

MEMORANDUM OF DETERMINATIONS

Expropriation Claim of Alliant Techsystems, Inc.
Ukraine-Contracts of Insurance Nos. D919 and D920

I. Claim

By letters dated November 20, 1998, with four volumes of supporting documentation, Alliant Techsystems, Inc. (together with its wholly-owned subsidiaries, "Alliant" or the "Investor") applied for compensation under the expropriation coverage of OPIC Contracts of Insurance Nos. D919 and D920 (the "Contracts") for the maximum insured amounts, \$1,500,000 and \$16,200,000, respectively (the "Claim"). The investment covered under Contract D919 is the value of services rendered to the foreign enterprise, JSC Alliant Kiev ("Alliant Kiev"), whereas Contract No. D920 covered an investment in equipment leased by Alliant to Alliant Kiev for its demilitarization project. OPIC has treated the two claims under the foregoing letters as a single claim because the related actions of the foreign governing authority were directed at the project and not the separate investments made in it.

The letters setting forth the Claim, the Executive Summary and the "Chronology of the Joint Stock Company Alliant Kiev" (the "Chronology") attached thereto may be found at Tab A and constitute a summary of the Claim presented by Alliant. Alliant responded to OPIC's requests for additional information by providing additional documents and explanatory material on March 11, March 24, April 14, April 26 and May 6, 1999.

OPIC's determination is that the Claim is valid. The amount of compensation shall be determined separately after further review of the supplementary information provided by Alliant.

II. The Insurance Contracts

The Contracts (Tab B) were executed by OPIC on January 21, 1994. Under Contract No. D919, an OPIC Form 234 KGT 12-85 (Second Revision) with standard amendments for technical assistance agreements and projects in the Newly Independent States of the former Soviet Union ("NIS"), OPIC insured Alliant's investments in the form of agency, management and engineering services (including equipment installation services) pursuant to agreements with Alliant Kiev dated September 17, 1993 (the "Agreements")(Tab C). Under Contract No. D920, an OPIC Form 234 KGT 5-88 CP with standard NIS and other amendments, OPIC insured hardware and supplies necessary to process munitions. The covered property was leased to Alliant Kiev under an Equipment Lease and Technology Agreement, also dated September 17, 1993 (the "Lease")(Tab D).

III. Factual Summary

In 1992, Alliant and Rapierbase LTD, a small British marketing firm, ("Rapierbase") signed preliminary agreements (Tab E/Exhs.1, 2,4&5¹) with the Government of Ukraine ("GOU"), represented by the Ministry of Defense ("MOD") and the Kiev Repairing Mechanical Plant (the "RMP") of the MOD (collectively the "Ukrainian Partners") for the formation of a joint venture for the "utilization" of obsolete munitions; i.e., the disassembly of munitions and processing of the components (e.g. metals and explosives) for sale. The objective was to eliminate potentially hazardous obsolete stocks of munitions held by the MOD without environmental damage or expenditures from the state budget. The business plan indicated that by utilizing an inventory of 220,000 tons of munitions, containing 38,000 tons of brass and copper that would yield high value by-products, and selling by-products abroad for hard currency, Alliant's investment could be recovered and the Alliant Kiev project could be self-sustaining and profitable (Tab F/Exh3).²

In 1993, the foundation agreement and charter of Alliant Kiev (Tab G/Exh.6) were signed, and Alliant, Rapierbase and the Ukrainian Partners entered into a series of agreements with Alliant Kiev for the implementation of the project. Under these agreements, the MOD³ was to supply obsolete munitions under a supply contract (Tab H/Exh.10) for processing by Alliant Kiev, using military personnel on military bases controlled by the MOD and equipment, technology, funding and management services provided by Alliant and for marketing of by-products abroad by Rapierbase (Tabs C, D&I/Exh.14)⁴. The equity ownership of Alliant Kiev was established as follows: 51 % GOU, represented by the State Property Fund, with 40% of the voting power; 10% Rapierbase, with 9% of the voting power; and 39% Alliant, with 51% of the voting power.

Decree #1079 of the Cabinet of Ministers, adopted December 31, 1993, (TabJ/Exhs.7&8) established the State Utilization Program, and Alliant Kiev was selected by the MOD as the foreign participant. Following a request submitted to the Cabinet of Ministers by Alliant Kiev for the export of munitions utilization by-products, Alliant Kiev was granted permission to export brass scrap by the Export Control Committee of the MOD.

In August, 1994, as Alliant Kiev was beginning to ship by-products, a negative news article was published regarding brass exports involving the MOD

¹ References to Exhibits are to the corresponding Exhibits included in the four volumes of supporting documentation submitted by Alliant in support of the Claim.

² The Ukrainian Partners, among other things, undertook in the business plan to provide Alliant Kiev with exclusive rights to the munitions indicated in the business plan, not to enter into any utilization project competing with Alliant Kiev, to obtain Ukrainian approvals for the sale of by-products in the foreign and domestic markets, obtain exemptions from all present and future taxes on exports of by-products, ensure that Alliant Kiev was in compliance with local laws and to obtain exemptions from future changes in Ukrainian law adversely affecting the operation and profitability of Alliant Kiev.

³ Through the Znamenka Repair Base, a military arsenal under the Central Rocket and Artillery Department of the MOD.

⁴ The Agreements and the Lease covered by Contract No. D919 and Contract D920 were superseded in part by agreements subsequently executed by Alliant and Alliant Kiev (Tab I/Exh.14).

and implicating Alliant Kiev. The article charged that revenue from the sale of brass was not flowing back into the country as required by law. As a consequence, the Military Prosecutor's office initiated an investigation, the MOD withdrew Alliant Kiev's export license, and a shut down of operations ensued (See attachment 1 to Chronology at Tab A). The inability to export limited Alliant Kiev's revenue generating efforts during the investigation (November 1994-October 1995) to domestic sales of propellant, which were not sufficient to cover costs. No formal charges were ever brought against Alliant Kiev or its personnel, and Alliant Kiev never received a report of the results of the criminal investigation.

On January 20, 1995, the Cabinet of Ministers, in Provision 40-1 (Tab L/Exh. 17), designated Alliant Kiev and the Commonwealth Association ("Commonwealth"), a Ukrainian company representing the interests of the Ukrainian defense plants, as participants in the Utilization Program and authorized the formation of an interdepartmental commission for the purpose of selecting by tender "performers" for utilization work. Although Alliant at the time was not aware of the consequences of the commencement of the tender process, this action created a competitor of Alliant Kiev in violation of Alliant's agreements with the Ukrainian Partners and set the stage for the award of control of all munitions to a third party. On completion of the tender, in December 1995, the interdepartmental commission formed pursuant to Provision 40-1 selected the "united project of Minmashprom" a planned association of enterprises of the Ministry of Machinery, Military-Industrial Complex and Conversion ("Minmashprom") as the winner of the tender (Tab M/Exh. 31). A representative of the interdepartmental commission advised Alliant Kiev that it would have to perform its work under the direction of Commonwealth (a competitor) until the winner of the tender was formed. Since the transfer of munitions from the MOD to Alliant Kiev required Minmashprom approval, Alliant Kiev was immediately adversely affected when Minmashprom began withholding its approval upon completion of the tender.

In June 1995, the MOD finally confirmed a munitions inventory, but the brass and copper content was now reduced to 33,000 tons from the 38,000 tons indicated in the original business plan.⁵

Following questions raised first by the office of the Military Prosecutor, in February 1995, and by the Deputy Minister of Foreign Economic Relations, in July 1995, regarding Alliant's investment contract, tax exemption issues and the special export regime granted to Alliant Kiev by the Ministry of Economic Relations, Alliant Kiev's application for an export exemption was rejected, resulting in the inability of Alliant Kiev to generate any revenue from the sale of brass by-products for several months. When Alliant Kiev was subsequently granted permission to export, it was required to use a government-approved agency that charged a 2.5% gross revenue fee. This had substantially the same economic impact on Alliant Kiev as an export tax and, in addition, difficulties in working with this agent caused shipping delays.

⁵ OPIC considered providing \$15.5 million in financing for the project in 1995, but decided not to proceed in view, among other things, of uncertainties regarding the availability of munitions to the project.

In April, 1996, Alliant Kiev received an interdepartmental commission report dealing with questions raised by the criminal investigation, which were referred to the interdepartmental commission by the Military Prosecutor's office, including alleged violations of Ukrainian law in connection with the organization of Alliant Kiev and its operations, company registration and Alliant's investment contract terms (Tab K/Exh.36). Ukrainian counsel, retained by Alliant Kiev to review Alliant Kiev documents in connection with efforts to resolve the issues raised in the report, recommended that, as a prerequisite to re-registration of Alliant-Kiev and any required changes in its foundation documents, a new supply contract be established between the MOD and Alliant Kiev that adequately specified operations, procedures and specified brass content was needed.⁶ A new supply contract was prepared and sent to the MOD in July, 1996, but it was never signed.

In June 1996, The GOU imposed a 50% export tax on all yellow metal (brass and copper) exports. Alliant Kiev's application for an exemption based on its participation in the Utilization Program was denied, and it was forced to market brass by-products in the domestic market at one-half of the world market price.⁷ At the same time there was significant interference by Commonwealth in Alliant Kiev's operations at several of the bases, which began to require additional payments for loading, unloading and other continuing services.

Following Alliant Kiev's unsuccessful attempts to negotiate a new supply contract with the MOD by March 1997, Alliant's accountants recommended a write off of Alliant's investment in Alliant Kiev unless a munitions supply commitment was obtained from the GOU. The urgency of receipt of a GOU munitions supply commitment was conveyed by Alliant representatives to U.S. Ambassador Miller (later succeeded by Ambassador Pifer) as an issue for the bilateral commission led by U.S. Vice President Gore and Ukrainian President Kuchma. Shortly thereafter, following advocacy efforts by the U.S. Departments of State and Commerce in a Gore-Kuchma process to resolve this and other foreign investment issues, on April 18, 1997, General Tsarik, the head of the MOD's Central Rocket and Artillery Department, signed a letter to Alliant Kiev confirming that Alliant Kiev would receive the balance of the 220,000 tons of the promised munitions with a minimum of 13% brass and copper content (28,000 tons)(Tab N/Exh.48), far less than the 38,000 tons of brass and copper indicated in the business plan for a profitable operation.

On May 12, 1997, however, Alliant was advised by the U.S. Department of Commerce during the course of the Gore-Kuchma meetings that the GOU continued to insist that Alliant Kiev work under agreements with Commonwealth in accordance with the tender award. Alliant immediately served notice on Alliant Kiev that it was in default on its debt repayment obligations to Alliant and

⁶ The supply contract did not include a munitions supply schedule or specific provisions with respect to the proportion and timing of the supply of brass containing munitions, both of which were vital to the funding of the early stages of the project.

⁷ Alliant invested in the project at the outset, and continued to invest while attempting to resolve project issues, despite the failure of the Ukrainian Partners to obtain tax exemptions and other investment protections specified in the business plan and other preliminary agreements.

that Alliant was suspending the funding of the completion of the grinder facility installation and RDX conversion work, adding that, in Alliant's view, the GOU position violated all agreements between Alliant and the GOU. Upon seeing a copy of General Tsarik's letter confirming the availability of munitions to Alliant Kiev, the Ukrainian Gore-Kuchma delegation changed its position and confirmed MOD's commitment to the project (TabO/Exh.51). Alliant then reconfirmed its commitment to the project and released funds for the grinder and RDX conversion.

In November 1997, the Cabinet of Ministers passed Provision #12/62 which allowed any GOU Ministry or agency to impose restrictions on scrap metal export (TabP/Exh.55). Additionally, in January 1998, President Kuchma's Decree #62/98 called for the inspection of the efficiency of the work of Alliant Kiev, as well as examination of the issue of all round utilization⁸ in its operations, prohibition of incomplete transfer of munitions elements,⁹ re-making of agreements with "work performers" under the Utilization Program, such as Alliant Kiev, and designation of the MOD as the agency responsible for munitions utilization (Tab Q1/Exh.58). In February, 1998, Cabinet of Ministers Bylaw #59-p established a state enterprise under the supervision of the MOD apparently vested with the exclusive right to sell scrap metal by-products from munitions utilization and other property of the armed forces. (Tab Q2/Exh. 3 to May 6, 1999 submission)

On February 4, 1998, presumably acting pursuant to Decree #62/98's call for an end to incomplete transfer of munitions elements, General Tsarik wrote to Alliant Kiev stating that while the MOD was carrying out its munitions transfer obligations, Alliant Kiev was not. He charged that Alliant Kiev was principally removing and selling brass and accumulating other munitions elements, including large quantities of hazardous propellant and projectiles, at the bases (Tab R/Exh.61). General Tsarik threatened termination of the MOD's agreements with Alliant Kiev if Alliant Kiev failed to carry out its obligations. Alliant Kiev replied that the sale of non-ferrous metals (brass and copper) was necessary to fund the installation of technical facilities and munitions transportation costs [not contemplated by the business plan] (Tab S/Exh.62) and proposed a program for removal of projectiles from the bases in connection with a comprehensive transportation and technology development plan. Alliant Kiev met with General Tsarik several times in an unsuccessful effort to resolve these issues¹⁰.

⁸ "All round utilization" or "whole round utilization" refers to the utilization (processing) of all of the components of the munitions provided at the time of transfer; i.e. without storing any components of the munitions for later processing.

⁹ "Incomplete transfer of munitions elements" refers to the transfer of less than all of the components of a particular type of munitions; for example, transfer by the MOD to Alliant Kiev of brass casing from shells, but not the contained powder.

¹⁰ A draft of the MOD's proposed program for the implementation of Decree #62/98 provided, among other things, for the prohibition of storage of munitions and elements on bases above standard levels and called for the Ministry of Finance to fund MOD Utilization Program expenditures directly and disregard as invalid Cabinet of Ministers' Decree #1079 and Provision #40-1, changes which would eliminate the principal elements for the establishment of Alliant Kiev (Tab T1/Exh. 59).

In April 1998, pursuant to provision #12/62, the Cabinet of Ministers' Special Export Committee imposed a stringent control procedure on the export of non-ferrous metals, which caused Alliant Kiev to shut down exports. In May 1998 Alliant advised President Kuchma that, if Alliant Kiev were not allowed to export and MOD were to change the utilization program to the detriment of the project, Alliant would seek recovery of its investment in international legal proceedings or through OPIC insurance (Tab T2/Exh. 60). Alliant further demanded that performers under the Utilization Program be given special export status and that the MOD sign a new supply contract allowing Alliant Kiev to execute its business plan "at the least cost to preserve the self-financing principle..." unless the GOU were willing to provide the program funding.

Alliant again declared Alliant Kiev in default, but, when Alliant Kiev received permission to export in late May, Alliant agreed to extend the default cure period until July 16, 1998, allowing for the execution of a new supply contract by the MOD.

In June, 1998, Col. Glazarin became head of the Central Rocket and Artillery Department of the MOD and immediately made scrap removal from any base subject to his approval. Shortly after his appointment, he told Alliant Kiev's General Manager that under Decree #62/98 the MOD was in charge of the Utilization Program and "that the MOD did not feel obligated to honor past commitments (p.24 of Chronology at Tab A)."¹¹ On July 2, 1998, The Cabinet of Ministers enacted Provision #999 providing for a new ecological tax on scrap metal exports that effectively increased Alliant Kiev's export cost by \$33 per ton. On July 27, 1998, the MOD Ichnya base commander notified Alliant Kiev of the suspension of munitions disassembly operations until removal of propellant accumulated from disassembly. The blockage of scrap metal shipments choked funding and brought Alliant Kiev's operations to a virtual stand-still by late August.

On September 8, 1998, Alliant Kiev advised the Minister of Defense that, since it could not ship its by-products, Alliant-Kiev was forced to stop operations for lack of funds and was preparing a claim for damages in respect of recently thwarted shipments. Alliant Kiev also advised the Minister that (i) Alliant had determined to remove its equipment since Alliant Kiev could not operate, (ii) that a request had been made for clearance for a site inspection visit by an Alliant representative in preparation for the removal of the equipment and (iii) removal of the equipment and legal claims could be avoided by the signing of a new MOD supply contract and a waiver of scrap export duties (TabU/Exh.96). Alliant also advised President Kuchma of Alliant's decision to remove its equipment and seek recovery of its investment by all legal means, while also urging him to take the steps necessary to accomplish the changes required to allow Alliant Kiev to operate and pay its debts (TabV/Exh.97).

¹¹ Similarly, during a monitoring inspection of the Ichnya base facility on July 21, 1998, OPIC officer Lori Leonard was told by the base commander, in effect, that the MOD would not have to honor past commitments under a new program being developed that could involve other companies working in competition with Alliant Kiev under a new law (or a proposed law about to be implemented) (See Chronology at p. 25, which varies in some minor details from Ms. Leonard's account.).

On September 15 and 16, Alliant's representative was denied access to the Tsevtokha and Ichnya bases for the purpose of the inspection required for equipment removal (Tab W/Exhs. 98 and 99). On October 19 and 20 Alliant Kiev employees were also denied access to the equipment for the purpose of removal (Tab X/Exh.115). Following several attempts to negotiate a resolution of the principal issues (a new MOD supply contract¹² and a special export regime for performers under the Utilization program) and resume shipments, Alliant terminated its investment contract and announced that it was withdrawing its equipment immediately (Tab Y/Exhs.118 and 119). A final attempt by Alliant to remove its equipment on October 28, 1998 was unsuccessful.

IV. Determinations Under the Contracts

- A. The actions taken by the Government of Ukraine in relation to Alliant's insured investment in Alliant Kiev constitute total expropriation within the meaning of the Contracts.

The scope of expropriation coverage is determined by Article IV of Contract No. D919 and Article II of Contract No. D920. Each provides, in Section 4.01 and 2.01, respectively, that compensation is payable for total expropriation, subject to exclusions and limitations, if four requirements are satisfied:

1. The acts are attributable to a foreign governing authority that is in de facto control of the part of the country in which the project is located.

The acts on which the Claim is based were actions taken by high officials and instrumentalities of the central government of Ukraine, which controls all of Ukraine.

The documents supporting the Claim established that the acts that are the basis of the Claim constituted official acts of the foreign governing authority taken by the President, the Cabinet of Ministers, the MOD, Customs, the Ministry of Foreign Economic Affairs and Trade, Minmashprom, and various committees or commissions established by some of them.

Each Contract contains an amendment (Section 10.02 of Contract 919, Section 8.02 of Contract No. 920) that defines foreign governing authority so as to exclude any entity in which the foreign governing authority has an ownership interest if the entity performs commercial functions directly related to the project. The MOD and certain departments of the MOD did perform commercial functions directly related to the project. This exclusion does not apply to this Claim, however, because actions of the President, the Cabinet of Ministers and other ministries and instrumentalities of the GOU, including actions taken by the MOD and its departments in compliance with actions of other GOU instrumentalities, were sufficient to constitute expropriation.

¹² The MOD asserted that Alliant Kiev unreasonably refused to sign the new contract proposed by the MOD, but Alliant Kiev replied that the contract was tendered too late and was unacceptable, among other reasons, because it did not specify inventory of munitions by type and location for the life of the contract and permitted unilateral termination (Tab Z/Exh. 123 and 124).

2. The acts are violations of international law (without regard to the availability of local remedies) or material breaches of local law.

The conditions on which Alliant invested in the project were clear and agreed upon by the representative of the GOU, namely, the MOD. Alliant's participation in the Utilization Program was approved subsequently by the Cabinet of Ministers. This determination is based upon the foreign governing authority's high level decisions to frustrate, repudiate or renegotiate under duress fundamental elements of the arrangement the GOU had negotiated with Alliant, in violation of international and local law.

The President, the Cabinet of Ministers, Minmashprom, and other agencies reconsidered the participation of Alliant in the Utilization Program and decided to reduce or eliminate Alliant's participation. This was accomplished by interrupting and reallocating the supply of munitions and reducing brass and copper content, restricting export sales, reducing income by imposing new taxes, costly shipping procedures and new transportation requirements, and ignoring, or attempting to override or renegotiate project agreements under duress.

Decisions made at the Presidential, Cabinet of Ministers and ministerial level undermined the basis on which Alliant's investments were made and denied Alliant any possibility of the recovery of its investment. These measures amounted to conscious repudiation of an investment agreement made by the GOU with Alliant, without compensation. "A state is responsible under international law for injury resulting from ...a repudiation by the state of a contract with a national of another state ...when the repudiation or breach is ...motivated by noncommercial considerations and compensation is not paid." The Restatement of the Law, Third, The Foreign Relations Law of the United States §312 (1987). Alliant was not merely the victim of a commercial breach of contract by the MOD and its departments as supplier and party to project agreements. The GOU decided as a political matter that the Alliant Kiev demilitarization project should be terminated or renegotiated under duress.

The GOU's actions violated not only customary international law but the terms of the bilateral investment treaty it signed with United States on March 4, 1994, and which became effective November 16, 1996. The parties agreed that "investments shall at all times be accorded fair and equitable treatment" and not to "in any way impair by arbitrary or discriminatory measures the management, operation...enjoyment...or disposition of investments." (Article II (2)(a)&(b)). The parties also specifically agreed that "investments shall not be expropriated or nationalized either directly or indirectly through measures tantamount to expropriation or nationalization...." except, among other things, upon payment of adequate compensation and in accordance with due process. (Article III (1))

The refusal to allow Alliant to remove its equipment was also in violation of Article 11 of Ukraine's Decree on the Regulation of Foreign Investments, which states that "...a foreign investor shall have the right to repatriate the investment either in kind or in currency not later than six months after the activity ceases...."¹³

3. The acts directly deprive the investor of fundamental rights in the insured investment (Contract D919) and directly prevent the investor, as owner of the covered property, from exercising its right pursuant to the Agreement to take possession of and/or dispose of the covered property (Contract No. D920).

With respect to the Agreements, acts of the GOU caused disruptions of operations and losses at Alliant Kiev which, therefore, was unable to pay Alliant for its investment in services.

With respect to the Lease, the MOD refused Alliant permission to withdraw the equipment from the military bases where it was located even though the MOD was on notice that Alliant intended to repossess the equipment and was entitled to remove all its equipment because Alliant Kiev was in default in its lease payments. The MOD and the Prime Minister (to whom both U.S. Ambassador Pifer and OPIC made direct appeals) were well aware that Alliant intended to repossess the equipment. The MOD nonetheless frustrated its right to do so.

4. The violations of law are not remedied and expropriatory effect continues for six months.

Section 4.01(d) of Contract No. D919 and Section 2.01(d) of Contract No. D920 require that the expropriatory effect shall have continued for six months. The Investor gave notice of a potential expropriation claim on May 15, 1998.

With respect to Contract No. D919, while the circumstances do not permit a precise determination, July 2, 1998 could well be the date on which the expropriatory effect commenced. By this time the Cabinet of Ministers had passed Provision #19/62 (Tab P/Exh.55) and various agencies had taken action restricting scrap metal export pursuant thereto, President Kuchma had issued Decree #62/98 (TabQ/Exh.58) calling for an end to the incomplete transfer of munitions elements, the MOD had stated that it was not obligated to honor past commitments and the MOD had suspended utilization operations until removal of accumulated propellant, bringing Alliant Kiev's operations to a virtual stand-still.

With respect to Contract No. D920, the expropriatory effect certainly commenced in September 1998, when Alliant's representative was first denied access to the

¹³ Col. Glazarin did state after such refusal, however, that "...the necessary permits [for equipment removal] would be issued with the fixed terms [referring to the six month period provided under Article 11 of the Decree on Regulation of Foreign Investments]." (Tab AA/Exh.123) That was a self-serving statement that twists the meaning of the Decree and does not negate the fact that Alliant was denied access to its equipment when it had a right to remove it. Six months later, in March 1999, permission still had not been granted.

equipment for the purpose of preparing for its immediate removal. Clearly, the expropriatory effect with respect to Contract No. 919 commenced no later than this date.

B. No exclusion applies

1. A preponderant cause of the loss was not unreasonable action attributable to the Investor.

Both Contracts provide that no compensation is payable if the preponderant cause is unreasonable actions attributable to the Investor. (§4.03(a) of Contract No. D919 and §2.02 of Contract No. D920.

There is no issue here. Alliant Kiev was taking steps to resolve the legal issues in the interdepartmental commission report stemming from the military prosecutor's investigation. Re-registration of the company, new investment and supply contracts and other related adjustments were part of the restructuring negotiations with the MOD, which were never successfully concluded.

The MOD's assertions that Alliant Kiev was not performing its obligations and that this had resulted in a hazardous accumulation of munitions elements failed to recognize the disruption of operations resulting from GOU action and the fact that the self-financing contemplated by the business plan involved processing brass and copper early in the program in order to fund installation of the facilities needed to process the less profitable munitions components. Alliant provided financing to Alliant Kiev so that equipment installation could proceed despite deficiencies in the mix of brass and copper in the munitions supplied by the MOD and a large quantity of explosive material was removed from the bases by Alliant Kiev.

2. The provision of Contract No. D920 (§2.03) that neither sums payable under the lease nor the proceeds from the sale of covered property are covered is inapplicable.

The Claim is based on the loss of the covered property itself.

3. The exclusion of §4.03 of Contract No. D920 for action taken by the foreign governing authority in its capacity or through its powers as a purchaser, supplier, creditor, shareholder, director or manager of the foreign enterprise is inapplicable.

Alliant had no dispute with its Ukrainian joint venture partner (the State Property Fund) nor any dispute with the Ukrainian management of the foreign enterprise.

This Claim is not based primarily on the actions of the MOD as a supplier. Rather, by a series of actions the foreign governing authority undermined known pre-conditions for the success of the project, of which the foreign governing authority was aware, based on its selection of the foreign enterprise as a participant in the Utilization Program and participation in its management, and took control of the project from the Investor. The powers of the foreign governing authority as a shareholder, director or manager were limited by the terms of the foundation agreement and charter of the foreign enterprise and are also not the basis of the Claim.

C. The Investor has complied with its duties under the Contracts.

1. The representations made in connection with the Contracts were true and complete when made and the investment was made as described.

There is no reason to believe that any representations made in connection with the Contract were not true and complete when made. The Investor will be required to so represent in the Settlement Agreement. The Claim and the supporting documents demonstrate that the Investor made the investment and attempted to implement the project as described to OPIC.

2. The Investor has remained at all times the beneficial owner of investment, eligible for OPIC insurance, and has continued to bear the loss of at least 10% of its investment.

The investor has provided a certificate as to its beneficial ownership of the investment and its continuing eligibility, and the determination of the compensation payable based on the cost data provided by the Investor assures that the Investor has borne at least 10% of the historical cost of the covered property.

3. The Investor notified OPIC promptly of the acts that gave rise to the Claim and has kept OPIC informed as to all relevant developments.

The Investor informed OPIC of the GOU tender offer for utilization of munitions in September 1995 and subsequent adverse actions taken by the GOU and of developments through the date of the Claim and thereafter. Written notice pursuant to the Contracts was provided in a letter dated May 15, 1998 (TabBB/Exh.75).

4. The Investor has not entered into any agreement with the foreign governing authority without OPIC's consent.

The Investor unsuccessfully tried to negotiate a new supply contract between Alliant Kiev and the MOD as part of a restructuring to overcome the project's difficulties. OPIC was kept informed of these developments, as well as Alliant's efforts to sell its interest in the foreign enterprise and the equipment to a third party.

5. The Investor implemented the investment and the project in all material respects in compliance with laws and procedures of the foreign governing authority.

While the interdepartmental commission report raised issues regarding violations of Ukrainian law in connection with the organization and operations of Alliant Kiev, no official charges of such violations have been asserted.

A publication issued by the RADA in February, 1998, referring to legislation passed much earlier, asserted that only state enterprises were permitted to manufacture and sell explosives, evidently restating an existing law that had not been enforced that was also cited in the interdepartmental commission's report. Alliant obtained a legal

opinion to the effect that as a participant in the munitions utilization program, it had the right to manufacture explosives as utilization by-products. (Tab CC/Exh. 64)

The interdepartmental commission's report asserted that the Znamenka Repair Base lacked authority to enter into the munitions supply contract with Alliant Kiev providing for the transfer of munitions to Alliant Kiev for utilization. Alliant Kiev, however, was selected by the MOD as the foreign participant in the munitions utilization program established by the Cabinet of Ministers in Decree #1079. Alliant Kiev, moreover, was advised by Ukrainian counsel in connection with the required re-registration of Alliant Kiev to seek a new munitions supply contract with the MOD which would clearly establish the quantity and quality of munitions to be provided. Despite the efforts of Alliant Kiev and Alliant, a new contract was not successfully negotiated and this issue was never resolved.

Also, Alliant Kiev erroneously registered the equipment covered by the Lease between Alliant Kiev and Alliant under both the Lease and their Investment Contract. After notice of this discrepancy, Alliant Kiev suspended registration of the equipment under the Lease and with the assistance of the State Property Fund sought a way lawfully to cancel the Investment Contract and re-register the leased equipment in a way that would avoid the imposition of duties and taxes, as contemplated by the business plan and undertaken by the Ukrainian Partners. Ultimately the Investment Contract was cancelled by Alliant in October 1998 when it sought to remove its equipment.

The Ukrainian law is unclear with respect to the above matters and it appears that Alliant made good faith compliance efforts. The record shows that Alliant Kiev operated in accordance with its charter as a participant selected by the MOD in the State Utilization Program established by the Cabinet of Ministers. Under these circumstances it would not be appropriate for the GOU to seek to shut down the operations of Alliant Kiev, or for OPIC to deny a claim, on the basis of local law violations asserted in the interdepartmental commission's report.

6. The Investor has observed or obtained a waiver of compliance with covenants in the Contracts regarding worker rights and the environment.

In March 1996 OPIC, based on information furnished by Alliant, agreed to waive the requirement in §10.15 of Contract No. D919 and §8.10 of Contract No. D920 that Alliant provide a base line environmental study. No other issues regarding compliance with environmental or worker rights requirements are outstanding under the Contracts.

7. The Insured retained legal title to the equipment throughout the term of the equipment lease, and legal title remains with the insured.

Section 8.07 of Contract No. D920 requires that the Investor retain legal title to the covered property through the term of the lease and upon its termination.

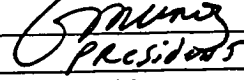
In October 1994, the Investor agreed to transfer title to the equipment to Alliant Kiev, subject to U.S. Government approval and payment in full of required

lease payments. The required lease payments were not made by Alliant Kiev, the transfer never occurred and, therefore, the Investor has not breached Section 8.07.

Conclusion

For the foregoing reasons, OPIC concludes that the Claim is valid. The amount of compensation to which the Investor is entitled shall be determined separately after completion of review of the supplementary information provided by the Investor.

OVERSEAS PRIVATE INVESTMENT CORPORATION

By: 
Its: President
Date: July 22, 1999