability in a part of the world that not so long ago was an alliance threatening the United States. Moreover, these initiatives translate into economic benefits for American workers, farmers, arid business people. In 1998, for example, aggressive advocacy by the U.S. Ambassador to Croatia and the Under Secretary of State for Economic, Business, and Agricultural Affairs resolved a number of obstacles with the Croatian Government. As a result, the San Francisco-based corporation Bechtel was able to sign a $600 million highway construction contract with the Croatian Government.

Since then, Bechtel has succeeded in concluding agreements to commence work on the first stage of the project and renegotiated the contract at greater value to provide a more extensive Croatian highway than was first planned.

Bechtel's story is only one of many. In recent days, work by the U.S. Ambassador in Sofia and others in the U.S. Government bore fruit when the Bulgarian Government finalized for signature a loan agreement with Citibank in connection with

Westinghouse's $77 million contract to upgrade the safety of the Kozloduy nuclear power plant. This project, which involves the first Ex-Im bank loan to Bulgaria, will make a vital contribution to improving nuclear safety in the region and improving the environment there.

Another recent success is the decision by the shareholders of Eastern Slovak Ironworks (VSZ) to endorse a deal by U.S. Steel to buy all steel and related assets of VSZ Kosice, the Slovak Republic's largest company. The deal will make U.S. Steel the largest U.S. investor and largest private sector employer in Slovakia.

In all candor, however, I must say that our budget and our personnel are stretched too thin to provide the protection American business deserves in today's global economy. If anything, America's economic well-being is becoming increasingly intertwined with decisions and developments around the world. We must bolster our ability to defend and promote our core interests overseas. U.S. diplomatic programs defend these core national interests, including commercial advocacy. Yet today only one penny out of every dollar the Federal government spends is devoted to international affairs.

We are not talking about foreign aid. Every year, when the State Department processes some 44,000 export licenses for defense articles valued at more than $25 billion, we sustain 120,000 American jobs. When the State Department negotiates agreements to safeguard U.S. intellectual property rights to save America's film, music and software industries as much as $200 billion a year, we do so not to aid others, but principally to advance *America's* prosperity. Even when the State Department promotes economic reform and good governance in Central and Eastern Europe, we do so not only to help these countries, but to promote America's economic *and* national security interests.

Thank you. I will be happy to respond to your questions.

Senator SMITH. We will call up next our second panel that will consist of Mr. Ronald S. Lauder, chairman of the Central European Media Enterprises. He will be followed by Mr. Kempton Jenkins, president of the Ukraine-United States Business Council, and they will be joined by Mr. Peter K. Nevitt, chairman of the board of Greenbrier Europe.

Welcome, gentlemen. Thank you all for coming and participating in this hearing, and we hope we can shine a light on some of the difficulties and make hopefully a better business climate in the future for both sides of the Atlantic and certainly for the prosperity of Central and Eastern Europe.

Mr. Lauder, welcome. The mike is yours.

## STATEMENT OF RONALD S. LAUDER, CHAIRMAN, CENTRAL EUROPEAN MEDIA ENTERPRISES, NEW YORK, NY

Mr. LAUDER. Thank you, Mr. Chairman. My name is Ronald Lauder, and the story that brings me here begins in 1986 when I had the privilege of representing the United States of America as the Ambassador to Austria in Vienna, in the heart of Central Europe. Vienna is just across the border from the country that was then called Czechoslovakia, a country that had been under Communist rule since 1947.

Sitting where I was in Central Europe, I witnessed the devastation that this part of the world had experienced from the Second World War, the Holocaust and the failure of the Communist system under which the Czech people had toiled for 40 years. Even before the fall of the Berlin Wall I set out to make a positive contribution in this part of the world through the Ronald S. Lauder Foundation by starting Jewish schools that have educated more than 10,000 children, schools in 15 countries in Eastern Europe.

The Velvet Revolution of 1989 brought great hope to the Czech people as they set out to create a democracy in a market-based economy. The fall of communism was a watershed event in the history of Central and Eastern Europe, and I was optimistic that I could also make a significant, positive contribution by establishing a free press.

Accordingly, I underwrote the establishment of independent television stations in the new democracies of Central and Eastern Europe. Under the Communist system, the government in these countries owned and controlled all forms of media, television, radio, and newspapers. I hoped to provide these societies with the same kind of free press that we enjoy here in this country.

The former Communist countries of Central and Eastern Europe needed and still need enormous capital investment. It was my hope that if my independent television stations were successful I would thereby create an example for other private investors who might in turn also want to invest in these countries.

In 1994, I brought Central European Media, or CME, to the United States capital markets and raised $66 million in initial public offering. CME thereby became a public company with shares traded on the NASDAQ Stock Exchange. The shares of CME were traded by well-known U.S. brokerage firms such as Merrill Lynch, Morgan Stanley, Dean Witter, Solomon Smith Barney, and Prudential Securities.

CME's shares were purchased by thousands of U.S. citizens, large and small, directly and indirectly, for their private accounts, mutual funds, pension plans, IRA's, Keogh plans, and for their children's education.

The first television station that Central European Media launched was TV Nova in Prague, the capital of the Czech Republic. TV Nova was an enormous success. Soon after its launch in 1994 the station had revenues of approximately $100 million per year, and was proclaimed by the news media to be the most successful launch of a TV station in history.

The success of TV Nova allowed Central European Media to return to the U.S. equity markets in 1995 and 1996 to raise an additional $220 million in equity and sell $170 million in bonds in 1997. Much of these proceeds were used to finance successful launches of stations in Romania, Slovakia, Slovenia, and Ukraine. To this day, Central European Media's television stations in Romania, Slovakia, Slovenia, and Ukraine are the leading independent television stations in those countries.

So what went wrong? How did hundreds of American taxpayers see their investments in Central European Media stock tumble, despite the fact that this country built one of the most profitable television stations in Europe? The answer is sad but simple. TV Nova was stolen.

TV Nova, a television station that generated $100 million of revenue every year in 1995, 1996, 1997, 1998, was stolen from CME by the joint access of the Czech Media Council and Vladimir Zelezny, CME's former business partner in TV Nova. The Media Council stole TV Nova by repudiating its prior official approvals on CME's position after TV Nova became successful. This was done by initiating administrative procedures attacking the business protections the Media Council had formerly guaranteed when it was soliciting CME's capital in 1993. And by affirmatively supporting Dr.

Zelezny's acts, rather than stopping him, when he violated obligations to CME that the Media Council was required by law to protect.

Vladimir Zelezny stole TV Nova by renouncing his agreement with CME and exercising improper influence on members of the Media Council. Zelezny officially threatened Czech political leaders with what was in many ways blackmail because of his ability to control the press.

Yet the TV Nova scandal is about even more than the theft of American investment. It is about the rule of law. This country and our taxpayers invested heavily in the hope of building a foundation for free markets behind the old Iron Curtain. The dream was that capitalism would take root quickly and secure freedom for the future. Sadly, the TV Nova scandal proves in the Czech Republic only crony capitalism has sprung up. The rule of law has been ignored in favor of insider connections and back-door deals.

More than investment decisions are at stake here. American foreign policy in the region must be reassessed in light of the reality that corruption, not capitalism, is growing there. TV Nova still exists and remains enormously profitable. However, the Czech Government maintains that CME does not own it. The advertising revenue of TV Nova no longer goes to the public shareholders of CME, many of whom are U.S. citizens. Instead, Vladimir Zelezny is pocketing TV Nova's $100 million of advertising revenue.

The position of the Czech Government today is a far cry from its position in 1993. When I considered making this investment in 1993, the Czech Government went out of its way to encourage U.S. investors to make an investment in a private television station. The Czech Government pledged to protect any investment U.S. investors would make in a television station. They pointed out that such an investment would be protected by the bilateral investment treaty between the United States and the Czech Republic. Signed in 1991, the treaty is a sovereign guarantee that specifically states that the U.S. investment in the Czech Republic may not be expropriated.

In the 1991 bilateral investment treaty the Czech Republic agreed to treat investments made by United States nationals fairly and equitably, to provide such investments full protection and security, not to impair the enjoyment of such investments through arbitrary or discriminatory measures, and not to expropriate such investments either directly or indirectly.

In making our investment in TV Nova, Central European Media took the bilateral investment treaty between the United States and the Czech Republic at its word. We made this investment with the knowledge that our television station was protected unequivocally under the bilateral investment treaty. We had every reason to expect that, should the Czech Government ever attempt to expropriate our television station, the U.S. Government would insist immediately that the Czech Government reverse any such expropriations.

I must say that our U.S. Ambassador there, John Shattuck, has been exemplary in this respect, speaking to the Czech Government on our behalf, yet the Czech Government has ignored his pleas and everyone else's pleas.

Almost one year ago on August 5, 1999, TV Nova's television signal was illegally terminated. The termination of our signal immediately deprived viewers of TV Nova's programming and our company of the lifeblood of any television station, the advertising revenue. On that day, Vladimir Zelezny began to broadcast a competing television signal instead, despite being legally bound to broadcast our signal under an exclusive contract officially blessed by the Czech Government at the time of our investment.

CME then immediately went before the Czech Media Council. The Czech equivalent of our FCC it is the government entity that officially blessed our exclusive contract at the time of our investment. CME demanded that the broadcast of our signal be resumed. The Czech Media Council refused. The Media Council effectively said, quote: "This is of no concern to us. This is merely a business dispute. Go to the courts."

CME has gone to the Czech courts. In fact, we recently received a decision by the court that our contract is exclusive and that Vladimir Zelezny must broadcast our television signal. When we then returned to the Media Council and showed them the court ruling that required Vladimir Zelezny to broadcast our television signal. Sadly, the Media Council again refused, saying we must await an appeal, a process that could take years.

In the meantime, Vladimir Zelezny continues to broadcast his television signal and pocket the $100 million per year of revenues that belong to the shareholders of Central European Media, many of whom are U.S. citizens.

The list of Zelezny's crimes is extensive. We have submitted proof to the Czech police that he forged false contracts to justify his illegal actions. We have submitted those false contracts to the Czech courts as proof of these crimes, including detailed expert reports demonstrating the forgery. This has also been ignored.

We have submitted proof that Zelezny has engaged in tax fraud and cut sweetheart deals with advertisers on TV Nova that stole revenues from CME with companies that he owned, but this proof, too, has been ignored by the Czech police. And on top of this he has stolen copyrights and lied under oath.

The response CME has received to its proof has made it clear that no matter what evidence CME presents, Czech prosecutors will not go forward without improper inducement. I, as a responsible businessman, operate under American law and rule of ethics, and will not provide these inducements.

There have been private detectives hired to stalk and intimidate CME employees and their families. It is rumored also, and widely rumored in the Czech Republic, that there are dossiers about the Czech Republic's leading politicians and threats, should anything ever happen, that these dossiers will be put on TV. And this has paralyzed many Czech politicians.

So what needs to be done? First, the State Department should demand, immediately and publicly, that the expropriation of TV Nova be reversed, not done in quiet diplomacy but publicly.

Second, the State Department should insist that the $100 million of advertising revenue that Vladimir Zelezny has pocketed over the last year be returned to CME. Make no mistake about it, the Czech Government has the ability to follow the rule of law. It is simply a matter of encouraging Prague to do the right thing. Perhaps the best way to get Czechs' attention is for the State Department to say loud and clear: Stop stealing from American taxpayers!

Third, the Treasury Department should demand that the international institutions funded by U.S. taxpayers cease giving financial support to the Czech Republic until the expropriation of TV Nova is reversed.

It is an insult to the American taxpayers that the European Bank for Reconstruction and Development, the International Monetary Fund, and the World Bank, funded by U.S. taxpayers, continue to give U.S. taxpayers' money to the Czech Republic. It is absolutely outrageous that the International Monetary Fund and World Bank are planning to reward the Czech Republic by holding their annual meeting in September in Prague.

American investors have already lost hundreds of millions of dollars from the expropriation of TV Nova. It compounds this crime to take tax dollars from the same investors to fund the EBRD, the IMF, and the World Bank, when these institutions show such little regard for U.S. taxpayers.

The future of former Communist countries of Central and Eastern Europe is not yet written. The United States can make a huge difference by insisting that our treaty be honored, that the rule of law be upheld. We need to reverse what has happened to TV Nova, not just for the sake of investors, but for the good of the Czech Republic and the United States.

Our goals in the region are clear, peace and prosperity. But history is also clear: peace and prosperity only follow the rule of law. What happened to TV Nova is not only a scandal in the region. Bribery and blackmail are commonplace in the region. And if this is allowed to stand, countless others will be inspired to follow the example. No one, be they Czech citizens or American taxpayers, can afford to see the rule of law ignored.

I thank you very much for the opportunity to tell the story of what happened to TV Nova, and I will be happy to answer any questions. Thank you.

[The prepared statements of Mr. Lauder follow:]

PREPARED STATEMENT OF RONALD S. LAUDER

Thank you, Mr. Chairman. My name is Ronald Lauder, and the story that brings me here begins in 1986, when I had the privilege of representing the United States of America as the ambassador to Austria in Vienna, in the heart of Central Europe.

Vienna is just across the border from the country that was then called Czechoslovakia, a country that had been under Communist rule since 1947. Sitting where I was in Central Europe, I witnessed the devastation that this part of the world had experienced from the Second World War, the Holocaust, and the failure of the Communist system under which the Czech people had toiled for forty years.

Even before the fall of the Berlin Wall, I set out to make a positive contribution in this part of the world through the Ronald S. Lauder Foundation by starting Jewish schools that have educated more than 10,000 children in schools in fifteen countries.

The Velvet Revolution of 1989 brought great hope to the Czech people as they set out to create a Democracy and a market-based economy. The fall of Communism was a watershed event in the history of Central and Eastern Europe, and I was optimistic that I could also make a significant positive contribution by helping to establish a free press.

Accordingly, I underwrote the establishment of independent television stations in the new democracies of Central and Eastern Europe. Under the Communist system, the governments in these countries owned and controlled all forms of media: television, radio and newspapers. I hoped to provide these societies with the same kind of free press that we enjoy in this country.

The former Communist countries of Central and Eastern Europe needed—and *still* need enormous capital investment. It was my hope that if my independent television stations were successful, I would thereby create an example for other private investors, who might, in turn also want to invest in these countries. In 1994, I brought Central European Media, (or CME), to the United States capital markets and raised $66 million dollars in an initial public offering.

CME, thereby, became a public company with shares traded on the NASDAQ stock exchange. The shares of CME were traded by well-known U.S. brokerage firms such as: Merrill Lynch; Morgan Stanley; Dean Witter; Salomon; Smith Barney and Prudential Securities. CME shares were purchased by thousands of U.S. citizens, large and small, directly and indirectly for their private accounts, mutual funds, pension plans, IRA's, Keogh plans, and for their children's education.

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Much of these proceeds were used to finance successful launches of stations in Romania, Slovakia, Slovenia and Ukraine. To this day, Central European Media's television stations in Romania, Slovakia, Slovenia and Ukraine are the leading independent television stations in those countries.

So what went wrong? How did hundreds of American taxpayers see their investments as Central European Media's stock tumble despite the fact that this company built one of the most profitable television stations in Europe?

The answer is sad but simple: TV Nova was stolen.

TV Nova, a television station that generated $100 million of revenue every year in 1995, 1996, 1997 and 1998 was stolen from CME by the joint access of the Czech Media Council and Vladimir Zelezny, CME's former business partner in TV Nova. The media council stole TV Nova by repudiating its prior official approvals of CME's position after TV Nova became successful, by initiating administrative and criminal prosecutions attacking the business protections it had formally guaranteed. When it was soliciting CME's capital in 1993, and by affirmatively supporting Dr. Zelezny, rather than stopping him, when he violated obligations to CME that the Media Council was required by law to protect, Vladimir Zelezny stole TV Nova by renouncing his agreements with CME, exercising improper influence on members of the media council, and threatening Czech political leaders with blackmail.Yet the TV Nova scandal is about even more than the theft of American investment, it is about the rule of law. This country—and our taxpayers—invested heavily in hope of building a foundation for free markets behind the old Iron Curtain. The dream was that capitalism would take root quickly and secure freedom for the future.

Sadly, the TV Nova scandal proves in the Czech Republic only crony capitalism has sprung up. The rule of law has been ignored in favor of insider connections and backdoor deals. More than investment decisions are at stake here. American foreign policy in the region must be reassessed in light of the reality that corruption, not capitalism, is growing there.

TV Nova still exists and remains enormously profitable. However, the Czech government maintains that CME does not own it. The advertising revenue of TV Nova no longer goes to the public shareholders of CME, many of whom are U.S. citizens. Instead, Vladimir Zelezny is pocketing TV Nova's $100 million of advertising revenue. The position of the Czech government today is a far cry from its position in 1993, when I considered making this investment.

In 1993, the Czech government went out of its way to encourage U.S. investors to make an investment in a private television station. The Czech government pledged to protect any investment U.S. investors would make in a television station, and pointed out that such an investment would be protected by the bilateral investment treaty between the United States and the Czech Republic, which was signed in 1991. This treaty is a sovereign guarantee that specifically states that U.S. investment in the Czech Republic may not be expropriated.

In the 1991 bilateral investment treaty, the Czech Republic agreed to treat investments made by United States nationals fairly and equitably, to provide such investments full protection and security, not to impair the enjoyment of such investments through arbitrary or discriminatory measures, and not to expropriate such investments either directly or indirectly.

In making our investment in TV Nova, Central European Media took the bilateral investment treaty between the United States and the Czech Republic at its word. We made this investment with the knowledge that our television station was protected unequivocally under the bilateral investment treaty. We had every reason to expect that should the Czech Government ever attempt to expropriate our television station, the U.S. government would insist immediately that the Czech government reverse any such expropriation. Unfortunately, this has not occurred.

Almost one year ago, on August 5, 1999, TV Nova's television signal was illegally terminated. The termination of our signal immediately deprived Czech viewers of TV Nova's programming and our company of the life-blood of any television station advertising revenue. On that same day, Vladimir Zelezny, began to broadcast a competing television signal instead, despite being legally bound to broadcast our signal under an exclusive contract officially blessed by the Czech government at the time of our investment.

CME immediately went before the Czech Media Council, the Czech equivalent of the FCC and the government entity that had officially blessed our exclusive contract at the time of our investment, and demanded that the broadcast of our signal be resumed. Sadly, the media council refused. The Media Council effectively said: "this is of no concern to us. This is merely a business dispute. Go to the courts."

CME has gone to the Czech courts. In fact, we recently received a decision by the court that our contract is exclusive and that Vladimir Zelezny must broadcast our television signal. We then returned to the Media Council and showed them the court ruling that required Vladimir Zelezny to broadcast our television signal. Sadly, the Media Council again refused, saying that we must wait to appeal—a process that could take years.

In the meantime, Vladimir Zelezny continues to broadcast his own television signal and pocket $100 million per year of revenue that belongs to the shareholders of Central European Media, many of whom are U.S. citizens.

The list of Zelezny's crimes is extensive. We have submitted proof to the Czech police that Zelezny has forged false contracts to justify his illegal actions and has submitted those false contracts to Czech courts. Our proof of these crimes, including detailed expert reports demonstrating the forgery, has been ignored. We have also submitted proof that Zelezny has engaged in tax fraud and cut sweetheart deals with advertisers on TV Nova that stole revenues from CME, but this proof, too, has been ignored by Czech police. On top of this, Zelezny has stolen copyrights, lied under oath, and even broke into CME's computer system in London.

The responses CME has received to its proof have made clear that no matter what evidence CME presents, Czech prosecutors will not go forward without inducements that I, as a responsible businessman operating under American law and rule of ethics, cannot and will not provide. Zelezny has hired private detectives to stalk and intimidate CME employees and their families. Vladimir Zelezny has dossiers on the Czech Republic's leading politicians, and his threats to expose on his television station the unseemly details of these politicians' lives have paralyzed the Czech government's ability to deal with this issue.

So what needs to be done? First, the State Department should demand immediately and publicly that the expropriation of TV Nova be reversed. Second, the State Department should insist that the $100 million dollars of advertising revenue that Vladimir Zelezny has pocketed over the last year be returned to CME. Make no mistake about it: the Czech government has the ability to follow the rule of law here. It is simply a matter of encouraging Prague to do the right thing. Perhaps the best way to get the Czech's attention is for the State Department to say, loud and clear: "stop stealing from American taxpayers!" Third, the Treasury Department should demand that the international institutions funded by U.S. taxpayers cease giving financial support to the Czech Republic until the expropriation of TV Nova is reversed.

It is an insult to American taxpayers that the European Bank for Reconstruction and Development, the International Monetary Fund and the World Bank, funded by U.S. taxpayers, continue to give U.S. taxpayers money to the Czech Republic despite the expropriation of TV Nova.

It is absolutely outrageous that the International Monetary Fund and World Bank are planning to reward the Czech Republic by holding their annual meeting in September in Prague' American investors have already lost hundreds of millions of dollars from the expropriation of TV Nova. It compounds this crime to take tax dollars from these same investors to fund the EBRD, the IMF and World Bank when these institutions show such little regard for U.S. taxpayers.

The future of the former communist countries of Central and Eastern Europe is not yet written, and the United States can make a huge difference by insisting that our, treaties be honored, that the rule of law be upheld and by not rewarding criminals. We need to reverse the expropriation of TV Nova. Not just for the sake of American investors, but in the larger sense, for the good of the Czech Republic and the United States. Our goals in the region are clear: peace and prosperity. But history is also clear: peace and prosperity only follow the rule of law.

Vladimir Zelezny is not the only thief in the region. Bribery and blackmail are not his alone. If the expropriation of TV Nova is allowed to stand, countless others will be inspired to follow his example. No one, neither Czech citizens, nor American taxpayers, can afford to see the rule of law ignored.

Thank you for the opportunity to tell the story of the expropriation of TV Nova. I would be happy to answer any questions.

* * *

*In addition to the direct testimony Mr. Lauder has presented, the following background information is offered as a more extensive examination of the TV NOVA scandal. A chronology of the scandal's major events is provided, as well.*

As the Rule of Law has continued to be frustrated inside the Czech Republic, Mr. Lauder and other American investors have been forced to seek justice outside the Czech system. The following information details the international arbitration Mr. Lauder has commenced that seeks to hold the current government of the Czech Republic accountable for its action.

It should be noted that while Mr. Lauder has personally initiated this action, he has pledged that any proceeds from a favorable ruling will be used to compensate other investors. In other words, Mr. Lauder is seeking justice here, not personal profit.

## I. INTRODUCTION TO THE ARBITRATION

Pursuant to Article 3 of the Arbitration Rules of the United Nations Commission on International Trade Law (the "UNCITRAL Rules"), Ronald S. Lauder has commenced arbitration against the Czech Republic. Mr. Lauder has launched this arbitration as a result of actions by the Czech Republic in breach of the Treaty Between the United States of America and The Czech and Slovak Federal Republic Concerning the Reciprocal Encouragement and Protection of Investment, executed on October 22, 1991 (the "Treaty"). The Czech Republic has assumed the rights and obligations of the Czech and Slovak Federal Republic under the Treaty.

After having recognized the need for foreign investment to foster the development of television broadcasting in the Czech Republic, and after having actively solicited and received foreign participation in its first nationwide private television station, the Czech Republic breached its Treaty obligations by taking affirmative steps to constrain the scope of the foreign investor's interest and by failing to protect the foreign investment that it specifically approved. Once the television broadcasting venture created with foreign capital became established and successful, and while the local Czech participants in the company organized to hold the foreign investment were arranging the sale of their interests at a substantial profit, the Czech Republic reversed its position on the fundamental nature of the foreign investment in a manner that favored local investors and critically undermined the value of the foreign investment. These actions have been unfair, arbitrary, unreasonable and discriminatory against the foreign investor, and have consequently constituted breaches of the Treaty.

The dispute between Mr. Lauder and the Czech Republic is an "investment dispute" as defined by Article VI(1) of the Treaty. As such, it is subject to arbitration pursuant to Articles V.E (2) and (3) of the Treaty.

The Treaty entered into effect in the Czech and Slovak Federal Republic on December 19, 1992. (Decree of the Ministry of Foreign Affairs No. 187/1993 Coll.) After the Government of the Czech and Slovak Federal Republic ceased to exist on December 31, 1992, the Czech Republic succeeded to the rights and obligations of the Czech and Slovak Federal Republic under the Treaty. (Article 5 of Constitutional Act No. 4/1993 Coll.)

As set forth in more detail below, the dispute arose on July 23, 1996. More than six months having passed without the settlement of the dispute through consultation and negotiation, Articles V.1 (2) and (3) of the Treaty provide that the dispute may be submitted to arbitration after the complaining national consents "in writing to the submission of the dispute for settlement by conciliation or binding arbitration" pursuant to any of the methods permitted by the Treaty.

Mr. Lauder has consented in writing to submit his dispute with the Czech Republic for binding arbitration pursuant to the UNCITRAL Rules (Letter from Ronald Lauder to the Ministry of Finance of the Czech Republic, dated August 19, 1999.)

Pursuant to Article VI(3)(b) of the Treaty, the Czech Republic has consented to submit the dispute to arbitration in a number of forums, including before an ad hoc tribunal established pursuant to the UNCITRAL Rules.

## II. THE ARBITRATION CLAIM

### *A. The Czech Republic Undertook Obligations to Promote and Protect Investments of U.S. Investors*

The Treaty sets forth an array of undertakings by both signing nations, designed to promote and protect investments in each nation by investors of the other nation. Among others, the Czech Republic, acting through the Council, has breached the following provisions of the Treaty:

a. "Investment shall at all times be accorded fair and equitable treatment, shall enjoy full protection and security and shall in no case be accorded treatment less than that which conforms to principles of international law' (Article II(2)(a));

b. "Neither Party shall in any way impair by arbitrary and discriminatory measures the management, operation, maintenance, use, enjoyment, acquisition, expansion, or disposal of investments" (Article II(2)(b)); and

c. "Investments shall not be expropriated or nationalized either directly or indirectly through measures tantamount to expropriation or nationalization ('expropriation') except for a public purpose; in accordance with due process of law; in a nondiscriminatory manner; upon payment of prompt, adequate and effective compensation; and in accordance with the general principles of treatment provided for in Article 11(2)" (Article III).

### *B. Mr. Lauder's Investment in the Czech Republic is Protected under the Treaty*

Mr. Lauder indirectly controls zeská nezávislá televizni spoleznost, spol. s r.o. ("CNTS"), a Czech corporation engaged in the business of providing broadcasting services for TV Nova, the Czech Republic's most popular and successful television station.

Mr. Lauder has direct voting control of Central European Media Enterprises Ltd. ("CME Ltd."), the leading commercial television company in Central and Eastern Europe. One of CME Ltd.'s wholly owned subsidiaries is CME Media Enterprises B.V. ("CME"). CME, in turn, holds a 99% equity interest in CNTS through its wholly owned subsidiary, CME Czech Republic B.V. Pursuant to Article I(1)(a) of the Treaty, the CME and CNTS assets in the Czech Republic constitute an "investment" of Mr. Lauder, who exercises ultimate control over CNTS and its operations in the Czech Republic, thereby entitling him to the benefits and protections of the Treaty.

### *C. By Unreasonably and Discriminatorily Depriving Mr. Lauder of His Investments, the Czech Republic Has Failed to Abide by its Obligations Under the Treaty*

#### *1. Background of Mr. Lauder's Investment*

On October 30, 1991, only eight days after the Treaty was signed, the Czech Republic's Act on the Operation of Radio and Television Broadcasting was adopted. (Act No. 468/1991 Coll, the "Media Law"). The Media Law empowered the Council to grant licenses for television broadcasting. In spite of the Treaty provisions protecting American investors from discrimination, the Council did not administer the Media Law in a manner that presented a level playing field for a foreign investor competing against Czech nationals.

In late 1992 and early 1993, the Council participated in negotiations with, among others, (*i*) the Central European Development Corporation GmbH ("CEDC"), a German company also controlled by Mr. Lauder and the predecessor to CME; (*ii*) Dr. Vladimir Zelezný, a Czech national, and (*iii*) CET 21, spol. s r.o. ("CET 21"), a Czech company. The goal of the negotiations was the issuance of a license and the formation of a company for television broadcasting in the Czech Republic.

In order to encourage a substantial foreign investment while at the same time preventing foreign ownership of broadcasting licenses, the Council required and approved a structure that would permit CEDC to obtain the use and economic benefit of a license issued to a Czech-owned company—CET 21.

Thus, on February 9, 1993, when the Council issued a license to CET 21 to operate the first nationwide private television station in the Czech Republic (the "License"), the License acknowledged CEDC's "substantial foreign capital participation" and CEDC's partnership with the holder of the License, CET 21. The Council's grant of the License to CET 21 was made expressly subject to, among other things, the condition that CET 21 form a joint venture with CEDC and use the License through that joint venture. When the Council issued the License, it knew that CET 21 and CEDC had explicitly agreed that neither of them would be authorized to broadcast commercial television without the other.

In April 1993, CET 21 and CEDC agreed on a Memorandum of Association ("MOA") for the creation of the required joint venture: CNTS. Under the MOA, CEDC contributed 75% of CNTS's start-up capital, and obtained a 66% ownership interest in return. The remaining 25% of start-up capital was contributed by zeská spozitelna a.s., a Czech bank, which obtained a 22% ownership interest. CET 21 contributed to CNTS the right to use the License "unconditionally, unequivocally and on an exclusive basis," and obtained a 12% ownership interest in return for this contribution. Dr. Zelezný served as the General Director and Executive of CNTS and as the General Director of CET 21.

The MOA reflected the organizational structure that had been negotiated with the intensive participation of the Council and under its oversight. The concept behind the structure was that CNTS would be the central and only operating company for the new television station. CNTS was to pay all costs and keep all revenues associated with operating the television station.

On April 20, 1993, the Council gave its formal approval to the MOA.

In February 1994, CNTS and CET 21 began broadcasting TV Nova under the License. TV Nova quickly became the Czech Republic's most popular and successful television station. In August 1994, CME took over CEDC's interest in CNTS, which it has held since May 1997 through CME Czech Republic B.V.

*2. Commencement of Dispute and Attempt at Resolution*

On July 23, 1996, citing a change in the Media Law, the Council commenced administrative proceedings claiming that the arrangement between CNTS and CET 21 amounted to an illegal transfer of the License. This action was directly contrary to the structure that the Council had approved a little more than three years previously for the express purpose of fostering foreign investment within the framework of the Media Law.

CME and CNTS opposed the Council's position in the administrative proceeding as unfair and without any basis in law. An opinion from the Institute of the State and Law of the Academy of Sciences of the Czech Republic released on August 13, 1996 supported CNTS and CME's position that the relationship initially approved by the Council was proper under the Media Law, as amended. CME and CNTS nevertheless also began negotiations to settle the dispute amicably. It was fundamental to CME's position that any settlement could not substantively affect its legal rights and the economics of its investment in the Czech Republic.

At the Council's insistence, CME was forced to accept a modification of the terms of its MOA with CET 21. Under the new terms, the language of the MOA in which CET 21 had contributed the "right to use" the License on an exclusive basis was amended to provide that CET 21 contributed to CNTS the "know-how" connected with the License, still on an exclusive basis. CME was repeatedly assured that this change would not alter the basic economic position of the participants in TV Nova.

At approximately the same time that the Council commenced administrative proceedings against CNTS, the local investors in CNTS began to sell their interests in CNTS to cash out their very substantial profits from the early success of the venture. On July 17, 1996, zeská spozitelna a.s. sold its 22% interest in CNTS to CME, raising CME's ownership share to 88%. Then, in December of 1996, various local investors who indirectly owned a 5.2% interest in CNTS through CET 21 sold that interest to CME. Dr. Zelezný, who acted as an intermediary for that sale, further arranged for the pooling of all but 1% of the remaining Czech ownership of CNTS into a new entity known as Nova Consulting a.s. ("Nova Consulting"). In conjunction with this reorganization, Dr. Zelezný purported to increase his ownership interest in CET 21 to a majority 60% share. On August 11, 1997, CME purchased Nova Consulting's 5.8% interest in CNTS for US$ 28.5 million. As a result of these transactions, CME had increased its ownership interest in CNTS from 66% to 99%, and local investors, through CET 21, retained only a 1% interest in CNTS.

In September 1997, having extracted the concessions regarding the MOA from CNTS and CME, the Council dismissed the administrative proceeding concerning TV Nova.

*3. Continuation of Arbitrary and Discriminatory Actions by the Czech Republic*

Contrary to CME's belief in late 1997 that the revised arrangements forced upon it by the Council would not adversely impact its investment in the Czech Republic, the events that ensued proved the opposite. At the instigation of influential Czech nationals (including principally Dr. Zelezný), the Council has used its power unfairly and unreasonably to undermine the value of the CNTS investment. In doing so, the Council has discriminated against CME as a foreign investor by providing favorable treatment for the business endeavors of the local investors (and, in particular, Dr. Zelezný), who had sold their interest in CNTS at great profit.

Relying on the changes in the MOA required by the Council, CET 21 and Dr. Zelezný, as the majority owner of CET 21, have recently taken the position that CET 21 is not required to honor its partnership with CNTS. In particular, they claim that CET 21 and CNTS do not have an exclusive relationship. This claim is completely at odds with the course of dealings the parties have followed from 1993 until October 1998, when CET 21 began to repudiate their longstanding arrangement. CET 21 and CME always understood that CNTS, exclusively, would pay all costs and provide all services associated with TV Nova. CET 21 and Dr. Zelezný assert that a non-exclusive relationship is required by the Council's reading of Czech law, and that the only right CNTS (or CME as its 99% owner) has obtained as a result of contributing all of the capital to create TV Nova is the right to compete with others for the provision of services. For the past year, CET 21 and Dr. Zelezný have been systematically repudiating all obligations to CNTS. These acts culminated on August 5, 1999, when CET 21 ceased broadcasting TV Nova with CNTS and announced that it would no longer obtain any services from CNTS.

While Dr. Zelezný and CET 21 have been pursuing their campaign to cripple CNTS for their own private profit, the Council has taken actions and issued opinions that were supportive of and essential to their efforts.

On March 3, 1999, Dr. Zelezný secretly wrote to the Council asking it to confirm several legal opinions that CET 21 wished to advance, all of which related to disputes between CET 21 and CNTS. On March 15, 1999, twelve days after Dr. Zelezný's letter, the Council responded. As requested by CET 21, it took the unfounded position that agreements between broadcast operators and service providers must be on a non-exclusive basis. In issuing this opinion, the Council did not disclose that it had received the secret communication from Dr. Zelezný or that it was adopting almost word for word the views that Dr. Zelezný had expressed in his March 3 letter. The Council's position in its March 15, 1999 letter was completely at odds with its 1993 approval of the exclusivity arrangement that was the foundation for the investment of foreign capital necessary to the formation of TV Nova.

As the scope of the rights of CNTS have become a matter of increasing dispute, including much litigation over Dr. Zelezný's and CET 21's entitlement to repudiate all rights of CNTS, the Council has refused to take actions that responsibly address the situation it was instrumental in creating. Its inaction has amounted to a failure to protect the legitimate interests of the foreign investors. On July 26, 1999, the Council informed the Czech parliament that it considers the current dispute to be of a merely commercial nature that should be resolved privately between CNTS and CET 21, a position that improperly takes no account of the critical role the Council has played by its disavowal of its original formal approval of CNTS's exclusive right to use the license.

The Council's actions have violated the Treaty and have contravened its purpose. The terms to which the Council agreed in 1993 were pivotal in leading CME to invest tens of millions of dollars into the Czech Republic. Once the local investors cashed out their positions in CNTS, causing their interests to diverge from Mr. Lauder's interests, the Council further took steps to benefit the local investors at Mr. Lauder's expense. As a result of the Council's earlier actions and its current refusal to remedy the situation, CNTS's business activity has come to a standstill, thus wholly undermining the value of Mr. Lauder's investment in violation of the terms of the Treaty.

Despite the efforts made on behalf of Mr. Lauder, the dispute has yet to be resolved satisfactorily. Mr. Lauder remains open to, and would welcome, an amicable settlement of this dispute. However, in light of the fact that the dispute has not been amicably settled over several years to date, and given the urgency the dispute has taken on as a result of the Council's recent behavior and the recent halt of all business activities of CNTS, it has become necessary to file this Notice of Arbitration.

### III. WHAT ARBITRATION CAN DO

Mr. Lauder has requested that the Tribunal provide the relief necessary to restore CNTS's exclusive rights to provide broadcasting services for TV Nova and thereby restore to his the economic benefit available under the arrangement initially approved by the Council. To this end, the Tribunal has been requested to order the Czech Republic to take such actions as are necessary to restore the contractual and legal rights associated with the claimant's investments. Among other things, the Czech Republic should:

a. be ordered to impose conditions on the License that adequately reflect and secure CNTS's exclusive right to provide broadcast services and its right to obtain all corresponding income in connection with the operation of TV Nova;

b. be required to enforce such conditions, including by revoking the License and reissuing it to CNTS or to such other entity and under such other circumstances as would restore the initial economic underpinnings of Mr. Lauder's investment; and

c. be held liable for the damages Mr. Lauder has incurred to date, in an amount to be determined by the Tribunal, taking into account, among other factors, the fair market value of Mr. Lauder's investment prior to the breaches of the Treaty.

The relief requested comports with the international law of state responsibility and is consistent with the calculation of expropriation damages in the Treaty. Article 111(1) of the Treaty indicates the compensation required in the event that an investment is expropriated or nationalized (directly or indirectly) in a manner that *is* based on a valid public purpose, *accords* with due process and *is not* discriminatory. In such cases, the "compensation shall be equivalent to the fair market value of the expropriated investment immediately before the expropriatory action was taken or became known; to be paid without delay; include interest at a reasonable market rate; and be freely transferable at the prevailing market rate of exchange on the date of expropriation."

1. In this case, while no official expropriation has been announced, the Czech Republic, through the actions of the Council, has deprived Mr. Lauder of the entire value of his investment *without* complying with the standards of fairness, non-discrimination and due process set forth in the Treaty. If an investor is entitled to the fair market value of its investment for an expropriation that comports with due process, is nondiscriminatory and serves the public interest, Mr. Lauder must be entitled to at least the same remedy in the circumstances presented here.

A Chronology of Events in the TV NOVA Scandal

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| Oct. 1991 | Czechoslovakia enters a bilateral investment treaty with the United States. |
| 1992 | Central European Development Corporation ("CEDC"), a predecessor company to CME, negotiates an agreement with Vladimir Zelezny ("VZ") and others prescribing a business relationship between CEDC and CET 21, whereby the parties would jointly apply for the Czech Republic's first nationwide private television license. |
| Feb. 3, 1993 | CET 21 and CEDC enter into an agreement entitled "Overall Structure of a New Czech Commercial Television Entity." The agreement provides for the formation of a new company—CNTS—that would be the "only" company to run the television station. In addition, CET 21 and CEDC agree that "neither party has the authority to broadcast commercial television without the other." |
| Feb. 5, 1993 | CET 21 and CEDC enter into a second agreement on the structure of a Czech Commercial Television Entity. As with the Feb. 3, 1999 Agreement, the Council for Radio and Television Broadcasting (the "Media Council") is notified of this Agreement and included in its official file. Both the Feb. 3 and the Feb. 5 Agreement are referred to in the license granted to CET 21 and CEDC. |
| Feb. 9, 1993 | The Media Council issues the Czech Republic's first nationwide private television license to CET 21. The license acknowledges CEDC's "substantial foreign capital participation" and CEDC's partnership with the license holder. |

A Chronology of Events in the TV NOVA Scandal—Continued

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| April 1993 | CET 21 and CEDC agree on a Memorandum of Association ("MOA") for the creation of CNTS. Under the MOA, CET 21 contributes to CNTS the right to use the license "unconditionally, unequivocally, and on an exclusive basis"; CEDC contributes 75% of the capital that CNTS needs; and Ceska sporitelna ("CS") Bank contributes the remaining 25%. In return, CET 21 has a 12% interest in CNTS; CEDC has a 66% interest; and CS Bank has a 22% interest. |
| April 21, 1993 | The Media Council approves the MOA. |
| 1994 | CEDC transfers its interest in CNTS to CME. |
| Feb. 2, 1994 | CET 21 and CNTS begin broadcasting TV Nova, which becomes the Czech Republic's most widely watched and successful television station. |
| Late 1995 or Early 1996. | VZ approaches CNTS claiming that a modification of the MOA is necessary because as written it amounts to an illegal transfer of the license from CET 21 to CNTS. |
| Jan. 1996 | The Czech Parliament amends the Media Law to more clearly distinguish license-holders and service providers. |
| July 23, 1996 | The Media Council commences administrative proceedings concerning TV Nova, arguing that the arrangement between CME and CET 21 is impermissible. |
| Aug. 1996 | CME, at the request of CS Bank, acquires CS Bank's interest in CNTS. Resulting ownership of CNTS: CME = 88%; CET 21 = 12%. |
| Oct. 4, 1996 | VZ acknowledges, in a letter to the Media Council, that CET 21 "has no authorization" to broadcast without the "direct participation of CEDC," pursuant to the agreements reached when CNTS was formed. |
| Nov. 14, 1996 | VZ offers assurances that CET 21 and CME can change the language of the MOA to satisfy the Media Council without affecting business arrangements between the parties in any way. Following negotiations with the Media Council, CET 21 and CME modify the MOA so that CET 21 now contributes the "know-how" connected with the license, still on an exclusive basis. |
| February 1997 | CET 21 amends its Memorandum of Association to increase VZ's ownership interest to 60%. |
| Aug. 96-Apr. 97 | With VZ acting as an intermediary, CME purchases a 5.2% interest in CNTS from owners of CET 21. During this same time period, CET 21 owners pool an additional 5.8% interest in CNTS and transfer this to Nova Consulting. Resulting ownership of CNTS: CME = 93.2%; Nova Consulting = 5.8%; CET 21 = 1%. |
| May 21, 1997 | As a result of pressure from the Media Council and at the recommendation of VZ, CNTS and CET 21 enter into a Services Contract, which makes CNTS "the exclusive object of the rights and obligations arising during its activity." The contract provides that CNTS shall incur all costs of providing services to CET 21 and, in return, shall collect all of TV Nova's advertising, sponsorship and other revenues, with 100,000 CzK per month going to CET 21. |
| Aug. 1997 | CME considers taking CNTS public in the Czech Republic, but its advisers later recommend against doing so based on market conditions, the likely valuation of CNTS, and other considerations. VZ concurs in this recommendation. |
| Aug. 11, 1997 | CME and VZ enter into a Share Purchase Agreement, pursuant to which CME purchases for $28.5 million the 5.8% interest in CNTS held by Nova Consulting. In the discussions leading up to the Agreement, VZ threatens that if CME does not purchase this interest, he will transfer it to third parties of questionable repute. He also refuses to accept payment in CME shares. The agreement includes broad non-compete and non-solicitation covenants by VZ. Resulting ownership of CNTS: CME = 99%; CET 21 = 1%. |

A Chronology of Events in the TV NOVA Scandal—Continued

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| Sept. 16, 1997 | Acknowledging the execution of the amended MOA and the Services Contract, the Media Council dismisses the administrative proceeding concerning TV Nova. |
| Jan.-Apr. 1998 | AQS, a competing program acquisition company controlled by VZ, is established. VZ causes CET 21 to enter into an agreement with AQS for the purchase of foreign and domestic programs. |
| Sept.-Oct. 98 | VZ represents TV Prima, TV Nova's primary competitor in the Czech market, in discussions involving the possible acquisition of TV Prima by SBS Broadcasting. |
| Sept.-Oct. 98 | All employees in the CNTS program acquisition department move to AQS. VZ announces AQS as the "exclusive programme acquisition arm" for TV Nova, which would "fully replace CNTS." VZ issues an unauthorized guarantee from CNTS, securing all obligations incurred by AQS in connection with program acquisitions in the Czech Republic. VZ grants AQS an unauthorized power of attorney from CNTS to enter acquisition agreements. |
| Late 1998 | In negotiations with CME, VZ seeks to replace the existing Services Contract with multiple new services agreements limiting CNTS compensation for services provided to CET 21. |
| Mar. 3, 1999 | VZ writes to the Media Council asking it to confinn several legal opinions of CET 21, all of which relate to disputes between CET 21 and CNTS. |
| Mar. 15, 1999 | The Chair of the Media Council writes back to VZ adopting virtually all of the opinions in VZ's letter, including the assertion that relationships between a broadcasting operator and a service organization are built on a non-exclusive basis. |
| April 1999 | VZ personally signs and causes to be filed with Czech Trademark Registry nearly 200 certificates of transfer purporting to convey, from CNTS to CET 21, registered trademarks and applications for trademarks for various important products and services owned by CNTS. Upon objection by CNTS, VZ withdraws the certificates. |
| April 19, 1999 | VZ is dismissed as General Director and Executive of CNTS. |
| April-May 1999 | VZ works to establish a new company to provide CET 21 with services for the operation of TV Nova, making a public announcement of his plans at the beginning of June. |
| April 26, 1999 | VZ's attorney writes to distributors informing them that AQS is the sole program acquisition entity for TV Nova and stating that "[o]nly programming purchased by AQS, a.s. will be broadcast on the channel TV Nova." |
| May-June 1999 | VZ (personally and through his agents) solicits CNTS employees, telling them to tender their resignations before June 30, 1999, so as to be able to start work at VZ's new services company by September. |
| May-July 1999 | VZ (through his attorney) writes to CNTS stating that CET 21 should receive all of TV Nova's advertising revenue. VZ and his attorney threaten to dissolve CET 21's contractual relations with CNTS unless CNTS agrees to relinquish advertising revenues by August 15. |
| June 1999 | VZ unveils "magic contracts" (previously unknown to CME), including: (1) a purported Annex to the CNTS-CET 21 Services Contract, under which CNTS is only entitled to receive advertising revenues corresponding to the amount of services CNTS provides to CET 21; and (2) a "General Agreement on the Transfer of Copyrights" between CNTS and CET 21, which appears to have the purpose of allowing CET 21 to re-invoice CNTS for the fees paid to AQS for the purchase of programs. |

A Chronology of Events in the TV NOVA Scandal—Continued

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| June 10, 1999 .......... | VZ announces the establishment of Czech Production 2000 ("CP 2000"), a new services company formed for the express purpose of "stimulating competition" with CNTS. VZ obtains funding for CP 2000 through a loan from IPB Bank, a Czech Bank that owns the license holder for TV Prima. |
| June 11, 1999 .......... | CET 21 enters into an agreement to transfer its 1% interest in CNTS to Produkce, prompting legal action by CNTS. |
| June 12, 1999 .......... | VZ causes the TV Nova broadcasting signal to be diverted from CNTS studios during the "Call the Director" talk show, thus making it temporarily impossible for CNTS to broadcast TV Nova programming. |
| June 29-30 ............... | 147 out of 500 employees resign from CNTS. |
| July 1, 1999 ............ | VZ causes CET 21's Memorandum of Association to be amended; the intended result of the change was to reduce his control over the company. |
| July 1999 ................. | VZ and CP 2000 announce that they are nearly ready to take over CNTS' entire role in TV Nova. |
| July 20, 1999 ........... | The Media Council announces that no media laws have been broken to date in the dispute over TV Nova. |
| Aug. 5, 1999 ............ | VZ, citing the failure of CNTS to provide CET 21 with TV Nova's play list for that day, cancels the Services Agreement. VZ announces that he will henceforth broadcast TV Nova without CNTS and announces that CP 2000 is now purchasing advertising for TV Nova. (He later announces that yet another company, Mag Media 99, will assume these functions.) CNTS employees are idled. |
| Aug. 5, 1999 ............ | CNTS requests that the Media Council call an extraordinary session to address VZ's latest action. A representative of the Media Council publicly states that the Media Council intends to consider the dispute at its scheduled meeting on August 17, 1999. Despite this statement, the Council takes no further action. |
| Aug. 6 and 13, 1999 | CNTS again requests that the Media Council address the wrongful conduct of VZ and CET 21. Among other requests, CNTS calls on the Council to commence proceedings to revoke CET 21's license. |
| Aug. 23, 1999 .......... | Ronald S. Lauder, as a shareholder with voting control over CME, initiates an arbitration claim against the Czech Republic based on violations of the Bilateral Investment Treaty between the United States and the Czech Republic. |
| Aug. 23, 1999 .......... | The Chairman of the Media Council states that the dispute is merely a commercial matter that must be settled by the courts. |
| Sept. 9, 1999 ........... | As a result of VZ's repudiation and the Media Council's continued inaction, CNTS is forced to suspend its technical and production operations and dismiss over two hundred employees. Fifty more employees are dismissed several weeks later. |
| Nov. 10, 1999 .......... | The arbitral tribunal in CME's arbitration against VZ grants an interim order directing VZ to take steps to restore CNTS to its prior position as an exclusive provider of critical services for TV Nova. Among other things, the order requires VZ to sever all dealings between CET 21 and other service providers and to resume exclusive relations with CNTS in the areas where CNTS was previously providing these services, including program acquisition, programming and broadcasting services, and brokerage of advertising and receipt of advertising revenues. The order is to remain in effect until the tribunal directs otherwise. |
| Nov. 10, 1999 .......... | VZ begins a campaign trumpeting his refusal to comply with the arbitral tribunal's interim order. |

A Chronology of Events in the TV NOVA Scandal—Continued

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| Dec. 8, 1999 ............ | CME applies to the arbitral tribunal for a partial final award embracing the terms of interim order and imposing substantial fines against VZ for his non-compliance with the order. |
| Dec. 21, 1999 .......... | The Media Council approves a scheme to increase CET 21's share capital that is subsequently implemented by VZ and CET 21. As a result of the scheme, VZ's interest in CET 21 is reduced (at least on the surface) from 60% to 11.8%, while his close associates receive substantial interests in the company in exchange for token consideration. The Media Council grants the approval despite having received a copy of the tribunal's interim order, and despite the widespread understanding that the purpose of the scheme is to frustrate enforcement of the interim order by nominally divesting VZ of control over CET 21, and to shield his assets from any final award of damages. |
| Jan. 19, 2000 .......... | The Czech State Attorney's Office concedes that local police and prosecutors have improperly handled criminal complaints filed by CNTS concerning, among other things, VZ's fabrication of contracts purporting to transfer valuable CNTS assets to CET 21. At the same time, the Office denies it has any ability to direct the local offices to take further action. |
| Feb. 22, 2000 .......... | CME (as a Dutch entity owning an investment in the Czech Republic) initiates an arbitration proceeding against the Czech Republic based on violations of the Bilateral Investment Treaty between the Netherlands and the Czech Republic. |

Senator SMITH. Ron, that is an incredible story. I wonder if you can tell me, is our Government, our State Department beginning any of the steps you suggested? What efforts are being undertaken to sort of go above, I guess, what—the delay in the courts of the Czech Republic is, you are saying that is sort of indefinite.

Mr. LAUDER. I think the feeling of the Czech Government is that they do not fear the State Department. I think what we are seeing over and over again in Eastern Europe and other places is that if something happens to an American citizen, if he is put in jail, the State Department will immediately react. The reaction is quite different when it is something economic. So the question is, what can be done?

I know there have been many, many conversations the State Department had with the Czech Government in private. I think it is very important that it be said in public. Let us be a public example. Also, there is nobody, no citizen today in the Czech Republic that does not understand what is happening, and what happened to TV Nova.

Senator SMITH. Is this story about TV Nova widely known in the Czech Republic?

Mr. LAUDER. I would say that there is nobody in the Czech Republic who does not know the story. It has been carried on all the media. And what has happened is, they have said to themselves this government is no different from the former governments in that the rule of law does not apply. The right people are above the law. Everyone knows what happened. And they watch the U.S. Government not be able to make a change, and they watch the

Czech Government stand on the side. The Czech Government could change this instantly if they wanted to.

Senator SMITH. Your feeling is the popular opinion in the Czech Republic does not support what happens, but perhaps feels powerless to do something?

Mr. LAUDER. I think the Czech people want to see excellent television. And they do not care, frankly, who puts it on.

Senator SMITH. And they are not seeing that any more?

Mr. LAUDER. They are seeing excellent television, but it is being put on by a stolen TV station. The result is that they also have seen that somebody can ignore the law and be successful. It sends a message. It sends a message not only in the Czech Republic, it sends a message throughout the region, and I think that is the critical element.

And frankly I think that in this region I am probably one of the best-known people because I have been there first. And I believe if this could happen to me, then it could happen to many, many other companies and probably has. They have been either too small, or they have had such excellent business elsewhere to complain about it. But I believe if it is happening here, it is happening all over.

Senator SMITH. So you are not here to recommend more U.S. investment in the Czech Republic today.

Mr. LAUDER. I am here to recommend that the State Department—I heard a few minutes ago about the CEPA, I guess it is called, where the State Department is recommending giving even more favorable terms to that region. I think instead of rewarding them for what they are doing they should be—in fact the money should be cut back from them.

I think at the same time that they are not following the rule of law, it is a mistake to be putting money into EBRD and putting money into one thing after another, funneling money into it. We, after all, watched what happened in Russia sometime ago. This is similar things happening on a smaller scale in the Czech Republic.

The person from the State Department spoke about a bank that just failed. The reason why that bank failed is—it is called the IPB bank—was that money was tunneled out of it. It was taken out. Literally, one asset after another was tunneled out, with the government's knowledge, and the bank failed.

Again, there are many other examples.

Senator SMITH. It is interesting, we received from the Czech Embassy an article today that was run in the Financial Times in the Czech Republic, and it says growth was driven by exports to Western Europe as well as the first increase in fixed capital investment for 11 quarters. Economists said foreign direct investment was the force behind both developments, with a record inflow expected again this year, after last year's $4.8 billion, the highest per capita figure in the region.

And there is a quote, "we are still living in a two-speed economy. One part is on the brink of bankruptcy, but a rising group of companies with the help of foreign investors are now performing reasonably well," and I will include that for the record.

[The article referred to follows:]

[From the Financial Times (U.S. Edition), Tuesday, June 27, 2000]

CZECH RECOVERY HOPES GROW

(By Robert Anderson in Prague)

The Czech economy is on the road to recovery, gross domestic product figures showed yesterday, with strong west European demand and record foreign direct investment making up for weak consumer spending and long-delayed corporate restructuring.

GDP increased by 4.4 percent year-on-year in the first quarter—double that expected by many economists—representing the first robust period of growth since the economy began to pull out of recession in spring last year. Compared to the previous quarter, seasonally adjusted GDP grew 1.3 percent.

Alone among the leading economies of central Europe, the Czech Republic went into recession in 1998-99 after a currency crisis and subsequent tightening of monetary and fiscal policy exposed and intensified structural problems in the financial and corporate sectors. Yesterday's figures give hope that the economy will converge with the European Union, rather than fall further behind.

However, economists warned that overall growth this year was still likely to reach only 2.5 percent at best because the rise in the first quarter was exaggerated by the low base last year, more working days and increased inventories.

“There are some positive signals but I would not dare in saying that we are back on track for strong sustainable growth,” said Pavel Sobisek, chief economist of Bank Austria Creditanstaft.

Growth was driven by exports in western Europe as well as the first increase in fixed capital investment for 11 quarters. Economists said foreign direct investment was the force behind both developments, with a record inflow expected again this year after last year's $4.88bn, the highest per capita figure in the region.

Although there is no sign yet of overheating, economists said the precarious state of many large corporates and banks—as well as institutional deficiencies such as the poor legal framework—would continue to hamper growth.

“We are still living in a two-speed economy,” said Mr. Sobisek. “One part is on the brink of bankruptcy, but a rising group of companies, with the help of foreign investors, are now performing reasonably well.”

Kamil Janacek, chief economist of Komercni Banka, said the credit squeeze and recession had accelerated industrial restructuring, with productivity now rising four times faster than real wages. This should help growth next year reach up to 4 percent. “From next year there is a strong probability we will again be catching up with the EU,” he said.

Senator SMITH. Ron, thank you, and we will use the influence of this committee to try and spur the interest of American citizens and to make sure that everybody plays by rules that we recognize as Western and as honest and available to the light of day. Those are the things that will either advance world prosperity or retard it, and we wish it to be advanced everywhere in Eastern and Central Europe.

Mr. LAUDER. All we want is transparency and the rule of law and, frankly, our station back.

Senator SMITH. And anything less than that will lead us backward.

Mr. Jenkins, welcome, sir.

## STATEMENT OF MR. KEMPTON JENKINS, PRESIDENT, UKRAINE-UNITED STATES BUSINESS COUNCIL, WASHINGTON, DC

Mr. JENKINS. Mr. Chairman, thank you very much. It is a poignant moment for me to be back in this august chamber. I first came here to argue with Senator Fulbright about maintaining Radio Liberty and Radio Free Europe. That was a few years ago, as you can imagine.

I also want to take note immediately of your comments about the Department of Commerce's absence, which I deeply regret. I used to direct that part of the Commerce Department, and I know there is a great reservoir of talent and knowledge about Central Europe. It is their prime responsibility, not the State Department's, to deal with business disputes, commercial disputes such as Ron has experienced, which are not unique. What he describes is particularly gruesome, I think, but there are similar tales throughout the area.

I also want to comment on European Union pressure on the countries of the area. I have experienced that in all of the various responsibilities I have had in that area over the last 20 years. It is common practice for these governments to be told by the Europeans, in some cases rather bluntly and in others rather delicately, that you had better remember which side your bread is buttered on when it comes to letting these contracts.

I know that IBM had problems in Poland, and certainly I have run into this in the Ukraine, where Ukraine, which aspires to be an EU member, has been told in various ways in various cases that these contracts better go to German or French companies, not American companies. I guess that is competition. I do not like it very much, and I am delighted that the State Department representative said that they do weigh in and are weighing in with the EU.

I am not sure that it does not need a somewhat higher level initiative on our part to be sure that it gets the attention it deserves. After all, we may be engaged in a more modified effort to improve conditions in Eastern Europe today, but we were the givers of the Marshall Plan who put the Europeans in business, and occasionally I think they need to be reminded of that.

Having said that, I want to introduce myself briefly, and then I will make a few comments and submit my full statement for the record.

Senator SMITH. We will receive that, and we thank you, and just for your notice I am told there are four stacked votes beginning at 3:30, and that is 20 minutes away, which probably means we have about 30 minutes for the balance of the hearing.

Mr. JENKINS. I will try to leave half of that for Peter.

I am Kempton Jenkins, president of the Ukraine-U.S. Business Council. We have some 40 major U.S. corporations who are doing or trying to do business in Ukraine. Our members have had very varied experiences in Ukraine, which illustrate both the potential of this entire rich market and the barriers and the frustration of bringing that potential to fruition.

Ukraine is a country of 51 million people. It is 95-percent literate. It possesses what is agreed to be the richest farm soil in the world, and it has long experience as the Soviet Union's aerospace center, with a concentration of scientific talent.

Today, it is led by President Kuchma and Prime Minister Yuschenko, and for the first time in its history a majority in the legislature who are all committed to economic reforms. This triad of political leadership came into being in December and we have seen some very significant progress already and are very hopeful that we are looking at the kind of blossoming in Ukraine which the State Department representatives spoke of.

Prior to becoming president of the council, I was a consultant to the Government of Romania, which had many of the same problems, and I worked on them to try and get them to introduce the rule of law and transparency and predictability and so forth. I was a corporate vice president of ARMCO, which is a major American steel company, for 10 years and I was president of the former U.S.-Soviet Trade Council when I first left government in 1980. For 30 years prior to that I was a career Foreign Service officer, with more than 15 of those years dealing with the Soviet Union and Eastern Europe.

In my written testimony I lay out both the region-wide barriers and, in discussing Ukraine specifically, I provide individual company-by-company score cards for some of the successes and some of the failures, and there are many of both.

I am heartened by the successes, and I am discouraged by the failures, but we have a very good ongoing dialog with the Ukrainian Government and with the U.S. Government, and I am optimistic that we are going to continue to see success outnumber or eventually overcome the failures.

From my perspective, which is fairly broad and long, I believe that Central and Eastern Europe today offer a very rich opportunity for us to participate in the inevitable development of these economies into a truly prosperous area. It seems clear that it is very much in the national interest of the United States to see that happen. After decades of irrational economic policies, it is hardly surprising to me, and what Ron is experiencing and I gather Peter, too, would have been almost predictable.

The road to progress is erratic. It is going to be rocky. It is, after all, only a decade since the Soviet Union collapsed, and that is not much time for a transition from Marxism-Leninism to free markets.

We believe, and I think I speak for all of my corporations, and I know it is generally agreed within the U.S. Government, that it behooves us to stay the course. Certainly our members share the expectation that there is great potential out there. I would like to simply stress a few additional points, and then let the record speak to the details.

I want to praise the committee for its decision to focus on this critical part of the world and the recognition that foreign investment and the conditions which promote foreign investment are, in fact, critical and central to the progress we want to see in Central and Eastern Europe. Without it, in my judgment, and I think everybody would agree, there is little hope for real democracy, and all of the conditions that that means, to grow.

There is a stark difference between individual countries. This is not one area with a uniform set of problems. There is a set of problems, and they do occur. Frequently they occur in one country or another, or eventually in all of them, but there is a big difference in the success and the progress they have made.

I am distressed to anticipate what Peter's problems in Poland may have been, and certainly the Polish performance in the EU question, where they have been really pretty aggressive, because they have had a dramatic economic recovery, and comparing that to Byelorussia gives you the parameters of the development in the area.

Byelorussia is still in the 18th century at this point, and I do not see much hope under the present political leadership, but the Poles really have accomplished a great deal, and their economy has really grown a lot. The standard of living is up. Politics are more open, predictable, and democratic.

I think it is also important to stress that we are talking about investment, not domestic or foreign investment. Both are necessary. If you have the rule of law in the Czech Republic you will have Czech capital return to the Czech Republic. There is more money out there for these countries which has flown from them, especially in the case of Russia, than the international institutions or the meager AID budget can ever provide to these economies, so investment conditions both domestic and foreign are what we are talking about.

Senator SMITH. You really cannot fool the marketplace. That is the thing I continue to impress upon European leaders. You cannot kid the market. It will react and it will move if you do not have transparency and a rule of law, things that we just take for granted, but unfortunately that lesson has yet to be learned, I guess.

Mr. JENKINS. Well, that is one of the points I wanted to make. It is very difficult for these countries and the leaders of these countries, and I know several of them, to really ingest the reality that they are competing with Mexico and Brazil and Korea. They are not just competing with Hungary and Bulgaria. They come from such sheltered or limited backgrounds that they have not really developed an appreciation of that yet. It is coming. It takes time, and implementation is much more difficult than actually understanding it.

President Kuchma in Ukraine fully appreciates this fact today, and he is driving very hard to implement that understanding within Ukraine. It is taking a long time, but today's Ukraine is only 9 years old, and I think we have to keep that in mind.

The other side of this is that Ukraine is also a huge marketplace and in potential value to the United States and the American business community it far exceeds a number of markets in the rest of the world, where we tend to concentrate our activities today. So I think Ron's foresight in moving into the television market in that part of the world is to be commended, and notwithstanding your Czech experience Ron I hope you are still there. During President Clinton's recent visit to Kiev, his speech was carried on the television station you have an investment in.

Senator SMITH. It is to be commended not to be confiscated.

Mr. JENKINS. That is true. I think it is very important also to recognize that these markets are not for the timorous or short-term investors.

Senator SMITH. Can you tell me, Mr. Jenkins, in your opinion would it be productive or unproductive for us to grant permanent normal trade relations to Ukraine?

Mr. JENKINS. I am glad you raised that. I was going to raise it if you did not. I think it borders on the obscene that we have played such a political game with this issue. I think it is very important to recognize and acknowledge and graduate countries who in fact have lived up to the purpose of the Jackson-Vanick amendment which was passed on my watch in the State Department. I understand it completely. It played a constructive role at a certain point.

Today, Ukraine is as free of anti-Semitism as the United States is, in my judgment, and I think that needs to be acknowledged. Not a lot of trade hard dollar effect would occur from this. President Kuchma when he was here 8 months ago met with members of the House International Relations Committee. He said, I am embarrassed that here we are, an outpost of democracy in Central Europe, but we are still treated as though we were North Korea.

I am disappointed the President did not take that "deliverable" with him when he went to Kiev. I think it is very important that we step up on that subject and move it. I know there is support. I have talked to members of the House Ways and Means Committee. I have talked to Members on the Senate side, and my hope is that this will happen quickly, but the administration should take the lead. I think what they are doing is playing a little bit of politics. They do not want to irritate Moscow by giving permanent MFN to Ukraine first.

Moscow continues to have a serious problem with anti-Semitism, Ukraine does not, and I think it would incentivize the Soviets—the Russians, excuse me, or the Soviets within Russia who continue to pursue these terrible policies to see Ukraine acknowledged by the United States. It is not a reward, it is an acknowledgement, and so I am pleased you raised that. I firmly believe that is a desirable thing to do.

Let me quickly wrap up, if I might, sir. I think basically these markets are worth the candle. I do not think we cannot be there. I think American corporations generally have recognized that. I think it is important to be very hard-nosed and gradual in the approach. Go in small. Develop relations. Train a staff. Make a small investment and then grow it.

People who go in with a $300 million investment are going to lose their shirts.

Senator SMITH. You make an interesting point that we need to be in there. Do they know we need to be in there, and does that work to our disadvantage in their knowing that?

Mr. JENKINS. I think that varies from country to country. I think the new members of NATO are now so self-satisfied that they have made the cut that they do not have that same urgent feeling of how important it is for the United States to be actively participating in their investments. In the Ukraine, that is not true.

Senator SMITH. The point you make I wish I could broadcast to the whole world, or at least all of Eastern and Central Europe, is that they are competitors for American capital. I mean, it is Brazil, it is Mexico, it is everywhere that you have an emerging economy.

Mr. JENKINS. Well, I am convinced that on the whole we are on the right path. I think the policies and actions and implementation thereof by our own administration in partnership with you, the Congress, could be more effective.

As Ron pointed out, he has found the State Department's representation a little too delicate to be effective, and I think that simple bureaucratic contradictions and policies and legislation reflecting our own domestic political interests frequently combine to undermine our overriding national security interest in the economic development of the area. My hope is we can improve the coherence of this policy and our resources and harness them more effectively to promote the investment climate in the entire area.

From our vantage point U.S. programs today are too diverse. They are seeking a wide range of desirable goals, from democracy and gender equality to child labor laws, environmental and education goals. In reality, the climate for such societal improvements must be based on economic progress, for which investment both foreign and domestic is central, and I would like to see—there are a number of steps other than permanent MFN I would be happy to talk about, but for Peter's sake I am going to save some time.

[The prepared statements of Mr. Jenkins follow:]

### Prepared Statement of Kempton Jenkins

#### INTRODUCTION

Mr. Chairman, I am Kempton Jenkins, President of the Ukraine-U.S. Business Council, a group of some 40 major U.S. corporations doing or hoping to do business in Ukraine. Our members have had varied experiences in Ukraine which illustrate both the potential of this entire rich market and the barriers and frustration of bringing that potential to fruition. Ukraine is a country of 51 million people, 95% literate, possessors of what is agreed to be the richest soil in the world, and with a long experience as the Soviet Union's aerospace center with its concentration of scientific talents. And today is led by President Kuchma, Prime Minister Yuschenko and for the first time a majority in the legislature all committed to economic reforms.

Prior to taking the chair as President of the Council, I have been a consultant to the Government of Romania, Corporate Vice President of ARMCO a major American steel company, President of the former U.S.-Soviet Trade Council, and for 30 years, a career Foreign Service officer with more than 15 of those years dealing with the USSR and Eastern Europe.

I firmly believe from this perspective that Central and Eastern Europe offer a rich opportunity for U.S. and other Western corporations to participate in the inevitable development of these economies into a truly prosperous area. It seems clear that it is very much in the national interest of the United States to see that occur. However, after decades of irrational economic policies, it is hardly surprising that the road to progress now is erratic and often very rocky. It has only been a decade since the Soviet collapse—for a transition from Marxism—Leninism to free markets. We believe it behooves us to stay the course. Certainly our members share the expectation that there is eventually a bright future.

I would like simply to stress a few additional points and submit my detailed statement for the record.

I want to praise the committee for its decision to focus on this critical part of the world and implicit recognition that foreign investment, and the conditions which could create incentives for investment constitute the most important key to producing viable, democratic members of a new Europe. Without such investment, critical economic development will continue to lag, and political commitment to democracy will continue to be frustrated.

#### TREATMENT OF U.S. BUSINESS—INVESTMENT CONDITIONS—VARIES SHARPLY AMONG THESE COUNTRIES

A stark contrast between Poland's unprecedented economic development today and the stagnation in Byelorussia serve to emphasize this point: Investment is the cardinal requirement for genuine economic development. Governments do not invest, corporations do. The countries of Eastern Europe and Central Europe succeed to the degree that they effectively establish business conditions which attract corporate investment, both foreign and domestic.

These nations are in fact in an intense global competition—to-date few have acted to aggressively engage, such as Poland has so successfully done.

*Long-Term Outlook Essential*

Engagement in these markets is not for the faint-hearted nor short-termers. Predictability and transparency run directly contrary to the Soviet culture which prevailed for decades. Western and especially American businessmen are too prone to continue to pick a favorite politician in a given country—a president who is accessible, while ignoring the emerging array of businessmen and even legislators who represent the future—in short, the need to build a diversified business presence is very important.

*U.S. Corporations Much More Sophisticated Today*

Fortunately, U.S. corporations today are sophisticated and far-sighted, in contrast to 20 years ago when as a U.S. Government official I found our timorous companies often out-strategized by European and Japanese competitors who inevitably benefited from their governments' subsidies. Generally speaking, there is now recognition that one must start small, build ties and access, create local management structures and plan in a multi-year framework.

*Challenges Not Really a Lot Different Than in Today's Third World Market*

It is important for us to recognize, as corporations have, that the barriers and frustrations we experience in Central Europe, are often even worse in other major markets where they have been operating—e.g. India, Indonesia and Brazil.

Finally I wish to say that it is my firm belief that these markets are decidedly worth the effort. As illustrated by Ukraine, basic positives are impressive—large educated population, strategically located and rich in natural resources. U.S. Government policy can effect the problems at the margin, and more could be done. But, I believe we will see economic progress in these countries, undergirding democratic regimes which become valuable members of Western Society. And I believe U.S. business will play a critical role in producing this happy result.

In closing, Mr. Chairman, it is also my judgment that the policies, actions, and implementation there of by our Administration in partnership with our Congress could be more effective. In some cases simple bureaucratic contradictions and in others, policies and legislation reflecting special domestic political interests, often combine to undermine our overriding national security interests in the economic and political development of this critical area. My hope is that we can improve the coherence of our policy and our resources and harness them more effectively to promote the investment climate for the entire area. From our vantage point, U.S. programs today are too diverse, seeking a wide range of desirable goals, from democracy and gender equality, to child labor laws, environmental, and education goals. In reality the climate for such societal improvements must be based on economic progress for which investment both foreign and domestic is central.

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## Additional Statement of Kempton Jenkins

### INTRODUCTION

Mr. Chairman, I am Kempton Jenkins, President of the Ukraine-U.S. Business Council, a group of some 40 major U.S. corporations doing or hoping to do business in Ukraine. Our members have had varied experiences in Ukraine which illustrate both the potential of this entire rich market and the barriers and frustration of bringing the potential to fruition. Mr. Chairman, Ukraine is a country of 51 million people, 95% literate, possessors of what is agreed to be the richest soil in the world, and with a long experience as the Soviet Union's aerospace center with its concentration of scientific talents.

Prior to taking the chair as President of the Council, I have been a consultant to the Government of Romania, Corporate Vice President of a major American steel company, President of the former U.S.-Soviet Trade Council, and for 30 years, a career Foreign Service officer with more than 15 years dealing with the USSR and Eastern Europe.

We firmly believe that Central and Eastern Europe offer a rich opportunity for U.S. and other western corporations to participate in the inevitable development of these economies into a truly prosperous area. We also believe that it is very much in the national interest of the U.S. to see that occur. We also are convinced that the barriers and frustrations which I now concern myself with in Ukraine are often common to the rest of the former Soviet Empire. After decades of irrational economic policies, it is hardly surprising that the road to progress is erratic and often very rocky. I believe it behooves us to stay the course and certainly our members share the expectation that there is eventually a bright future in front of us.

## A TOUGH MARKETPLACE

Business problems, opportunities and successes in the entire area are products, above all, of the historic emergence of new independent states from the Soviet cocoon. It should not be a surprise to anyone that it is not easy!

First, the former pieces of the Soviet Empire both historically independent East European countries and the newly independent former autonomous republics of the USSR itself are a collection of widely varying governments, natural resources, cultures, and economies. There is no single formula or laundry list which applies to all of them.

Second, notwithstanding these wide disparities, and the historic adjustments involved, the entire area is a very important economic piece of the global economy and offers perhaps more potential for growth and progress than much of the rest of the world.

Third, U.S. corporations today are a far cry from 20 years ago when I was working with them in dealing with the Communist world. U.S. corporations are now sophisticated and strategically wise, a far cry from 1980 when most corporations looked at "long-term" as two years or in some cases three quarters! We have globalized perhaps better than others, even though we started out well behind traditional European and Japanese trading companies.

Fourth, this means that while U.S. corporations are not going to jump in with large initial investments in recently converted Communist economies, they are also not going to walk away from Eastern Europe which has obvious lucrative potential: educated populations, rich natural resources and impressive industrial know-how (even though it is often encrusted with decades of Soviet mismanagement). U.S. corporations have demonstrated impressive staying power in the entire region.

Finally, it is very important to keep a realistic perspective on the market choices U.S. corporations face in the global market place. Dealing with the full array of barriers, problems and downright hostility is not new to U.S. corporations. They have coped with unpredictable and often bizarre behavior in countries like Brazil, Indonesia, and India; all of which are major markets which cannot be ignored, but which have always been very frustrating places to do business.

And, if in acknowledging the traditional difficulties in these third world major markets isn't enough, think for a moment of the myriad difficulties U.S. companies have trying to do business—bid processes, zoning requirements, petty corruption, licensing and inspection barriers, supplier uncertainty and Government intervention, in the U.S. Try dealing with local, state and federal officials on a port, housing or agriculture project in New Orleans, Newark or Las Vegas or any other major city in the U.S.

## COMMON PROBLEMS

### *Soviet Mentality*

To obviously varying degrees among these countries in the area the basic instinct to preserve "Government Control" has made Western investment impossible at worst or very slow at best. Letting "the market decide," especially in the politically sensitive area of resource allocation, is a new concept and often perceived as unfair and contrary to political stability (reads control).

### *Nationalism*

Where the Soviet collapse has created a vacuum, the old centralized non-market culture has often found a new political basis in old-fashioned nationalism—protect our home industries, don't close facilities because workers will lose jobs, do not permit foreign ownership in general especially of our land, telecom and basic industries.

### *Natural Resources*

Raw material costs have no predictable supply and demand basis because there has been no marketplace to provide it. U.S. companies agree that the single most powerful market factor for Ukrainian consumers is price. Coca Cola, an initially great sales success, has steadily been undermined by lower cost and inferior concentrate so that, today other (inferior in quality in the eyes of consumers) beverages are taking market share from Coca Cola even though Coca Cola is preferred by consumers.

Costs in genuine market economies are more or less predictable, permitting producers to set price and plan ahead. In traditional non-market economies there is little concept of pricing based on cost and supply and demand. This is a hard lesson to learn and clearly it is taking time to imbue these concepts.

*Labor*

Often underestimated, labor skills in most of the former USSR and Eastern Europe are impressive and can be a significant advantage for Western companies. On the other hand, Soviet labor practices created a solid tradition based on security not incentives and today in most of Eastern Europe it is extremely difficult, if not impossible, to pare back on labor costs. Instead U.S. companies are faced with the ingrained expectation that the government (or employer) will provide all basic needs such as housing, health care, and transportation as well as job security. This expectation is changing, but slowly.

There are numerous, encouraging examples of the value of young skilled technical workers providing excellent bases for new entrepreneurs. The renowned Hugo Boss clothing company now provides a significant share of its "up-market" clothing in Ukraine for its international market. An American investor recently told me that he has found that for top quality, low-cost software engineers, Kiev is the place to be. Computer parts producers are finding Bulgarian labor a real "gold mine" in their words. In short, the younger workforce is potentially a major asset.

*Management Skills*

Most U.S. Companies throughout the area are finding it very difficult to build mid-level management. Virtually none of the 35-55 year old pool while technically impressive has the managerial instincts required to produce on the basis of market demands, or develop such things as advertising programs based on market surveys.

Many companies are hard at work developing in-country training programs and in some cases bring mid-level and upper-level people to the U.S. for training. These programs obviously are the road to long-term success, but take time. Generally, young managers from Eastern European countries are quick to learn and clearly more adept than most of their third world counterparts, reflecting the superior technical education traditions in their countries. On the other hand senior management people have much more to overcome and often are less successful in making the transition.

I must point out that U.S. company training programs are complicated and even aborted by arbitrary U.S. consular treatment of visa applications for trainees, especially for young, promising women. I fully appreciate the immigration legislation restraints on American consular officers—I was a vice consul in my first foreign service assignment in 1951 and had to deal with waves of displaced persons from Central Europe. However, there is clearly a need for reform of Administration guidelines and the mentality of our consular officials which often exceed legislative requirements in order to appear "tough" to the home office. U.S. policy to promote investment in these countries needs to extend down to the consular appreciation of the value of business training exchange.

*Financial Infrastructure*

Few Eastern or Central European countries began the last decade with viable commercial financial institutions in place operating under the rule of law. Central Banks were traditionally relatively well-connected with their Western counterparts and viewed as islands of "business and financial wisdom" in the otherwise dismal economic landscapes of Eastern European countries. However, commercial (as opposed to macroeconomic) financial capacity was virtually non-existent.

To varying degrees progress is unfolding in this arena, but once again this is a subject which requires decades not years. And, in this area, the former Soviet Empire is generally behind other third world countries. It will be years before Ukraine and other former Soviet Republics have established fmancial services in place. It is no accident that much of today's news regarding oligarchs, corruption and scandals in Russia and Central Europe centers on new bank based empires.

*Lack of Other Internal Business Structure*

In most of the area, acceptable hotels, airline connections, telecommunication, and adequate clerical help was not available as the decade of freedom began. Today in the more successful countries, four and five star hotels have sprung up, modern telecommunications and bilingual support staff are available as well. However, there is a wide disparity in availability of these services. In Ukraine, e.g., there is a good pool of bilingual support staff, but no adequate hotel accommodations. Most of the countries have adequate airline connections, but not all. These factors may seem frivolous or bordering on "pampering U.S. executives." However in today's highly competitive global market place, U.S. companies which have pared down their executive staff to a Spartan level, consider "executive time" a critical factor in investment decisions. What Vice President will choose to visit a Central Asia capital if it is just as important to visit Sao Paulo? As a practical matter, selections for investment are often influenced by these amenity factors.

In practice the creation of reasonable hotel facilities has proven especially subject to corruption and mismanagement. Power struggles and the appetite for "a piece of the pie" have blocked or delayed many obviously necessary hotel projects throughout the area.

*Corruption*

I give corruption a special section because symbolically it is so critical. Even though "corruption" is a challenge for businesses everywhere—including the U.S.—the extent and intractability of corruption in the former Soviet Republics is one of the first things one hears whenever business conditions are discussed. And, it is generally perceived by businessmen that "corruption" is very serious and largely uniform throughout the former Soviet Union. In the Eastern European countries the problem while present is considered less of a problem.

It is important to point out that corruption covers a wide range of activities of varying seriousness. In some cases there is an actual concern for individual safety. In some cases businessmen have been roughed up by hired hooligans. More often the traditional shake down process to compensate for pitiful salaries among customs, licensing, and tax authorities and even senior officials is the problem. Oddly, IMF and World Bank constraints have often worked against needed salary increases, thereby unwittingly contributing to continuation of petty corruption.

*Arbitrary Political Leadership*

American and other Western businessmen are not unacquainted with the challenges in doing business in countries ruled by corrupt, violent and unpredictable despots. Sukarno's Indonesia, the Shah's Iran, Papa Doc's Haiti, Merciar's Slovakia and Lukashenko's Byelorussia illustrate the international nature of the problem. Suffice it to say the "the personna at the top" is a very serious factor. Shervardnadze clearly is a major factor in attracting what little foreign investment has occurred in Georgia. There is undeniably an immeasurable value to a country's appeal to Western investors if the national leader is respected and considered to be an effective executive as well as a true patriot—if he is also committed to Democracy, that is icing on the cake. Ukraine is fortunate in this regard.

AS AN ILLUSTRATION, LETS LOOK AT UKRAINE

In November 1999, Ukraine reached a watershed point in its 9 year independent history. President Leonid Kuchma faced off—head to head—with the leader of the Communist Party. Notwithstanding a discouraging 9 year history of steadily declining standards of living, the people of Ukraine rejected the Communist appeals to turn back to Soviet "good old days" and re-committed Ukraine to a market economy and democracy.

President Kuchma, fresh from his solid victory, committed Ukraine to a new beginning and selected Central Bank President Viktor Yuschenko—a highly regarded reformer—as his new Prime Minister.

In the first 6 months since the "new beginning" Ukraine has racked up impressive increases in economic activity in the first quarter including:

a. Capital investment has grown 26%;
b. Individual savings are up 130%;
c. Hard currency investment is up 20%;
d. GDP is up 5.5%; and
e. Industrial production is up 10%.

In addition the following reforms have moved ahead:

- Most important, the creation of a pro-reform majority in the legislature (Rada) and election of a new Speaker (Plyuishch) and Deputy Speaker (Medvechuk) who support Kuchma's reform agenda was accomplished;
- The new Rada majority now includes key committee chairmen who are themselves businessmen and are committed to attracting investment;
- Major Government restructuring was implemented. A consolidation of Ministries, (35 to 17) has reduced bureaucratic delays and tempting opportunities for corruption;
- Combination of licensing and registration functions under new leadership was carried out;
- A Presidential decree was issued abolishing remaining collective farms, privatization of grain silos has advanced and is now virtually complete. Past farm debts to the government were forgiven;

- The new Rada passed a new balanced budget consistent with IMF standards;
- The Prime Minister succeeded in restructuring the commercial debt with 100% subscription by Ukraine's commercial lenders;
- The Rada, on May 18, adopted the enabling legislation (with U.S. participation in the process) for oil and gas exploration profit sharing by a solid majority vote;
- On May 4, the administration submitted a major revision of the tax code to the Rada which would dramatically reduce and simplify tax rates and presumably lead to a significant increase in tax collection;

  The current tax code was a historic break with the Soviet past. It is considered compatible with European codes and has produced some increases in collections (47%). The new draft code which would have been "dead on arrival" in the old Rada, has a good chance to make it through the new reform minded Rada and could add significant momentum to other economic improvements which we have already seen.

UNFULFILLED GOALS—AGRIBUSINESS OPPORTUNITIES AND CONSTRAINTS IN EASTERN EUROPE

(The non-profit agriculture investment organization Citizen's Network for Foreign Affairs has assisted in the preparation of this section.)

The markets of Eastern Europe, including Russia and Ukraine, represent unprecedented opportunity for American agri-businesses, particularly U.S. manufacturers of farm equipment, crop protection products, seeds and food processing equipment. In Russia and Ukraine alone, the market potential for large tractors and harvest combines is enormous. It is estimated that for farm equipment suppliers, even for the replacement of decaying field inventories only, these two markets present a potential for 53,000 tractors and an estimated 14,000 combines, figures in excess of current U.S. production. The potential annual market for seeds, fertilizers and crop protection products runs anywhere from 6 to 10 billion dollars annually. Yet, with the exception of Hungary, the promise of these potentially huge markets lies largely unfulfilled.

The lack of privatization and reform in the agriculture sectors, the lack of privatization of land and the restructuring of farms, corruption, price controls, inept and ill-advised tax policies, and the lack of credit and fmancial institutions have largely left American companies not only frustrated, but in some cases the recipients of substantial accounts receivable. In Ukraine alone, American manufactures of crop protection products are facing bad debts amounting to over $150 million.

This lack of reform which has limited the prospects of U.S. agribusinesses has also resulted in depressing agriculture production, particularly in Russia and Ukraine, greatly limiting these countries' prospects for economic growth as well as threatening political stability. Russia today is a recipient of U.S. food aid, and Ukraine, once known as the bread basket of Europe, is producing at less than one fifth of its potential and is facing the prospect of its worst harvest since 1945.

Chief among the limitations facing American agribusiness companies is the lack of access to adequate short- and medium-term financing, whether through commercial finance channels or through guarantees. While the U.S. ExIm Bank has provided some financing backed by sovereign guarantees, it has been woefully inadequate and has been essentially limited to two transactions. Local commercial bank financing is also nonexistent, and the farms themselves remain essentially unrestructured and often bankrupt.

The lack of farm restructuring, as well as the lack of privatization of state input supply, has also been a severely limiting factor. Land, largely still in the hands of collective agriculture enterprises, cannot be bought or sold and, importantly, cannot be used as collateral. What bank can lend where it cannot protect its exposure?

In Ukraine, commercial finance in the agriculture sector simply does not exist, and the banking sector is weak and undercapitalized. Interest rates are upwards of 60% and multi-year midterm finance (three to five years) essential for financing large scale, high-priced equipment such as tractors and combines is totally unavailable.

In Russia, the 1998 financial crash all but wiped out the few banks engaged in providing agriculture loans. SBS Agro, the largest agriculture bank, is essentially in government receivership, and the relatively small financing provided by the government was decimated by the ruble devaluation.

Also, U.S. agribusiness companies which have sought to finance sales through commodity backed contracts where payment is made through agriculture production have seen these efforts largely fail because of high risk, high cost, as well as government interference and corruption. This has particularly been the case in Ukraine where the govermnent proclaimed supremacy in its claims on agriculture production and has essentially confiscated production committed to the repayment of American suppliers.

Ukraine has recently further limited the viability of commodity backed credit transactions through ill-timed and unwise tax policy. In order to protect a small number of politically well-placed owners of Ukrainian sunflower processing facilities, Ukraine last year implemented a 23% tariff on the export of sunflowers. The chilling effect on all commodity backed credit transactions was substantial. The export of sunflowers had been Ukraine's largest cash crop, and had been the source of currency needed to pay U.S. and other Western suppliers. Also, the tax has depressed sunflower production as farmers have been forced to absorb the tax.

Similar situations have occurred in Russia where local oblast governments have restricted the movement of commodities that have left U.S. companies unable to export part of a crop as a method to pay for inputs and equipment they have provided.

While arbitrary export taxes have hindered the ability to earn hard currency to pay for imports of equipment and farm inputs, other flawed tax policies continue to impede investment. A critical issue, for example, is the VAT tax that in Ukraine is 20% and which applies up front to the purchaser. This substantial penalty upon the purchaser has had a chilling effect on the potential sales of high-ticket agriculture equipment. The fact that these taxes apply to the import of "the means of production" and that purchasers have to pay "up front" and are not allowed to amortize over a three to five year term is a significant hurdle.

The lack of privatization of state input and commodity monopolies has also hindered opportunities for U.S. agribusinesses particularly in Ukraine. Though headway has been made in recent months with the privatization of grain storage facilities, the continued existence of the Government monopoly, which attempts to maintain its control over the distribution of commodities such as wheat, hinders competition and threatens the emergence of new private distribution structures as well as processors.

Prime Minister Yuschenko last week announced that the Government of Ukraine will place top priority on agricultural reforms in the second half of 2000.

### INTERNATIONAL MONENTARY FUND

IMF assistance is critical to the efficacy of the often tough reforms which are essential in the massive economic re-structuring of the former Soviet empire. Russia is the most dramatic illustration of these difficulties which have produced repeated suspensions of credits. The IMF continues today to be central to Russia's economic struggles. Ukraine's dependence on the IMF, like Russia and much of the region, is also central.

Late last year, the IMF e.g., was seized with the problem that Ukraine's National Bank (then led by current Prime Minister Yuschenko) had misstated its reserves in order to meet IMF hurdles for additional assistance to Ukraine. As a result the flow of IMF funding has been suspended while an independent audit was undertaken. The results are awaited.

### ILLUSTRATIVE SPECIFIC PROBLEMS

While there is growing recognition of the importance of this major market, corporate strategic vice presidents are all too often disheartened, frustrated and cynical about promised reforms. To take Ukraine, again, as an illustration, a partial list of American complaints about business conditions in Ukraine is instructive:

- More generally, past debts of Ukrainian farmers, state collectives, and national entities totaling some $150 million have led several major U.S. agro-industry providers to limit sales of critically needed fertilizer, pesticides, and seed to a cash on the barrel-head basis for businesses—which has sharply reduced their inputs. As a result Ukraine's harvests have steadily declined for over 5 years. If you are a major agricultural society and have only very limited access to the products of *DuPont, Dow, Monsanto* and others, it will and has led to depressed productivity. The Prime Minister has acknowledged this input debt and instructed that the back payments be made—to date payments have not eventuated.
- A very promising joint venture between *United Technologies* (Otis Elevator) has been driven to the brink of bankruptcy because municipal authorities throughout Ukraine have not received pledged housing funds which permit them to pay the Otis joint-venture.
- Ukraine has become the number one producer and exporter of pirated optical discs in Eastern and Central Europe. President Clinton in his visit to Kiev last month raised the issue and received reassurances that new tougher legislation

will be enforced. The two Presidents in fact issued a joint statement approving an action plan calling for closure of pirate plants and taking action against infringement.

- *Honeywell,* a world renowned leader in energy efficiency and airport systems has been a major investor in Ukraine. In May of this year Ukrainian authorities placed a moratorium on all payments for the modernization of Kiev's central airport—all work is suspended and Honeywell's participation in Ukraine is in jeopardy. This sort of problem is not new, but it produces a great sense of frustration and has a chilling effect on corporate interest in investment.
- U.S. corporations (*Phillip Morris* and *RJ Reynolds*) have been frustrated while new, presumably more efficient licensing procedures are installed. The result has been the parking of millions of dollars worth of product in expensive European warehouses. This problem comes on top of years of contraband and counterfeit problems, fostered by a Byzantine system of licenses, fees, and regulatory bodies.
- *Ceres Terminals,* a reputable container port management firm from New Jersey was one of the most impressive success stories. Working intelligently with Odessa customs officials and the port authority, Ceres created a world class container operation with dramatically increased volume and efficiency in Ukraine's principle port.

  Unfortunately, Ceres has just this month withdrawn in frustration from this joint venture in Odessa. Basically this has occurred because the Port Authority has squeezed Ceres for more expenses and violated the terms of their joint venture agreement. Frequent visits from health inspectors and tax officials were a consistent irritant.

This tendency to milk any successful agreement, violating contractual agreements in the process is all too typical throughout the former Soviet empire.

## SUCCESS STORIES

While the frustrations are wide-spread and serve as disincentives for the vitally needed foreign investments, there are success stories which clearly demonstrate that determined U.S. corporations with reasonably patient time-tables can succeed:

- *John Deere* has made major sales of over 1600 units of farm equipment in transactions which have proven to be successful. Just last month Deere and its joint venture partner in Ukraine opened a $2 million facility to coordinate its distribution, parts, and service network throughout Ukraine.
- *Pioneer,* after more than two years finally collected $400,000 in December and today expects to receive final settlement of their $2 million claim. This will allow Pioneer to proceed with a major investment to expand their seed project in Ukraine.
- Most recently *Cargill* after years of frustrating efforts to resolve past input debts, completed negotiations to open a new $50 million sunflower seed processing plant in Donetsk. The plant will create 400 jobs, reliable income for Ukraine's seed producing farms and valuable tax income for the Government.
- *Coca Cola,* while suffering today from raw material cost increases, has become a major presence in Ukraine with a national bottling plant network.
- *BRIM,* a University of Michigan Corporation, has successfully set up a joint venture employing space based imaging to map Chernobyl fall out movements from fires and floods, as well as mapping natural resource deposits.
- *Morrison-Knudsen* has been a major contractor in the joint Ukraine-U.S. program to dismantle the infrastructure and weapons from Ukraine's formerly formidable nuclear rocket force. Morrison-Knudsen characterizes their cooperation—as "outstanding" as they carry out their strategically critical efforts.
- *Boeing,* in a unique joint venture (Sea-Launch) with Ukraine, Russia, and the Norwegian ship building firm Kvaemer, has successfully launched a commercial demonstration space satellite and is now engaged in a regular production line in this cutting edge activity. Boeing does point out that additional improvement in the business climate, especially protection of investors assets will be critical to foreign investment. They continue to see Ukraine as a potentially lucrative market for aircraft sales.

These are but a few of the successes and the problems which illustrate the complexity and challenges of doing business in this disparate area. I am firmly convinced that the entire region—from the former Soviet zone of Germany to the Pacific Coast of Russia presents an immense opportunity. And, when U.S. firms are resolute, patient and politically sensitive, they stand a chance to reap the immense benefits. For this to happen they need the full support of the U.S. government. The contributions of U.S. corporations have been and increasingly will be a critical factor to the evolution of the former Soviet vassal states into prosperous participants in the new global economy.

Senator SMITH. Thank you very much. Peter.

## STATEMENT OF MR. PETER K. NEVITT, CHAIRMAN OF THE BOARD, GREENBRIER-EUROPE, SAN FRANCISCO, CA

Mr. NEVITT. Good afternoon, Mr. Chairman. Thank you for taking the initiative to hold a hearing before this distinguished subcommittee on the important subject of investment in Eastern Europe, and with the chairman's permission I will submit my testimony in writing and then just summarize it quickly for the committee at this time.

My name is Peter Nevitt. I am chairman of Greenbrier-Europe, which is a subsidiary of the Greenbrier Companies. Greenbrier is one of the largest manufacturers of rail cars in North America. We are headquartered in Lake Oswego, Oregon. Its largest manufacturing facility is in Portland. We have about 1,400 employees. Last year's sales were about $619 million, and our stock is traded on the New York Stock Exchange.

In 1997, Greenbrier decided to expand its operations. Manufacturing operations to Europe. Our Portland plant had been operating at capacity for several years. We wanted to move to Europe to serve our customers and after a careful consideration of all the relevant factors we selected Poland because of its commitment to a free and open economy and to the rule of law.

The Polish Government assured us that our investment in Poland would be welcomed, and that Greenbrier would be treated fairly as a Polish company. Therefore, based on those assurances, we decided to invest in Poland and acquired controlling interest in a factory located in southwestern Poland.

After acquisition, Greenbrier took a number of steps to improve the factory and to improve the working conditions for its employees. We increased the number of employees from 550, who were mostly on furlough. There were only about 25, I think, in the factory because I visited it at that time, to 880 active employees today.

We increased the salaries of our employees by nearly 80 percent. We have invested heavily in training our workers, and we have sent 61 workers to the United States and Canada for training here, and we have invested an additional $20 million in the factory itself to purchase equipment and to improve working conditions for our workers.

We are pleased with our investment in Poland, and we have been successful in winning contracts to manufacture rail cars in Western Europe, and Greenbrier's exports of rail cars from Poland to Western Europe is very important to Poland for its foreign exchange. Our factory is now profitable and, as I indicated, we are quite satisfied with our investment.

However, we have encountered one major disappointment, and that disappointment is that Greenbrier has been, or had been at least arbitrarily excluded from selling rail cars to the Polish National Railroad, PKP, which is practically the only customer for rail cars in Poland.

To make a long story short, PKP, certain individuals within PKP conspired to form a consortium to monopolize the sale of rail cars to PKP, to themselves, in effect. They arranged a rigged bid, and they awarded the rigged bid to friends, and this is a case, of course, of crony capitalism, to which the chairman referred earlier in his remarks.

However, I am pleased to report that thanks to the help provided by yourself, Senator Smith, and by other concerned parties in the Government and Congress, and including the U.S. Embassy in Poland, which has been quite helpful, communication was made to responsible individuals in the Polish Government and the unfair rigged bid of PKP was withdrawn and replaced with a transparent bid and a level playing field.

I want to reiterate, Mr. Chairman, that Greenbrier is very pleased with its investment in Poland. We are profitable, and on behalf of Greenbrier's CEO, Bill Furman, who could not be here today because of previous commitments, and on behalf of the thousands of employees of Greenbrier, we want to extend a heartfelt thank-you to you personally and to the U.S. Congress and the administration for the superb assistance you gave to Greenbrier as it established itself in Europe.

[The prepared statement of Mr. Nevitt follows:]

## Prepared Statement of Peter K. Nevitt

### I. INTRODUCTION

Good afternoon, Mr. Chairman, and members of the Subcommittee. Thank you for inviting me to testify this afternoon before this distinguished panel. My name is Peter Nevitt and I am the Chairman of Greenbrier-Europe, a subsidiary of The Greenbrier Companies. Greenbrier is one of the largest manufacturers of railroad freight cars in North America.

Greenbrier is headquartered in Lake Oswego, Oregon. Its largest manufacturing facility is in Portland, Oregon where it has 1,400 employees. Greenbrier operates additional facilities in the states of Arkansas, Kansas, Texas, California and Washington. Greenbrier also has factories in Canada, Mexico, and Poland, as well as an engineering and design center in Germany. Greenbrier's total sales last year were $619 million. The company's stock is traded on the New York Stock Exchange.

### II. GREENBRIER DECISION TO INVEST IN POLAND

In 1997 Greenbrier decided to expand its manufacturing operations to Europe. This decision was based on a desire to serve the European market, including certain American railroad companies that were beginning to invest in Europe. The European market also offered an opportunity to increase U.S. revenues through the export of technical, engineering and design skills.

Greenbrier employment in the United States has been increased to provide support services to Greenbrier's European activities. I should note that it is impossible to export rail cars manufactured by Greenbrier in the United States to Europe because of the high cost of shipping such cars to Europe.

Greenbrier was very particular and selective in determining the country in Europe that offered the best location for the start of its European operations. After careful consideration of all relevant factors, we selected Poland because of its stable government, its geographic proximity to major commercial markets, its commitment to a free and open market economy, its strong relations with its traditional trading partners, and its dedicated, skilled workers. Furthermore, Greenbrier received strong encouragement from Polish government officials to invest in Poland. The Polish government assured Greenbrier that its investment in Poland would be welcome and that Greenbrier would be treated fairly as a Polish company.

After Greenbrier investigated a number of possible factory sites in Poland, Greenbrier opted to acquire the WagonySwidnica factory, located in Silesia, close to the German border. At the time of our acquisition, the factory had little work, few employees, and practically no customers. However, the city of Swidnica and the surrounding area provided a pool of highly skilled workers. Therefore, based on the assurances Greenbrier had received from the Polish government, Greenbrier decided to invest in Poland and acquire a controlling interest in WagonySwidnica.

### III. THE GREENBRIER COMMITMENT TO WAGONYSWIDNICA HAS BEEN SIGNIFICANT

Greenbrier took possession of the WagonySwidnica factory on March 9, 1998. Since that time, Greenbrier has:

- Increased the number of employees at WagonySwidnica from 550 (mostly on furlough) to 880 active employees.
- Increased salaries of its workers by nearly 80%.
- Invested heavily in the training of its workers and sent 61 workers to the United States and Canada for additional specialized training.
- Invested an additional $20 million in the factory to purchase equipment and to improve working conditions for its employees.
- Increased the WagonySwidnica backlog of orders for rail cars from about $3 million to $47 million.
- Supported the local community through contributions to local charities and sponsoring local civic functions.

Greenbrier is very pleased with its investment in WagonySwidnica. Our employees at WagonySwidnica are highly skilled and have a solid work ethic. Labor unions representing our workers in Poland have been supportive of our efforts to improve production and increase economic opportunity for all employees.

Under Greenbrier management and with Greenbrier investment, WagonySwidnica has been successful in winning contracts to manufacture and sell rail wagons in Western Europe. ("Rail cars" are referred to as "rail wagons" in Europe.) Our European customers report that the quality of WagonySwidnica products is excellent.

Early this year, Greenbrier acquired the Adtranz freight wagon supplier from Daimler-Chrysler. Adtranz is based in Siegen, Germany, near Frankfurt. This acquisition makes Greenbrier one of the major freight wagon suppliers in Europe and one of Europe's leading design and engineering centers for freight wagons. As a result of this acquisition, Greenbrier intends to expand its rail wagon manufacturing in WagonySwidnica and possibly elsewhere in Poland. This acquisition could result in a significant number of additional jobs for Poland, so long as the political and economic environment rewards new investment from companies such as Greenbrier.

Greenbrier exports of rail wagons from Poland provide Poland with much needed foreign exchange. Unlike many foreign investors in Poland that cater exclusively to the internal Polish market, Greenbrier has significant sales to foreign markets. At the same time, Greenbrier expects fair treatment and a level playing field to compete in the Polish market.

### IV. GREENBRIER HAS BEEN ARBITRARILY EXCLUDED FROM SELLING RAIL CARS TO THE POLISH NATIONAL RAILROAD, PKP

Greenbrier's major disappointment in conducting business in Poland has been the arbitrary action by certain individuals within the Polish state-owned railroad, Polish National Railways (herein called PKP). These improprieties have prevented WagonySwidnica and Greenbrier from building wagons for PKP. This condition, which apparently has been corrected, was unfair to Greenbrier and to its workers at WagonySwidnica. The short history of Greenbrier's initially disappointing relationship with the Polish state-owned railroad, PKP, is as follows:

*A. Conspiracy to Monopolize Sales to PKP:* Certain individuals within PKP conspired to form a consortium to monopolize the sale of rail wagons to PKP. This consortium, known as Consortium Taborowa, is composed of PKP and a number of companies in Poland including three manufacturers of rail wagons. PKP owns about 90% of the stock of this consortium, known as Consortium Taborowa. Certain key PKP officers that control equipment acquisitions by PKP have always been and presently are the principal officers of the Consortium Taborowa. At the direction of these key officers, PKP granted this Consortium Taborowa the exclusive right to issue tenders for rail wagons on behalf of PKP.

*B. PKP Awarded an Order for Rail Wagons to its Friends Rather Than Through a Transparent Bidding Process:* In April of 1999, Consortium Taborowa issued a tender for 4,500 rail wagons. This tender contained requirements that made it impossible for any bidder to qualify to participate in the tender except for the two rail car manufacturers that were members of the Consortium Taborowa. Furthermore, the bids were reviewed and awarded by officers of PKP who also were officers of

Consortium Taborowa, rather than by any independent party. Not surprisingly, the Consortium Taborowa awarded the entire contract for 4,500 wagons to its own members. The bidding procedure adopted by PKP in this case did not begin to meet the requirements for transparency required by the United States, the European Union, and the international financial institutions such as the World Bank and EBRD.

*C. Greenbrier's Bid on the Tender Rejected on Arbitrary Grounds:* Greenbrier attempted, in good faith, to bid on the tender by submitting a bid to the Consortium for 1,500 wagons. Greenbrier's pricing was competitive and, in fact, somewhat lower than the pricing offered by the factories that were awarded this work. The requested delivery dates were within the time period requested by the Tender. Greenbrier merely asked for a share of the 4,500 wagon order, not the entire order, so that other Polish manufacturers and their workers might share in the contract. Greenbrier's bid was rejected on the grounds that it did not comply with the terms of the tender bid. As noted previously, the terms of the tender made it impossible for any company to qualify other than the members of the Consortium.

*D. Greenbrier Has Appealed the Arbitrary Rejection of its Bid:* When Consortium Taborowa rejected Greenbrier's bid on grounds designed to disqualify any manufacturer except members of Consortium Taborowa, Greenbrier appealed the decision to the Public Procurement Office. Greenbrier felt it was critically important that it try to protect its workers' jobs. The Public Procurement Office was sympathetic to WagonySwidnica's plight, and critical of the conduct of Consortium Taborowa. The appeal, however, was denied on very narrow grounds concerning the lack of jurisdiction of the Public Procurement Office, because PKP represented that no State funding of the transaction was involved.

During the hearing before the Public Procurement Office, Consortium Taborowa represented that neither the credit of PKP nor the credit of the Polish government would be utilized in financing the 4,500 wagons. Since that time, however, the fact has become clear that the 4,500 wagons can not be financed without support from either (or) all of the Polish government, PKP, the assignment of PKP receivables, the Consortium (90% owned by PKP), or by some other State corporation. In view of this misrepresentation of facts, further appeal by Greenbrier to the Public Procurement Office is possible and appropriate.

Greenbrier also has argued that the Consortium Taborowa bid award violates the Polish anti-monopoly laws. WagonySwidnica has filed an appeal with the Polish Office for Competition and Consumer Protection, which has commenced an aggressive investigation of this conspiracy.

V. GREENBRIER APPEARS TO BE ACHIEVING A RESOLUTION OF ITS PROBLEMS WITH PKP

*A. Intervention by Polish Government Officials Has Blocked the Award of the Rigged Bid and Resulted in Transparency of a New Bid Tender:* I am pleased to report that the intervention of responsible Poland government officials in the bidding procedure followed by PKP appears to have resulted in the cancellation of the tender bid for the 4,500 rail wagons. We are told that PKP has no intention of implementing the awards made pursuant to the 4,500 rail car tender. We also are told that PKP will issue no further tenders through the Consortium Taborowa. If this is true, Greenbrier is deeply grateful to those Polish officials who insisted from the beginning that the Consortium Taborowa and its rigged tender should have no role in a modern, market-oriented Poland.

*B. Greenbrier is Bidding on a New Tender by PKP:* Currently Greenbrier is bidding on a new tender by PKP for 1,000 freight wagons. I am pleased to report that this bidding procedure appears to be transparent. This bid request, however, contains a number of requirements for financing terms that are not commercially acceptable to anyone in light of PKP's precarious financial condition. To further complicate things, the tender includes a provision that all of the terms of the tender are "non-negotiable," thus precluding even minor changes typically necessary to meet the needs of lenders and lessors. Therefore, in the tender's present form, it is impossible for anyone to file a firm response.

Greenbrier is hopeful that the very stringent requirements of this bid request are due to inexperience rather than intent. Consequently, Greenbrier has asked PKP to eliminate the "non-negotiable" provision from the tender. If that requirement is removed, a bidder can be chosen on the basis of the merits of its bid as to specifications, price and delivery dates subject to final negotiation of financing arrangements. Because of the complexity of the financing and the need to involve third party financial institutions, we believe that such a procedure is the only feasible way to successfully conclude that tender.

*C. Poland has Been Successful in Establishing a System of Commercial Law:* I am pleased to report that Poland has been generally successful is establishing a commercial and legal environment conducive to American investment. The Public Procurement Office and the Office for Competition and Consumer Protection are examples of conscientious agencies that offer protection from arbitrary and abusive conduct.

*D. The Chairman of PKP has Been Particularly Helpful:* The current Chairman of the Management Board of PKP, Mr. Krzystof Celinski, is a very capable executive. He has been sympathetic to Greenbrier's experience with Consortium Taborowa. However, certain persons within PKP seem to operate independently of supervision. Unfortunately, a large state-owned company such as PKP is difficult for a responsible Polish official to manage effectively, because of the social upheaval a railroad strike would cause. Certain management people within the present structure of PKP sometimes use their ability to ferment labor unrest in order to achieve their own ends.

The PKP situation is further complicated by the fact that the company is hemorrhaging money on a daily basis and needs to be privatized as quickly as possible. Such privatization will require large reductions in personnel. The Sejm, hopefully, will pass the privatization legislation this summer. The Polish presidential election is scheduled for early October and parliamentary elections are expected by March or April next year. Failure to enact the PKP privatization legislation this Summer probably would delay action until next Spring. Financing for PKP and its freight car orders will be needed before then. We understand that Citibank and Salomon Smith Barney are trying to arrange this financing. The attitude toward this financing by Mr. Bauc, the new Finance Minister, seems favorable, provided that the pending privatization legislation is passed by the Sejm.

## VI. NUMEROUS UNITED STATES OFFICIALS HAVE COME TO THE AID OF GREENBRIER AND HAVE BROUGHT THE DISPUTE TO THE ATTENTION OF POLISH GOVERNMENT OFFICIALS

As an American businessman with a major problem abroad, I was immensely surprised and gratified at the assistance Greenbrier received from the United States Government. Both the Legislative and Executive branches made impressive efforts to help prevent an injustice from being inflicted upon our company. Frankly, I had no idea that such assistance was available and Greenbrier is immensely grateful for it.

*A. Congressional Assistance:* When this difficulty first arose just over a year ago, Greenbrier brought the matter to the attention of the fine Chairman of this body, Senator Gordon Smith. Senator Smith and his excellent staff, including, in particular, Rob Epplin and Martha Cagle, worked hard to ensure that the matter was brought promptly to the attention of the Polish Ambassador here in Washington, to the United States Ambassador in Warsaw and to key officials in the Administration that deal with such disputes. He had the matter investigated thoroughly and met repeatedly with the Polish Ambassador to obtain regular updates on the progress of our discussions. He encouraged the Polish government to address the matter promptly and fairly. Senator Smith's credibility at the Polish Embassy and throughout the Polish government was extremely high due to his long-standing friendship with the country and his tireless efforts on behalf of Poland's membership in NATO; throughout this dispute, we heard repeated statements of admiration for the Senator from numerous Polish officials.

Other members of Congress also expressed their willingness to be of assistance, particularly Senators Patty Murray and Max Cleland. We at Greenbrier will always remember the tireless efforts of the Senator from Georgia. He personally engaged the assistance of Vice President Gore, the National Security Advisor, key officials at the Departments of State, Commerce and Defense and made regular contact with the Polish Ambassador here in Washington and the United States Ambassador in Warsaw. Senator Cleland clearly was going to see that Greenbrier was treated fairly in Poland. He never asked for special favors or special treatment; he simply asked that American companies, including Greenbrier, be given an opportunity to compete fairly and openly abroad.

*B. Assistance from the Clinton Administration:* Again, I personally was amazed and gratified by the assistance that Greenbrier received from key representatives of the Clinton Administration. I simply had no idea that our government was so willing to be of assistance to American companies that attempt to seize new business opportunities abroad. I couldn't possibly name here all of the hard-working individuals that took an interest in Greenbrier's plight, but the following must be noted:

1. *U.S. Department of State:* The assistance that we received from Ambassador Daniel Fried and his excellent staff in Warsaw (including the DCM, Michael Mozur; the Political Counselor, Jeffrey Goldstein; the Economic Counselor,

John Hoover) was very impressive. Likewise, we received regular and valuable assistance from then-Under Secretary Stuart Eisenstat and the Poland Desk Officer, Jim Wojtasiewicz.

2. *U.S. Department of Commerce:* We received valuable assistance from Under Secretary David Aaron, Assistant Secretary Patrick Mulloy and Poland Desk Officer, Amy Zona. Their assistance included numerous meetings with representatives of the Polish Embassy and meetings in Warsaw with key Polish officials.

3. *U.S. Department of Transportation:* Secretary Rodney Slater and Federal Railroad Administrator, Jolene Molitoris, were extremely helpful to Greenbrier's efforts to resolve this controversy. They and their key staff (including DOT Chief of Staff, Jerry Malone; Deputy Chief of Staff, Norma Krayem; Associate FRA Administrator, Charles White; and Director of International Policy, Ted Krohn) jumped immediately on this issue and had numerous meetings in Warsaw, Swidnica and Washington, D.C. with key Polish officials. Greenbrier is indebted to the energetic efforts expended in its behalf by these valued public servants.

4. *So Many Others:* Greenbrier received valuable assistance and support from the U.S. Trade and Development Agency (particularly from Director Joe Grandmaison), the Overseas Private Investment Corporation (particularly from Managing Director for Business Development, Joan Edwards) and from the U.S. representatives at the World Bank and European Bank for Reconstruction and Development. The hard work of these individuals was extremely helpful to Greenbrier's efforts to resolve this matter.

## VII. POLISH GOVERNMENT OFFICIALS HAVE BEEN HELPFUL TO GREENBRIER

Poland is blessed by the fact that patriotic officials who are concerned with the welfare and future of Poland lead its major political parties. All the major political parties are pro NATO, pro American, pro free enterprise, and anxious to meet the stringent requirements for joining the EU. Whatever political party is in power makes a real effort to place highly qualified individuals in positions of responsibility. Encouraging foreign investment and particularly American investment in Poland is a high priority of these individuals. They are very concerned with the creation of a fair and efficient political environment, the establishment of workable commercial laws, and the dismantling of needless protectionism.

*A. Polish Embassy:* Greenbrier has been extremely gratified by the support it has received from the Polish Embassy here in Washington D.C. Then-Ambassador Jerzy Kozminski was extremely sympathetic to Greenbrier's plight and worked hard to correct it. Greenbrier feels deeply indebted to Ambassador Kozminski and his excellent staff, including Krzysztof Wybieraiski, Mariusz Handzlik and Andrzej Dziekonski.

*B. Ministry of Finance:* Greenbrier has been very impressed with Dr. Leszek Balcerowicz, until recently Finance Minister and Deputy Prime Minister, and the architect of the financial stability that has been achieved in Poland. Dr. Balcerowicz expressed to PKP his dismay at the tender procedure for the 4,500 rail cars described above.

The new Finance Minister, Jaroslaw Bauc, was a deputy minister to Dr. Balcerowicz and hopefully will continue Dr. Balcerowicz' policies. There is some concern in the financial community that Mr. Bauc was not also appointed Deputy Prime Minister as was customary with previous Ministers of Finance. We are pleased with our initial contact with Minister Bauc and look forward to working with him in the months ahead.

Another avid defender of privatization and outstanding talent is Mrs. Korniasiewicz, a Deputy Minister of the Treasury.

*C. Office of the Prime Minister:* Prime Minister Jerzy Buzek has been a strong supporter of free enterprise and adherence to principles of transparency in bidding. Mr. Buzek is said to have been re-energized by the recent reorganization of the Polish government. His strong support is expected to achieve passage by this September of needed legislation to enable privatization of PKP.

*D. Office of the President:* President Aleksander Kwasniewski is a strong supporter of American and other foreign investors in Poland. Mr. Kwasniewski's political party is SLD, the successor to the old communist party. However, as noted earlier, SLD and all the major political parties favor free enterprise, NATO membership, entry into the EU, and encouraging foreign and particularly American investment. Mr. Kwasniewski is strongly favored to be re-elected President this October.

*E. Minister of Transportation:* Mr. Jerzy Widzyk is the new Minister of Transportation. His reputation is that of a trouble-shooter, and he seems well fitted to help manage privatization of PKP. Greenbrier looks forward to working with Minister Widzyk.

Deputy Minister of Transportation, Witold Chodakiewicz, has provided fair consideration of Greenbrier issues.

Former Minister of Transportation, Boguslaw Liberadzki, who is now Vice Chairman of the Transportation Committee of the Sejm, strongly favors transparency.

VIII. CONCLUSION

Greenbrier is very pleased with its investment in Poland. Although Greenbrier has experienced some difficulties in establishing its Polish factory, responsible Polish government officials have made Greenbrier feel welcome and have addressed problems that would otherwise discourage American investment. Poland has great potential as a nation and as a loyal ally of the United States. We look forward to expanded operations and opportunities in Poland.

In conclusion, Mr. Chairman, on behalf of Greenbrier's CEO, Bill Furman, who could not be here today because of other previous commitments, and the thousands of employees of Greenbrier, we want to extend a heartfelt "thank you" to the United States Congress and to the Administration for the superb assistance you gave to Greenbrier as it has established itself in Europe.

Senator SMITH. Thank you. I am delighted to learn of your overall satisfaction in your dealings in Poland. I am very familiar with the bid that you describe. As you noted, we have been trying to nudge things along and make them transparent, and I am pleased it has turned out better.

I wonder if you have any reason to believe or suspect that any of the U.S. companies in Poland have been singled out for sort of discrimination under pressure from the European Union? Do you have that sense?

Mr. NEVITT. Well, I have not heard it admitted by any public officials. I think that that certainly is a possibility. I do not know of any such instance, though, Mr. Chairman.

Senator SMITH. I do not either. That is why I asked the question. I got it in writing in other countries, which was shocking.

Mr. NEVITT. The Poles love Americans, and they are very anxious for American investment, and frankly more American companies should go to Poland. The welcome mat is out, and fortunately the political atmosphere in Poland, the politicians on either of the three major parties are all pro-American and pro-NATO, and welcome American investment, and are for the rule of law.

There are always going to be groups somewhere, somehow, who are going to try to set up their own little honey pot, so to speak, but there is legal recourse available within Poland. It is finding its way. It is new. It has only been in existence for about 8 years.

Senator SMITH. Do you sense any reluctance on the part of the Polish Government to continue forward with more and more privatization?

Mr. NEVITT. I think they are very anxious for privatization, particularly privatization of companies that can export, because they need foreign exchange. They do have a balance of trade problem. Part of that is because they are making investments in capital improvements that are being imported into Poland. The government itself, under former Finance Minister Balcerowicz, was running a very, very tight economic ship, and I hope they continue to do so.

Senator SMITH. Is there anything we should be doing as the U.S. Government to encourage more transparency in Poland, or do you think it is moving ahead at the right pace?

Mr. NEVITT. I think there is good communication with the responsible individuals in government in Poland, and I think it is working very well. I might also add that Poland is almost key to Ukrainia. The Poles look forward to building trade with Ukrainia, and they frankly look forward to Ukrainia getting admission into NATO. They want somebody between them and Mother Russia.

Senator SMITH. You had a comment, Mr. Jenkins.

Mr. JENKINS. Yes, Mr. Chairman. In the catalogue of things we would like to see the U.S. Government do better, one of them is visa policy.

Our corporations, to succeed, must build mid-level management cadres and that frequently requires bringing people to the United States for training. Time and time again, arbitrary policies and decisions by vice consuls—and I was a vice consul, and I was engaged in this problem a long, long time ago—result in the fact that there will be 10 people invited over for a training course and four will be denied, usually young women.

There is a very discriminatory attitude within the Consular Service of the United States representing consular policy in the U.S. Government that people will be brought over to the United States only if they can be certain they will return, and they just jump at the conclusion that young women are more likely to stay. This has been very upsetting to our corporations, who cannot operate effectively in that part of the world if they cannot train people in the process.

Senator SMITH. I thought we were trying to export, what was it, some notions of political correctness. This does not comport with that.

Mr. JENKINS. I am in trouble at home already on this, but I think that is important, and I think it would be very helpful if the committee and the Congress generally would call this up. It conflicts directly with what we are trying to do at the national policy level.

Senator SMITH. Is this the State Department's responsibility?

Mr. JENKINS. It is the State Department's responsibility. I say that sadly, having spent 30 years of my life in the State Department.

Senator SMITH. You did not fix it while you were there.

Mr. JENKINS. It actually was running pretty good.

I would like, if I could, Mr. Chairman, to insert in the record a classic case, at a much lower level than Ron's, of essentially a foul-up bureaucratic snafu within our own Government which has caused so far a defeat for an investment effort involving the Defense Department and various elements within the Defense Department. It illustrates the fact that we do not have a coherent priority within our administration with congressional support to move ahead on this issue, which is such an important historic opportunity, in my judgment.

Senator SMITH. We will receive that without objection and include it in our record.

[The insert referred to, a letter from DCI, Inc., is on page 59.]

Senator SMITH. I think, Mr. Jenkins, somebody in Commerce heard your comment, because we have just had delivered to us some testimony from Charles M. Ludolf, who is Deputy Assistant

Secretary for Europe from the Commerce Department, so while he is not here, we will include his testimony in the record.

[The statement referred to is on page 62.]

Senator SMITH. We are glad they have at least showed up in that way, and I know the Commerce Secretary is involved in a political campaign, and whenever his replacement gets here we will ask him to come up and talk to this issue as well.

Gentlemen, thank you very much. Part of the role of the U.S. Congress is transparency, and this is about oversight, and this is not just about what benefits Americans and American capital but ultimately what benefits these other countries we care about as well, because the market, free enterprise plays by the rules of openness and fair play, and where it is not, it will retard the development of these countries and take opportunities away from Americans and Europeans. We do not want that.

So that is the spirit in which this hearing has been held, and we thank you for your contributions. The hearing is adjourned.

[Whereupon, at 3:35 p.m., the subcommittee adjourned.]

## ADDITIONAL QUESTIONS SUBMITTED FOR THE RECORD

### RESPONSES OF HON. E. ANTHONY WAYNE TO ADDITIONAL QUESTIONS FOR THE RECORD FROM SENATOR GORDON H. SMITH

*Question.* The European Union has repeatedly stated that the Czech Republic is far behind the West in dealing with corruption and crony capitalism. Do you agree?

Answer. There is some truth in such a view, but I would caution that the difficulties of economic transition from socialism to a market-based economy also far exceed the problems faced by most West European economies.

Crony capitalism and corruption have been problems and, in fact, have tarnished the view many Czechs have of capitalism and democracy. Yet, I sincerely doubt that many Czechs would exchange their current economic and political states for those of the old regime prior to the "Velvet Revolution."

In our bilateral contacts and in various multilateral organizations the U.S. Government is encouraging our Czech counterparts to emphasize good governance and transparency in economic processes in order to relegate crony capitalism to the dustbin containing some other famous "-isms." The Czech Government sent a high level delegation to the Global Forum On Fighting Corruption hosted by Vice President Gore in February 1999. The Czechs also attended a follow up Regional Conference for Central and Southern European Nations hosted by the Romanians with U.S. support in March of this year. We have urged them to participate as fully as possible in the next Global Forum to be hosted by the Netherlands in May 2001.

The Czechs have participated in regional anti-corruption seminars conducted by the Department of Justice. I also am pleased to bring to your attention that, as of January this year, the Czech Republic is now a full party to the Bribery Convention of the Organization for Economic Development and Cooperation (OECD). Although the Czech implementing legislation has some weaknesses, this very positive step makes the Czech Republic an ally in a broader effort to curb international business bribery.

Another positive development, which the U.S. Government has had no direct role in, is that in October 1999, the Czech Republic signed the Council of Europe Criminal Law Convention Against Corruption. The Convention is significant for the Czech Republic, and for the rest of Central and East Europe, because the Council of Europe is the organization that traditionally sets the criminal law norms for Western Europe.

*Question.* The U.S. Government encourages investment abroad, and in particular investment in countries formerly dominated by the Soviet Union. What steps has the State Department taken to protect American investors in Central Europe? What steps does the State Department plan on taking in the future?

Answer. Continuing to expand the U.S. Bilateral Investment Treaty (BIT) program is the single best action the U.S. Government can take to protect U.S. investors abroad. The U.S. Government already has BITs in force with numerous countries in Central Europe with the Czech Republic, the Slovak Republic, Bulgaria, Poland and Romania, and we are currently in BIT negotiations with Slovenia. In addition to the BITs with the Central European countries formerly dominated by the Soviet Union, the U.S. has negotiated BITs with Russia (not yet in force), Ukraine (in force) and many of the newly independent states.

BITs ensure U.S. investors are entitled to be treated as favorably as their competitors, establish clear limits on expropriation of investments, prohibit various performance requirements, afford U.S. investors the right to transfer funds freely, and give U.S. investors the right to submit an investment dispute with the treaty partner's government to international arbitration. This last aspect of the BIT is the closest thing to an insurance policy ensuring that U.S. investors will be treated fairly. However, it is the BIT's overall focus on encouraging adoption in foreign countries of market-oriented policies—especially related to improving investment regimes—and supporting the development of international law standards that will benefit U.S. investors the most in the long run. Countries' implementation of these investment sector reform policies will not only improve their investment climates, but should also create additional opportunities for U.S. investors.

In addition to the protections afforded by our BITs, it is standard practice for the U.S. Government to assist U.S. investors who are interested in investing abroad or who have already invested abroad and have run into problems. We are aware of ongoing investment disputes involving U.S. investors in every Central European country. Several of these disputes have gone to international arbitration under BITs. The U.S. Government is monitoring such cases and is providing appropriate assistance to the U.S. investors. In many instances, U.S. Government officials have met with the appropriate host government officials to insist that U.S. investors receive all due consideration under local and international law. U.S. Government officials also actively support U.S. investors in Central Europe by advocating at the highest levels a level playing field for investment.

*Question.* The right to pursue international arbitration as a dispute resolution mechanism is seen by foreign investors and creditors alike as essential to any major infrastructure project. In fact, the European Union requires such a mechanism in order to meet the requirements of accession to the E.U. In this regard, what has the government of Bulgaria done to move swiftly in adopting such a measure? Are there any obstacles that you are aware of? In addition, what is the United States Government doing bilaterally, or through its participation in the Stability Pact, to encourage the immediate adoption of international arbitration legislation?

Answer. The EU's identification in December 1999 of Bulgaria as a candidate for accession followed the Bulgarian government's intensified economic reform efforts in 1999, and since has provided impetus for continued reform. Recent reforms have included taking initial steps to improve investors' ability to use international arbitration to settle disputes.

On March 21, 2000, Bulgaria became the 149th signatory of the International Center for Settlement of Investment Disputes (ICSID) Convention. Bulgaria has yet to ratify the Convention, but has taken the first step toward fulfilling the commitment Bulgaria made under the Stability Pact's Investment Compact on accession to international conventions on arbitration and enforcement of arbitral awards. Bulgaria was already a member of the 1958 New York Convention on the Recognition and Enforcement of Foreign Arbitral Awards and the 1961 European Convention on International Commercial Arbitration.

The U.S. Government is also pursuing several different avenues to help Bulgaria improve its judicial system, including the use of arbitration as a valid and available option to settle disputes. In particular, we are supporting the American Bar Association's Central and East European Law Initiative (ABA/CEELI), which is working with the Bulgarian Judges Association to introduce Alternate Dispute Resolution (ADR) to the court system.

We are also working actively with the Bulgarian Government on fulfillment of Stability Pact commitments. To that end, we have been instrumental in the establishment of mechanisms for coordinating and monitoring progress on reform commitments in each of the signatory countries. The Investment Compact commitments include agreements to accede to international arbitration conventions, to increase transparency of the legal and regulatory framework, to establish an open and transparent government procurement process, and to fight corruption. With respect to corruption, it is significant that the Government of Bulgaria has both ratified and implemented the OECD Bribery Convention.

Finally, after the U.S.-Bulgaria BIT went into force June 2, 1994, Bulgaria committed to a range of dispute settlement procedures starting with notification and consultations. Bulgaria accepts binding international arbitration under ICSID rules in disputes with U.S. investors. The U.S. is committed to ensuring that U.S. investors in Bulgaria are able to achieve their rights under the BIT.

The U.S. Government has worked to encourage the adoption by the Bulgarian Government of investment-sector related reforms that will improve Bulgaria's investment climate. Through the Bilateral Investment Treaty, the U.S. Government has ensured that U.S. investments in Bulgaria are protected and U.S. investors have the right to take investor-state disputes to international arbitration.

*Question.* In most of the infrastructure projects in Bulgaria, particularly those in the energy sector, private investors are not capable of securing financing for their projects unless the investment is backed by a sovereign guarantee from the government of Bulgaria. We understand that the Bulgarian Government is very limited in the issuance of such guarantees through its program with the International Monetary Fund. What is the U.S. Government doing to ensure that U.S. companies that are seeking such guarantees are in a competitive position with their European counterparts?

Answer. The U.S. Government has advocated actively for U.S. companies that are interested in investing in the energy and other sectors in Bulgaria in an effort to ensure they are able to compete fairly. State, Commerce, and Energy Department officials have had frequent discussions with Bulgarian Government officials, including Prime Minister Kostov, in meetings here and in Sofia.

We are mindful of the importance of the Bulgarian Government living up to its commitments with the IMF and maintaining litnits on debt. We support the IMF program in Bulgaria and do not advocate that Bulgaria undermine its hard-earned macroeconomic stability by assuming sovereign guarantees in excess of the ceiling. At the same time, however, we are maintaining close communication with the highest level Bulgarian Government officials, to underscore the benefits of U.S. investments and services, especially in the energy sector. These benefits include improved environmental and nuclear safety and contributions to economic growth (through capital and technology transfers and increased, energy efficiency).

Our efforts have enabled U.S. companies to obtain highly-sought-after contracts. The Bulgarian Government recently signed a $77 million credit agreement with Ex-Im Bank for a contract with a U.S. company to upgrade nuclear safety at Kozloduy nuclear power plant, the first Ex-Im transaction in Bulgaria since 1967. The financing for this project is included on the Bulgarian Government's priority list of projects for which a government guarantee is available.

Projects on which U.S. exporters are competing do not necessarily require Bulgarian Government guarantees. In addition to being open for short, medium, and long-term transactions in the public sector, Ex-Im Bank is also open for short and medium-term transactions in the Bulgarian private sector. Ex-Im Bank is also prepared to consider financing in support of U.S. exports for Bulgarian borrowers with independent access to private international capital markets and their own credit ratings from recognized rating agencies. Ex-Im Bank will also consider projects that can be secured through the assignment of hard currency earnings.

We will continue to pursue these and other ways to assist U.S. companies interested in investing in Bulgaria. We will also continue to urge high level Bulgarian Government officials to ensure fair and equitable treatment for all foreign investors.

*Question.* I understand that you are aware of problems investors have had in withdrawing funds from Polish National Investment Funds, that were originally created to back the transition of roughly 500 state-owned businesses to privatized companies. Could you describe what actions the U.S. Government has taken and will take to resolve this issue, which affects the investments of many American citizens.

Answer. We are aware of a dispute involving the U.S. investors in the Polish National Investment Fund (NIF) named Octava. We understand that the dispute arose last year when a majority of Octava's shareholders, including representatives of the U.S. investors, voted in favor of authorizing a share buyback program. The buyback program would allow interested shareholders to withdraw funds from (or more specifically sell back their shares to) Octava.

The Polish Ministry of State Treasury ("Ministry"), which is both a shareholder in and regulator of all the NIFs, opposed the share buyback program and filed a lawsuit in an attempt to reverse its decision. The Ministry argues that share redemptions are not permitted under the 1993 law that created the NIFs, since actions that serve to reduce the capital of a NIF could undermine the primary objective of the funds, namely increasing the value of the privatized companies they control. However, the Ministry is aware that investments in the NIF funds are not performing as investors had hoped and that some structural changes will be required; the Ministry reportedly wants such changes to take place in a manner that will not result in an increase in the Polish Government's stake in the NIFs, as this would run counter to the goals of its privatization program.

The court case is still pending. In the meantime, the court has prevented Octava from implementing the share buyback program. Simultaneously, Octava's management, representatives of the U.S. investors, and the Ministry have been holding negotiations to find a compromise solution. It is our understanding that the parties recently reached a working level agreement that is acceptable to all sides, including the U.S. investors. Although we have not been able to learn the exact details of the accord, we have been informed that it is currently awaiting the signature of the Treasury Minister.

At this time we are unaware of any other instances of U.S. investors facing difficulties in divesting from Polish NIFs. In the case of Octava, Department of State and U.S. Embassy-Warsaw officials have followed the dispute from the beginning. Embassy officials have met with all the principals involved and have urged the Government of Poland to seek a fair and rapid resolution to this case. We will continue to provide all appropriate assistance to the U.S. parties in this dispute, and will continue to raise our concerns with high-level Polish government officials, and, as appropriate, encourage the Government of Poland to bring this issue to closure.

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RESPONSE OF HON. E. ANTHONY WAYNE TO ADDITIONAL QUESTION FOR THE RECORD FROM SENATOR CHUCK HAGEL

*Question.* You have outlined very effectively the problems that U.S. businesses encounter with foreign governmental agencies, taxing methods, power supply, etc., in setting up operations in NIS and former Soviet bloc countries. Are you aware of any problems that have been caused by our own governmental agencies in this part of the world? What kind of cooperation have you experienced with the U.S. Government in, for instance, establishing joint ventures between U.S. companies and former Communist governments in privatization efforts and in advancing mutually beneficial trade, economic development, and regional or national security goals?

Answer. One area where the U.S. Department of State has cooperated with the Department of Commerce and some 17 other agencies is the Trade Promotion Coordinating Committee (TPCC). Over the last seven years, the TPCC has responded to the immediate needs of U.S. businesses, large and small, who are interested in entering or expanding into the countries of the former Soviet Union. The TPCC Interagency Working Group on Energy has worked towards the rapid, safe, and environmentally-sensitive development of energy resources with the Newly Independent States (NIS) of the former Soviet Union. Business Development Committees (BDCs) with Russia, Ukraine, and Kazakhstan are working to promote and facilitate U.S. trade and investment by identifying and working to eliminate barriers.

In December 1999, the Commerce Department and State Department successfully persevered in the forum of the U.S.-Kazakhstan BDC and Joint Commission to overcome obstacles to trade and increase market access. We have seen progress in customs, labeling regulations, and currency restrictions.

In Russia, we have worked hard, together with Commerce, to relieve some of the most onerous problems facing U.S. businesses in Russia. We have made concrete progress through the Binational Commissions (an OVP initiative jointly supported by State and Commerce) on tax, customs, and regulatory issues. In the energy area, we have had a strong team working together from State and Commerce (and Treasury) to push Russia to pass Production Sharing Agreement (PSA) legislation and complete the PSA framework. In sum, cooperation has been good, progress has been made in some areas, and there is a clear game plan that we are all working from to make real progress in the future.

Energy developments and transportation initiatives in the Caspian Basin continue to be a central focus of interagency efforts that support the expansion of mutually beneficial relations with the states of the NIS. Recent discussions have focused on regional oil and gas transportation, the improvement of legal frameworks necessary to support enhanced U.S. commercial energy investment in Kazakhstan and Uzbekistan, and with respect to the latter, currency convertibility issues. Several outreach initiatives have been undertaken and coordinated in the energy sector that support U.S. commercial ties in the NIS. Other programs are outlined in the Report on Implementation of Section 303 of the Freedom Support Act.

We in the State Department play a central role in working with American companies and with the firms, governments and other institutions in Central and Eastern Europe to create open markets and rule of law to attract private sector U.S. investment. In partnership with our colleagues at the Department of Commerce and governments of the former Soviet Union, we are working to address U.S. business concerns and help foster a framework that opens these countries further to American business and investment.

There are a number of overarching efforts such as battling corruption through our joint State-Commerce efforts to battle corruption through encouraging countries in the region that have signed the OECD Anti-Bribery Convention to ratify and fully implement it. The Czech Republic and Hungary, both of which are members of the OECD, have ratified and implemented the Convention, as have Bulgaria and the Slovak Republic. We are working with other USG agencies to press governments in Central and Eastern Europe to take action to protect intellectual property rights. Bulgaria has made significant progress here.

We jointly have pursued bilateral investment treaties (BITs) with many countries in the region. The basic aims of the BIT program are to protect U.S. investment abroad. We currently have signed BITs with 15 countries in the region. Twelve of these are now in force.

There are also a number of specific initiatives geared to particular parts of the region designed to improve the investment and business climate. One such international partnership is the Stability Pact for Southeast Europe. The Pact was announced at the July 30, 1999, Sarajevo Summit with President Clinton and European leaders.

Results on the trade front are already impressive in Central Europe. In 1991, U.S. companies exported $1.6 billion worth of goods to the 15 countries of Central and Eastern Europe. By the end of 1999, U.S. exports had doubled, to $3.2 billion.

U.S. firms have made inroads with opportunities from Greenbrier's investment to produce railroad cars in Poland to Bechtel's $600 million highway construction contract with the Croatian Government.

Our embassies, with State officers and Department of Commerce FCS personnel, constantly work hard on behalf of American commercial interests. In Russia and Central and Eastern Europe—from the Baltics to the Balkans—U.S. Ambassadors and Embassy Senior Commercial and Economic Officers are the eyes, ears and in-country negotiators for U.S. commercial and economic interests—from trade and investment to anti-corruption, environmental safeguards, and cultural exchanges. Furthermore, as experts on host-country markets and business practices, these State and Commerce officials can and do identify opportunities for American firms and advocate on their behalf, companies that range from small and medium enterprises like bagel bakeries to major firms such as Enron and Ford.

During the absence of an FCS officer from AMEMB Tashkent, for example, Commerce relied on the State Department to support our coordinated efforts to work for market access in the U.S.-Uzbekistan Trade, Investment and Energy Committee.

In Washington, the State Department's Office of Commercial and Business Affairs (CBA) is teamed with the Department of Commerce's Advocacy Center (AC) and Market Access and Compliance (MAC) to help individual American companies go after lucrative opportunities abroad. The two offices conduct joint project advocacy on behalf of U.S. business interests. At this time, we are currently collaborating on updating the interagency Advocacy Guidelines that are used by Commerce and State officers both in Washington and overseas. For large or complex cases, Commerce and State Department staff routinely come together with interagency backing for U.S. companies. CBA, AC and MAC collaboration is producing numerous success stories ranging from Williams in Lithuania; to Boeing in Russia, to NRG in Estonia (which will be the biggest single foreign investment in Estonia's history) to Westinghouse Electric's nuclear safety project in Bulgaria (which has resulted in the first Eximbank transaction in that country since 1967).

In short, State and Commerce work together closely and quite successfully both in Washington and abroad, to advance U.S. commercial interests. It is a natural partnership.

## ADDITIONAL STATEMENTS AND MATERIAL SUBMITTED FOR THE RECORD

AMERICAN CHAMBER OF COMMERCE IN POLAND,
WARSAW FINANCIAL CENTER, UL. EMILLI PLATER 53, 00-113,
*Warsaw, Poland, June 27, 2000.*

Senator JOSEPH R. BIDEN, JR., RANKING
*Subcommittee on European Affairs,*
*United States Senate,*
*Washington, DC.*

DEAR SENATOR BIDEN:

It is our understanding that the Subcommittee for European Affairs will hold a hearing on June 28th concerning the experience of American investors in Central and Eastern Europe. It is our pleasure to add our voice to the hearing through this letter.

The American Chamber of Commerce in Poland represents the largest bloc of foreign direct investment in Poland through its over 300 member companies. The rapidly rising level of investment by American firms in Poland is a testament to the economic reform progress Poland continues to make and the vision of our member firms. To date, American companies have invested over $7.5 billion dollars with an additional $3.5 firmly committed in the near term.

It is our experience that in every country there are individual companies which experience problems due to a lack of transparency, inefficient bureaucracies or unfair practices. We are pleased to say that in Poland this is definitely the exception, rather than the rule. The American Chamber of Commerce works diligently with the government and opposition on continuing reform and on behalf of our member firms when they experience any of the conditions mentioned. While some occasional difficulties remain, we see strong evidence of improvement from year to year in Poland.

Successive governments in Poland have continued their practice of working closely with the American Chamber of Commerce in fiscal, tax, labor market, macro-economic, licensing, concession, intellectual property and public procurement areas—to name but several—with the aim of using our organizations depth of expertise and experience to further improve the attractiveness and competitiveness of the Polish economy. Our involvement directly in the reform process allows us to gauge the changes which have been made, are underway or planned. The success of our member firms speaks strongly about the results achieved to date.

More than eighty Fortune 500 companies have made investments in Poland, along with many U.S. small and medium sized enterprises and a growing number of entrepreneurs starting businesses in this dynamic economy. Poland is continuing its solid growth, aided by American investment and providing a dynamically growing market for American companies, goods and services.

We would be pleased to provide any additional information on American investment and our companies experience in the market if it will be of assistance to the Subcommittee.

Sincerely,

MAC RACZKIEWICZ, *Chairman.*

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DIE CASTERS INTERNATIONAL, INC.,
ONE SPRUCE TERRACE,
*Wayne, NJ, June 20, 2000.*

The Honorable KEMPTON JENKINS
*President, Ukraine-U.S. Business Council,*
*1615 L Street, N.W., Suite 900,*
*Washington, DC 20036.*

DEAR KEMPTON:

I understand that you have been invited to testify before the Senate Foreign Relations Committee on the state of U.S. business interests in Central Europe. In Ukraine, too often failures are attributed to corruption, frequently by Ukraine government officials, as well as to the onerous and numerous risks and instabilities inherent within the business and legal environment in that region of the world today. However, sometimes failures are created by the U.S. government. Our project is a classic example of exactly the latter situation. The following could be included in the record as to how one agency in the Department of Defense has unilaterally decided to throw away $3 million of public investment despite a decision to the contrary by the Office of the Secretary of Defense and despite the continual support of the Ukraine government.

For two and one-half years, Die Casters International, Inc. (DCI) has had $3 million of high technology equipment, seventy percent American that was designed and purchased with DCI and Nunn-Lugar funds, uselessly warehoused in Kyiv, Ukraine and in Tiraspol, Moldova, while DCI attempted to have available and assigned funding from the U.S. Department of Defense (DoD) released to complete DCI's defense conversion project. In May of this year, the Office of the Secretary of Defense (DoD-Policy) reaffirmed a decision it made in January to release $560,000 to DCI Last week, the Defense Threat Reduction Agency (DTRA) took unilateral action contrary to this decision and informed DCI that DTRA will not fund the project. DTRA now plans to close DCI's contract as a failure. DCI is working hard to have this astonishing decision by DTRA reversed with the help of the Ukraine government.

*Background*

In October 1995, DTRA (then known as the Defense Nuclear Agency) awarded DCI a $4.1 million contract for Ukraine. Under the contract, using $3 million of Nunn-Lugar funds and $1.1 million of DCI funds, DCI was to establish a die cast manufacturing site in Ukraine through a joint venture with a Ukrainian defense conversion partner, Meridian. However, the Meridian project turned out to be a pure startup for which required outside financing could not be obtained. So, in 1997, with the support of the Ukraine government and approval of DoD, DCI and Burevestnik agreed to work together to form a joint venture to produce die castings. By the beginning of 1998, DCI had achieved most of the project's objectives, including:

- DCI designed and had manufactured $3 million of high-techology, capital equipment to be contributed to the joint venture with its Ukraine defense conversion partners, Burevestnik and TechnoMet. Seventy percent of this equipment was produced in the United States, thirty percent in Moldova and Russia.
- Under DCI's leadership, a former Soviet manufacturer and a leading U.S. manufacturer collaborated to produce new machines designed and built with American technologies for the Ukrainian and Russian markets.
- DCI developed and negotiated a joint venture agreement and charter with its Ukraine partners, to form a Ukrainian closed joint stock company where DCI will control the Board of Directors and business flow.
- DCI has organized a team of leading experts from America, Ukraine and Russia that will help ensure the success of the conversion project.
- DCI's Ukrainian partners have agreed to contribute to the joint venture buildings, manufacturing equipment and a strong backlog of manufacturing orders. The current operations are profitable, with over eighty percent of $2.2 million sales exported to Europe and East Europe.
- DCI had obtained agreements to transfer Russian furnace technology to North America with General Signal and to transfer to America Ukrainian metallurgical technology to recycle manufacturing metal waste.

*DCI's. Efforts to Complete the Project*

However, DCI's original contract funds from DTRA ran out in 1998. Since then, DCI has requested $730,000 in additional funds to complete the project by registering the joint venture, upgrading the plant facilities, installing the equipment, providing operator training and incorporating quality control equipment and practices. DCI has continued operations in order to obtain those funds. Meanwhile, the following events have occurred:

- June 1998: After identifying $750,000, DoD executed an agreement with the Ukraine Ministry of Defense to fund the additional needs of the DCI-Burevestnik conversion project. At that time, $500,000 was allocated for DCI-Burevestnik and $250,000 for a project that has never developed.
- December 1998: Senator Strom Thurmond, then Chairman of the Senate Armed Services Committee, wrote a letter to Secretary Cohen requesting full funding of the DCI project. (*See* attached letter).
- February 1999: Secretary Cohen responded that DoD plans to provide the additional funds to DCI, subject to negotiations with DTRA. (*See* attached letter). Immediately after this letter, DCI went to DTRA at DTRA's request to negotiate, but DTRA did not negotiate then and has not negotiated since.
- March-August 1999: DCI sent letters and used other means of communication to reach key government officials, such as Secretary Cohen, Vice President

Gore, and Ambassador Pifer, asking them to save the valuable DCI-Burevestnik project in Ukraine. (*See* attached letter).

- August 1999: Assistant Secretary of Defense Edward Warner wrote to DCI that DoD shares DCI's interest but does not have the $730,000 requested by DCI available and could not proceed until some Defense Contract Audit Agency (DCAA) issues were resolved first. Those issues have since been resolved, having been determined to have no impact on the funding or the project.
- January-May 2000: Deputy Assistant Secretary of Defense Susan Koch, who reports to Dr. Warner, decided to provide $560,000. DCI adjusted its operating plans to complete the project within those funds. Dr. Koch reaffirmed her decision in early May 2000, and DTRA was tasked to implement her decision.
- May 2000: DCI had to engage a Washington law firm to stop DTRA from taking unilateral action to move $2 million of the project's equipment to an undisclosed location without DCI's consent. DTRA would not answer DCI's simple questions, such as how it planned to move the equipment and how it planned to ensure that supplier support and warrantees would remain effective. The manner in which DTRA took such unilateral action has caused additional project restart costs of approximately $115,000.

*DCI's Need for Relief*

Throughout this time, DCI has received continued support from its Ukraine partners and from the Ukraine government. Yet, after more than a month following Dr. Koch's May decision and without negotiating, over the past week DTRA has informed DCI that it will not provide either a contract modification or a grant to complete the project. This indicates that DTRA unilaterally plans to terminate the project as a failure, something that should be unacceptable by all parties, American and Ukrainian.

DCI needs to have DoD-Policy's decision implemented immediately, with DTRA providing the $560,000 as a grant. In addition, DTRA should pay directly the $115,000 costs caused by DTRA's conduct last month. Only in this way can DCI save what can surely be a successful defense conversion project.

*Political Ramifications*

There are several serious political ramifications if the project is not completed, including:

- Instead of producing $6 million of new export sales for a severely depressed Ukraine economy, instead of providing an additional 100 to 150 jobs in Ukraine, and instead of having American technologies showcased in the capital of Ukraine for export to Russia and Ukraine, the $3 million of equipment purchased by DCI and DoD has been gathering dust in storage for more than 2.5 years.
- Instead of providing a model American-Ukrainian enterprise to showcase how the two countries can work together, the only showcase will be how DoD did not honor its June 1998 commitment.
- Instead of one successful conversion project with an American company, for the nearly $100 million of taxpayers' Nunn-Lugar funds invested under the oversight of DTRA since 1994 ($20 million in Ukraine), DTRA and DoD will have a string of failed projects. Compounding this is the loss of the future prospect the DCI project presents. With the successful completion of the first DCI model joint venture, DCI plans to replicate that model, similar to franchising, into a string of up to ten additional joint ventures that would provide for well over 3,000 additional jobs in Ukraine and Russia, significant hard currency cash flow, and considerable export sales of American technology.
- Instead of having a model industrial operation that could be replicated in Kharkiv, Ukraine as part of the Kharkiv Initiative, the failed DCI project will only support the broken U.S. Government promises similar to those articulated in the New York Times on June 6: "Deprived Ukraine City Finds U.S. Help No Help."
- Instead of allowing DCI to showcase a DoD defense conversion project where American technologies can be exported into Russia and Ukraine and where Russian and Ukrainian technologies could be transferred to America, those technologies remain dormant at the detriment of American industry.

*The Key Players*

The key DoD personnel involved with this project are:

- Dr. Edward Warner, Assistant Secretary of Defense, Strategy and Threat Reduction (STR).

- Dr. Susan Koch, Deputy Assistant Secretary of Defense, STR/Cooperative Threat Reduction.
- Mr. Marc Palevitz, Administrator in Dr. Koch's office, and lead policy person on the DCI project.
- Brigadier General Thomas Kuenning, Ret., Director—Threat Reduction Implementation Office, DTRA.
- Mr. Edward Archer, Senior Contracts Officer, Contracts and Acquisition Office, DTRA.

*Conclusion*

It is such a waste for DoD not to release funds that it has been sitting on for five years and that were promised to the Ukraine government two years ago, and thus preventing the United States and Ukraine governments from demonstrating at least one successful conversion project between American and Ukrainian companies. After failures with over $100 million of Nunn-Lugar funds allocated to DTRA's oversight and with the $70 million of Nunn-Lugar funds given to the Defense Enterprise Fund, the chance for one success should be absolutely and earnestly pursued by DoD. Yet, DTRA makes its own policy decisions and takes unilateral actions that go against that logic.

Very truly yours,

ALAN C. FREDERICKSON, *President.*

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PREPARED STATEMENT OF CHARLES M. LUDOLPH, DEPUTY ASSISTANT SECRETARY FOR EUROPE, INTERNATIONAL TRADE ADMINISTRATION, U.S. DEPARTMENT OF COMMERCE

I. INTRODUCTION

Mr. Chairman, I am pleased to be with you this afternoon to discuss U.S. business activity in Central and Eastern Europe and to review what the Commerce Department's International Trade Administration is doing to advance U.S. commercial interests in this important region. In the ten years that have passed since the countries of Central and Eastern Europe (CEE) rid themselves of communism, considerable progress has been made in the region to secure democracy and establish free-market economic systems. The pace and depth of political and economic reform has varied in Central and Eastern Europe and progress has sometimes been uneven, but the course is clear. Democratic values are taking hold and central planning has given way to free-market principles throughout the region. The private sector in Central and Eastern Europe is vibrant and growing and the countries are moving closer towards membership in the European Union (EU).

The Commerce Department's International Trade Administration (ITA) has been a very active player within the USG in encouraging and supporting the economic transformation of Central and Eastern Europe. We have a unique interaction with the U.S. business community, and have been able to significantly expand America's commercial presence in the region and to protect U.S. economic interests already there. As a result, U.S. foreign policy objectives in Europe have been furthered and peace has been made more secure. Today, I would like to review the extent of U.S. commercial activity in Central and Eastern Europe, the opportunities for American firms in the region, and the extensive program of support that Commerce ITA offers to the U.S. business community to help them compete, including efforts to overcome market access problems that they confront. We have been very successful in our efforts and we have several examples to relate to you.

II. STATUS OF U.S. EXPORTS AND INVESTMENT IN CENTRAL AND EASTERN EUROPE

During the last decade, U.S. firms have learned to view CEE not only as an emerging market, but also as an emerging marketplace. American companies have grown increasingly sophisticated in their understanding of the opportunities, difficulties, and challenges of doing business in the region. As a result, both U.S. exports and investment in CEE have dramatically increased.

*Trade:* Since 1991, U.S. firms have dramatically increased their trade and investment activities in Central and Eastern Europe. In 1991, U.S. companies exported $1.6 billion of goods to the fourteen countries of Central and Eastern Europe: Albania, Bosnia-Herzegovina, Bulgaria, Croatia, Czech Rep., Estonia, Hungary, Latvia, Lithuania, FYR Macedonia, Poland, Romania, Slovakia, and Slovenia. By the end of 1999, U.S. exports had doubled to $3.2 billion. U.S. companies exported more than $338 million of meat, $295 million of aircraft, and $295 million of machinery in the first three months of 2000. Between 1991 and 1999, imports from the region increased from $3.7 billion to $6.7 billion.

Poland, with a population of almost 40 million, is the largest market in the region. In 1999, U.S. firms exported more than $825 million worth of goods to the Polish market. During this same year, U.S. companies exported $610 million of goods to the Czech Republic and $503 million worth of goods to Hungary. Together, these three markets account for more than 60 percent of U.S. exports to Central and Eastern Europe. In 1999, the United States imported $813 million worth of goods from Poland, $754 million of goods from the Czech Republic, and $1.89 billion worth of goods from Hungary. Imports from these three countries equaled 47 percent of total imports from the region (for detailed export and import data by individual country, see Annex 1).

*Foreign Direct Investment:* U.S. investment in Central and Eastern Europe also has risen dramatically over the past decade. By the end of 1999, U.S. companies had invested more than $16 billion in the region. American firms have invested more than $7 billion in Hungary, $5.1 billion in Poland, and $1.5 billion in the Czech Republic. Together these three markets have attracted 85 percent of all U.S. investment in the region.

One clear indication of increased U.S. business presence in Central and Eastern Europe is the exponential growth of membership in American Chambers of Commerce (AmCham) in the region. In the 10 years since the first AmCham was formed in Hungary, 1,885 individual companies have joined the 11 separate AmChams established throughout the region. U.S. Embassies in Albania and Macedonia are currently working with representatives of local U.S. companies to open AmChams in their respective countries; this would mean AmChams in 13 of the region's 15 countries. AmChams are important because they offer U.S. companies active in these markets a vehicle to express their views and concerns on doing business to host-country governments and they help build confidence in the local market for prospective new U.S. commercial partners.

## III. BUSINESS OPPORTUNITIES IN CENTRAL AND EASTERN EUROPE

The appeal of the Central and East European markets to U.S. exporters and investors stems from opportunities created during (1) their transition from centrally-planned to market economies and (2) the process of modernizing their economies in an effort to meet EU standards as they vie for eventual EU membership. The transition period has opened up these markets to Western goods, forced old industries to retool and reshape themselves, and created entirely new companies and industries in the region. The last decade has witnessed the massive privatization of state enterprises and utilities and the modernization of infrastructure. All of this change has increased the prospects for U.S. companies.

The potential for future growth is a source of optimism about these countries. In 1999, Poland's growth rate was 4.0 percent, the Czech Republic's was zero, and Hungary's was 4.2 percent. The European Bank for Reconstruction and Development forecasts real GDP growth for 2000 to be 4.5 percent for Poland, 2.0 percent for the Czech Republic, and 4.0 percent for Hungary. Their prospects for growth are expected to rise further as economic reforms continue and as they approach EU membership.

*Trade:* Part of the uniqueness of these markets is that Western consumer products had very little penetration prior to 1989. Now, CEE consumers' strong desire to take advantage of their new range of choices and their growing purchasing power translates into market opportunities for U.S. exporters. Additionally, the services sector in these countries was virtually non-existent prior to the transition. In the last decade, U.S. companies have successfully introduced services ranging from insurance to consulting to dry cleaning.

During the transition, CEE companies have had to modernize themselves to become competitive under free market conditions. They have sought U.S. technology and inputs in their restructuring efforts. Further, the CEE countries' drive to modernize their economies and prepare for EU accession has resulted in great efforts to develop basic infrastructure, such as telecommunications networks and roads. Strong projections for increased energy demand in the future have resulted in ambitious government plans to increase generation capacity and to upgrade distribution networks. U.S. companies have been at the forefront of both enterprise restructuring and infrastructure development.

The environmental technologies sector has particularly strong prospects for U.S. business. The environmental legacy of communist industry was polluted air, water, and soil. Meanwhile, the EU accession process has forced the CEE countries to bring their environmental standards in line with those of the EU. The result is significant opportunities for the sale of environmental technologies and services in the CEE region.

As the CEE economies recover and grow, CEE government procurement has become a significant source of opportunities. CEE governments are in the process of procuring products as diverse as aircraft, municipal water treatment systems, computer networks, and medical equipment. U.S. companies are lead competitors in these procurements.

Finally, in Southeast Europe, internationally funded reconstruction and development efforts are underway. New activities in the areas of energy, transportation infrastructure (including roads, ports, and bridges), and construction create opportunities for U.S. firms in this relatively unexplored region. However, since the majority of the large infrastructure projects will be funded by the EU, and implemented through tenders limited to companies located in the EU, American companies face a significant challenge when bidding on internationally-funded projects.

*Foreign Direct Investment:* The U.S. is already a major foreign investor in Central and Eastern Europe. American investors are taking advantage of the strategic location, good infrastructure, skilled and educated labor, and relatively low labor costs (compared to the EU), of countries such as Hungary, the Czech Republic, and Poland. In some cases, U.S. companies have invested to supply CEE domestic markets. In other cases, U.S. companies are placing investment in CEE countries to manufacture products which are then exported to the much larger EU market. Industrial products manufactured in CEE countries enter the EU duty-free as a result of the Europe Agreements—commonly referred to as the association agreements—that the CEE countries have signed with the EU. In addition, seven countries in the CEE region have entered into a multilateral free trade agreement, the Central Europe Free Trade Agreement (CEFTA). Those countries include Poland, Hungary, Czech Republic, Slovakia, Slovenia, Romania, and Bulgaria.

U.S. investment has taken several forms. Massive privatization efforts are attracting American companies to the telecommunications, energy, and light and heavy manufacturing sectors, to name a few. Further, CEE companies of all sizes are seeking U.S. joint venture partners. American companies have formed many successful partnerships with CEE companies, in particular, using the CEE companies' knowledge of local market conditions. Finally, U.S. companies are building greenfield manufacturing sites, and increasingly are investing in more high-tech, value-added facilities in the electronics, information technology and automobile parts sectors.

Overall, the prospects for doing business in the CEE region are strong and diverse for both U.S. exporters and investors. If companies are willing to be flexible to changing conditions, there are significant emerging opportunities to pursue in this dynamic region.

## IV. USDOC/INTERNATIONAL TRADE ADMINISTRATION (ITA) PROGRAMS

### *A. Market Entry*

ITA supports U.S. companies interested in Central and Eastern Europe both here at home and overseas through a variety of means. Various ITA units help introduce American firms to the region's markets. But ITA's efforts do not stop there. ITA counsels and supports U.S. firms during the entire commercial undertaking, ensuring that the playing field is level and that American companies are treated fairly.

*Central and Eastern Europe Business Information Center (CEEBIC):* The heart of ITA's program for the region is our Central and Eastern Europe Business Information Center (CEEBIC), located in ITA's Market Access and Compliance unit. CEEBIC is a ten-year old program, funded by USAID, that serves as the USG's central clearinghouse for all economic, commercial, and financial information on 15 countries of Central and Eastern Europe. In particular, CEEBIC's overseas network of 13 foreign national trade specialists develops detailed information on new commercial opportunities in Central and Eastern Europe. That information is sent back to Washington where CEEBIC's headquarters staff puts it on CEEBIC's website and in its several publications for wide dissemination to the U.S. business community.

Our website—CEEBICNet—is a highly popular service receiving more than 135,000 inquiries weekly. It contains not only trade and joint venture leads for U.S. companies but a broad range of information products including market research, information on sources of finance, fact sheets, unclassified U.S. Embassy reporting cables from throughout the region, and materials provided by the CEE countries themselves. It also contains important links to other USG websites, as well as those maintained by Central and East European countries and institutions. CEEBIC maintains a database of over 11,000 U.S. companies which regularly use its services (for a breakdown of the database by state, see Annex 2). CEEBIC has a monthly publication—*Commercial Update*—and a weekly internet publication—*Southeast Europe Business Brief*, both of which offer timely and substantive information on CEE markets to potential U.S. business partners.

CEEBIC also provides crucial support to the Administration's efforts to secure peace, build democracy, and create long-term prosperity in Southeast Europe in the aftermath of the Kosovo conflict. CEEBIC is adding foreign national trade specialists in Kosovo and in Northern Greece to serve the Balkan region. It also is the USG's leading source of information on reconstruction and economic development projects under the Stability Pact for Southeast Europe—a multilateral initiative of the United States and other G-8 countries designed to strengthen the war-torn Balkan region economically and politically. In furtherance of this objective, CEEBIC will conduct business seminars and briefings for U.S. firms to help them better understand the new commercial opportunities stemming from the Stability Pact and other projects being funded through international financial institutions.

CEEBIC is much more than just an information service. It also provides a highly effective business counseling and commercial development function. Once U.S. firms have been given information about the CEE markets and have begun to interact with their CEE counterparts, CEEBIC continues to guide and counsel them through that initial interaction and their negotiations with CEE companies and governments. We vigorously advocate for them against foreign competition, and when necessary, we work to protect their interests. This function is highly important for U.S. companies which face the many uncertainties of the CEE markets and their frequently difficult business climates.

*U.S. Commercial Service:* ITA's U.S. Commercial Service (CS) is committed to assisting U.S. firms in realizing their export potential by providing expert counseling and advice, information on markets abroad, international contacts, and advocacy services. In Central and Eastern Europe, 11 American CS officers provide in-country support and expertise as for U.S. companies doing business in this dynamic market. They also manage a network of 46 foreign national employees in the region to provide U.S. firms with hands-on support and guidance in these complex markets.

The U.S. Commercial Service provides timely and customized business solutions to assist U.S. firms to enter the new markets of CEE. This is done through a combination of cost effective basic and specialized services, including the following:

- *Agent-Distributor Service:* CS specialists locate potential partner companies in Central and Eastern Europe that are interested in distributing U.S. products overseas;
- *Gold Key Service:* CS specialists identify and organize individual meetings between U.S. companies and potential CEE partners and/or key government officials.
- *International Company Profile:* To address concerns about potential partners, CS specialists perform background checks on CEE companies to reduce the commercial risk of a transaction.
- *Showcase Europe:* In support of increased U.S. exports to Europe, the integration of Central and Eastern Europe into the global economy, and the development of an export strategy that views Europe as a single export market, CS offices throughout the CEE region and Western Europe are working together to promote export opportunities to U.S. companies.

*Advocating for American Business:* ITA's Advocacy Center acts as a unique, central coordination point marshaling the resources of 19 U.S. Government agencies in the Trade Promotion Coordinating Committee (TPCC) to ensure that sales of U.S. products and services have the best possible chance abroad.

Advocacy Center assistance in Central and Eastern Europe is broad and varied, but most often involves companies that must deal with CEE governments or government-owned corporations in some way. Assistance can include: (1) visits to a key CEE minister or deputy minister by a high-ranking U.S. government official; (2) direct support by U.S. officials (including Commerce and State Department officers) stationed at U.S. embassies in the CEE region; and (3) action coordinated by U.S. government agencies to provide maximum assistance in a case. The Advocacy Center is at the core of the President's National Export Strategy; its goal is to ensure opportunities for U.S. companies throughout the new markets of Central and Eastern Europe.

In the CEE region, the Advocacy Center has aggressively pooled the strength of numerous U.S. Government agencies, including Commerce, State, and Treasury, to support U.S. companies as they bid for major projects. For example, in 1998, the Advocacy Center wrote highly effective Secretarial letters on behalf of the U.S. company Parsons Power Group Inc. to the Croatian government to support Parsons' successful attempts to win a $96 million contract to upgrade a power plant in Croatia. Parsons had been introduced to the Croatian market during its participation in former Secretary Brown's trade mission to Croatia in 1996.

The Advocacy Center is currently assisting 40 U.S. companies pursuing projects in Central and Eastern Europe valued at $11.7 billion.

*Trade Promotion Coordinating Committee (TPCC):* Through the Trade Promotion Coordinating Committee, other U.S. Government agencies also are active in promoting U.S. commercial development in Central and Eastern Europe. Specifically, the Trade Development Agency (TDA), the Overseas Private Investment Corporation (OPIC) and Eximbank all are working with ITA to increase U.S. commercial presence in the region. For example, TDA and OPIC are co-located with our commercial office in Zagreb, Croatia to identify new infrastructure projects of potential interest to U.S. investors.

*B. Assuring Market Access*

While good opportunities exist, the CEE markets also pose significant challenges. U.S. firms often face considerable obstacles when investing in or exporting to Central and Eastern Europe. These barriers usually stem from one of the following elements: (1) the transition from a centrally-planned to a market economy and (2) the EU accession process.

*1.) Non-Tariff Barriers*

A majority of the non-tariff barriers in Central and Eastern Europe are a direct result of the region's inexperience with a market economy and the immature legislative and regulatory environment that governs market relations in the region. As the CEE countries develop, the severity of many of these challenges is reduced and market forces become a determining factor in business relations. Poland, Hungary, and the Czech Republic have seen the most significant gains in this area, while the countries in Southeast Europe, particularly Albania and Bosnia and Herzegovina, still face severe market barriers. The primary non-tariff barriers in CEE are:

*Corruption:* Corruption is cited often by American firms as the most significant problem when doing business in the CEE region. Specifically, many companies face difficulties: when processing goods through customs, when applying for a business license, and when bidding on government procurements.

In Southeast Europe, in particular, ITA is playing a lead role in the U.S. Government's aggressive approach to combating corruption by actively fighting corruption through various international fora. ITA's Assistant Secretary for Market Access and Compliance Patrick Mulloy, as one of.the U.S. Government's OSCE Commissioners, has championed the involvement of the OSCE in the fight against corruption in Central and Eastern Europe. Also, in cooperation with other members of the Stability Pact, we have lobbied the countries of Southeast Europe to adopt and implement the Stability Pact's Anti-corruption Initiative. This program outlines numerous measures that must be implemented in order to create an environment conducive to non-corrupt business practices.

*Lack of Transparency:* A second problem, closely related to corruption, that is prevalent throughout Central and Eastern Europe is the lack of transparency in decision-making, tendering, and government procurement. Decisions that affect legislation governing the business climate, specific government tenders, regulatory decisions, and judicial processes are often implemented in a non-transparent manner. To tackle this specific problem, ITA has encouraged the CEE countries to support U.S. Government efforts in the World Trade Organization that focus on improving transparency, especially in the area of government procurement. ITA is also actively engaged in the Stability Pact for Southeast Europe's fight to improve transparency in the region. ITA played an instrumental role in the drafting of the Stability Pact's Investment Compact, which places significant importance on improving transparency in the region.

*Lack of Protecting Intellectual Property Rights (IPR) Protection:* Through the Special 301 process, the U.S. Government monitors the enforcement of intellectual property rights around the world. In Central and Eastern Europe, this program is especially important due to high levels of IPR infringement, especially in the pharmaceutical, audio recordings, and optical media sectors. In the Special 301 review for 2000, five CEE countries (Czech Republic, Hungary, Latvia, Lithuania, and Romania) were placed on the Special 301 Watch List, while Poland was placed on the Priority Watch List for significant copyright infringements on sound and video recordings.

*2.) Tariff Barriers*

*Tariff Differentials:* While the U.S. Government supports EU enlargement into Central and Eastern Europe, one serious concern is the tariff differentials arising from the Europe Agreements—commonly referred to as the association agreements—that these countries have signed with the EU. (See Annex 3 for list of countries that have signed Europe Agreements.) Under these agreements, CEE countries give EU exports duty-free treatment while still retaining Most Favored Nation (MFN) rates for U.S. exports. Once the CEE countries enter the EU, they will bring their tariffs in line with the EU's Common External Tariff (CXT). For industrial tariffs, this will generally result in a reduction of CEE tariffs to the CXT level.

This tariff differential problem could affect whether CEE countries continue to receive U.S.-Generalized System of Preferences (GSP) benefits. Under the GSP statute, GSP may not be extended to countries that give more favorable tariff treatment to another developed country (such as the EU) than they do to the United States, if such preferential treatment has, or is likely to have, a significant adverse effect on U.S. commerce. U.S. GSP law requires that a country affording such preferential treatment be excluded from the U.S. GSP program if the President determines that it is providing such adverse preferential treatment.

In August 1999, the Senate Finance Committee raised its concerns about this matter in the report on the bill which extended the GSP statute for another three years. Chairman Roth of the Senate Finance Committee, Senators Biden, Levin and Hollings, Chairman Archer of the House Ways and Means Committee, Congressman Visclosky, and Congressman Bliley have sent letters to Secretary Daley expressing their concerns about the tariff issue.

The ITA, in conjunction with State and USTR, is encouraging CEE countries to reduce their applied industrial tariffs to the level of the E.U.'s CXT before full accession to provide relief to U.S. exporters. In addition to consultations with CEE officials visiting Washington, ITA Assistant Secretary for Market Access and Compliance Patrick Mulloy traveled to Poland, Hungary and the Czech Republic in June 1999 to press this issue and has written often to regional officials to follow up. Assistant USTR Catherine Novelli traveled to the those countries in March 2000 to press them to move on tariffs on products of particular interest to U.S. trade. In April 2000, A/S Mulloy returned to the Czech Republic and went to Slovakia and Slovenia to urge immediate tariff reductions to the CXT. In all of these meetings, the linkage of the tariff issue with GSP benefits was raised.

The President's Compliance Initiative seeks increased resources to combat this and other market access issues in Central and Eastern Europe and elsewhere in the world.

## V. ITA SUCCESS STORIES

Since the collapse of communism in CEE, ITA has been extremely successful in supporting U.S. companies as they take advantage of market opportunities in the region. Working together, the Central and Eastern Europe Business Information Center (CEEBIC), the U.S. Commercial Service, the Advocacy Center, and other ITA offices, have supported the presence of American firms and products throughout the region.

CEEBIC has been especially successful at supporting small and medium sized U.S. companies (SME's) as they expand into the region. Since 1990, when CEEBIC was founded, the support from CEEBIC staff for SME's has been considerable and successful, as evidenced by the following examples.

### *A. Helping Small and Medium Companies Expand into Central and Eastern Europe*

*CEEBICNET Leads to Exports for Illinois Manufacturer:* Global Development/ Aaron Equipment is a small manufacturer based in Chicago, Illinois, with offices in Portland, Oregon and Sarasota, Florida. The company has been involved in environmental technology since 1960 and is a supplier of environmental equipment to many major U.S. and multinational firms.

In January 1998, Global Development's President, Dan Burda, e-mailed CEEBIC informing that, "We have been investing in the Czech Republic in heavy industry and feel that it has been possible through information we obtained by your site [on the World Wide Web]." During follow-up conversations with Mr. Burda, CEEBIC learned that Global Development consults CEEBICNET regularly for both trade and investment leads and current commercial and economic information. The company's involvement with a Czech recycling and co-generation facility is the result of a trade lead published on the CEEBIC web-site. Global Development is exporting $25 million in environmental technology and equipment to the Czech firm. Mr. Burda was very complimentary of CEEBIC urging, "Keep up the good work!"

*CEEBIC assists Idaho firm with new-to-market Sales in Latvia:* In January 1998, Brian Page of Dome Technology, a small Idaho company beginning its international expansion, was unable to find a shipping company that could ship $2 million worth of construction materials to Latvia. In a conversation with a CEEBIC Washington-based Trade Specialist about Latvian tax rates, Mr. Page was pleased to learn that CEEBIC provided a substantial amount of additional market and country information, and was well informed about shipping companies that regularly send goods to

Central and Eastern Europe, including Latvia. CEEBIC provided Mr. Page with a list of shipping companies with services and experience in the region. According to Mr. Page: "We went with one of these lines. Thank you so much. We had no luck anywhere else we turned to."

*Florida Investor Continues Airline Services in Croatia with CEEBIC/FCS Assistance:* John Barber invested over $750,000 in Croatia in 1992 to begin his own Airline, Ivan-Air, Ltd. This small firm provides airline services in-country for tuna fishermen, among other Croatian businesses, needing to get their goods to market. In the summer of 1997, the American investor experienced difficulty with the Croatian Ministry of Communication in getting an Air Operator Certificate (AOC) re-issued. Ivan-Air, Ltd. suspected unfair practices and approached the Commercial Section of the U.S. Embassy in Zagreb for assistance. From August to November 1997, Ivan-Air, Ltd. was losing $1,000 daily.

The Commercial Service's Patrick Hughes along with CEEBIC representative Damir Novinic advocated on Ivan-Air's behalf and had U.S. Ambassador to Croatia Peter Galbraith write a letter to Croatian Minister Luzavec. Within ten days of this letter, on November 24, 1997, the Air Operator Certificate was re-issued to Ivan-Air, Ltd. Mr. Barber thanked the Embassy expressing his "sincere appreciation in particular to Patrick Hughes and Damir Novinic" citing that their assistance "made a significant difference" in keeping his business alive. This joint effort by FCS and CEEBIC allowed Mr. Barber to continue his airline services in Croatia and illustrates how FCS and CEEBIC work together on important market access issues affecting U.S. business.

*B. Ensuring Market Access for U.S. Companies in Central and Eastern Europe*

*Slovenia Reducing Industrial Tariffs to EU's Common External Tariff (CXT):* The ITA, working in conjunction with State and USTR, has encouraged CEE countries to reduce their applied industrial tariffs to the EU's common external tariff (CXT) prior to accession. This is the best way to help minimize the tariff differentials that arise as part of the Europe Agreements that the CEE countries have signed with the EU. For example, in Slovenia, the trade weighted average MFN tariff facing top 100 U.S. exports to Slovenia in 1998 was 8.12 percent. If Slovenia adopted the CXT on those same products, the trade weighted average would be 2.02 percent, an improvement of 6.10 percent.

During 1998 and 1999, the ITA and other USG officials met with and wrote to senior Slovene officials about this issue. As a result, the Slovene Ministry of Economic Relations and Development drafted a tariff strategy to phase-in tariff reductions on all industrial products to reach the level of the CXT by 2003. Slovenia began lowering tariffs on a temporary basis in 1999. In April 2000, ITA's Assistant Secretary for Market Access and Compliance Mulloy traveled to Slovenia to urge the Slovene Government and Slovene parliamentarians to pass legislation that would implement the comprehensive tariff reduction plan and make tariff changes permanent. This legislation is moving forward in the Slovene parliament.

*Bulgaria Cracks-down on Optical Media Piracy:* Working together with the U.S. Trade Representative (USTR) and the State Department (State), ITA was especially successful in pressuring the Bulgarian Government, through the Special 301 program, to aggressively tackle the severe levels of optical media (compact discs and CD-rom) piracy. In April 1998, Bulgaria, at that point the world's second largest producer of counterfeit optical media, was elevated to the Special 301 Priority Watch List and informed that they would be elevated even further, to the Priority Foreign Country list, if substantial improvements were not made in their enforcement regime. After significant pressure by ITA, USTR, and the State Department, Bulgaria introduced a stringent enforcement program and closed all factories that were producing unauthorized optical media.

*Southeast Europe: Commercial Opportunities and Partnerships:* On October 31–November 2, 1999, Secretary Daley led an interagency delegation to Sofia, Bulgaria to host the "Southeast Europe: Commercial Opportunities and Partnerships Conference." The Conference, which attracted more than 100 U.S. companies, achieved three objectives: It (1) provided U.S. companies the most current information about business opportunities in the region; (2) identified economic reforms needed in Southeast Europe and ways to improve the region's business environment; and (3) arranged more than 250 matchmaking meetings between 76 American and 62 regional companies.

The Conference advanced the Stability Pact's goal of increasing the role of Southeast Europe's private sector in the economic development of the region. Regional companies forged partnerships with U.S. companies and were briefed on current and future reconstruction and development priorities for the region. The Investment Roundtable furthered the Stability Pact's Investment Compact by encouraging regional governments to improve the climate for investment in their countries. Finally, the issue of corruption, which is a central theme in the Stability Pact, was discussed at length during the Investment Roundtable.

*CEEBIC to Host a Central and Eastern Europe Open House and a Business Forum on Southeast Europe:* On July. 14, the Central and Eastern Europe Business Information Center (CEEBIC) will celebrate its 10-year anniversary by hosting an open house for U.S. companies. CEEBIC Washington staff and CEEBIC employees from twelve countries in Central and Eastern Europe, will discuss new trade and investment opportunities with interested U.S. firms. Earlier that day, CEEBIC will host the Southeast Europe: Project and Financing Opportunities Forum. This inter-agency forum will explore financing and project opportunities for U.S. companies resulting from the multilateral Stability Pact for Southeast Europe and the U.S. Government's Southeast Europe Initiative. CEEBIC expects more than 300 U.S. firms to attend these events.

## ANNEX 1

U.S. Trade With Central and Eastern Europe, 1991–1999—Total U.S. Exports

[In Calendar Year and Millions of U.S. Dollars]

| Country | 1991 | 1992 | 1993 | 1994 | 1995 | 1996 | 1997 | 1998 | 1999 |
|---|---|---|---|---|---|---|---|---|---|
| World | 421,730 | 448,164 | 465,091 | 512,626 | 583,031 | 622,827 | 687,598 | 680,474 | 692,821 |
| Albania | 18 | 36 | 34 | 16 | 14 | 12 | 3 | 15 | 25 |
| Bosnia-Herzegovina | 0 | 5 | 25 | 39 | 28 | 59 | 102 | 40 | 44 |
| Bulgaria | 142 | 85 | 115 | 110 | 132 | 137 | 104 | 115 | 103 |
| Croatia | – | 91 | 103 | 147 | 140 | 106 | 139 | 97 | 108 |
| Czech Republic | – | – | 267 | 297 | 363 | 410 | 592 | 568 | 610 |
| Czechoslovakia | 123 | 413 | – | – | – | – | – | – | – |
| Estonia | – | 59 | 54 | 33 | 139 | 83 | 48 | 87 | 162 |
| Hungary | 256 | 295 | 435 | 309 | 295 | 331 | 486 | 482 | 503 |
| Latvia | – | 55 | 90 | 101 | 89 | 165 | 219 | 187 | 218 |
| Lithuania | – | 44 | 57 | 41 | 52 | 63 | 87 | 62 | 66 |
| Macedonia | – | 4 | 11 | 14 | 21 | 14 | 34 | 15 | 59 |
| Poland | 459 | 641 | 912 | 625 | 776 | 968 | 1,171 | 882 | 825 |
| Romania | 209 | 248 | 324 | 340 | 256 | 266 | 254 | 340 | 177 |
| Slovakia | – | – | 34 | 43 | 61 | 63 | 82 | 111 | 127 |
| Slovenia | – | 38 | 92 | 96 | 110 | 131 | 113 | 123 | 113 |
| Federal Republic of Yugoslavia | – | 39 | 2 | 1 | 2 | 46 | 49 | 74 | 59 |
| Yugoslavia | 371 | 225 | – | – | – | – | – | – | – |
| Total Central Europe | 1,578 | 2,278 | 2,555 | 2,211 | 2,479 | 2,854 | 3,483 | 3,198 | 3,199 |

## Total U.S. General Imports—Customs Value

[In Calendar Year and Millions of U.S. Dollars]

| Country | 1991 | 1992 | 1993 | 1994 | 1995 | 1996 | 1997 | 1998 | 1999 |
|---|---|---|---|---|---|---|---|---|---|
| World | 487,129 | 532,665 | 580,659 | 663,256 | 743,505 | 791,315 | 869,874 | 913,885 | 1,024,766 |
| Albania | 3 | 5 | 8 | 6 | 9 | 10 | 12 | 12 | 9 |
| Bosnia-Herzegovina | – | 10 | 7 | 4 | 3 | 10 | 8 | 7 | 15 |
| Bulgaria | 56 | 79 | 159 | 215 | 183 | 126 | 172 | 219 | 200 |
| Croatia | – | 47 | 106 | 115 | 93 | 71 | 83 | 73 | 110 |
| Czech Republic | – | – | 277 | 316 | 364 | 482 | 610 | 672 | 754 |
| Czechoslovakia | 145 | 241 | – | – | – | – | – | – | – |
| Estonia | – | 12 | 20 | 29 | 62 | 60 | 77 | 125 | 237 |
| Hungary | 367 | 347 | 401 | 470 | 547 | 677 | 1,078 | 1,567 | 1,892 |
| Latvia | – | 11 | 22 | 41 | 86 | 99 | 149 | 115 | 229 |
| Lithuania | – | 5 | 16 | 15 | 26 | 34 | 80 | 81 | 97 |
| Macedonia | – | 47 | 111 | 82 | 89 | 125 | 147 | 175 | 136 |
| Poland | 357 | 375 | 454 | 651 | 664 | 627 | 698 | 783 | 813 |
| Romania | 69 | 87 | 69 | 195 | 222 | 249 | 400 | 393 | 434 |
| Slovakia | – | – | 65 | 131 | 129 | 124 | 166 | 166 | 169 |
| Slovenia | – | 101 | 229 | 265 | 289 | 290 | 277 | 287 | 276 |
| Federal Republic of Yugoslavia | – | 39 | 0 | 0 | 0 | 8 | 10 | 13 | 5 |
| Yugoslavia | 674 | 225 | – | – | – | – | – | – | – |
| Total Central Europe | 1,671 | 1,631 | 1,944 | 2,537 | 2,768 | 2,993 | 3,965 | 4,688 | 5,376 |

Prepared by: U.S. Department of Commerce, Central and Eastern Europe Division, June 2000.
Source: U.S. Department of Commerce, Bureau of the Census.

## Annex 2

### CEEBIC Database by State

[As of June 15, 2000]

| | | | | | |
|---|---|---|---|---|---|
| Alabama | 53 | Louisiana | 45 | Ohio | 635 |
| Alaska | 5 | Maine | 51 | Oklahoma | 64 |
| Arizona | 109 | Maryland | 431 | Oregon | 116 |
| Arkansas | 41 | Massachusetts | 507 | Pennsylvania | 527 |
| California | 1,171 | Michigan | 276 | Rhode Island | 60 |
| Colorado | 128 | Minnesota | 192 | South Carolina | 73 |
| Connecticut | 324 | Mississippi | 27 | South Dakota | 9 |
| Delaware | 22 | Missouri | 142 | Tennessee | 88 |
| Florida | 471 | Montana | 8 | Texas | 482 |
| Georgia | 205 | Nebraska | 42 | Utah | 35 |
| Hawaii | 18 | Nevada | 21 | Vermont | 39 |
| Idaho | 19 | New Hampshire | 75 | Virginia | 739 |
| Illinois | 693 | New Jersey | 446 | Washington | 172 |
| Indiana | 149 | New Mexico | 24 | Washington, DC | 785 |
| Iowa | 65 | New York | 1,205 | West Virginia | 25 |
| Kansas | 41 | North Carolina | 205 | Wisconsin | 207 |
| Kentucky | 60 | North Dakota | 14 | Wyoming | 3 |
| | | | | Total | 11,387 |

ANNEX 3

CEE Europe Agreement with European Union

| Country | Year Signed | Year Tariff Reductions (for EU) Began |
|---|---|---|
| Poland | 1991 | 1992 |
| Hungary | 1991 | 1992 |
| Czechoslovakia [1] | 1991 | 1992 |
| Romania | 1993 | 1993 |
| Bulgaria | 1993 | 1993 |
| Estonia [2] | 1995 | 1995 |
| Latvia [2] | 1995 | 1995 |
| Lithuania [2] | 1995 | 1995 |
| Slovenia | 1996 | 1997 |

[1] Note: After their split at the end of 1992, the Czech Republic and Slovakia signed separate Europe Agreements with the EU in 1993.
[2] In the case of the Baltics, Free Trade Agreements were signed in 1995, which went into effect immediately. The FTAs were later incorporated into Europe Agreements.

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## PREPARED STATEMENT OF PATRICIA SCHAUB, ENTERGY CORPORATION

### EXECUTIVE SUMMARY

It is a pleasure to submit this statement to the European Affairs Subcommittee on the experience of the Entergy Corporation in doing business in Central and Eastern Europe. Our statement will specifically discuss Entergy's experience in the energy sector in Bulgaria. Entergy will be rehabilitating an existing 840 MW lignite-fired electric power generating facility located adjacent to Bulgaria's largest lignite mine in the Southeastern part of the country.

In summary, we believe that Entergy's investment in Bulgaria is a win-win situation. It enables the Entergy Corporation to position itself in a strategic emerging energy market. On the Bulgarian side, our investment provides much needed improvements to a facility that has not been able to meet the environmental, health and safety standards required by the European Union. The rehabilitation will allow the plant to operate safely for many years, providing energy to a growing economy. While there continue to be obstacles to finalizing this project, we have been working as partners with the Bulgarian government to remove remaining impediments—which will benefit not only Entergy, but future investors, and ultimately, the Bulgarian economy.

### ENTERGY CORPORATION

Entergy is a global energy company, headquartered in New Orleans, Louisiana. The company is engaged in a wide range of power production and distribution operations, as well as in a number of other diversified service areas. The company is a leading provider of wholesale energy marketing and trading services, as well as a recognized leader world-wide in power development and nuclear power operations.

Currently, Entergy owns, manages and invests in power plants with a generating capacity of nearly 30,000 megawatts both domestically and internationally and delivers electricity to about 2.5 million customers in portions of Arkansas, Louisiana, Mississippi and Texas. In 1998, Entergy ranked among the largest U.S. utility companies, with total revenues of more than $8 billion dollars and total assets of more than $22.9 billion dollars.

Entergy Wholesale Operations (EWO)—the wholesale power development, trading and marketing unit of Entergy—is primarily focused on emerging competitive markets of North America and Europe. Its portfolio of assets currently includes roughly 12,700 megawatts of gross generation capacity in operation, under construction or announced development projects around the world. The portfolio includes fifteen assets located in nine countries.

One of Entergy's most important priorities as a company is its commitment to conduct its operations, both domestically and internationally, in a manner that places a high premium on health, safety and the environment. Entergy also places a high priority on its ability to give back to the communities it serves. This commitment can be seen in the company's sponsorship—at home and abroad—of a variety of education and literacy projects, community and economic development programs, health and social service projects and environmental improvement programs.

THE MARITZA EAST III PROJECT

In October 1998, Entergy signed a joint development agreement with the Bulgarian National Committee of Energy CoE (*now called the State Agency for Energy and Resources (SAEER)*), and the National Electric Company (NEK) to develop a project to own, operate and refurbish the Maritza East III power plant in Bulgaria. Entergy sees the "Maritza East III project" as the beginning of an important relationship between the company and its Bulgarian partners.

The Maritza East III plant is a lignite-fired facility located in south-central Bulgaria near the town of Stara Zagora. The facility is currently owned and operated by the NEK and is located 37 miles from the Turkish border. Lignite-burning plants currently supply 30-35% of power in the country. Lignite reserves at the site are estimated at approximately 2 billion tons and represent approximately 80 percent of the country's domestic coal reserves.

The scope of work for the Russian-designed power plant, which was originally commissioned between 1978 and 1981, consists of replacing worn-out boiler parts and making a variety of additional upgrades to turbines, plant control and pollution control systems. This work is of critical importance to the Bulgarian people and to the residents of the region. For example, like many other power plants in Eastern Europe, the Maritza East III plant is not currently fitted with modern pollution control equipment. Installation of new flue gas desulphurization (FGD) equipment as part of the Entergy refurbishment effort will reduce sulfur dioxide (SO2) pollution emissions by at least ninety percent (90%), or by over 1000 tons of SO2 per day. This reduction will mean that for the first time, SO2 emissions from the Maritza East III plant will meet World Bank SO2 emission limits. Furthermore, with the addition of this equipment, ground level concentrations for SO2 emissions in the vicinity of the Maritza East III plant will meet the E.U. and Bulgarian SO2 air quality standards that were established to protect public health.

All electricity generated by the plant will be sold to the NEK in accordance with Bulgaria's new energy law, which was passed in July 1999. The new law aims to bring the country in line with the E.U. electricity directive and is part of Bulgaria's overall E.U. accession program.

CURRENT STATUS OF THE PROJECT

Entergy has overall responsibility for the development of the project and is also leading the development effort, with support from NEK in several areas.

The total project cost is approximately $450 million dollars. The rehabilitation work and the installation of the FGD equipment is expected to take 36 months. However, during the rehabilitation program, each unit will be rehabilitated in turn, while the remaining three units will continue to operate. This will enable the total capital cost to be partly offset by internally generated funds.

Much of the initial permitting and licensing work has already been completed on the project. In addition, environmental approval for the project has been granted by the Bulgarian Ministry of Environment and Waters. Work to obtain the remaining approvals needed for the project is underway.

BULGARIA AT A CROSSROADS

Bulgaria is at a critical point in its history. Under the leadership of Prime Minister Ivan Kostov, Bulgaria has worked very hard over the past two years to turn its economy around and recover from years of mismanagement under socialist rule. The efforts of Prime Minister Kostov and his pro-reform government have recently been praised by a variety of world leaders. It is the goal of the Bulgarian government to be admitted to the European Union by 2006.

Major government accomplishments to-date include: reversing the country's economic decline; turning over 70 percent of the country's economic assets to private hands; and restoring 95 percent of the country's nationalized farmland under communism back to its original owners. Inflation in the country dropped from triple digits to 6.2 percent in 1999 and the economy grew by 2.5 percent—with 4 percent growth targeted for 2000. The government has pledged to continue its tough anti-corruption and anti-crime programs, its judicial reform programs and to find new ways to help alleviate widespread poverty and unemployment in the country.

The government has also committed to continue its focus on: privatization; attracting investment to Bulgaria's infrastructure sector; improving the country's overall business environment; and dismantling unnecessary licensing and regulatory barriers. In 1999, Bulgaria concluded 1,100 privatization deals, with payments totaling $587 million. Within the investment arena, Bulgaria's energy sector has been called one of the most attractive investment opportunities for foreign investors.

The energy sector is undergoing major restructuring to comply with IMF targets and to meet the deregulation and environmental standards of the European Union. The reforms, which will begin in earnest this year, attempt to eliminate state subsidies, close inefficient production facilities and encourage investment. An IMF-approved plan, which calls for the separation of power generation, transmission and distribution, will be submitted for government approval this year. Experts have noted that a number of major safety and environmental upgrades and improvements still need to be made in a number of Bulgaria's energy facilities before the sector will be safe or ready for E.U. accession.

THE BOTTOM-LINE IMPORTANCE OF THE MARITZA EAST III PROJECT

The Maritza East III project is an important test case, as it is the first privatization in the energy sector. If successful, it can serve as a catalyst for attracting much-needed foreign capital to Bulgaria. Moreover, the project is fully consistent with the efforts to upgrade the energy sector in advance of E.U. accession, and helps the country achieve the targets for energy restructuring set forth by the IMF and the World Bank. Since the signing of the Entergy deal, another U.S. investor, AES, has announced its intention to construct a thermal plant of 600 MW.

The implementation of the Maritza East III project will help ensure Bulgaria has sufficient, reliable electric capacity as it moves to close down the four oldest units of the Kozloduy nuclear plant. These four Soviet designed nuclear reactors have combined installed capacity of 1,760 MWs. Kozloduy 1-4 have been deemed unsafe by E.U. standards. As part of its commitment to join the E.U., Bulgaria has agreed to shut down the first two units by 2003 and the second two units by 2006.

The project will also help bolster the Bulgarian economy in other ways, as the Improvement Works contract includes more than $75 million dollars worth of local goods and services and will lead to the creation of 600 construction jobs. Over the long term, the number of staff directly employed at the plant (currently 1,600) will be reduced. However, the project upgrades will play a key role in securing the future of the remaining workers at the plant and at the mines. To assist the employees, who will lose their jobs, the project has targeted $5 million dollars over a three-year period to assist in the area of employee transition.

In addition to reductions in air emissions, the project will deliver other significant environmental benefits as well. These benefits include: reusing plant waste water and thereby substantially reducing water withdrawals from the Rosov Reservoir; cleaning up past land and water contamination; adding modern fugitive dust controls throughout the plant and plant site; treating plant domestic waste water; and improving treatment of plant oily waste water.

During the development of the project, Entergy will use its vast experience to introduce international management techniques and practices, drawing from its experience in similar projects in the U.S. and the U.K.

Entergy is working with the communities surrounding the power plant to identify priority projects for social investment and has set aside $250,000 per year for such efforts. The first project identified in this area is the installation of a central heating system in the primary school located in the village of Glavan. Entergy worked with the local municipalities to identify and fund this project which represents the first such partnership between an American company and a Bulgarian municipality.

Entergy is committed to making its investment in Bulgaria successful and to continuing its efforts to make Bulgaria an important, reliable and efficient energy hub in the Balkan region. In turn, the Maritza East III plant was identified as one of four projects to move forward in the energy sector in the recently published Governmental Program "Bulgaria 2001."

CHALLENGES THAT REMAIN FOR THE COMPLETION OF THE PROJECT

*1. Governing Law and International Arbitration*

Bulgarian law requires that contracts between Bulgarian entities must be governed by Bulgarian law and be subject to Bulgarian arbitration. Such arrangements are not usually acceptable to lenders. Bulgaria needs to adopt a law that guarantees companies like Entergy the right to international arbitration as a dispute resolution mechanism. The adoption of such a law is also a requirement for accession to the European Union.

This issue will be critical for all foreign investment projects undertaken on a "project finance/limited recourse" basis, and the government has recently stated that it will make the necessary changes to the law.

*2. Ability of the Government to Provide a Government-backed Guarantee*

NEK, the electricity off-taker, is a state-owned entity and by itself does not have the credit capacity to stand behind this or other similar large projects. Under this circumstance, lenders to Entergy are insisting upon government support for project agreements. While the government has the capacity to offer such guarantees, this capacity is restricted by current budget commitments to the IMF. The process therefore is very competitive, as other major investors in the infrastructure sector may require similar commitments.

*3. New Energy Law*

In July of 1999, the government passed a new energy law aimed at bringing the country in line with European Union electricity directives. The law introduces a new State Agency for Energy and Energy Resources and a new independent regulator. The law is now in force. However, the secondary legislation, which will define the detailed rules for the system's operation, is still being prepared. This task should be completed by April 2000. Entergy is thus initiating its project while the country's energy sector is still in a state of transition. The challenge for Entergy is to ensure that its contract agreements anticipate market changes.

*4. Economy in Transition*

Since the Maritza III project is the first privatization in the energy sector, Bulgaria finds itself confronted with decisions it has not previously had to make. This is compounded by the fact that its political and decisionmaking structure is evolving. This is a difficult situation for both Bulgaria and for power development. Efforts to streamline decisionmaking processes and to boost the government's capacity to deal with these types of transactions are critical to Bulgaria's ability to attract the capital it needs.

## CONCLUSION

Entergy is proud of its investment in and partnership with Bulgaria—and believes that the work that the company is doing in Bulgaria now—will ultimately lead to better lives for many future generations of Bulgarians.

Entergy looks forward to working with its Bulgarian government counterparts in coming months to resolve remaining project challenges and to ensuring that the Maritza East III project moves forward as quickly and as smoothly as possible.

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## PREPARED STATEMENT OF MR. PAUL SINGER, ELLIOTT ASSOCIATES, L.P.

### "UNFAIR TREATMENT OF AMERICAN INVESTORS BY THE GOVERNMENT OF POLAND"

Mr. Chairman and Members of the Committee:

Thank you for allowing me to present today for the Committee's consideration Poland's mistreatment of American investors in Poland's Mass Privatization Program.

Let me say at the start that our company, as well as many American companies, has welcomed Poland's entry into the world economy. These are not mere words; Americans have invested heavily in Poland's future. Elliott Associates, L.P., on whose behalf I appear, is one of many American companies that have invested over $100 million in Poland's Mass Privatization Program alone.

That is why we are particularly shocked by Poland's improper efforts over the past year to prevent American investors from receiving lawful profits on our investments. It is our hope—both that of Elliott Associates and that of other American investors in Poland—that efforts by the United States Government such as this hearing today will help to dissuade the Polish authorities from discriminating against American investors and interfering with lawful corporate activities. Poland's current course harms both American investors and the future economy of Poland.

For purposes of this Committee's inquiry into the treatment of American investments throughout the new market economies of Central Europe, I should add that Elliott Associates, like many other American companies, has also invested elsewhere in the region. Although Hungary has also faced a difficult transition from a centralized, state-owned system to the free market, our investments in Hungary have not encountered the same improper and discriminatory efforts to control lawful corporate activity that have plagued our Polish investments. In the case of Hungary, American investors are reaping the rewards earned by their willingness to take on the risk of investing in a transitional economy. We are confident that such rewards could accrue to American investors in Poland, as well, if Poland will allow American investors to profit from their investments.

## BACKGROUND: POLAND'S MASS PRIVATIZATION PROGRAM

In the mid-'90s, the Polish government launched its Mass Privatization Program to let free market forces reshape the face of medium-sized industry in Poland. Under this Program, the Polish government sought to privatize 512 medium-sized, grossly mismanaged Polish businesses that had previously been wholly owned by the Polish government. To this end, the Polish Parliament enacted a special law to create fifteen National Investment Funds ("NIFs") that would hold shares in the 512 newly-privatized companies. The fifteen NIFs, which are in effect mini-mutual funds, would themselves be publicly traded on the Warsaw Stock Exchange.

## AMERICAN INVESTMENTS IN POLAND'S PRIVATIZATION PROGRAM

To provide the capital and management skills needed to make this ambitious program work, the Polish government actively sought Western investors and managers. Attracting Western capital and bringing market discipline to the previously mismanaged companies was a primary goal of the Program. To encourage Western and Polish investors alike, the new law creating the NIFs guaranteed that the funds would, with a few exceptions not relevant here, be able to conduct business as normal joint stock corporations with all of the protections and powers such corporations normally have under the law.

Elliott Associates was one of the many American investment companies that answered Poland's call and invested heavily in the NIFs. Elliott Associates and other American firms believed that Poland was truly committed to market reform. We saw investment in a free market Poland as a "win-win" situation—American investors could earn a profit, and the Polish economy would get a vital injection of foreign capital and expertise to speed Poland's transition to a free-market economy. As noted above, conservative estimates place American investment in Poland's Mass Privatization Program in excess of $100 million.

## ACTIONS BY THE POLISH TREASURY TO PREVENT AMERICAN INVESTORS FROM RECEIVING PROFITS

One of the NIFs in which Elliott Associates invested was "NIF #8," known as "Octava." Octava became one of the few NIFs to earn a profit. On September 1, 1999, Octava shareholders voted overwhelmingly to amend Octava's Charter to permit redemptions of its shares for remuneration—a corporate practice commonly used throughout the United States and Europe to enable companies to distribute profits to shareholders by buying back shares. The resolution was passed with a 77% vote.

The proposed change to the Octava Charter was fully consistent with Polish law. The Polish government's equivalent to our Securities and Exchange Commission, the body charged with regulating securities markets, recently ruled that the share redemption amendment was perfectly consistent with Polish law. This opinion is seconded by opinions of leading Polish legal counsel. The NIF law provides that NIFs have the same power as other joint stock companies, except as otherwise provided in the NIF law. Neither the NIF law nor other Polish statutes contain any restrictions that would prevent an NIF from amending its articles of incorporation to permit share redemption. The Polish Commercial Code permits share redemptions, and in fact share redemptions have been employed by several Polish companies traded on the Warsaw Stock Exchange. Even the Prospectus, the document by which the Ministry of the State Treasury officially offered shares in Octava for public sale, referred to the lawful possibility of share redemptions.

Nonetheless, on September 9, 1999, the Polish Ministry of State Treasury moved to block Octava's steps to allow share redemptions. This is particularly disturbing, because the Treasury Ministry is the agency charged with leading Poland's privatization effort. Previously, the Treasury Ministry had proposed that Octava distribute its profits through a cash dividend. But the vast majority of shareholders, including many small Polish investors, realized that this would work to their disadvantage and voted to reject the Treasury plan. So the Ministry changed its position completely and sought to enjoin the distribution of profits, arguing for the first time that distributing profits would violate the NIF law.

The primary reason for the Ministry's improper, anti-market position soon became apparent. On Thursday, September 9, 1999, Deputy Minister of the State Treasury Alicja Kornasiewicz stated that the MST was opposed to the buy-back plan because it would allow "*large shareholders, e.g. American investment funds, the possibility to withdraw their money from the NIFs at a profit*" (Quoted by the Polish Press Agency, 9/9/99).

The inability of NIF investors to have their shares redeemed has been very damaging to the NIF shareholders and the value of their investments. Since the stock of the NIFs, including Octava, trade on the Polish market at a deep discount to their net asset value, this method of distributing profits is the only meaningful way for foreign investors to generate a significant return on their investment. Additionally, the mistreatment of investors in the NIFs has caused many investors to shun this asset class, leading to a distinct lack of liquidity in NIF shares. Hence, by preventing NIFs from redeeming shares, the Polish Treasury Ministry has effectively precluded large investors from exiting their investments in the NIFs and de facto confiscated their capital.

Since last fall, Elliott Associates has been in repeated contact with the United States Embassy in Warsaw. Our Ambassador and embassy personnel have contacted the Polish government, all to no avail. Elliott is currently involved in settlement negotiations with the Ministry in an attempt to avoid a drawn-out legal proceeding that will itself serve Poland's improper—and ill-advised—purpose of tying up American capital in Poland. We are told that the working level officials in the Ministry are in full agreement with our current proposal. We hope that higher Polish authorities, despite the current governmental difficulties there, will see the wisdom of reaching an agreement that will enable the shareholders of Octava to proceed on their chosen, lawful course.

## LONG TERM EFFECTS OF POLISH ABUSES OF LAW

Poland's clearly discriminatory action has the potential to do immense harm to both foreign investors and the Polish market as a whole. The Polish government, with American encouragement, established the NIFs to attract foreign capital to Poland and help the state-dominated economy transition to an open, free-market economy. If American and other foreign investors cannot reasonably rely on Polish law to permit investors to have access to a fair return on their investments, all incentive to continue investing capital in Poland will disappear. It was in part with this in mind that the United States and Poland in 1990 agreed upon—and the U.S. Senate ratified—the bilateral Treaty Concerning Business and Economic Relations that seeks to protect each country's investments against discriminatory treatment.

The transition of the Central European states to Western economies has not been without problems; nevertheless, the law creating the NIFs was a step in the right direction for Poland. The action by the Ministry of State Treasury, opposing the exercise of the legal rights of shareholders, sends an ominous signal to potential future investors. This harms Americans, but it will just as surely harm the future Polish economy.

## CONCLUSION

Elliott Associates hopes that this hearing, as well as continued efforts by the United States Government and other friends of Poland in other venues, will help to convince the Polish authorities to stop their obstructionism and allow American and other investors to reap the profits of their investments. If Poland will let the market work, the market will work for Poland.

Thank you very much for allowing Elliott Associates to present this testimony today, and we look forward to working with the Committee further on this matter.