BEFORE THE
OFFICE OF IMPORT ADMINISTRATION
INTERNATIONAL TRADE ADMINISTRATION
DEPARTMENT OF COMMERCE
WASHINGTON, D.C. 20230

Case No. A-834-807
Silicomanganese from Kazakhstan

SILICOMANGANESE FROM KAZAKHSTAN:
INQUIRY INTO KAZAKHSTAN'S STATUS AS A NON-MARKET ECONOMY UNDER THE ANTIDUMPING AND COUNTERVAILING DUTY LAWS

COMMENTS OF BETHLEHEM STEEL CORPORATION; LTV STEEL COMPANY, INC.; NATIONAL STEEL CORP.; AND UNITED STATES STEEL LLC

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December 10, 2001

TABLE OF CONTENTS

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These comments are submitted on behalf of Bethlehem Steel Corporation; LTV Steel Company, Inc.; National Steel Corporation; and United States Steel LLC, in response to the Department's request for comments dated November 9, 2001.[1] The American steel industry opposes any change in the status of the Kazakhstan as a non-market economy ("NME") for purposes of the U.S. antidumping ("AD") and countervailing duty ("CVD") laws. It was precisely because of concern over the potentially disruptive effects of non-market economies on U.S. companies and workers that Congress enacted rules for addressing such countries under the U.S. trade laws, including (in 1988) specific criteria for determining the existence of a non-market economy.[2]

There is no credible basis for a finding that Kazakhstan has subsequently become a "market economy" under the criteria established by the statute and refined by Departmental precedent. Indeed, Kazakhstan observers themselves – many of whom are cited in this document – offer the most scathing critiques of the failure of a market economy to develop in Kazakhstan. Even the government of Kazakhstan recognizes that they have not completed the transition to a market economy:

> *{the} economy faces some continuing transition challenges that remain to be met before it can fully realize the economic fruits of its market-based liberalization process.*[3]

The NME statute does provide that in making an NME determination, the Department can consider "such other factors as the administering authority considers appropriate,"[4] but it is a rule of statutory construction that such general catchall provisions are defined by reference to the specific factors which precede them. Because the five factors preceding the catchall clause all relate to economic matters or governmental and institutional factors with a direct bearing on the economy, the "other factors" considered by the Department should be limited to such other aspects of the Kazakh economy and/or Kazakh institutional factors as relate to the economy.

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1 *See Silicomanganese from* Kazakhstan, 66 Fed. Reg. 56,639 (Nov. 9, 2001) (Preliminary Determination of Sales at Less Than Fair Value) ("Kazakhstan *NME Review*").

2 19 U.S.C. § 1677(19)(B) (1995).

3 Paper prepared by Mr. Kanat Saudabayev, Ambassador from Kazakhstan to the United States, "Foreign Direct Investment in Kazakhstan," presented to the Global Forum on International Investment, OECD (Nov. 27, 2001) at 1 ("*Saudabayev Paper*").

4 19 U.S.C. § 1677(19)(B) (1995).

The statutory test of nonmarket economy status, added to the AD law in 1988, was designed to guide the Department in an assessment of the actual economic condition of a country at issue.[5] The legislative history of the statute indicates that the test added in 1988 was intended to address domestic trade deficits, exchange rate stability and "enhance the competitiveness of American industry" – in other words, economic concerns affecting the interests and well-being of U.S. producers and workers.[6] The drafters defined the phrase "nonmarket economy" in narrow economic terms:

> *any foreign country that Commerce determines does not operate on market principles of <u>cost or pricing structures, so that sales in the country do not reflect the fair value of the goods</u>.*[7]

The Department in all NME reviews to date has consistently applied this narrow focus on economic factors and institutional factors directly related to the economy.

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5 The Department itself played a major role in the evolution of the current narrow, economic-based statutory NME criteria. These criteria codified the Department's own prior practice, specifically, the analysis utilized in two cases decided by the Department immediately prior to the enactment of the six-part test involving NME countries. In *Petroleum Wax Candles from the People's Republic of China*, the following factors were considered: 1) degree of government ownership of production; 2) degree of centralized government control over resource allocation; 3) degree of centralized government control over output; 4) relative convertibility of their currency; 5) degree of government control over trade. When making this determination, Commerce focused on the operation of these factors in the industry in question, the candle sector. Additionally, the Department considered the state of the Chinese economy generally with reference to the following factors: 1) insulation of producers from market factors; 2) the requirement of licenses for all imports; 3) existence of foreign exchange and import/export controls. These cases, especially the China case, provided the predicate of the current NME statute. *See Truck Trailer Axles from Hungary*, 46 Fed. Reg. 46,152 (Sept. 17, 1981) (Preliminary Determination of Sales at Less Than Fair Value); *Petroleum Wax Candles from the People's Republic of China*, 51 Fed. Reg. 6016 (Feb. 19, 1986) (Preliminary Determination of Sales at Less Than Fair Value) 51 Fed. Reg. 25085 (July 10, 1986) (Final Determination of Sales at Less Than Fair Value) ("*Petroleum Wax Candles from China*").

6 Although earlier versions of the statute referred to nonmarket economies in the context of the antidumping laws, until 1988 there were no provisions for analyzing whether a country was or was not a market economy.

7 *Omnibus Trade and Competitiveness Act of 1988: Conference Report*, Pub. L. No. 100-418, v. 5, 591 (Apr. 20, 1988) ("*1988 Act*") (emphasis added).

I. Congressional intent and its own past practice should guide the Department in the current investigation.

Summary of comments. (1) Congress did not intend to limit NME status to countries with centralized government-run economies, but also contemplated situations in which subject economies were dominated by regional or local government authorities. (2) Congress did not intend "market economy" status to be conferred upon NMEs which were in the process of making a *transition* to market economy, but only to countries which had *completed* that transition successfully. (3) The Department must base its assessment on actual economic conditions in Kazakhstan, not on the mere existence of legislation, which, on its face, might be construed as evidence of the existence of a market-based system.

A. Congress did not intend to limit NME status to countries in which only the central government exercises pervasive control.

In general the NME statute enacted in 1988 established criteria that were virtually identical to those used by the Department prior to 1988. There was, however, one important distinction between the Department's prior practice and the wording of the new statute. In its case decisions preceding the legislation, the Department had utilized criteria that assessed the "degree of centralized government control over resource allocation" and the "degree of centralized government control over output."[8] The NME statute however, dropped the word "centralized" in the criteria applicable to government action, while retaining the remaining criteria utilized by the Department in prior cases. In so doing, Congress embraced a broader notion of government action, encompassing not only central but regional and local governmental entities. This broader definition of government action is important in the present investigation because much of the economic authority and ownership and control functions exercised by the central government under the Soviet Union has devolved upon governmental authorities in Kazakhstan since 1991.

B. Congress intended that economies still "in transition" should retain full NME status.

Kazakhstan is commonly described as a country "in transition" from a nonmarket to a market economy. Its "transitional" status provides no basis for a finding that it has become a market economy. The NME statute was drafted to permit a change in the NME status *only* of countries that had fully transitioned into working market economies -- not countries "in transition," e.g. which had implemented an array of partially effective and/or incomplete reforms. During the pendency of the NME legislation, while an NME determination regarding China was ongoing, the Committee for Fair Trade for China proposed to add a category of countries (to existing market and NME designations) called

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8 *Petroleum Wax Candles*, 51 Fed. Reg. at 6016; 51 Fed. Reg. at 25,085.

"Planned Market Economy Countries."[9] This proposed new category was defined to include a nation implementing economic reforms that would eventually enable the country to have a working free market economy. Although intended to allow the U.S. to recognize "the sweeping political reforms occurring in countries like China," opponents to the proposal argued that the new category would reward countries that merely have planned market economies and provide no incentive to actually move to a market economy.[10] The Department rejected this notion.[11]

C. The Department must ultimately rely upon *de facto* considerations when examining NMEs.

The government of Kazakhstan's current request for market economy status relies heavily on the existence of various provisions and guarantees in the *text* of the Kazakh constitution and in national laws and regulations. While *de jure* considerations are one element of an NME determination, the *de facto* existence of the basic elements of a functioning market economy is the ultimate test of whether a change in status is warranted. The distinction between *de jure* and *de facto* circumstances is particularly important in a situation in which, as here, the subject country is characterized by a wholesale disregard for constitutional and legislative guarantees and the rule of law.

The following sections apply the criteria established by Congress, as developed and refined by the Department, for determining the existence of a market economy to the actual circumstances prevailing in Kazakhstan.

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9 This was proposed by the Committee on March 6, 1987.

10 Other proposals put forth at the time were adopted, such as the sectoral analysis to determine whether a non-market economy product is the result of market or non-market forces.

11 The creation of a hybrid third category to encompass economies attempting to transition was subsequently rejected by Congress and by the Department when the issue was revisited in 1995. The Clinton Administration made two proposals to congressional committees designed to create interim designations, and changes in treatment under the U.S. trade laws, for NMEs in transition. These proposals were not adopted. The U.S.-Russia Business Council also proposed changes to both Congress and the executive branch to create a new category for economies in transition. Again, these proposals were rejected. *See* Robert H. Lantz, *The Search for Consistency: Treatment of nonmarket economies on transition under United States antidumping and countervailing duty laws*, 10 AM. U.J. INT'L L. & POL'Y 993, 1051, 1053 (1995) at 1053 (*"Lantz"*) (citing Carey et al., *Transitional Relief for Russia Under the U.S. Trade Laws: New Policies for Assisting Russia's Entry into U.S. and Global Markets*, U.S.-Russia Business Council (prepared by Steptoe and Johnson), sec. 1, at 3). "The economies in transition proposal would have been effective for five years, during which time no other United States unfair trade statute would apply to NMEs in transition." *Lantz* at 1051.

II. Market economy status is not warranted.

In September 2001, the Department rejected Kazakhstan respondents' request for market oriented industry ("MOI") status in the case of *Hot-Rolled Carbon Steel Flat Products from Kazakhstan.*[12] This finding that Kazakhstan did not meet the statutory criteria necessary to demonstrate that market forces establish pricing and input is extremely significant in the present case, as MOI status is considered an interim measure before revocation of NME status. Since September, the remainder of Kazakhstan's economy, labor force, currency, investment laws and privatization efforts have not made any additional progress toward becoming a market economy. Therefore, if Kazakhstan's large-scale industries cannot satisfy this interim test, then, for antidumping purposes, Kazakhstan remains a nonmarket economy.

A. The Statute specifies the only criteria for NME review.

Congress clearly intended a purely economic test of whether a country's economy was based on a functioning market, as the NME review statute states that a "nonmarket economy country" means,

> *any foreign country that Commerce determines does not <u>operate</u> on market principles of <u>cost or pricing structures</u>, so that sales in the country do not reflect the fair value of the goods.*[13]

To make this determination, section 771(18) of the Act requires the Department to look at six factors to determine whether a nonmarket economy has completed the transition to a market economy. These factors entail:

(i) the extent to which the currency of the foreign country is convertible into the currency of other countries;
(ii) the extent to which wage rates in the foreign country are determined by free bargaining between labor and management;
(iii) the extent to which joint ventures or other investments by firms of other foreign countries are permitted in the foreign country;
(iv) the extent of government ownership or control of the means of production;
(v) the extent of government control over the allocation of resources and over the price and output decisions of enterprises;
(vi) such other factors as the administering authority considers appropriate.

Although some may argue that framing the six factors in terms of "the extent" to which the transition has been made suggests "that complete *laissez faire* or a perfectly

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12 *Issues and Decision Memorandum for the Less Than Fair Value Investigation of Hot-Rolled Carbon Steel Flat Products from Kazakhstan*, from Joseph Spetrini to Faryar Shirzad, U.S. Department of Commerce (Sept. 21, 2001) at 5 (*"Spetrini Memorandum"*)..

13 *1988 Trade Act* (emphasis added).

competitive market economy is not the applicable standard," the legislative history of the statute demonstrates otherwise.[14] It is well recognized, however, that the NME transition determination is based on an analysis of both *de facto* and *de jure* considerations, and despite arguable improvements in the legal framework, Kazakhstan clearly is not a market economy for anti-dumping purposes.

B. Omnibus Trade Act of 1987 amendments to the Tariff Act of 1930.

Added in 1988 as an amendment to the Tariff Act of 1930, the statutory test of nonmarket economy status was intended to measure the actual economic status of a country at issue. Although earlier sections of the statute referred to nonmarket economies in the context of the dumping laws, originally there were no provisions for analyzing whether a country had transitioned in a market economy. The legislative history of the statute illustrates that this new test was intended to address domestic trade deficits, exchange rate stability and "enhance the competitiveness of American industry." This targeted focus on true economic indicators has been consistently applied in all NME reviews thus far.

In the first successful NME review granted to Poland in 1993, the Department stressed in their conclusion,

> *[The] economy operates on the basis of market principles to such an extent that [the] domestic prices can reasonably be used as a basis for calculating foreign market value within the meaning of the U.S. antidumping law.*[15]

The treatment of a nonmarket economy under the Act is entirely based on the actual economic status of the country, not on the potential economic status or relevant economic legislation. For example, the Ukraine also applied for a change of status in 1994, and in the denial of this request, the Department cited to the requirement that fifty percent of all foreign export earnings be converted into hyrvnia (the Ukrainian currency) as proof that the currency was not convertible. Furthermore, all treatment of NMEs under the Tariff Act of 1930 is concentrated on economics, as with the Department's use of a surrogate country to determine the foreign market value of the goods at issue.[16] Surrogates are chosen from countries with comparable levels of economic development, per capita gross national product (GNP), growth rate in per capita GNP, and the national distribution of labor.

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14 *Sandabayev Paper* at 5.

15 U.S. Department of Commerce Internal Memorandum from A. Hsu to the File, Case No. A-455-802 (June 21, 1993) at 37 (*"Poland NME Review"*).

16 *See 1988 Act* at Section 773(c).

Just this year, Kazakhstan failed to achieve market oriented industry ("MOI") status for its steel industry. This designation is granted to sectors within an NME that can demonstrate that their industry is sufficiently divorced from government control. This designation is made if the Department finds that:

> *1) there is virtually no government involvement in setting prices and setting volume of production;*
> *2) the entire industry is characterized by private or collective ownership; and*
> *3) all but an insignificant portion of all material and nonmaterial inputs have been purchased at market-determined prices.*

Created by the Department after the Federal Circuit held in 1986 that the CVD statute could not be applied to NMEs, the MOI was a direct response intended to create an interim category for market in transition.

In light of the continued rejection of other interim measures for transition economies, in 1988, 1992 and 1996, this is the only measure for addressing markets in transition. As further support that presently granting Kazakhstan market economy status would be contrary to Congress' intended economic focus, the Department stated in September that:

> *In this case, there appears to be significant evidence that the Kazakhstan hot-rolled carbon flat steel industry does not satisfy the third prong—that prices for virtually all input be market determined.*[17]

Therefore, it would be ridiculous to grant Kazakhstan market economy status, when this lower test is not even met by the Kazakh sectors that have been the subject of dumping cases before Commerce.

In keeping with the Congressional intent of an economic focus, the Department must be consistent in its application of the statute when reviewing Kazakhstan's NME status by focusing on the state of the market economy in Kazakhstan, as was done in all previous NME reviews. Just as the Department cited the lack of functioning market as a primary reason for denying a change to MOI status, so must it do in this review of Kazakhstan:

> *Many of the state controls have been abandoned, but that does not mean that functioning markets have replaced controls. Because the evidence does not demonstrate that prices and costs in {the foreign country} adequately reflect market considerations, we cannot at this time alter {the foreign country's} designation as a nonmarket economy.*[18]

[17] *Spetrini Memorandum* at 5.

[18] *1995 Russia NME Review* at 16,443.

Intended as neither a carrot nor a stick, the NME test was created to measure true economic progress. The NME statute was not designed to punish communist countries, nor was it tailored to specifically address market concerns in communist countries. Because this review does not measure *intended* progress or promises to privatize, but only actual economic conditions, Kazakhstan must still be considered a nonmarket economy.

III. Criterion 1: The extent to which the currency of the foreign country is convertible into the currencies of other countries.

Summary of comments. Because de facto considerations are a key element in the NME determination, basic currency convertibility is not sufficient to satisfy this criterion. An examination of business transactions in Kazakhstan reveals that hard currency does not play a major role in the current economy. Rather, the widespread use of barter and transfer pricing, and continued problems with capital flight demonstrate that the tenge is not functioning as a currency of a market economy.

Discussion. The first factor cited in the NME statute for determining the existence of a market economy is "the extent to which the currency of the foreign country is convertible into the currency of other countries. " The Department made findings in the Slovakia and Czech Republic NME reviews that these countries had liberalized their foreign exchange regimes, but cited a number of remaining restrictions limiting full convertibility.[19] In the case of Kazakhstan, citizens are not free to make portfolio investments abroad, and restrictions more onerous than those cited in the Slovakia and Czech Republic cases continue to hinder free convertibility of the tenge. These restrictions have a significant negative effect on the commercial and investment environment, as well as important macroeconomic effects, all of which the Government of Kazakhstan ("GOK") is well aware:

> *The positive tendencies in the Kazakh economy are not stable yet, Kazakh Prime Minister ...Tokayev said.... Tokayev announced that non-payments remain a serious problem perpetuating barter exchanges and the use of other undesirable non-cash settlements.*[20]

A. Barter is used instead of the tenge.

Although the tenge, Kazakhstan's official currency, is nominally convertible, currency does not play a role in a large part of the market. Kazakhstan's experience with barter has been similar to those of most former Soviet states, where a significant share of all economic activity has been conducted through non-monetary media over a prolonged period. The extent to which an economy is de-monetized—subject to barter or non-cash transactions—"is symptomatic of major institutional failure" and creates "large economic

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19 Poland's zloty, for example, was freely convertible internally, but could not be freely exchanged outside of Poland for foreign investment goods, and capital account transactions remained restricted. ("*Poland NME Review*"). *See also*, U.S Department of Commerce Internal Memorandum from B. Carreau to R. LaRussa, Case No. A-859-801 at 4-5 (Oct. 13, 1999) ("*Slovakia NME Review*"); U.S Department of Commerce Internal Memorandum from J. Brinkman and N. Cannon to R. LaRussa, Case No. A-851-802 at 5 (Nov. 29, 1999) ("*Czech Republic NME Review*").

20 "Positive Tendencies in Kazakh Economy Still Unstable," *Interfax* (April 23, 2000).

distortions."[21] Despite efforts to curtail it, barter continues in Kazakhstan today. In the World Bank's most recent year 2000 review, Kazakhstan survey respondents indicated that approximately 17 percent of company sales were still being conducted through barter.[22] The World Bank likewise reported that in 1999, some 17.9 percent of transactions in Kazakhstan were conducted through barter, while that figure was almost 21 percent in 1996.[23] This is about three times the Czech Republic rate. The private sector and government acknowledge the prevalence of barter in the Kazakhstan economy today:

> *The challenges in Kazakhstan range from bartering with customers...to trying to persuade people to pay for electricity. ... When the company started selling electricity in northern Kazakhstan, even big commercial customers did not have cash to pay. AES agreed to barter arrangements, trading electricity for cars used by its staff, rail transportation, and in some cases, vodka and other products that could be sold by middlemen. "That was the only way to do business," Mr. Lee, a Kazakh national, said.*[24]

The EBRD noted that, "Metal products accounted for about 30 percent of total CIS barter exports in 1998-1999."[25] This observation is particularly important since the government retains control over much of the metal and minerals sectors—therefore, the continued use of barter transactions is being facilitated, and in fact favored by the government for a substantial part of Kazakhstan's market.

> *The government of Kazakhstan has said that the privatization of power distribution companies has been unsatisfactory.... The large accounts receivable and payable and the large share of barter operations in payments aggravate the economic position of the distribution companies, he said.*[26]

Although the government may criticize its industries for continuing to use barter instead of hard currency, the government itself is facilitating and participating in many barter

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21 "Measuring Governance, Corruption, and State Capture: How Firms and Bureaucrats Shape the Business Environment in Transition Economies," World Bank Policy Research Working Paper (Apr. 2000) at 30. Exh. 1.

22 *Id.* at 31. Exh. 1.

23 World Business Environment Survey, World Bank-EBRD 1999 as reprinted in "Barter in Transition Economies: Competing Explanations Confront Ukranian Data," (Jan. 2000) at 3. Exh. 2.

24 "Generating Much Heat But No Kazakh Profits," *New York Times* (May 13, 2001). Exh. 3.

25 *Kazakhstan: Investment Profile 2001*, European Bank for Reconstruction and Development (Apr. 2001) at 19. (*"Kazakhstan: Investment Profile 2001"*) Exh. 4.

26 "Kazak Govt Not Pleased With Privatization of Power Companies," *Interfax* (Apr. 2, 2001).

transactions as well. In fact, the payment by the Russian government to Kazakhstan to lease the former Soviet Union's Baykonur Cosmodrome for $115 million per year is even paid in barter.[27]

Whether officially sanctioned or not, as a matter of fact, barter is a matter of GOK policy today insofar as the government engages in it with foreign governments, particularly in commodity transactions:

> *An agreement about supplies of 1 million tonnes of oil from Kazakhstan to {Belarus} was for the first time reached this year. . . . Payments are planned to be carried out on a barter basis. Belarus will pay for oil with chemical and industry goods.*[28]
>
> *Kazakhstan has decided to barter grain for 1,000 Belarussian MTZ-82 tractors. . . . Kazakhstan's agricultural minister, said Kazakhstan was hoping to buy the tractors at the equivalent of $9,000 each with payment in installments over five years.*[29]
>
> *The barter agreement signed by the prime ministers of the three countries [Uzbekistan, Kazakhstan, Kyrgystan] in the Kyrgyz capital of Bishkek enables Kyrgyzstan to benefit . . . from its . . . surplus production of electricity.*[30]

Such prevalent use of barter over currency transactions in both governmental and industrial sectors demonstrates that a market economy does not exist in Kazakhstan.[31]

B. Capital flight and manipulated transfer pricing are widespread.

The GOK has not ceased regulating foreign currency in Kazakhstan. As a result of the Central Bank's imposition of a 50 percent surrender requirement on all hard currency export earnings in 1999, Kazakhstan's oil-related exporters began under-declaring the true value of their sales through offshore transactions in the Caribbean, thus

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27 *Kazakhstan: Investment Profile 2001* at 20. Exh. 4.

28 "Belarus Negotiates Imports of 1 Million Tonnes of Kazakh Oil," *Minsk Belarusian Televisoni* (April 6, 2001).

29 "Kazakhstan to Barter Grain for 1,000 Belarussian Tractors," *Interfax* (Mar. 2, 2000).

30 "Kyrgyzstan Secures Vital Barter Deal," *Financial Times Energy Newsletters* (May 7, 1998).

31 "The wide use of the barter system hinders capital inflow in the mineral resource industry....non-payments and the associated risks compensated for by rises in prices are the reason for the overpricing of metal products in the CIS, and therefore their noncompetitiveness." *Kazakhstan: Investment Profile 2001* at 19. Exh. 4.

avoiding selling hard currency to the government.[32] This surrender requirement was scrapped in November 1999, but oil exports to the Caribbean continued to rise steadily thereafter. In the first half of 2000, for example, approximately $1.1 billion of Kazakhstan's total $1.6 billion in oil exports went to the Caribbean. This means that some 70 percent of oil exports in year 2000 constituted capital flight as a direct consequence of GOK currency policy. Like barter, capital flight is a critical consideration when gauging the success of a recently converted currency, and is viewed by economists as a negative indicator in the transition to a market economy.[33]

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32 Interview with Grigori Marchenko, head of the National Bank of Kazakhstan in "Kazakhstan: Trade fraud spells loss of hundreds of millions of dollars," *Times of Central Asia* (Dec. 18, 2000).

33 Capital flight is one of the factors considered in "The Transition Economies after Ten Years," Stanley Fischer and Ratna Sahay, IMF Working Paper, WP/00/30 at 13, 31-32. This paper considers capital flows among a number of factors in its assessment of the progress of economies in transition to market economy status. Capital flight can be comprised of funds earned through honest activities that are only illegal in that they breach capital controls or evade taxes; or they may be fully legal, but caused by weak political and economic institutions, such as macroeconomic instability, irrational tax rates, a weak banking system, widespread corruption, undefined property rights, etc. There is a strong negative correlation between capital flight and FDI, for example.

IV. Criterion 2: The extent to which wage rates in the foreign country are determined by free bargaining between labor and management.

Summary of comments. In Kazakhstan, trade unions that purport to represent workers are weak or corrupt, strikes are widely considered illegal and are often suppressed when they do occur, and the government rarely enforces laws that purport to guarantee labor rights. Kazakhstan workers' wages often go unpaid, and workers are commonly subject to arbitrary reprisals by their employers if they seek to improve compensation or working conditions. More significantly, the GOK's aversion to independent unions has led to the use of censorship laws to imprison workers who actively protest their working conditions.

Discussion. The NME statute provides that a subject country's transition to market economy status is to be determined, in part, by reference to "the extent to which wage rates in the foreign country are determined by the free bargaining by labor and management."[34] In its recent Latvia determination, the Department noted with approval a variety of "employee and employer freedoms" which,

> *Together with unrestricted labor mobility and an unemployment insurance program comparable to those of OECD countries, make it possible for both workers and employers to bargain over wages.*[35]

In the Slovakia and Czech Republic determinations, the Department cited labor-related laws and institutions safeguarding workers' rights, including the ability to form unions, collective bargaining and the right to strike.[36] Kazakhstan's labor policies and practices stand in considerable contrast to those examined in the Latvia, Slovakia, and Czech Republic determinations, and are an indicator that Kazakhstan has not developed conditions of free bargaining between labor and management which are characteristic of a market economy.

There are very few unions in Kazakhstan, and those that do have membership are highly ineffective. Membership in free trade unions not associated with the state-sponsored Federation of Trade Unions is almost non-existent—only 6 percent of union members are in free trade unions created independent of former state-sponsored, Soviet-era unions. Because the mere existence of labor unions is insufficient to satisfy this factor, Kazakhstan again fails to demonstrate that it is a market economy.

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34 19 U.S.C. § 1677(18)(B)(ii) (1995).

35 *Latvia NME Review* at 7-8.

36 *Slovakia NME Review* at 5-7; *Czech Republic NME Review* at 5-7.

A. Kazakhstan's legal foundations for labor relations are weak.

As of January 2000, a new Labor Law came into effect in Kazakhstan that partially supercedes portions of the 1972 Labor Code of the Kazakh Soviet Socialist Republic.[37] This legislative change is critical in the assessment of the degree of free bargaining between labor and management in Kazakhstan. There is a general consensus among international analysts, and provisions of this law demonstrate, that the law has degraded workers' rights compared with the Soviet-era Labor Code:

> *"The New Law outlines the Employer's rights more clearly than did the previous law and extends both the number of rights and their content. Given the growing unemployment in the {Kazakhstan} today, the employer will have the upper hand."*[38]

A number of legal analysts and international observers have documented the weakening of worker rights under this law stem from the declawing of labor unions, the minimization of collective bargaining, and the overwhelming power of employers over workers.[39]

B. Labor unions are ineffective and collective bargaining is minimized.

The principal effect of the new law has been to replace collective agreements previously negotiated by unions with separate employment contracts to be negotiated between individual employees and employers.[40] While the law allows for the formation of, and membership in, unions—as did the previous Labor Code—analysts universally

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37 "Kazakhstan: Labor Law 1999 in force 1 January 2000," Natlex database, International Labor Organization. "Kazakhstan: Proposed New Labor Laws," International Market Insight, Department of Commerce (Dec. 16, 1999) at 2. It should be noted that a draft of the new law was never made available to the public prior to its coming into effect; as a result, interested parties had no opportunity to participate in its final formulation. The new law took six years to pass and during that time, labor unions reportedly lobbied heavily to preserve their status under the law, but "largely failed in this attempt." Exh. 5.

38 *Effectiveness and Application of the New Labor Law in the Republic of Kazakhstan*, Elshat Seksembayeva, Senior Attorney, Squire Sanders & Dempsey LLC (Feb 2000) ("*Effectiveness and Application of the New Labor Law*") at 3: "The level of legal guarantees for the Employee under the New Law has been considerably reduced."; *Kazakhstan's New Labor Law*, Thomas Johnson and Alyona Smith, CMS Cameron McKenna ("*Kazakhstan's New Labor Law* ") at 68: "{S}everal provisions newly favor employers."

39 *See Effectiveness and Application of the New Labor Law*; *Kazakhstan's New Labor Law*; "Kazakhstan: Proposed New Labor Laws," International Market Insight, Department of Commerce (Dec. 16, 1999); and "Kazakhstan: Monthly Economic Update-Dec. 99," International Market Insight, Department of Commerce (Jan. 21, 2000).

40 "Kazakhstan: Proposed New Labor Laws," International Market Insight, Department of Commerce (Dec. 16, 1999) at 1; *Effectiveness and Application of the New Labor Law* at 2; *Kazakhstan's New Labor Law* at 69; and "Kazakhstan: Monthly Economic Update-Dec. 99," International Market Insight, Department of Commerce (Jan. 21, 2000) at 1.

agree that, in practice, the role of trade unions in negotiating labor contracts has been dramatically reduced as a consequence of this aspect of the new law and that the law "favours the already existing trend among enterprises to encourage short term individual contracts rather than collective agreements."[41] Previously, the terms of contracts were set only by law and by collective bargaining agreements within a framework similar to that described by the Department in its Latvia, Czech Republic, and Slovakia determinations. In analyzing those economies, the Department underscored the existence of a "tripartite arrangement" between trade unions, employer organizations, and the government in the wage negotiation process. As a result of the elimination of labor unions from the bargaining process in Kazakhstan--from collective to individual contracts-- this tripartite dynamic, cited by the Department as the underpinning of free bargaining between labor and management in previous successful determinations-- has been eliminated from the Kazakhstan system.

A specific example of the reduced role of unions and collective bargaining is the fact that the new law does not contain language similar to that of the previous labor code providing that cancellation of an employment contract by the employer only be permitted with the consent of the union.[42] With respect to termination, the new law is "twice as favorable for employers," because whereas under the old labor code, a redundant employee received two month's notice of termination and two month's salary; the new law requires only one month's notice and one month's salary.[43] Furthermore, the old labor code requirement that the employer offer the redundant employee another job at the same, or another company, or offer re-training, does not exist under the new law.

C. Only a partial revocation of the Soviet-era system.

Kazakhstan's new Labor Law was not introduced in the form of a code. As a result, existing Soviet-era legislation that does not directly conflict with specific provisions of the new Labor Law is still in effect, leaving some aspects of the old Soviet system intact and considerable room for inconsistent application of the law.[44]

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41 "Kazakhstan: Proposed New Labor Laws," International Market Insight, Department of Commerce (Dec. 16, 1999) at 1; *Kazakhstan's New Labor Law* at 69; "Kazakhstan: Monthly Economic Update-Dec. 99," International Market Insight, Department of Commerce, January 21, 2000 at 5; "Country Reports on Human Rights Practices-2000: Kazakhstan," released by the Bureau of Democracy, Human Rights, and Labor, Department of State (Feb. 2001) at 24 ("*Bureau of Democracy Report*"); *Annual Survey of Violations of Trade Union Rights 2001*, International Confederation of Free Trade Unions (2001) at 109 (*"Annual Survey of Violations of Trade Union Rights"*).

42 Article 35 of the Soviet Labor Code provided that the union had to consent before an employee could be terminated. *Effectiveness and Application of the New Labor Law in the Republic of Kazakhstan* at 2.

43 *Effectiveness and Application of the New Labor Law* at 2; *Kazakhstan's New Labor Law* at 69.

44 Existing legislation anticipated by international analysts to engender conflict includes: Law on Collective Agreements (1992), Law on Labor Protection (1993), Law on Professional Unions

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International legal analysts have already identified potential conflicts. Because the new law does not contain provisions regarding professional unions, for example, unions will continue to be regulated by the 1993 Law on Professional Unions.[45]

In practice, much of the labor union structure of the old Soviet system remains in place.[46] Most workers in Kazakhstan (reported approximately 4 million) remain members of state-sponsored trade unions, all members of the pro-government Federation of Trade Unions, established during the Soviet period when membership was obligatory.[47] The state unions under the Communist system were, and for the most part still are, organs of the GOK and work with management to enforce labor discipline and to discourage workers from forming or joining independent unions. Independent trade union membership is reported to be only 6 percent of membership in the state-sponsored trade unions.[48] Whatever voice Kazakh workers were afforded by the Soviet-era system has been further muffled by the enactment of this new law.

D. No free bargaining—the employer sets the terms.

Under the new Labor Law, the employer unilaterally sets the terms of the new individual employee contracts, beginning with the salary. The employer also sets the terms of renewal of contracts and can change the contract during the course of employment. If an employee does not agree to continue working under the altered terms, the employee can be dismissed upon the employer's initiative. Furthermore, the new law does not provide mechanisms to protect workers who join independent unions from threats or harassment by enterprise management or state-run unions. There is no legal protection against antiunion discrimination.[49]

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(1993), Law on Collective Disputes and Strikes (1996), Law on Employment of Population (1998). *Effectiveness and Application of the New Labor Law*; *Kazakhstan's New Labor Law* at 68.

45 *Kazakhstan's New Labor Law* at 68; *Effectiveness and Application of the New Labor Law* at 1. Other such potential conflicts include: the 1992 Law on Collective Agreements, the 1993 Law on Labor Protection, the 1996 Law on Collective Labor Disputes and Strikes, and the 1998 Law on Employment of Population.

46 To obtain legal status, an independent union must apply for registration with the local judicial authority at the oblast level and with the Ministry of Justice. Registration is generally lengthy, difficult, and expensive. The process of registering a union appears to be completely subjective, with no published criteria. No unions were registered or denied registration during the year. The two major independent trade union confederations are registered. Courts may cancel a union's registration, as a provincial court did in Kentau in 1998.

47 *Bureau of Democracy Report* at 23.

48 Membership in these unions is reported to be approximately 4 million, while membership in independent trade unions is reportedly approximately 250,000. No data on increasing union membership are in the evidence submitted by either petitioners or the government of Kazakhstan.

49 *Bureau of Democracy Report* at 23.

E. The *de facto* lack of protections for workers.

Recent labor legislative initiatives in Kazakhstan aside, the Department uses a *de facto* analysis in its assessment of whether the labor practices of a subject country meet market economy standards. Abundant anecdotal evidence of worker rights abuses suggest that Kazakhstan has not yet developed the conditions of free bargaining between labor and management that are *de facto* characteristic of a market economy.

The U.S. Department of State concluded in its February 2001 review of Kazakhstan that the GOK limited worker rights in practice. According to the State Department, GOK tried to limit the influence of independent trade unions, both directly and through its support for state-sponsored unions, and members of independent trade unions were harassed.[50] Members of independent unions have been dismissed, transferred to lower paying or lower status jobs, threatened, and intimidated. Furthermore, according to independent union leaders, state unions work closely with management to ensure that independent trade union members are the first fired in times of economic downturn.[51]

The State Department further observed that while there were peaceful, unsanctioned demonstrations by workers and pensioners protesting difficult economic conditions and the nonpayment of wages in Kazakhstan in 2000, the GOK consistently used minor infractions of the 1998 Law on Public Association, which "contains severe restrictions on the right to free assembly,"[52] to arrest and detain government opponents, including those who are labor leaders. Examples of abuses are documented below:

- On April 6, 2000, authorities in Almaty arrested, tried, and convicted labor movement leader Madel Ismailov[53] for organizing an unsanctioned demonstration and for contempt of court. The demonstration involved a regular monthly pensioners' protest over living conditions earlier in the year. Ismailov, perhaps Kazakhstan's most vocal union activist, was imprisoned for a year in 1998-1999;[54]

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50 The International Confederation of Free Trade Unions, a non-profit association of independent trade unions worldwide, reported 2561 episodes of harassment of trade union members in Kazakhstan as of its Annual Survey 2001, but comprehensive and historical data on trade union activity in Kazakhstan, as a general matter, are unavailable.

51 *See Bureau of Democracy Report.* In this, the State Department's most recent report on Kazakhstan, the State Department concluded that "{t}he Government's human rights record remained poor;" and "{t}he Government restricted freedom of speech and of the press."

52 *Nations in Transit 2001-Kazakhstan,* Freedom House (May 21, 2000) at 212 (*"Freedom House"*). Exh. 6.

53 Ismailov served a one year prison sentence in 1998-1999 for publicly calling the President a "scoundrel." *Bureau of Democracy Report* at 5; *Annual Surveyof Violations of Trade Union Rights* at 110.

54 Ismailov went to the courthouse on April 5 but refused to enter when, he and press reports alleged, the authorities refused to allow his lawyer or supporters to enter with him. While the Constitution

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- On April 20, 2000, the city court of Ust-Kamenogorsk suspended the activities of the local chapter of the Pokoleniye pensioners' movement for 3 months, charging that the group systematically carried out unsanctioned demonstrations;[55]

- On December 13, 2000, the Bostandyk district court of Almaty found Sakhib Zhanabayeva guilty of organizing an unsanctioned mass gathering and sentenced her to 5 days in jail. Zhanabayeva is an activist of the Kazakhstan Workers Movement;[56]

- In March 2000, workers of the Uralsk "Mettalist" factory, led by the independent trade union of the factory, conducted mass meetings demanding the full payment of salaries. The company subsequently prohibited one of the union's leaders, Vladimir Podzhidaev, from entering the factory's territory. Police detained and imprisoned the union's chairman, Ainur Kurmanov;[57]

- During 2000, Marut Urtanbaev, a trade union delegate at TngizChevriOil, was fired for collecting proof of trade union right violations.[58]

The poor state of workers generally is reflected in declining life expectancy rates, and other socio-economic indicators. As noted by the World Bank, "the deliberate cuts in spending resorted to in Kazakhstan in response to the fiscal pressures is of serious concern, as it risks under-investment in the human capital stock of the country and thereby undermines the future growth potential."[59] In the absence of official statistics on the protection of worker rights in Kazakhstan and in the presence of ongoing documentation of labor rights violations, it is fair to say that there has been little real labor reform in Kazakhstan. Moreover, from a legislative standpoint, the trend is moving in the wrong direction in Kazakhstan. The new Labor Law is evidence of a trend toward erosion of legal protections for workers. That fact, along with ongoing documentation of rights violations in Kazakhstan, is an indication that Kazakhstan has not developed conditions of free bargaining between labor and management characteristic of a market economy.

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establishes that trials are public; in the case of labor movement leader Madel Ismailov, the Medeu district court in Almaty refused to allow the public access to the trial. The contempt of court charge stemmed from Ismailov's purported refusal to answer a summons to appear in court on April 5. *Bureau of Democracy Report* at 5-6.

55 *Id.* at 11.

56 *Id.*

57 *Id.* at 23.

58 *Annual Survey of Violations of Trade Union Rights* at 110.

59 Asad Alam & Arup Banerji, *Uzbekistan and Kazakhstan: A Tale of Two Transition Paths,* The World Bank Poverty Reduction and Economic Sector Management Unit (Nov. 2000), WPS# 2472 ("*Uzbekistan and Kazakhstan: A Tale of Two Transition Paths*") at 10. Exh. 7.

V. Criterion 3: The extent to which joint ventures or other investments by firms of other foreign countries are permitted in the foreign country.

Summary of comments. Inconsistent regulation, and the failure to enforce existing laws to protect investors' rights has led to the *de facto* prohibition of foreign direct investment ("FDI") in Kazakhstan. Reflecting these problems, Kazakhstan receives less than $70 per capita in FDI, compared with $436 for the Czech Republic and $277 for Slovakia. Furthermore, widespread corruption at both business and governmental level significantly deters future FDI.

Discussion. The NME statute provides the third criterion for determining a subject country's transition to a market economy is "the extent to which joint ventures or other investments by firms of other foreign countries are permitted in the foreign country."[60] In all previous NME investigations, this has entailed an examination of both the laws of the foreign country, as well as how those laws are actually implemented and enforced.

Latvia's liberal policies with respect to FDI were a significant factor in the Department's recent determination that it had become a market economy, as it was for other NME reviews.[61] The Czech Republic's relatively large amount of FDI was a major factor in the Department's affirmative determination of transition to market economy status.[62] Slovakia was found to be relatively open to FDI, although the Department noted some factors that tended to inhibit inward foreign investment.[63] Kazakhstan is deficient in positive factors affecting FDI cited by the Department in its Latvia and Czech Republic determinations, and the negative factors deterring FDI identified by the Department in its Slovakia determination are present to a much more aggravated degree in Kazakhstan. As summarized by one observer:

> *Privatisation of several major enterprises has been partial and state influence remains excessive. This is a source of much corruption.*[64]

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60 19 U.S.C. § 1677(18)(B)(iii) (1995).

61 *Latvia NME Review* at 8-10. The Report next found that Latvia has a "generally favorable business environment," all sectors of the Latvian economy are open for investment, and one hundred percent ownership of a company is permitted. Additionally, where operating and licensing requirements restrict investment sectors, such requirements do not treat foreigners differently, but apply to both Latvians and outside investors. While the Department mildly noted that in Latvia "{c}orruption is undermining business confidence and the rule of law," the extent of organized crime's influence in Kazakh business and industry has become notorious worldwide.

62 *Czech Republic NME Review* at 6-7.

63 *Slovakia NME Review* at 7-8. The NME review for Slovakia noted that FDI is permitted in most sectors, although foreigners could not own real estate or acquire shareholdings in strategic sectors such as gas, electricity, telecommunications and armaments production.

64 *Kazakhstan: The Economic Base*, APS Review Downstream Trends (July 17, 2000).

In light of these comparisons, Kazakhstan fails to satisfy the third statutory factor necessary to demonstrate a market economy.

A. Kazakhstan's low FDI levels reflect larger market problems.

Despite contentions that FDI in Kazakhstan "reinvigorated" since 1999, the EBRD reports that FDI inflows have actually dropped, from $106 per capita in 1999, to $77 per capita in 2000.[65] In 2000, FDI inflows to Kazakhstan fell to $1.15 billion, and the EBRD predicted only a slight increase to $1.8 billion for 2001.[66] As one foreign company put it:

> *Kazakhstan is basically still a barter economy so it's ripe for bad debts.*[67]

In fact, the OECD considers the low levels of FDI in Kazakhstan are "characterized by pre-privatization {levels} of the FDI."[68] The FDI that has been injected into Kazakhstan's economy is largely confined to the extractive industries, mainly the oil and gas sectors, with low multiplier effects on other parts of the Kazakh economy.[69]

B. Kazakhstan's failure to uniformly enforce laws significantly deter FDI inflows.

Managers of firms surveyed by the World Bank consider numerous obstacles to exist to doing business in Kazakhstan, despite touted institutional reforms. In fact, Kazakhstan is seen to be even more hostile to business than Uzbekistan.[70] Specifically,

> *{A} relatively narrow tax base coupled with poor administrative and legal environment has meant that a small group of businesses (including start-ups) have been frequently harassed by inspectors. As a result, the business environment in Kazakhstan is one often fraught with unexpected transactions{sic}costs, especially for those who are not "insiders." Thus, partial reforms—and less than fully synchronized policy and institutional reforms—may have undermined potentially very successful economic outcomes in Kazakhstan.*[71]

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65 *2001 Transition Report Update*, European Bank for Reconstruction and Development (Apr. 2001) at 22 (*"Transition Report")*. Exh. 8.

66 *Transition Update* at 22. Exh. 8.

67 "A Stake in the Stans: Oil, Gas, Power Companies," *Energy Economist* (Sept. 1, 1997).

68 "By the end of the nineties, only Hungary {out of Central and Eastern Europe and CIS countries} had shifted to post-privatization FDI, with annual inflows standing at USD 1.5-2 billion without privatization projects." *Recent Trends in Foreign Direct Investment*, Organization for Economic Cooperation and Development (2000) at 37 (*"Recent Trends in FDI")*. Exh. 9.

69 *Uzbekistan and Kazakhstan: A Tale of Two Transition Paths* at 8. Exh. 7.

70 *Id.* at 20, Figure 8. Exh. 7.

71 *Id.* at 21. Exh. 7.

The reference to "insiders" highlights the pervasive problem of corruption in both government and business transactions. While corruption not only signals a failure of the market, it also creates a significant impediment to foreigners who want to invest in Kazakhstan. Adding insult to injury, foreign businessmen who highlight corruption are silenced by the government:

> *But despite progress, Kazakhstan is far from developing a transparent, Western-style business climate. 'There are still some sticking points for foreign investors, and bribery is as big a problem as it ever was,' said an American business executive, who insisted that his name not be used because Western companies signed an agreement with the government not to criticize it in the press.*[72]

According to the EBRD, FDI to Kazakhstan in 2000 totaled $1.15 billion. Observers have remarked on the fact that low levels of FDI are most demonstrative of the lack of opportunities for true investment; the low FDI levels in Kazakhstan do not compare to the significantly greater levels of FDI in other countries whose status has recently changed from NME to market economy. Compared to countries like the Czech Republic and Slovakia, whose 2000 FDI levels per capita are $434 and $278 respectively, Kazakhstan received only $77 per capita in FDI in 2000.[73]

The EBRD recently concluded that, "Land reform and ownership also have to be addressed, as well as judicial reform, including the training of commercial judges. In order to attract more foreign direct investment, open and competitive tender procedures and property and contract rights need to be established."[74]

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72 "Generating Much Heat But No Kazakh Profits," *New York Times* (May 13, 2001). Exh. 3.

73 *Transition Update* at 22. Latvia, who most recently transitioned, received $166.25 per capita in FDI in 2000. *Id.* Exh. 8.

74 *Kazakhstan: Investment Profile 2001* at 3. Exh. 4.

VI. Criterion 4: The extent of government ownership or control of the means of production.

Summary of comments. The only privatization occurring in Kazakhstan since the breakup of the Soviet Union has taken place in peripheral sectors of the country's highly concentrated economy, leaving government ownership and control largely intact in Kazakhstan's core industries. In such core sectors, to a considerable extent, "privatization" has involved a mere transfer of ownership from one government entity to another, or has culminated in "renationalization" as ownership has passed from private hands back into those of a federal, regional or local government entity. The GOK's privatization program has been at a near standstill since the onset of the Asian and Russian financial crises in 1998.

Discussion. The fourth criterion established by Congress to determine transition to a market economy is "the extent of government ownership or control of the means of production."[75] The Department has considered the inability to fully satisfy this factor as grounds for not transitioning to a market economy. In fact, the Department pointed to *partial* government ownership as evidence *against privatization progress*:

> *{E}ven though the Government of Ukraine's submission indicate that in 1995 and 1996, 34% and 44% respectively of state-owned enterprises were privatized, it is unclear whether those figures reflect 100 percent privatization of the enterprises in question, or some continued level of government ownership....*[76]

In the Latvia determination, the Department found that by the end of 1998, as a result of government privatization efforts, "virtually all enterprises were in private hands, and the private sector accounted for 65 percent of GDP."[77] In the Slovakia determination, the Department found that by the end of 1997, less than 3 percent of Slovakian enterprises were state-owned and the private sector accounted for 75 percent of GDP.[78] In the Czech Republic determination, the Department found that by the end of 1997 the private sector accounted for 75 percent of GDP.[79] Kazakhstan's present situation with respect to government ownership and control stands in sharp contrast to all three of these recent determinations. GOK ownership and control of the productive enterprises that constitute the Kazakh economy remains extensive and progress toward further privatization has been at a standstill for at least three years.

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75 19 U.S.C. § 1766(B)(iv) (1995).

76 *Certain Cut-To-Length Carbon Steel Plate From Ukraine*, 62 Fed. Reg. 61,754, 61,756 (Nov. 19, 1997) (Notice of Final Determination of Sales at Less Than Fair Value).

77 *Latvia NME Review* at 12.

78 *Slovakia NME Review* at 10.

79 *Czech Republic NME Review* at 11.

A. Only 25 percent of Kazakhstan's major enterprises are privatized.

Despite privatization efforts beginning in 1994, a large percent of Kazakhstan's industry is still government owned or controlled. According to an EBRD 2001 report, only slightly more than 25 percent of large-scale enterprises are privatized in Kazakhstan. In fact, the EBRD classifies Kazakhstan's privatization of large-scale enterprises as having achieve a "3" rating.[80] The relevant rating descriptions are:

> *Rating 3:* *"More than 25 percent of large-scale enterprise assets in private hands or in the process of being privatized (with the process having reached a stage at which the state has effectively ceded its ownership rights), but possibly with major unresolved issues regarding corporate governance."*
>
> *Rating 4:* *"More than 50 percent of state-owned enterprise and farm assets in private ownership and significant progress on corporate governance of these enterprises."*[81]

By giving Kazakhstan a "3" rating, the EBRD has determined that Kazakhstan has neither achieved even a 50 percent level of privatization for large-scale enterprises, nor intends to significantly privatize other enterprises in the near future.

The claim by the government of Kazakhstan that over 75 percent of the workers in Kazakhstan are employed in the private sector is unsupportable.[82] As reported by the EBRD:

> *Around 5,000 medium-sized enterprises and 1,000 large enterprises remain in majority state ownership.... More than 300 of the largest enterprises remain fully state owned.*[83]

These numbers are corroborated by recent OECD report stating that:

> *Many large important enterprises remain under state ownership. Though few in number, these large enterprises dominate the economy. The state is still the sole owner of 333 of these enterprises, and they account for about a third of the GDP....*[84]

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80 *Transition Report 2000: Employment, skills and transition*, European Bank for Reconstruction and Development (Nov. 2000) at 14 (emphasis added). Exh. 11.

81 *Id.* at 15. Exh. 11.

82 *Saudabayev Paper* at 6.

83 *Kazakhstan: Investment Profile 2001* at 11. Exh. 4.

84 *Corporate Governance in Kazakhstan*, Organization for Economic Development (in cooperation with the World Bank) (Oct. 2000) at 16. ("*OECD Corporate Governance Report*"). Exh. 10.

Furthermore the OECD identified those enterprises that had been transferred to "trust management" as "still under state ownership," specifying that this was not privatization and that "trust management should not be a permanent solution."[85]

B. Privatization efforts are not moving forward.

Such conclusions are in-line with reports from the government of Kazakhstan. The "Blue Chip Program" for the sale of blocks of shares in large enterprises was postponed, due to unfavorable conditions on international markets.[86] EBRD reports show that these plans will not significantly change the outlook for privatization progress—and Kazakhstan's EBRD ranking—until genuine efforts begin.

According to the current IMF program, privatization receipts in 2000 were targeted at 2.8 percent of GDP, and actual receipts in 2000 were well below this target.[87] In fact, despite promises of privatization, Kazakhstan has failed to fulfill any of their major privatization goals. Specifically, although regional power distributions, telecom, railway and water utility monopolies were slated to be privatized in 2001, these privatizations have not occurred. In fact, the EBRD found that, "No large-scale firms have been privatized, compared with the programme target of four enterprises by the end of March 2000 and 10 enterprises by the end of 2000."[88]

> *The lack of progress in bringing these large state-owned enterprises towards international standards and practice has proved to be an obstacle to structural reform. If the privatization process is to regain momentum, it will require a renewal of political effort.*[89]

The telecom industry is a perfect example of Kazakhstan's hollow promises to privatize:

> *{S}tate-owned Kazaktelecom, Central Asia's biggest telecommunications operator, holds an exclusive license to operate the public telecommunications network and to provide international and long distance telephony services until 2005, with an option to extend the license for another six years.*[90]

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85 *OECD Corporate Governance Report* at 16. Exh. 10.

86 *Saudabayev Paper* at 7.

87 *Kazakhstan: Investment Profile 2001* at 6. Exh. 4.

88 *Id.* at 11. Exh. 4.

89 *Id.* at 11. Exh. 4. *Annual Survey of Violations of Trade Union Rights* at 110.

90 *Id.* at 22. Exh. 4.

Clearly, the longevity of this company's market dominance has been secured, and the government is not planning to relinquish its monopoly position any time soon.

The only way to claim that a larger percentage of enterprises were already privatized would be to use unconventional and incorrect categorizations. The Kazakh definition of "private enterprises" apparently includes enterprises that are partially private but partially government owned and controlled; (2) companies "privatized" by the federal government but purchased by other governmental entities may be considered to be in "private" hands; (3) in many significant cases, after a privatization has been ostensibly completed, regional and local governments have stepped forward to acquire ownership and/or control of a nominally "private" enterprise.

VII. Criterion 5: The extent of government control over the allocation of resources and over the price and output decisions of enterprises.

Summary of comment. Kazakhstan's federal, regional and local governments regulate many prices directly through *price controls*. Additionally, government-owned enterprises in large, key sectors of the Kazakh economy frequently set prices or collect payments based on policy objectives as opposed to profit-maximization objectives.

Discussion. Even when enterprises are partially under private ownership, the government still exercises disproportionate control, relative to their percentage of ownership. Another major factor underlying Kazakhstan's poor economic performance has been the distortion of prices and output throughout the Kazakh economy by federal, regional, and local governments.

In addition to insufficient privatization efforts, any privatization which has occurred is not *de facto* privatization, since the government still exercises majority control even when only a minority shareholder. Recently, the OECD stated that:

> *The state still has significant ownership share in Kazakhstani firms....Many Kazakhstani firms complain that while the state has minority shareholdings, the state representative to the Board can block certain decisions.*[91]

This is particularly true in the oil and gas sectors, where the government's significant interests provide it with great leverage over the industry. Recently, an EBRD report stated that the government requested "international oil companies operating in Kazakhstan to provide the domestic market with oil and gas at lower prices."[92] Such influence is not confined to these sectors though, as "in many other CIS countries, most mining industries are vertically integrated with state control of all activities."[93] Such price controls on major inputs, like coal and electricity, especially impact the market and prevent prices from reflecting fair market values. The Department considers this control to be so critical, that in previous MOI investigations governmental prices setting of major inputs like coal, was considered justification for denying MOI status.

The government ownership of both the national electricity transmission networks and of the majority of regional distribution companies creates significant influence over

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91 *OECD Corportate Governance Report* at 16. Exh. 10.

92 *Id.* at 15. Exh. 10.

93 *Id.* at 18. Exh. 10. The EBRD specifically notes that the government owns 32 percent of the only aluminum producing company in Kazakhstan, and entirely owns the largest iron ore company, which controls 39.5 percent of the industry. *Id.* at 19.

all industries since power is such a critical input.[94] Accordingly, the GOK's control of electricity prices results in market distortions for all economic sectors:

> *The government ... managed to antagonize Tractabel (Belgium), which runs the Almaty electricity utility, by freezing electricity prices at the level prior to the April devaluation to help control inflation.*[95]

The IMF considers this problem to be so pervasive that certain IMF programs were suspended until the government relinquishes control:

> *The close interaction between the government and the oil market sufficiently concerned the IMF that, "The IMF's dissatisfaction has led to the temporary suspension of its three-year EEF {Extended Fund Facility} programme....{T}he IMF has indicated that mismanagement of oil wealth and failure to introduce transparent practices could deter investors, which would be of concern to the entire economy.*[96]

Due to the high degree of government control of companies, there are few company decisions that are made without the approval of the GOK.

The most transparent means by which the Kazakh governments control prices is through direct price regulation. The government sets the prices of nearly all goods and services in the energy, transportation, and communication fields. In addition to predominant government ownership in these sectors, the federal government has identified hundreds of specific enterprises for which the government has directed authority to set prices because the enterprise is considered to be a "natural monopoly."

It is important to note that the term "natural monopoly" as used in the Kazakh context is somewhat different than the definition as conventionally employed in the West. Whereas a "natural monopoly" in the West describes an enterprise in a sector for which the technology (or production function) inherent in the production of the good favors a single supplier as the low-cost solution (usually due to a declining, rather than increasing, cost curve), in the Kazakh context the term "natural monopoly" is used far more broadly for any enterprise, almost always a former Soviet enterprise, that dominates a sector or geographic region (or both) to such a degree that its commercial and political power can prevent potential competitors from entering the sector or region. In other words, in the Kazakh context the term "natural monopoly" often applies to sectors, such as the

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94 David Kennedy, *Regulatory reform and market development in power sectors of transition economies: the case of Kazakhstan*, European Bank (June 2000) at 3. It is important to note that the GOK considers this report to be so authoritative that is was cited in their own NME submission.

95 *2002 Index of Economic Freedom*, The Heritage Foundation and *Wall Street Journal* (2001) at 254. Exh. 4.

96 *Kazakhstan: Investment Profile 2001* at 7. Exh. 4.

automobile industry, whereas a Western economist would be unlikely to use the term because of the lack of an inherent, technological ("natural") barrier to entry for competitors.

Claims of inability, or impracticability of privatizing such "natural monopolies" are based more on the government's reluctance to loose control of the sector, rather than its inherent nature as a monopoly. The government's role in the pricing decision for these hundreds of core Kazakh companies goes well beyond ensuring that they do not charge monopoly prices. Indeed, the stated goal of price-setting in these "natural monopolies" often relates to ensuring the sector remains subsidized and competitive with foreign enterprises, or that macroeconomic goals—such as low inflation—are achieved.

VIII. Criterion 6: Such other factors as the administering authority considers appropriate.

Summary of comments. In addition to the five specific criteria set forth in the NME statute for assessing whether a subject country has become a market economy, Congress directs the Department to consider "such other factors" that it "considers appropriate."[97] The Department has considered a variety of "such other factors" in its recent determinations with respect to the transition of Slovakia, the Czech Republic, and Latvia to market economy status. In general, an application of these factors to Kazakhstan simply underscores how sharply differentiated its situation is from the countries that have been found to have successfully made the transition.

Discussion. In past NME reviews, the Department has considered several other factors when determining that a country has made sufficient progress to be considered as having a market economy. These factors include trade liberalization, corruption and the rule of law, and relationships with multilateral organizations like the WTO, OECD and the EU. In all these areas, Kazakhstan is wanting.

A. Kazakhstan is not a member in multi-national organizations.

The Department regards the degree of integration of a subject country into the multilateral trading system as a factor to be considered in determining whether the country has made the transition to market economy status. Thus, one factor cited by the Department in summarizing its determination that Latvia had made the transition to a market economy was its finding that:

> *Full trade liberalization has reintegrated Latvia into the multilateral trading system, linking prices, producers and consumers in Latvia to world markets.*[98]

Similarly, the Department stated in its affirmative determination of the Czech Republic's transition to market economy status that the country had liberalized trade and "successfully integrated itself into the global community." The Department indicated in its Czech decision that while integration into the world economy was not itself dispositive of a successful transition to a market-based economy, it was nevertheless a significant step.[99] In its affirmative determination with respect to Slovakia's transition to a market economy, the Department commented:

> *As a participant in the Uruguay Round of multilateral trade negotiations, Slovakia significantly reduced its trade-weighted average tariff rate and*

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97 19 U.S.C. § 1677(18)(B)(vi) (1995).

98 *Latvia NME Review* at 1.

99 *Czech Republic NME Review* at 16.

bound 100 percent of its industrial tariff lines, resulting in a post-Uruguay Round average tariff rate of just under four percent. The Uruguay Round helped to consolidate and institutionalize the broad range of trade reforms Slovakia had undertaken to date.[100]

By contrast, Kazakhstan has not only failed to integrate into the multilateral system, but has also produced and is producing severely disruptive effects within that system. The extent to which Kazakhstan's foreign trade enterprises and the Kazakh customs and trade bureaucracy are engaged in criminal activity underscores the fact that Kazakhstan is not yet – and may not be for some time – "integrated" into the multilateral system. Kazakhstan has not made substantial progress toward joining the EU. Unlike countries that have recently transitioned from an NME designation, like the Czech Republic, Poland, Latvia and Slovakia, Kazakhstan is not actively aiming at EU accession.[101] Kazakhstan is not a member of the OECD, and is not anticipated to achieve membership in the near future. Although Kazakhstan initially expressed active interest in joining the WTO, with accession talks beginning in 1997, that commitment has virtually been abandoned, as "Kazakhstan failed to submit a number of documents to the WTO Secretariat as programmed and a planned meeting of the WTO accession committee was postponed."[102]

B. A lack of general progress in other macroeconomic indicators.

The World Bank recently concluded, when comparing Kazakhstan and Uzbekistan, that, "in two institutional areas critical for transition success—enterprise restructuring and governance, and competition policy—the institutional framework is equally deficient in both countries."[103] Contrary to Kazakhstan's contention that their GDP levels have consistently increased, the World Bank stated that Kazakhstan's GDP shrank by 9 percent from 1995-1999.[104]

Land cadastres (registries) for registering rights in fixed property have been fully established in only a limited number of regions, most notably Almaty and Astana. The use of mortgages on real estate has begun, but legal and banking expertise in this area is limited.[105]

The government of Kazakhstan relies heavily upon statistics to demonstrate that economic reforms and efforts to transition to a market economy have been successful.

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100 *Slovakia NME Review* at 14.

101 *Recent Trends in FDI* at 36. Exh. 9.

102 *Kazakhstan: Investment Profile 2001* at 3, 11. Exh. 4.

103 *Uzbekistan and Kazakhstan: A Tale of Two Transition Paths* at 2. Exh. 7.

104 *Id.* Exh. 7.

105 *Kazakhstan: Investment Profile 2001* at 9. Exh. 4.

However, it is widely recognized "that the statistics are very unreliable, with the state statistical agencies unable to accurately gauge the extent of market activity."[106]

Despite claims that market and social reforms are improving general conditions in Kazakhstan, the country's freedom ranking has fallen since 1994, according to the Freedom House annual "Freedom Survey." Measuring relative levels of political rights, civil liberties, and freedom, Kazakhstan received the lowest ranking of "not free" every year from 1994-2000, thereby underscoring the lack of progress in the country's overall reform efforts.[107]

C. Widespread bribery and corruption poisons all of Kazakhstan's economy.

Widespread corruption is recognized as a failure of the market to enforce rights and generate respect for the rule of law. Not only does corruption dissuade businesses and investors from bringing their FDI to Kazakhstan, but it also prevents citizens from trusting their own funds to banks and investment houses. Analysts have observed that, "One particular area in which there is a lack of infrastructure is in the control of corruption and the control of bribery."

International organizations recognize the significance of this failing as a serious impediment to becoming a market economy. As noted by the World Bank:

> *Corruption is higher in the Commonwealth of Independent States (CIS) than in any other region in the world. The EBRD ranks Azerbaijan, Kazakhstan, Russia, Ukraine, and Uzbekistan highest for corruption of public officials....*[108]

In the *Transparency International 2001 Corruption Perception Index*, Kazakhstan scored an abysmal 2.7 on a 10-point scale, ranking it among the most corrupt at 73rd out of 91 countries surveyed.[109] This report is especially authoritative since the *Index* is created by compiling surveys conducted by other international organizations, like the IMF, the OECD, and the EBRD.

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106 *Uzbekistan and Kazakhstan: A Tale of Two Transition Paths* at 22. Exh. 7.

107 *Annual Survey of Freedom Country Scores 1972-73 to 1999-00, Freedom House.* Exh. 6.

108 *World Bank 1997 Transition Report* based on estimates by the London-based Economist Intelligence Unit and the DRI/McGraw Hill Global Risk Service. Both organizations are consultants who evaluate investment risks for potential foreign investors. Exh. 13.

109 *Global Corruption Report 2001: Transparency International 2001 Corruption Perceptions Index*, Transparency International (Oct. 15, 2001) at 235 (*Global Corruption Report).* Exh. 14.

These surveys took account of corruption both high and low governmental levels, such as the following:

> *A diplomat confirmed in early July 2000 that Swiss authorities had frozen bank accounts in Geneva at the request of the U.S. Justice Department, as part of a corruption investigation into a US businessman suspected of funneling million of dollars from U.S. oil companies to top Kazakh officials, including the President.*[110]

Such corruption at the highest levels has devastating effects on the progression toward a functioning economy since many high level officials, including the President, hold office for life, and "the state remains captured" by corruption.[111]

The ability to detect and remove corruption is further hindered by laws severely limiting freedom of speech and freedom of the press. As noted by Transparency International,

> *An article in the {Kazakh} Criminal Code ensures that any 'insult of the honour and dignity' of the President is subject to criminal prosecution....Critics compare the code with the notorious paragraph ten of Stalin's article 58.*[112]

Such provisions not only result in general censorship, but also allow authorities to prosecute nearly anyone who criticizes governmental policy, as with the case of union workers.[113] However, revealing corruption outside of the governmental sphere is also dangerous, as journalists are also subject to threats of physical violence:

> *While the constitution guarantees freedom of speech and prohibits censorship, the current Law on Media, adopted in 1999, is a pale shadow of the 1991 law created on the wave of Mikhail Gorbachev's* perestroika. *There is common agreement that the rights and freedoms of the media exist only on paper.*[114]

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110 *Global Corruption Report 2001* at 111 ("*Global Corruption Report*"). Exh. 14.

111 *Global Corruption Report* at 116. Exh. 14.

112 *Id.* at 118. Exh. 4.

113 Discussed *infra* at IV.

114 *Global Corruption Report* at 118. Exh. 14.

IX. Conclusion.

Based on the foregoing discussion, it is clear that Kazakhstan is not a market economy. From the widespread use of barter and a lack of free bargaining between workers and employers, to low FDI levels and government ownership and control of a majority of Kazakhstan's enterprises, none of the statutory criteria are satisfied. Kazakhstan's numerous failings on the path to becoming a market economy, both *de jure* and *de facto* demonstrate that much progress must be made before it can transition to a market economy for anti-dumping purposes.

Graduating Kazakhstan from NME to market economy status prematurely would not only create dangerous precedent, but subvert Congressional intent regarding the treatment of nonmarket and transition economies. As specified in the legislative history, the NME test is concerned only with the present condition of the economy of the country at issue. Although Kazakhstan may promise future progress and transformation, until that transformation is complete it fails the statutory test. Clearly, if any country, including Kazakhstan, does not fully meet the statutory criteria, then it can not be classified as a market economy for anti-dumping purposes.