

UNITED STATES DISTRICT COURT
DISTRICT OF MAINE

CIVIL ACTION NO. 00-306-PH
1999 JUL 24 1-5-28

DEPUTY CLERK

FORUM FINANCIAL GROUP, LIMITED
LIABILITY COMPANY and JOHN Y. KEFFER,

Plaintiffs,

v.

PRESIDENT AND FELLOWS OF
HARVARD COLLEGE, JONATHAN R. HAY,
and ANDREI N. SHLEIFER,

Defendants.

COMPLAINT AND DEMAND FOR JURY TRIAL

I. INTRODUCTION

1. The Plaintiffs Forum Financial Group, Limited Liability Company ("Forum"), a mutual fund administrative services provider, and John Y. Keffer ("Keffer"), Forum's owner, bring this action against the Defendants President and Fellows of Harvard College ("Harvard"), Jonathan R. Hay ("Hay") and Andrei N. Shleifer ("Shleifer") for common law fraud, tortious interference and negligence. In 1992 and 1995, the United States government, via the United States Agency for International Development ("USAID"), entered into two contracts to pay Harvard Sixty Million (\$60,000,000) Dollars to provide the Russian Federation ("Russia") with advice and technical assistance for privatization, legal reform and the creation of capital markets. Harvard employed

Shleifer and Hay to create and manage Harvard's program in Russia (the "Russia Program") and implement the tasks called for in Harvard's contracts with the United States government.

2. Harvard failed to supervise and monitor the services Shleifer and Hay provided to Russian officials and, further, failed to supervise their use of the USAID funds under their control. As a direct and foreseeable consequence of Harvard's lack of oversight and abdication of its responsibility under the USAID contracts, Hay and Shleifer used their Harvard positions and influence with Russia officials to obtain for their own personal benefit Russian business interests. These relationships facilitated their defrauding of Keffer and Forum to own and/or control the first Russian specialized depository, i.e. the management and custodian service company necessary to administer mutual funds. Shleifer and Hay were aware that the development of a mutual fund industry in post-communist Poland had been financially successful and intended to duplicate that success in Russia and personally reap its benefits. Shleifer and Hay lacked, however, the capital, technical expertise and industry credibility required to create and license a specialized depository. They were aware that Forum was successfully providing third-party administrative services in Poland and thus would be able to create similar services in Russia.

3. Shleifer and Hay agreed and conspired to misappropriate the first Russian specialized depository from Keffer and Forum. They were joined in this unlawful conspiracy by Beth Hebert ("Hebert"), Hay's girlfriend at the time who is now his wife, Nancy Zimmerman ("Zimmerman"), Shleifer's wife, and Julia Zagachin ("Zagachin"), a former Russia Program associate who had worked with Hay on privatization projects. As

a direct result of Harvard's abdication of its oversight responsibilities, Shleifer and Hay fraudulently induced Forum and Keffer to create a specialized depository in Russia which Shleifer, Hay and their co-conspirators misappropriated for their own benefit. As a result of Hay's and Shleifer's actions and Harvard's negligence, Plaintiffs have suffered significant harm.

II. PARTIES

4. Plaintiff Forum is a Delaware limited liability company with a principal place of business at Two Portland Square, Portland, Maine.

5. Plaintiff Keffer is an individual residing in Cumberland, Maine. Keffer owns Forum.

6. Defendant Harvard is a corporation incorporated under the laws of the Commonwealth of Massachusetts with a principal place of business in Cambridge, Massachusetts. Harvard conducted business in Russia as the Harvard Institute for International Development, otherwise known as "HIID".

7. Defendant Hay is a United States citizen currently residing in Moscow, Russia. He received a bachelor of arts degree from Williams College in 1984. He also holds both a law degree and doctorate in economics from Harvard. At all times relevant to this Complaint Hay was an employee and agent of Harvard.

8. Defendant Shleifer is an individual residing at 38 Bracebridge Road, Newton, Massachusetts. Shleifer is a tenured Professor in Harvard's Department of Economics. He holds an undergraduate degree from Harvard as well as a doctorate from the Massachusetts Institute of Technology. Shleifer has also held teaching positions at Princeton University, Columbia University, and the University of Chicago. At all times

relevant to this Complaint Shleifer was an employee and agent of Harvard.

III. JURISDICTION AND VENUE

9. This Court has subject matter jurisdiction pursuant to 28 U.S.C. §1332 because diversity of citizenship exists between all Plaintiffs and all Defendants, and the total amount in controversy exceeds \$75,000. Venue is proper in the United States District Court for the District of Maine.

10. This Court has personal jurisdiction over the Defendants pursuant to 14 - A M.R.S.A. §704A on the grounds that the Defendants in person or through their agents did or caused a tortious act to be done, or caused the consequences of the tortious act to occur, within the State of Maine. As more specifically described in this Complaint, the Defendants were acting as each other's agents, co-conspirators, and/or joint-tortfeasors in committing tortious acts of fraud, interference with the prospective economic advantage and negligence against Forum in Maine. In addition, Harvard is further subject to personal jurisdiction within the State of Maine pursuant to 13-A M.R.S.A. §1213 on the grounds that Harvard carries on continuous and systematic activities within the State of Maine, including, but not limited to, sending its employees into Maine every year to recruit residents of Maine to attend and pay tuition to Harvard, generating substantial revenues each year from tuition payments received from Maine residents, sending marketing materials into Maine every year, and owning real estate in Maine.

IV. FACTS

A. The USAID Grants and Shleifer's and Hay's Authority and Influence

11. After the fall of communism in Eastern Europe and the Soviet Union in the late 1980's, the United States devised a foreign policy initiative to provide financial and

technical support to Russia to assist its development of a legal and economic infrastructure based upon the capitalist model.

12. In October 1992, the United States Congress enacted the Freedom for Russia and the Emerging Eurasian Democracies and Open Market Support Act of 1992. 22 U.S.C. §§ 5801 et seq. This Act authorized a program, to be implemented primarily by USAID, to help the states of the former Soviet Union carry out political and economic reform in support of open markets, including "establishment of transparency in regulatory and other governmental decision making." 22 U.S.C. § 5811(6)(B). USAID sought to accomplish the task, in part, through two Cooperative Agreements with Harvard.

13. In 1992, USAID awarded Harvard Cooperative Agreement Number CCN-005-A-00-3023-10 (hereinafter the "1992 Agreement"), in the initial amount of Two Million One Hundred Thousand (\$2,100,000) Dollars. The 1992 Agreement was amended nine times between its initial award and September, 1995, which increased its funding to a total of Forty Million Four Hundred Thousand (\$40,400,000) Dollars. Pursuant to the terms of the 1992 Agreement, Harvard was to develop "the legal and regulatory framework that sets out the procedures for . . . institutions to ensure competition, transparency, and fair play," including specifically "the development of a Securities and Exchange Commission and its early regulatory and enforcement activities . . . and private sector self-regulatory initiatives". The 1992 Agreement stated that "HIID's role in the project is unique in that it . . . operate[s] in a supervisory and regulatory capacity to the overall project."

14. In 1995, USAID awarded Harvard Cooperative Agreement Number EPE-A-95-5122-02 (hereinafter the "1995 Agreement"), in the initial amount of Seventeen

Million Four Hundred Twenty-Three Thousand Ninety (\$17,423,090) Dollars, entitled "Impartial Oversight and Strategic Guidance for Privatization and Market Reform Programs in Russia in Support of the Russian Privatization Effort". The 1995 Agreement was amended in September, 1995, to increase its funding by One Million Seven Hundred Thousand (\$1,700,000) Dollars. Pursuant to its terms, Harvard was required "to provide unbiased input into, and overall day-to-day management, review, and evaluation of, the privatization and market reforms". Harvard's role was to provide strategic guidance to the capital market development effort. The 1995 Agreement stated: "The ultimate success of these programs is of the utmost importance to USAID and to the Government of Russia." The 1995 Agreement further provided that the "recipient must develop the complete confidence and trust of the host government and also the array of donor agencies" and that "a completely neutral third party, void of any vested interest in the contracting process, is required." The 1992 Agreement and the 1995 Agreement are hereinafter collectively referred to as the "USAID Agreements". USAID awarded Harvard the USAID Agreements without competitive bidding based upon Harvard's "stature" and its expertise in Russia.

15. From 1992 through 1997, as a result of the USAID Agreements, Harvard received in excess of Sixty Million (\$60,000,000) Dollars from the United States government. This amount included the sum of Three Million (\$3,000,000) Dollars from the 1995 Agreement specifically earmarked for contract administration.

16. Additionally, in recognition of Harvard's expertise about Russian affairs, USAID gave Harvard responsibility for the coordination and impartial oversight over the other USAID contractors who were providing various consulting services to Russia in the

areas of privatization and capital market development. These contractors included Arthur Andersen, PricewaterhouseCoopers LLP, BSMG Worldwide and the International Finance Corporation. These entities' contracts in the aggregate were worth in excess of Three Hundred and Fifty Million (\$350,000,000) Dollars. As a result of the USAID Agreements as well as its coordination responsibilities for the other USAID contractors, Harvard exercised effective control and authority over the United States' economic reform initiatives in Russia.

17. The USAID Agreements included express language specifically prohibiting Harvard and its representatives from having any financial interest in Russia. The USAID Agreements provided that "no [Harvard] employee shall engage directly or indirectly, either in the individual's own name or through the agency of another person, in any business, profession, or occupation in the foreign country to which the individual is assigned, nor shall the individual make loans or investments to or in any business, profession, or occupation in the foreign country to which the individual is assigned". The USAID Agreements also provided that any violation of the policy had to be reported by Harvard to USAID.

18. In addition, the Cooperative Agreements incorporated 22 C.F.R. § 226.42 or its similar predecessor provision. 22 C.F.R. § 226.42 provides:

[T]he recipient shall maintain a code of standards of conduct that shall govern the performance of its officers, employees or agents in the awarding and administration of contracts using AID funds. Conflict of interest situations involving employees, officers or agents or their immediate families shall be avoided. The recipients' officers, employees or agents shall neither solicit nor accept gratuities, favors or anything of monetary value from contractors or potential contractors.

19. Harvard had similar express policies against financial conflicts of interest.

A Conflict of Interest Statement included in Harvard's technical proposal for the 1995 Agreement set forth Harvard's commitment "to maintaining an objective and unbiased role in advising the officials of foreign governments". In addition, Article XIV of Harvard's own Administrative Manual: Overseas Activities dated July 1, 1992 and entitled "Conflicts of Interest and Illegal Transactions", similarly restricted the activities of Harvard employees and their family members within a project country.

20. In or about 1993, Harvard appointed Shleifer as Home Office Coordinator/Principal Investigator of its Russia Program, giving him the authority to act on Harvard's behalf concerning the Russia Program. Shleifer had the authority and primary responsibility for creating, overseeing and managing Harvard's Russia Program and insuring adherence to all of Harvard's obligations under the USAID Agreements.

21. In 1993, Harvard hired Hay, Shleifer's former student, to work with Shleifer as Harvard's Field Associate in Russia. Soon thereafter, Harvard, at Shleifer's recommendation, promoted Hay to General Director/Field Coordinator of the Russia Program. Hay reported directly to Shleifer and the two of them shared responsibility for management and control over Harvard's performance under the USAID Agreements. Their control included: determining how the United States funds would be spent in Russia; identifying policy objectives; identifying and retaining subcontractors; controlling the other USAID contractors; hiring and firing employees; and setting employee compensation, benefits and housing allowances. Shleifer and Hay also had authority, and were expected, on behalf of Harvard to advise Russian government officials on issues of economic policy and reform.

22. Harvard at all times held out Shleifer and Hay as competent and qualified to

direct all aspects of its Russia Program in a fair, honest and unbiased manner and in accordance with all USAID and Harvard policies and procedures, including, but not limited to, those governing conflicts of interest.

23. Shleifer's and Hay's employment and executive positions with Harvard and the Russia Program, including their authority over the USAID initiative in Russia, allowed them to have relationships of influence, trust and reliance with high ranking Russian government officials.

24. Harvard failed to establish a competent system to administer, audit, oversee, supervise and/or control Shleifer's and Hay's exercise of their duties, responsibilities, authority and influence in Russia.

25. As a direct and proximate result of Harvard's lack of supervision and oversight, Hay and Shleifer were able to use USAID funds to improperly influence Russian government officials. For instance, Hay and Shleifer provided Russian government officials and/or their families and friends with cash, no-show jobs, exorbitant and unjustified compensation and benefits, and exorbitant and unjustified housing allowances. These monetary payments were frequently deposited into foreign bank accounts to evade the imposition of Russian taxes.

26. As part of their efforts to gain influence with Russian officials, in or about 1995, Shleifer and Hay used United States funds to established a Russian non-profit corporation, the Institute for Law-Based Economy ("ILBE"). They then caused Harvard to execute a subcontract with ILBE. Pursuant to this subcontract, between 1995 and 1997, ILBE spent almost all of the remaining funds from the USAID Agreements, approximately Seventeen Million (\$17,000,000) Dollars. ILBE had inadequate financial and

administrative controls and was formed as a vehicle for creating and funding, among other things, the no-show jobs and exorbitant salaries. Harvard knew, or had reason to know, that ILBE did not have in place the necessary financial and administrative controls to protect against such misuse of United States funds by Shleifer and Hay.

27. Harvard mismanaged and failed to supervise properly the Russia Program, and failed to safeguard the USAID funds entrusted to Harvard. Harvard was paid by USAID specifically to provide this type of administrative oversight, but failed in its obligation to do so properly. Instead, Harvard administrators were aware of abuses and allowed them to continue. For example, the HIID Assistant Director for Contract Administration was aware of and repeatedly objected to the high salaries and perks given to certain Russia Program staff members with USAID funds. She complained that some of the payments were “double-dipping” and wrote to Shleifer, “I can’t imagine that you will do anything about this, but I believe that it is not right all around and does not show good faith on anyone’s part.” On another occasion, this Contract Administrator also warned that she would “rue the day” for Harvard and HIID that these “salaries and add-ons” became known to USAID.

28. Harvard financial administrators and/or staff were also aware that numerous employees on the USAID funded payroll at Harvard’s subcontractor, ILBE, were hired for improper reasons, were unqualified and/or did not show up for work on a regular basis other than to collect their pay.

29. As a direct and proximate result of Harvard’s lack of supervision and oversight, from in or about 1994 through 1997, Shleifer and Hay made investments in Russia in violation of the USAID Agreements, Harvard policy and Federal regulation.

These investments included, but were not limited to, investments in Russian stocks and Russian government debt. USAID funded staff and offices were used to set up and operate a Russian trading company to facilitate their investments.

30. Over time, some Harvard employees in Russia became concerned about the propriety of Hay's use of USAID funds and his conflicts of interest. Among the persons whose salaries and benefits Harvard employees were objecting to were those involved in assisting Hay and Shleifer with their various private businesses and investments. When some of these Harvard employees confronted Hay and Shleifer about Hay's conduct they were subsequently terminated or demoted by Hay or Shleifer. This was allowed to occur because Harvard failed to establish and administer a structure to supervise Hay's and Shleifer's operation of Harvard's Russia Program.

B. Shleifer's and Hay's Influence Over the Russian SEC

31. The USAID Agreements required Harvard to provide advice and USAID funding for the creation of Russian capital markets, including the creation and operation of a Russian securities commission. Shleifer and Hay developed a relationship of trust and reliance with officials of the newly created Russian Federation Commission on Securities and the Capital Market (the "Russian SEC"), including its Chairman, Dimitri Vasiliev ("Vasiliev"), an appointee of Russian President Boris Yeltsin, and Albert Sokin ("Sokin"), Vasiliev's political advisor who had close ties to the Yeltsin Administration.

32. Shleifer and Hay improperly influenced Sokin by employing him as a Harvard Project Associate and by paying him an exorbitant salary funded with USAID funds. Payments to Sokin were made by Harvard to a foreign bank account to evade the imposition of Russian taxes. Sokin was also provided with an unjustifiable housing

allowance and car service. High paying Harvard jobs and similar illegal payment arrangements also were provided to some of Sokin's associates.

33. Shleifer and Hay, in their capacities as agents of Harvard, controlled all of the technical assistance provided to the Russian SEC by Harvard and the other USAID contractors. Shleifer and Hay created and staffed the Resource Secretariat, a think tank for the Russian SEC, and through it, coordinated the work of the other USAID contractors in advising the Russian SEC. Shleifer and Hay, through their influence over the Resource Secretariat, directed the other USAID contractors to hire specific employees and dictated their work plans.

C. Shleifer's and Hay's Conspiracy to Own and/or Control the First Russian Specialized Depository

34. In the summer of 1995, Russian President Yeltsin issued a presidential decree establishing a Russian mutual fund industry in order to stimulate investment in newly privatized Russian companies. The Yeltsin administration heralded the creation of a government regulated mutual fund industry as an important step to resolving the ponzi scheme scandals that had plagued the Russian economy in the early 1990's. The creation of a regulated Russian mutual fund industry providing investor protection became a highly politicized subject and indeed was a primary objective of the political platform of the Yeltsin Administration.

35. In October, 1995, during the time Shleifer and Hay were advising Vasiliev and the Russian SEC, the Russian SEC adopted regulations which required that mutual fund administrative and custody functions be performed by so-called "specialized depositories" licensed by the Russian SEC. By regulation, these specialized depositories

had to be under ownership separate from the mutual funds they administered, purportedly to obviate conflicts of interest and to protect Russian investors. Consequently, no mutual fund could be started unless it had a service contract with a licensed specialized depository. To the extent few or no additional licenses were issued, the first licensed Russian specialized depository would have a virtual monopoly and would profit grandly from its sole authority to hold and control mutual fund assets and serve as the administrator, custodian, registrar, transfer agent and fund accountant for all mutual funds in Russia. Beginning in late 1995 or early 1996, Hay, Hebert, Shleifer, Zimmerman and Zagachin put together a plan to launch the first Russian mutual fund and the first Russian specialized depository.

36. Hebert had experience as a mutual fund manager from her employment with Flemings (CIS) Limited but had no experience in fund administration. Similarly, neither Shleifer, Hay, Hebert nor Zagachin had the requisite expertise, technology or capital resources to create the specialized depository or to supply its fund administration, custody, accounting and transfer agency services. The development of these functions would require large investments in computer hardware, software, operational procedures, trained staff and the institutional credibility to obtain a license.

37. Throughout 1995 and into 1996, numerous international banking and mutual fund companies, including Credit Suisse First Boston ("Credit Suisse") and Pioneer Group, Inc. ("Pioneer"), were requesting permission from Vasiliev and the Russian SEC to operate mutual funds and specialized depositories in Russia. Due to their international financial experience and expertise, these financial institutions had the immediate ability to operate and administer mutual funds in Russia. Notwithstanding this fact, the Russian SEC

failed to act on their license applications despite public statements that a Russian mutual fund industry was imminent. The reason for Vasiliev's inaction was that Shleifer and Hay had convinced Vasiliev not to grant other requests, thereby giving Shleifer and Hay time to complete their goal of securing for themselves and their co-conspirators the first licenses for a specialized depository and a mutual fund.

38. Shleifer, Hay, Zimmerman, Hebert and Zagachin agreed and conspired together to misappropriate the first Russian specialized depository from Keffer and Forum. To accomplish their ends, Shleifer, Hay and their co-conspirators used Shleifer's and Hay's Harvard positions to fraudulently induce Keffer and Forum to come to Russia and use their resources to create the specialized depository by falsely promising that Forum would own and manage it.

D. The Defrauding of Forum

39. Forum is in the business of the administration and operation of mutual funds in the United States, Poland, Bermuda and Malta. Its expertise includes the technical end of operations management using portable technology, *i.e.* personal computers, with a particular expertise in the operation and administration of mutual funds in foreign countries. In fact, by 1996, Forum had developed the technical, management and operations support necessary to administer mutual funds in Poland, which had proved to be a lucrative market. Forum was the first company to provide independent third-party fund administrative services in Poland. Shleifer and Hay were aware of the financial success of the first Polish mutual fund and were aware that Forum was successful in providing third-party fund administrative services to mutual funds in Poland.

40. Hay and Shleifer knew that Forum had the resources and experience in the

financial services industry to develop in Russia a specialized depository framework, capitalize the specialized depository, review and draft government regulations and secure the requisite license. They knew that given its operations in the United States and Poland, Forum had the credibility needed to secure the license.

41. In furtherance of the conspiracy, Hebert telephoned Keffer at Forum's offices in Maine in February, 1996, and advised him that she and Zagachin planned to launch a mutual fund in Russia. Hebert further informed Keffer that they were considering Forum as their fund administrator and she invited him to travel to Russia to meet with them.

42. Shortly thereafter, on or about February 28, 1996, Hebert sent a letter by facsimile to Keffer at Forum's offices in Maine asking about Forum's interest in creating a mutual fund administrative services company in Russia and requesting an opportunity for Hebert and Zagachin to visit Forum's Poland operations. Hebert in her correspondence related that she had been in contact with the Russian SEC the previous day and had been informed that it would prefer to have fund administrative services performed in Russia rather than in another location such as Poland or the United States. Specifically, Hebert stated: "For your information, the Russian SEC indicated to me yesterday that they have a 'strong preference' for the administration to be done in Russia and that this may be expressed in the regulations in the future". Hebert sent a second letter by facsimile to Keffer at Forum's offices in Maine on February 28, 1996, with more information about her and Zagachin's plans for mutual fund administration. Copies of Hebert's February 28, 1996 correspondence are attached hereto as Exhibits "A" and "B".

43. On February 29, 1996, Hebert sent another letter by facsimile to Keffer at

Forum's offices in Maine with more information about their plans. A copy of Hebert's February 29, 1996 correspondence is attached hereto as Exhibit "C".

44. Only four days later, on March 5, 1996, Keffer received at Forum's offices in Maine, via facsimile, a letter from Vasiliev, drafted by Hay encouraging Keffer and Forum to establish "a company in Russia that would supply fund administration services to the large number of mutual funds that are being launched in Russia". The letter further stated: "The Federal Russian SEC would work closely with you to support the establishment of a successful operation for fund administration in Russia," and asked Keffer to allow Vasiliev's advisor, Hay, to visit Forum's offices in Poland on March 7th and 8th to acquaint himself with Forum's operations. Vasiliev also informed Keffer that: "The Federal Russian SEC planned to support one or more efforts to establish fund administration units in Russia. It is likely that technical assistance funds would be used for this purpose... . The Federal Russian SEC is interested in seeing the administrative function established as an independent business in order to ensure that these services were available to multiple funds and to ensure that there were no conflicts of interest with individual fund management companies". He concluded his letter by stating: "The rapid expansion of fund management requires that problems of fund administration receive immediate attention. I invite you to travel to Russia in the coming weeks to meet with myself, staff and advisors to consider your proposals and explore possible forms of cooperation". A copy of Vasiliev's March 5, 1996 letter is attached hereto as Exhibit "D".

45. On March 6, 1996, Keffer responded by letter to Vasiliev's March 5, 1996 letter and indicated Keffer's and Forum's interest in establishing a mutual fund

administration company in Russia but noting that they would need technical assistance funds and would need them on a timely basis.

46. Hay did not visit Forum's Poland offices on March 7 and 8, 1996. Significantly, however, two of his co-conspirators, Hebert and Zagachin, did appear and were provided with a tour of Forum's Polish operations.

47. On March 18, 1996, Keffer traveled to Russia to meet with Hay and Vasiliev. Keffer first met with Hay. During this meeting, Hay identified himself as working for Harvard, and explained that he was using USAID grant money to assist the Russian government on the capital market project. Hay gave Keffer his Harvard business card, which clearly identified his Harvard affiliation. A copy of that business card is attached hereto as Exhibit "E". Hay stated that he and Vasiliev wanted Forum to create a specialized depository in Russia immediately. In order to induce Keffer and Forum to commit substantial resources to Russia, Hay represented to Keffer that his position with Harvard gave him the responsibility and authority for devising and implementing the agenda for capital market reform in Russia on behalf of the United States government. Hay stated that the cornerstone of the United States' reform efforts for the capital markets was the creation of a mutual fund industry with a specialized depository which would be specially licensed by the Russian SEC to provide fund administrative services to all of the Russian mutual funds. Hay stated to Keffer that creation of the specialized depository was vital both to the interests of Russia and the United States. Hay further represented that Keffer and Forum would have management control and a substantial ownership interest in the specialized depository. Hay also stated that the Russian SEC had technical assistance funds available, through USAID or the World Bank, to hire a

consultant such as Forum to develop an operational and regulatory framework for a Russian specialized depository (the "Consulting Contract"). Hay indicated that the Consulting Contract was an opportunity for Forum to earn revenues which would support at least a portion of the start-up costs associated with Forum maintaining a high-level staff in Russia to create and operate a specialized depository. At the time Hay made his representations about Keffer's and Forum's ownership and management control of the specialized depository, and Forum being paid under the Consulting Contract, he knew they were false.

48. Following this initial meeting, Hay took Keffer to meet Vasiliev. Vasiliev told Keffer that Hay was in charge of creating the first Russian specialized depository on behalf of the Russian SEC (the "Specialized Depository Project") and that Keffer should follow Hay's instructions and directives. Vasiliev and Hay stressed to Keffer that time was of the essence. They told Keffer that Vasiliev was under orders from the Russian government to have a mutual fund industry, including a specialized depository, operational before the July, 1996 Presidential elections. They further explained that Vasiliev was already behind schedule since the original plan had been to have the industry operational by January 1996. Keffer responded that Forum had the resources and ability to create an operational specialized depository within sixty (60) days, but that he had concerns about investing the time of Forum's senior management and technical staff, and a significant portion of Keffer's and Forum's capital, to an untested venture. Keffer informed Hay and Vasiliev that Keffer and Forum would not create the specialized depository without the support of technical assistance funds. Vasiliev stated that the Russian SEC would provide what Forum needed and that Keffer should give Hay a list of

everything Forum required. Vasiliev also reiterated that Hay represented Vasiliev and the Russian SEC in all respects concerning the Specialized Depository Project.

49. In subsequent meetings between Hay and Keffer, Keffer told Hay that Forum would not make the enormous investment of its senior management and technology staff in Russia and incur all of the attendant expense unless Keffer and Forum had ownership and management control of the specialized depository. In response, Hay told Keffer that forthcoming Russian SEC regulations would likely require that Forum relinquish fifty-one percent ownership to Russian owners, but promised that Keffer and Forum would retain management control of the specialized depository. Hay knew when he made these representations that they were false and were made to induce Keffer and Forum to send its senior management and technical staff from Maine to Russia and create a specialized depository which Hay, Shleifer and their co-conspirators would then appropriate for themselves. Hay asked Keffer to send Hay a proposal to contract with the Russian SEC for providing the necessary consulting services to revise the Russian SEC regulations and create the internal operational procedures, computer technology, staff training and other necessary functions of a specialized depository.

50. On March 22, 1996, Hay faxed correspondence to Keffer at Forum's offices in Maine which instructed Keffer to direct all future correspondence to Hay in Russia in care of HIID. Hay's correspondence states: "Hope to hear from you soon. We are working as fast as possible on this." A copy of Hay's facsimile is attached hereto as Exhibit "F".

51. In or about March of 1996, Zagachin, in furtherance of the conspiracy, visited Forum's office in Maine to meet with Keffer and observe Forum's operations in

order to assist Hay in determining whether Forum was capable of creating the specialized depository in Russia.

52. On March 24, 1996, Forum sent from its offices in Maine to Hay at HIID in Moscow an initial proposal to contract with the Russian SEC to consult on the Specialized Depository Project. On April 12, 1996, Shleifer and Hay caused Vasiliev to fax to Forum in Maine a Terms of Reference for the Specialized Depository Project asking Forum to submit another proposal for the Specialized Depository Project in response to the Terms of Reference. The Terms of Reference stated that the Consulting Contract would be funded by the World Bank up to Two Million Five Hundred Thousand (\$2,500,000) Dollars. On April 25, 1996, Forum submitted its proposal for the Specialized Depository Project pursuant to the Terms of Reference sent by Vasiliev on April 12, 1996.

53. During this same period of time, Hay instructed Harvard Russia Program employees to develop a proposal to present to the World Bank to support the World Bank's funding of the Specialized Depository Project. Unknown to Keffer and Forum, Harvard's Moscow employees, including the Deputy Director of the Resource Secretariat ("Deputy Director") openly disagreed with Hay concerning the propriety of this plan. They objected to having Russia borrow from the World Bank to establish a privately owned specialized depository. The Deputy Director argued that World Bank loan proceeds should not be used to fund commercial ventures such as the creation of a privately owned specialized depository, particularly when other entities, such as Credit Suisse and Pioneer were willing and abundantly qualified to create depositories with their own resources. When the Deputy Director asked Hay about who would own the specialized depository, Hay responded "California investors". The concerned Harvard employees, however, had no avenue to

pursue these serious misgivings due to Harvard's lack of oversight. In fact, when the Deputy Director later traveled to Cambridge, Massachusetts to confront Shleifer about Hay's conduct, she was promptly demoted and ultimately terminated.

54. As a result of Shleifer and Hay's influence, on May 13, 1996, the Russian SEC mailed to Forum in Maine written notification, on Russian SEC stationery signed by a Harvard employee, that Forum's proposal had been selected by the Russian SEC. Forum was requested to begin negotiating the terms of the Consulting Contract with the Russian SEC.

55. After Forum received notice of the Russian SEC's selection of its proposal, Hay requested Forum to immediately begin work on the services to be provided under the Consulting Contract based upon its importance to the interests of Russia and the United States. Hay assured Keffer and Forum that Forum would be paid for its services after the Consulting Contract was committed to writing and signed. Hay reiterated Vasiliev's instructions to Keffer that Hay was in charge of the Specialized Depository Project on behalf of the Russian SEC. In reliance on Hay's position with Harvard, his promises of payment under the Consulting Contract, and his promises of Keffer's and Forum's ownership and management control of the specialized depository, Keffer and Forum sent Forum's senior management and technology personnel from Maine to Moscow where they began the work of reviewing and revising Russian SEC regulations, creating operating procedures for a specialized depository and forming a specialized depository company to seek a license from the Russian SEC. In furtherance of the conspiracy, Shleifer and Hay planned to influence the Russian SEC to withhold payments due Forum under the Consulting Contract so that they could use the resulting financial pressure on Forum as

leverage to force Forum to relinquish ownership and control of the specialized depository to them and their co-conspirators after Forum had obtained the license.

56. Hay and his co-conspirators immediately sought to profit from Keffer's and Forum's forthcoming creation of the specialized depository by offering it and the first Russian mutual fund for sale to American investors. Unknown to Keffer and Forum, and contrary to all of his prior representations to Keffer and Forum, Hay, with the approval of Shleifer and Zimmerman, tried to convince Zimmerman's business partner to buy the specialized depository and first Russian mutual fund. On May 14, 1996, (one day after Forum was notified that its proposal was selected by the Russian SEC), Hay sent an offering memorandum ("Hay's Memorandum") to Thomas F. Steyer, Senior Managing Member, of Farallon Capital Management, LLC ("Farallon Capital") (based in California), offering to sell ownership of the first Russian specialized depository and the first Russian mutual fund for an investment of One Million Two Hundred Thousand (\$1,200,000) Dollars. Steyer, through Farallon Capital, was part owner with Zimmerman in Farallon Fixed Income Associates Limited Partnership. A copy of Hay's Memorandum is attached hereto as Exhibit "G".

57. Unknown to Keffer and Forum, Hebert was also actively marketing to American investors ownership of both the first Russian mutual fund and specialized depository for an investment of Three Million Five Hundred Thousand (\$3,500,000) Dollars. Hebert's business plan predicted Twenty-Eight Million (\$28,000,000) Dollars in pre-tax profits in the first five years of operations. Hebert described the "management team" as Hebert as Chief Executive Officer and Zagachin as Chief Operating Officer. Hebert based her profit predictions on her management team's position of trust with the

Russian SEC and the hiring of ILBE as a consultant.

58. Keffer and Forum were unaware that Shleifer and Zimmerman were also marketing the sale of the first Russian mutual fund and specialized depository to American investors. Shleifer attended two meetings with Zimmerman and representatives of Aldrich, Eastman & Waltch and/or its affiliates ("AEW") to discuss Zimmerman and AEW's potential investment in the first Russian mutual fund and specialized depository. Shleifer and Zimmerman traveled to Moscow to meet with Zagachin, Hebert and Hay concerning their investments in the first Russian mutual fund and specialized depository. On May 1, 1996, Zimmerman proposed to Hebert and Zagachin that Zimmerman's "investor group" acquire forty-nine percent of the specialized depository in exchange for \$600,000 in equity investment and twenty percent of the mutual fund in exchange for \$600,000 in equity investment. Keffer and Forum were not aware of any of these activities.

59. In or about May, 1996, Hebert formed Pallada Asset Management ("Pallada") for the purpose of obtaining the first Russian mutual fund license. At the same time, Hebert also formed Boston Capital Management Group LLC, a holding company to own Pallada. ("Boston Capital Management Group LLC" and "Pallada" are herein collectively referred to as "Pallada".)

60. In order to accomplish the goals of the conspiracy, Shleifer and Hay wrongfully used USAID funds to facilitate Hebert's creation of Pallada and to generate business for Pallada. Hebert and Pallada were provided with the services of Harvard employees, office equipment and office space, all financed with USAID funds. Hebert and Pallada received free legal and accounting advice from Harvard and ILBE professionals as well as from other USAID contractors, all at the direction of Hay. Hay,

Hebert and Sokin traveled by airplane to the Urals, Russia's industrial heartland, to generate investment interest in Pallada. The promotional trips for Pallada were paid for with United States funds.

61. From on or about May 14, 1996 to July 25, 1996, Hay intentionally delayed and prolonged negotiations of the written Consulting Contract in order to increase Keffer's and Forum's financial exposure through its ongoing commitment of its senior management, technical staff, and mounting expenses, prior to execution of the written Consulting Contract. Hay achieved this end by continually changing the form of the Consulting Contract as negotiations neared completion. For example, Hay initially provided a lump sum contract and then changed it to a time and materials contract. Subsequently, Hay insisted on a different form of time and materials contract. During this period of time, May 14, 1996 to July 25, 1996, Hay continually promised Keffer and Forum that Forum would be paid for the time and expenses Keffer and Forum were incurring in performing work under the unexecuted Consulting Contract. Hay also instructed Forum to delay the work of revising Russian SEC regulations and to work on creating the operational procedures necessary to create and license the specialized depository. Hay stressed that Vasiliev wanted the specialized depository licensed and operational as soon as possible and instructed Forum to perform work on only those portions of the Consulting Contract. Hay also directed Forum to postpone work on the portions involving the creation of the mutual fund infrastructure, including the regulatory framework for a mutual fund industry. Hay continually represented to Forum that the creation of the specialized depository was an important privatization priority of Russia and also vital to the interests of the United States.

62. Keffer and Forum created Forum Financial Group Russia, LLC ("Forum Russia") as the holding company for Keffer's and Forum's anticipated ownership interest and management control of the specialized depository. The specialized depository was organized by Keffer and Forum as a subsidiary under the laws of the Russian Federation under the name The First Russian Specialized Depository, a limited liability company (the "FRSD"). Keffer and Forum provided all of the resources needed to create and operate the FRSD. Keffer and Forum also created Forum Financial Group Consulting, LLC ("Forum Consulting") to provide consulting services under the Consulting Contract. Keffer and Forum provided all of the employees for Forum Consulting and paid all of the operating expenses incurred by Forum Consulting. Keffer owned ninety-nine percent of Forum Russia and ninety-nine percent of Forum Consulting. Another Forum entity, Forum Financial Holding, Inc., owned the remaining one percent of Forum Russia and Forum Consulting. Forum Financial Holdings, Inc. has assigned all of its rights and claims against the Defendants to Forum.

63. From May 14, 1996 through June, 1996, Keffer and Forum proposed prospective Russian investors to own fifty-one percent of the FRSD. During this time period, Forum also proposed ownership structures that would give Forum Russia management control and forty-nine percent ownership of the FRSD. Hay rejected these proposals and stated emphatically that Zagachin was the only person qualified to have a substantial ownership interest in the FRSD and to have a role in management. Hay said that the Russian SEC wanted Zagachin to be co-owner of the FRSD with Keffer. Keffer expressed concerns to Hay about giving Zagachin majority ownership and management authority over the FRSD, because Zagachin did not have the qualifications to operate a

specialized depository. However, as a result of Hay's insistence, the Plaintiffs eventually agreed to employ Zagachin at the FRSD, but stipulated that she would not have management control and reserved the FRSD's right to terminate her.

64. By the beginning of July, even though Hay and Keffer had not yet agreed to an ownership structure for the FRSD, Hay instructed Keffer and Forum to have the FRSD apply for a specialized depository license with Forum Russia as one hundred percent owner. Hay gave this instruction because he and his co-conspirators had to get the FRSD licensed quickly so it could serve as Pallada's specialized depository and thereby position Pallada to receive the first Russian mutual fund license. Pallada needed to have an agreement with a specialized depository to conduct its mutual fund administration in order to be eligible for a Russian mutual fund license.

65. A prerequisite for obtaining a specialized depository license required Keffer and Forum to capitalize the FRSD by depositing Four Hundred Thousand (\$400,000) Dollars in a cash custody account in Russia. The Russian SEC regulations required that the Four Hundred Thousand (\$400,000) Dollars were to be held in a custody account until the Russian SEC issued the specialized depository license, at which time the funds were to be transferred to the FRSD's operating account.

66. In further reliance on Hay's representations, on July 5, 1996, Keffer and Forum deposited Four Hundred Thousand (\$400,000) Dollars into a cash custody account at Citibank's Moscow branch, to "capitalize" the FRSD. A copy of the Cash Custody Agreement is attached hereto as Exhibit "H".

67. On July 25, 1996, Forum Consulting and the Russian SEC finally executed the Consulting Contract. The Consulting Contract provided for a Four Hundred Fifty

Thousand (\$450,000) Dollar initial payment to Forum Consulting within ten days.

68. On or about August 1, 1996, the Russian SEC granted the FRSD, owned one-hundred percent by Forum Russia, the first license to operate a specialized depository.

69. On August 1, 1996, Forum Consulting made a written request that the Four Hundred Fifty Thousand (\$450,000) Dollar advance payment under the Consulting Contract be paid to Forum Consulting within ten days of July 25, 1996 as required by the terms of the Consulting Contract.

70. On August 8, 1996, Pallada received the first Russian mutual fund license from the Russian SEC. Pallada's license application described the FRSD as its specialized depository. However, Shleifer and Hay needed the FRSD to commence its fund administration services to Pallada before Pallada could sell shares to investors. Hay requested that the FRSD commence fund administration services to Pallada. Keffer and Forum were not willing to allow the FRSD to begin administering Pallada's mutual fund until the drafting and revising of the necessary Russian government regulations was completed and Pallada had a prospectus that disclosed its operating procedures.

71. In furtherance of the conspiracy, to put maximum financial strain on the Plaintiffs, Hay informed Keffer that Forum Consulting would not be paid under the Consulting Contract unless: (i) Zagachin owned fifty-one percent of the FRSD; (ii) Zagachin had management control of the FRSD; and (iii) the FRSD began administering Pallada's mutual fund by September 2, 1996. Hay further informed Keffer that Forum's role in the FRSD would be limited to providing capital and technology. Keffer told Hay that these demands were unacceptable.

72. Hay then proposed a meeting with Keffer and Forum to resolve these issues. He recommended that Michael Butler, Esquire (hereinafter "Butler") act as a neutral mediator. This was done in furtherance of the conspiracy, because Butler was not neutral but was hired by Harvard pursuant to Shleifer's request. Butler at the time worked directly with Hay and Shleifer on Harvard's Russia Program and, more specifically, represented Harvard, Shleifer and Hay in a Federal investigation concerning the administration of the Harvard Russia Program. Hay intentionally failed to disclose to Forum and Keffer his and Harvard's relationship to Butler and that Hay's and Shleifer's administration of Harvard's Russia Program was the subject of a Federal investigation.

73. On August 19, 1996, Keffer, Forum staff members, Hebert and Hay met with Butler. Unknown to Keffer and Forum, Shleifer and Zimmerman had arrived in Moscow that same day and had had a private meeting with Zagachin, Hay and Hebert. At the meeting with Butler, Keffer and his staff made full disclosure to Butler about how Hay's conduct was preventing Forum Consulting from completing the necessary recommendations for revisions to the Russian SEC regulations and how Forum Consulting was not being paid for its work. They also informed Butler that Hay insisted that Zagachin have ownership and management control and that Zagachin was not qualified to manage the FRSD. Keffer and his staff further informed Butler of Hay's insistence that the FRSD administer Pallada's mutual fund when the Russian SEC regulations had not been revised and Pallada did not have an adequate prospectus.

74. After meeting with Butler, Hay sent Keffer a term sheet entitled "Mike's [Butler's] Proposal". A copy of that term sheet is attached hereto as Exhibit "I". Hay and Butler proposed that Keffer sell both Forum Consulting and Forum Russia (owner of

the FRSD) to Zagachin for Four Hundred Thousand (\$400,000) Dollars (an amount equal to the capital Keffer and Forum had already deposited in the Citibank custody account). Hay and Butler further proposed that Zagachin, despite her patent lack of qualifications, continue to perform the obligations set forth in the Consulting Contract, under Forum Consulting's name, and be paid by the World Bank. Finally, Hay and Butler proposed that Forum perform "precisely defined" services as a "subcontractor" and in particular, "Forum would process for the first fund to go live on September 2, 1996".

75. On August 20, 1996, Hay took preemptive action to effectuate the conspiracy by attempting to misappropriate Keffer's and Forum's capital investment. Zagachin, under Hay's direction, went to Citibank and instructed Citibank employees to transfer the Four Hundred Thousand (\$400,000) Dollars from the cash custody account into the operating account of the FRSD. This was done to enable Hay through Zagachin to have access to the funds. However, Citibank notified Forum of this attempt and Forum immediately told Citibank that Zagachin did not have the authority to transfer the funds, and Citibank consequently refused to conduct the transaction.

76. Still unaware of Hay's improper influence over Vasiliev and the Russian SEC, Keffer sent a letter to Vasiliev on August 23, 1996, requesting a meeting with him to discuss Keffer's grave concerns about Hay's insistence that the FRSD administer live operations for Pallada's mutual fund on September 2, 1996. Keffer informed Vasiliev that such an undertaking "is both commercially premature and damaging to the prospects of long term development of a stable mutual fund industry". A copy of Keffer's August 23, 1996 correspondence is attached hereto as Exhibit "J".

77. Vasiliev quickly responded with a terse one page fax on Resource

Secretariat letterhead which ignored all of Keffer's concerns and demanded a "work plan." Keffer sent Vasiliev another letter on August 23, 1996, reiterating Keffer's concerns, including the commercial immaturity of the mutual fund infrastructure and Keffer's position that the FRSD would not administer a live mutual fund on September 2, 1996. A copy of Keffer's additional August 23, 1996 correspondence is attached hereto as Exhibit "K".

78. On August 27, 1996, Vasiliev responded in writing to Keffer's August 23, 1996 letters and took a position which was inconsistent with the terms of the Consulting Contract. Vasiliev disregarded Keffer's warnings that the critical legal and institutional infrastructures for the specialized depository specified in the Consulting Contract and referenced in Vasiliev's March 5, 1996 letter, had not been completed. Vasiliev simply repeated Hay's demand that Keffer and Forum have the specialized depository working pursuant to an "aggressive time line," stating that "the World Bank contract which you signed on July 25, 1996 calls for the creation of a specialized depository". Vasiliev ignored the other prerequisites of the Consulting Contract, including those provisions specifying the creation of the legal and institutional infrastructure necessary to protect the Russian investors, about which Hay had instructed Forum to postpone completion in order to focus all attention on creating the FRSD. Vasiliev rejected Keffer's idea of a demonstration rather than an actual mutual fund administration as inconsistent with the terms of the Consulting Contract and unacceptable to the Russian SEC. Vasiliev requested that Keffer provide the Russian SEC with a proposal for altering the ownership of the FRSD. Vasiliev promised to work with Forum on its problems with the Consulting Contract once ownership of the FRSD was "stabilized". A copy of Vasiliev's

August 27, 1996 letter is attached hereto as Exhibit "L".

79. It now became clear to the Plaintiffs that Vasiliev was controlled by Hay and the representations that Hay had made to them about the ownership and control of the FRSD and receiving payment under the Consulting Contract were false. The Plaintiffs consequently concluded that they had no choice but to stem their mounting financial losses by selling Forum Russia, including Forum Russia's ownership of the FRSD, to Zagachin, as requested in the proposal from Hay and Butler for Four Hundred Thousand (\$400,000) Dollars. Hay and Hebert then proceeded to negotiate with Keffer the terms of the sale to Zagachin and to arrange financing for the sale. Copies of Hebert's letter setting forth the terms of the sale and financing is attached hereto as Exhibit "M".

80. On September 3, 1996, with financing provided by Hay, Oasis Financial Services, LLC ("Oasis") purchased Forum Russia, including the FRSD, from Keffer and Forum Financial Holdings, Inc., for Four Hundred and Eight Thousand (\$408,000) Dollars. Zagachin was the record owner of 99% of Oasis and also the record owner of Sage Capital, which owned the remaining 1% of Oasis. Zagachin's ownership was for her benefit and the benefit of Hay, Shleifer and Hebert.

81. Hay and Shleifer and their co-conspirators had now completed the goal of their conspiracy with the sale of Forum Russia and the FRSD to Oasis.

82. The acts committed in furtherance of the conspiracy include, but are not limited to, the acts described above in paragraphs 41 through 80.

83. By letter dated May 20, 1997, USAID suspended the USAID Agreements based upon findings by its Inspector General of misconduct by Shleifer and Hay in Russia. A copy of USAID's letter suspending the Agreement and a related press release

are attached hereto as Exhibit "N." The letter stated, inter alia, as follows:

Activities for individual gain by personnel placed in a position of trust in Russia and financed under these USAID cooperative agreements is not in the national interest of the United States. Through these cooperative agreements, the General Director in Moscow and the Project Director have gained influence over nascent Russian capital markets. They have abused the trust of the United States Government by using personal relationships, on occasion, for private gain. USAID has been trying to explain to key Russian Government counterparts the value of open and transparent processes, and the importance of avoiding conflicts of interest, as ways to increase investor confidence in the Russian capital markets. These were some of the key objectives of the subject cooperative agreements. The private activity of the General Director in Moscow and the Project Director, supported by staff and equipment paid for with U.S. Government funds, conveys exactly the wrong message to the Russians.

84. On May 23, 1997, Harvard removed Shleifer and Hay from their positions with HIID and Harvard's Russia Program. A copy of Harvard's letter to this effect is attached hereto as Exhibit "O".

85. On August 1, 1997, USAID terminated Harvard's USAID Agreements. A copy of USAID's letter taking this action is attached hereto as Exhibit "P".

86. On or about February 7, 2000, Harvard disbanded HIID.

87. On September 26, 2000, the United States filed a civil action in the United States District Court, District of Massachusetts, against Harvard, Shleifer, Hay, Zimmerman and Hebert alleging against them inter alia, claims for violations of the False Claims Act (31 U.S.C. §3729), and for fraud and civil conspiracy arising from their activities in Russia, including their conspiracy to launch the first Russian mutual fund management company and the first Russian specialized depository.

V. CAUSES OF ACTION

COUNT I

The Plaintiffs v. Hay (Fraudulent Misrepresentation)

88. The Plaintiffs repeat and reallege paragraphs 1 through 87 as if each were fully set forth herein.

89. Hay made false representations to the Plaintiffs of certain material facts, including, but not limited to, that Plaintiffs would own and have management control of the Specialized Depository.

90. Hay knew that those representations were false or he made them with reckless disregard of whether they were true or false.

91. Hay made the false representations for the purpose of inducing the Plaintiffs to act in reliance on them by creating the FRSD.

92. The Plaintiffs justifiably relied upon Hay's false representations as true and acted upon them to their detriment, by among other things, creating the FRSD which Hay and Shleifer then usurped for their own gain.

93. Hay's false representations have caused the Plaintiffs to suffer damages.

94. Hay is liable for the damages the Plaintiffs have suffered, which are the profits and value of the FRSD, and the financial benefit the Plaintiffs would have received from an increase in their international business.

COUNT II
The Plaintiffs v. Shleifer
(Aiding and Abetting Fraudulent Misrepresentation)

95. The Plaintiffs repeat and reallege paragraphs 1 through 94 as if each were fully set forth herein.

96. Hay made false representations to the Plaintiffs of certain material facts, including, but not limited to, that Plaintiffs would own and have management control of the FRSD.

97. Hay knew that those representations were false or he made them with reckless disregard of whether they were true or false.

98. Hay made the false representations for the purpose of inducing the Plaintiffs to act in reliance on them by creating the FRSD.

99. The Plaintiffs justifiably relied upon Hay's false representations as true and acted upon them to their detriment, by creating the FRSD which Hay and Shleifer then usurped for their own gain.

100. Hay's false representations have caused the Plaintiffs to suffer damages.

101. Shleifer knew that Hay made fraudulent misrepresentations to the Plaintiffs and gave substantial assistance and encouragement to Hay to make such fraudulent misrepresentations.

102. Shleifer committed these tortious acts in concert with Hay's fraudulent misrepresentations and pursuant to a common design with Hay.

103. The Plaintiffs suffered damages as a result of Shleifer's conduct.

104. Shleifer is liable for the damages the Plaintiffs have suffered, which are the profits and value of the FRSD and the financial benefit the Plaintiffs would have received from an increase in their international business.

COUNT III
The Plaintiffs v. Hay
(Negligent Misrepresentation)

105. The Plaintiffs repeat and reallege paragraphs 1 through 104 as if each were fully set forth herein.

106. Hay in the course of his business, profession or employment, provided false information to the Plaintiffs to guide them in their business transactions.

107. Hay owed a duty to the Plaintiffs to exercise reasonable care or competence in obtaining or communicating the information to the Plaintiffs.

108. Hay breached his duty of care by failing to exercise reasonable care or competence in obtaining or communicating the information to the Plaintiffs and thereby caused harm to the Plaintiffs.

109. The Plaintiffs justifiably relied upon Hay's false information.

110. Hay is liable for the damages the Plaintiffs have suffered, which are the profits and value of the FRSD and the financial benefit the Plaintiffs would have received from an increase in their international business.

COUNT IV
The Plaintiffs v. Shleifer
(Aiding and Abetting Negligent Misrepresentation)

111. The Plaintiffs repeat and reallege paragraphs 1 through 110 as if each were fully set forth herein.

112. Hay in the course of his business, profession or employment, provided false information to the Plaintiffs to guide them in their business transactions.

113. Hay owed a duty to the Plaintiffs to exercise reasonable care or competence in obtaining or communicating the information to the Plaintiffs.

114. Hay breached his duty of care by failing to exercise reasonable care or competence in obtaining or communicating the information to the Plaintiffs and thereby caused harm to the Plaintiffs.

115. The Plaintiffs justifiably relied upon Hay's false information.

116. Shleifer knew that Hay provided false information to the Plaintiffs and Shleifer gave substantial assistance and encouragement to Hay to provide that false information to the Plaintiffs.

117. Shleifer committed these tortious acts in concert with Hay's negligent misrepresentations and pursuant to a common design with Hay.

118. The Plaintiffs suffered damages as a result of Shleifer's conduct.

119. Shleifer is liable for the damages the Plaintiffs have suffered, which are the profits and value of the FRSD and the financial benefit the Plaintiffs would have received from an increase in their international business.

COUNT V

The Plaintiffs v. Hay

(Tortious Interference with Prospective Economic Advantage)

120. The Plaintiffs repeat and reallege paragraphs 1 through 119 as if each were fully set forth herein.

121. The Plaintiffs had a prospective economic advantage to own and manage the first licensed specialized depository in Russia, namely the FRSD.

122. Hay, through fraud and intimidation, interfered with the Plaintiffs' prospective economic advantage.

123. Hay's wrongful interference caused the Plaintiffs to suffer damages.

124. Hay is liable for the damages the Plaintiffs have suffered, which are the profits and value of the FRSD and the financial benefit the Plaintiffs would have received from an increase in their international business.

COUNT VI
The Plaintiffs v. Shleifer
(Aiding and Abetting Tortious Interference
with Prospective Economic Advantage)

125. The Plaintiffs repeat and reallege paragraphs 1 through 124 as if each were fully set forth herein.

126. The Plaintiffs had a prospective economic advantage to own and manage the first licensed specialized depository in Russia, namely the FRSD.

127. Hay, through fraud and intimidation, interfered with the Plaintiffs' prospective economic advantage.

128. Hay's wrongful interference caused the Plaintiffs to suffer damages.

129. Shleifer knew that Hay's conduct constituted wrongful interference with the Plaintiffs' prospective economic advantage, and gave substantial assistance and encouragement to Hay to engage in such conduct.

130. Shleifer committed these tortious acts in concert with Hay's wrongful interference and pursuant to a common design with Hay.

131. The Plaintiffs suffered damages as a result of Shleifer's conduct.

132. Shleifer is liable for the damages the Plaintiffs have suffered, which are the profits and value of the FRSD and the financial benefit the Plaintiffs would have received from an increase in their international business.

COUNT VII
The Plaintiffs v. Harvard
(Vicarious Liability)

133. The Plaintiffs repeat and reallege paragraphs 1 through 132 as if each were fully set forth herein.

134. At all relevant times Hay and Shleifer were agents of Harvard.

135. At all relevant times Shleifer and Hay purported to act or speak on behalf of Harvard.

136. At all relevant times Hay and Shleifer engaged in their tortious conduct while acting within the scope of their apparent authority from Harvard.

137. The Plaintiffs' relied upon Shleifer's and Hay's apparent authority.

138. Hay and Shleifer were aided in accomplishing their tortious conduct by the existence of their agency relationship with Harvard.

139. Harvard is liable for the damages caused by the tortious conduct of Hay and Shleifer as stated in Counts I-VI, which are the profits and value of the FRSD and the financial benefit the Plaintiffs would have received from an increase in their international business.

COUNT VIII
The Plaintiffs v. Harvard
(Vicarious Liability)

140. The Plaintiffs repeat and reallege paragraphs 1 through 139 as if each were fully set forth herein.

141. At all relevant times Hay and Shleifer were employees of Harvard.

142. At all relevant times Hay and Shleifer acted within the scope of their employment.

143. Harvard is liable for the damages caused by the tortious conduct of Hay and Shleifer as stated in Counts I-VI, which are the profits and value of the FRSD and the financial benefit the Plaintiffs would have received from an increase in their international business.

COUNT IX
The Plaintiffs v. Harvard
(Negligence)

144. The Plaintiffs repeat and reallege paragraphs 1 through 143 as if each were fully set forth herein.

145. Harvard owed a duty to the Plaintiffs to supervise, oversee and manage Shleifer's and Hay's operation of its Russia Program, including the Specialized Depository Project, with reasonable care, including the duty to retain and supervise its agents and employees in a reasonable manner.

146. Harvard breached its duty of care by failing to act reasonably in its supervision, oversight and management of Shleifer's and Hay's operation of its Russia Program, including the Specialized Depository Project, and in its retention and supervision of its agents and employees.

147. As a direct, proximate and foreseeable result of Harvard's breach of its duty, Shleifer and Hay engaged in tortious conduct which caused harm to the Plaintiffs.

148. Harvard is liable for the damages the Plaintiffs have suffered, which are the profits and value of the FRSD and the financial benefit the Plaintiffs would have received from an increase in their international business.

COUNT X
The Plaintiffs v. Hay, Shleifer, and Harvard
(Punitive Damages)

149. The Plaintiffs repeat and reallege paragraphs 1 through 148 as if each were fully set forth herein.

150. At all relevant times Hay and Shleifer were employed by Harvard in management positions and they committed the acts alleged herein while acting within the scope of their employment.

151. Hay's and Shleifer's conduct towards the Plaintiffs was motivated by ill will against them and was so outrageous that it constituted malice.

152. The Defendants' conduct justifies the imposition of punitive damages.

153. The Defendants are liable to the Plaintiffs for punitive damages.

VI. REQUEST FOR RELIEF

154. **THEREFORE**, the Plaintiffs ask this court to:

- a. enter judgment in their favor on all counts;
- b. award them damages, including compensatory, special and consequential damages, plus interest and costs as to each count;
- c. award them punitive damages; and
- d. grant them such other and further relief as this court deems just and proper.

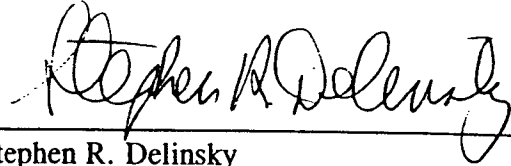
VII. JURY CLAIM

The Plaintiffs demand a trial by jury on all of the Counts alleged herein.

Respectfully submitted,

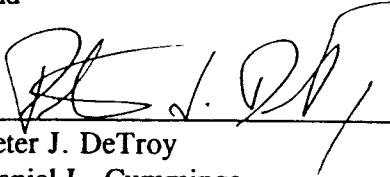
**JOHN Y. KEFFER AND
FORUM FINANCIAL GROUP, LLC**

By their attorneys,



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Dated: October 24, 2000

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28th February 1996

John Y. Keffer
President
Forum Financial Group
Two Portland Square
Portland, ME 04101

By Facsimile 207 879 1900

Dear John,

It was a pleasure speaking with you yesterday. Your insights gave Julia and I greater clarity on what it is we are trying to accomplish and how to do it.

We would very much like to progress the discussions with you as quickly as possible so that we can decide upon which route to take and with whom to work. Unfortunately, I will not be in the US this week as I had planned. Perhaps the next step should be:

(i) for us to describe how we currently envisage the operations and to get some feedback from you. For this purpose I attach some work flows. I would appreciate it if you would review the attached graphs and comment on (i) any important steps we have missed, (ii) any additional controls that should be in place, and (iii) the efficiency of the proposed work flows.

(ii) for you to design a model administration bureau providing details on number and type of employees; office space; telecommunication requirements; computer hardware and software requirements; other office equipment requirements and other significant cost items. The Russian-specific items we will be able to provide cost estimates.

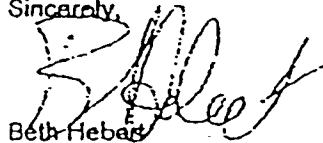
(iii) for us to view your administration in Poland. We would be prepared to do this next week.

(iv) we need to clarify the costs/benefits of performing the administration all in Russia or having only the front end in Russia and the processing off-shore (in Poland). For your information, the Securities Commission indicated to me yesterday that they have a "strong preference" for the administration to be done in Russia and that this may be expressed in the regulations in the future.

(v) If we decide to proceed to create a full bureau service in Russia how we can work together to do this on a cost-efficient basis. What sort of skills would we hope to bring in from a Russian partner (computer technology/programming)? How would it be financed? Who would market the services to third party clients? How long would it take to establish a full bureau service (if this is deemed to be the right way to go).

Please contact either myself or Julia Zagachin as soon as possible in Moscow at 7-503-956-9100 or by fax 7-095-956-1800.

Sincerely,



Beth Hebart
General Manager

FLEMINGS

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E-MAIL : C-USRR.A.KOYMARL@CUSTOMERS.UNIPRUC.MOS

To : John Keffert
Forum Financial Group

From : Beth Hebert

Date : 28th February 1996

Re : Mutual Fund Administration

-
1. Number of Accounts first month: 8,000
 2. Average size of initial amount: \$2,500
 3. Number of new accounts per month: 1350
 4. Average size of new accounts: \$1,000
 5. growth 5%/month
 6. ?
 7. 68%/50%/40%/30% y-o-y inflation
 8. 1996 4500 - 5500 -- thereafter adjust with inflation.

9. Labor costs:
 - a) specialised degree in economic/finance (\$1,000/ month with no experience)
 - b) University graduates (\$800/month)
 - c) processors (\$300/month)
 - d) customer service personnel (\$800/month)

The above figures are net of taxes. Taxes will add another 100% to the cost of labor. There will be ways to structure the company to reduce labor costs.

10. Space Costs \$450-750/sq ft/year

11. telecommunications costs

- a) Comstar telephone charges: Moscow to UK = \$1.72/minute
 - b) hook up to Comstar = \$500/install a line plus \$150/month

12. customs duty on hardware = 20% VAT + 20% import duties + 10% excise

It might be possible to avoid the full load of duties and taxes by, for example, registering for accreditation.

To : John Keffer
From : Beth Hebert
Date : 29th February 1996
Pages : 1 of 3

Julia took a crack at designing her own registrar. Will you see attached and let us know whether you think we have made reasonable assumptions?

She has assumed we need 10 data entry clerks given the following new account creation schedule:

month 1	month 2+3	month 4 on
8,000	3,000	1,500

We have not made any assumptions about turnover (redemptions) per unit account as there is no relevant experience here to draw from. What has experience been in Poland?

Beth

	Apr	May	Jun	Jul	Aug	Sep	Oct	Nov	Dec	Y1	Y2	Y3	Y4	Y5
Staff	12,920	12,920	12,920	12,920	12,920	14,060	16,810	16,910	15,910	142,310	180,500	180,500	180,500	180,500
Start Up	57,360									87,350				
Rent	5,833	5,833	5,833	5,833	5,833	5,833	5,833	5,833	5,833	58,333	70,000	70,000	70,000	70,000
Telecom	1,500	1,500	1,500	1,500	1,500	1,500	1,500	1,500	30,000	30,000	30,000	30,000	30,000	30,000
Audit									5,000	5,000	24,000	24,000	24,000	24,000
Insurance	2,000	2,000	2,000	2,000	2,000	2,000	2,000	2,000	2,000	20,000	324,500	324,500	324,500	324,500
Supplies	109,603	22,253	22,253	22,253	22,253	23,393	26,243	26,243	61,243	357,983	324,500	324,500	324,500	324,500
Total Pre-Tax	109,603	22,253	22,253	22,253	22,253	23,393	26,243	26,243	61,243	357,983	324,500	324,500	324,500	324,500
Tax 35%	38,361	7,789	7,789	7,789	7,789	8,188	9,185	9,185	21,435	125,298	113,575	113,575	113,575	113,575
No. # of accounts														
Cost per account										15,500	31,500	47,500	63,500	79,500
										31.18	13.91	9.22	6.90	5.61

[illegible]

Russian Staff Costs

Position	Head Count	Monthly head	Annual total	Apr	Mar	May	Jun	Jul	Aug	Sep	Oct	Nov	Dec	Y1	Y2	Y3	Y4	Y5
Accountant	1	1,500	1,500	1,500	1,500	1,500	1,500	1,500	1,500	1,500	1,500	1,500	1,500	15,000	15,000	15,000	15,000	15,000
Operating Officer	1	2,000	24,000	2,000	2,000	2,000	2,000	2,000	2,000	2,000	2,000	2,000	2,000	20,000	20,000	20,000	20,000	20,000
Manager	1	1,300	15,800	1,300	1,300	1,300	1,300	1,300	1,300	1,300	1,300	1,300	1,300	13,000	13,000	13,000	13,000	13,000
Entry Operators-Mail clerk	10	300	36,000	900	900	900	900	900	900	1,500	3,000	3,000	3,000	8,000	8,000	8,000	8,000	8,000
Service manager	1	800	9,600	800	800	800	800	800	800	800	800	800	800	8,000	8,000	8,000	8,000	8,000
Administrative Assistant	1	300	3,600	300	300	300	300	300	300	300	300	300	300	3,000	3,000	3,000	3,000	3,000
al	15		90,300	6,800	6,800	6,800	6,800	6,800	6,800	7,400	8,900	8,900	8,900	74,800	95,000	95,000	95,000	95,000
			81,270	6,120	6,120	6,120	6,120	6,120	6,120	6,580	8,010	8,010	8,010	67,410	85,500	85,500	85,500	85,500
			177,570	12,920	12,920	12,920	12,920	12,920	12,920	14,080	16,910	16,910	16,910	145,310	180,500	180,500	180,500	180,500

Assumptions:
 Limited launch April/Full launch Sep.
 Data entry operators will work in several shifts.
 10 Data entry operators are added in October.
 Client service manager/creates units/destroys units.

Equipment

		Start Up Costs		
Item	Description	Amount	Cost per unit	Total
Computer	486	15	800	12,000
Printer		2	1,300	2,600
Fax		4	1,000	4,000
Xerox		1	10,000	10,000
PBX		1	20,000	20,000
Server		1	16,500	16,500
Software (Quasar)		1	0	0
Misc		1	4,000	4,000
Desks		15	200	3,000
Chairs		15	150	2,250
Cabinets		40	200	8,000
Telecom	Comstar	10	500	5,000
Total				87,350
Recurring Equipment Costs				
1. Comstar \$150 per month per line			1,500	
2. Quasar maintainace 18% of GBP 60,000			10,800	17,280



**Федеральная комиссия по ценным бумагам и фондовому рынку
при Правительстве Российской Федерации**

117938, ГСП-1, Москва В-49, Ленинский проспект, 9
Тел. 234-53-84, факс: 234-12-28

№ _____
На № _____ от _____

March 5, 1996

Mr. John Y. Keffer
President
Two Portland Square
Portland, Maine 04101
USA
Fax: 207 - 879 - 6050

Dear Mr. Keffer,

I am writing to you to encourage you to consider the establishment of a company in Russia that would supply fund administration services to the large number of mutual funds that are being launched in Russia.

One of my advisors, Mr. Jonathan Hay, will be in Poland on Thursday, March 7 and Friday, March 8. I understand that you have a fund administration business in Poland, and I would appreciate if you could acquaint Mr. Hay with its operation. I will be looking forward to his report.

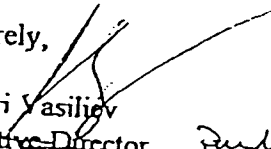
The Federal Commission plans to support one or more efforts to establish fund administration units in Russia. It is likely that technical assistance funds will be used for this purpose. A number of foreign and Russian organizations have already made their interest known and have submitted informal proposals that we are considering.

The Federal Commission is interested in seeing the administrative function established as an independent business in order to ensure that these services are available to multiple funds and to ensure that there are no conflicts of interest with individual fund management companies. These policy objectives are likely to be reflected in the licensing policies of the Federal Commission.

From a regulatory and political point of view, it is important that fund administration services be established in Russia. The Federal Commission would work closely with you to support the establishment of a successful operation for fund administration in Russia. We have had many experiences with financial scandals that might have been averted had the appropriate administrative procedures been put in place.

The rapid expansion of the fund management requires that problem of fund administration receive immediate attention. I invite you to travel to Russia in the coming weeks to meet with myself, staff and advisers to consider your proposals and explore possible forms of cooperation.

Sincerely,


Dimitri Vasiliev

~~Executive Director~~

[Federal Commission for Securities and the Capital Market of the Russian Federation]

And + E.D.

E.

"D"

Jonathan Hay

General Director
HIID / Moscow

011-7-503-

~~455-5888~~

(1) (3) (1) (1)

Ducat Place, 5th Floor
8/10 Ul. Gasheta
125047 Moscow, Russia
Telephone: 956 6622
Telefax: 956 3837
Inside CIS code 095
Outside CIS code 503
E-mail: jhay@ias.apc.org

*Harvard Institute
for International Development*

E-mail: bhebert@flemings.msk.ru

March 22, 1996

To: Mr. John Y. Keffer
Fax: 207 - 879 - 6050

From: Jonathan Hay

You can send me email at jhay@lrp.glas.apc.org.

Fedex or DHL should be sent to:

Mr. Jonathan Hay, Harvard
Ducat Place, 5th Floor
8/10 UL Gasheka
125047 Moscow, Russia
Tel: 011-7095-258-35-70

Hope to hear from you very soon. We are working as fast as possible on this.

G.

MAY-20-1996 17:02 FROM ILBE

TO

8101617345373 F.02

300K (want 1K euros)

①
②
③

GLOS

May 16, 1996

To: Tom Steyer

Re: Specialized Depository

Real Estate Licences
for Interval Fund

FAIRWAY

1.0 Introduction. As you know, we are seeking USD 1.2 million to create a fund management company and a fund administrator/custodian ("Specialized Depository") in Russia. I understand from Nancy that you wish to have some more information on the specialized depository. This note explains a) the function of a specialized depository, b) why the Specialized Depository that we create is likely to be successful, c) our assumptions about profitability, d) our competition, and e) the link with the proposed Fund Management Company.

much

Relat

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Uolote

Accepted

28 pt.

2.0 Function of Specialized Depository. Under recently issued mutual fund regulations (which were drafted by the Russian legal team that I manage), fund management companies must sign a contract with an independent Specialized Depository. Under the regulations, the Specialized Depository provides custodial services and is responsible for the compliance of fund management companies with certain parts of the regulations (e.g. restrictions on the investment portfolio). In practice, the Specialized Depository will also be responsible for a) maintaining a registry of unit holders (including issuing and cancelling units), b) the accounting for fund assets and transactions, and c) pricing of assets (on a daily basis in the case of open mutual funds). The Annex to this note describes in more detail the function of the Specialized Depository.

① Jonathan

② 51. Assets

3 Quarters

3.0 Why we expect our Specialized Depository to succeed? The reasons have to do with a) regulation, b) management, c) first mover advantage, d) assured client base, e) presence of a strategic partner and e) the availability of subsidy. These reasons are discussed below.

3.1 Regulation. Both investment fund managers and specialized depositories must be licensed. The regulatory requirements for getting a fund management license are relatively light. The regulation of fund managers is mostly delegated to the market, to the choices of investors. The Federal Commission for Securities and the Capital Market (e.g. the Russian SEC) recognizes that it should not be in the business of choosing fund managers for investors. On the other hand, the regulatory requirements for specialized depositories are severe. Before issuing any licenses to potential specialized depositories, the Federal Commission will ensure the integrity of systems for processing flows of units and finance between investors and the fund, b) the proper maintenance of the registrar of investors, c) the adequacy of accounting for assets, and d) the safekeeping of assets. Regulations provide many mandatory procedural and processing requirements for specialized depositories. The requirements will be made more detailed on the basis of the Federal Commission's experience with our Specialized Depository. Specialized Depositories will be audited

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Fabio Impresario & Beth

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501. Fee 2 positions

① No more earn

② Everything else

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CONFIDENTIAL

F 01160

frequently by the Federal Commission. The Federal Commission expects to issue few licenses to specialized depositories which means that a) the market for these services will be divided between few organizations (in the short to medium term we expect to capture most of the market) and b) pricing is likely to be less than perfectly competitive.

Our project stands to benefit more than any other from the Federal Commission's approach to regulation. This is for three reasons. First, we have the best probability of receiving a license. Our project is the flagship Specialized Depository of the Federal Commission designed to set the standard for the market place and to be used to define the operational and procedural thresholds that must be met by others to enter the business. Every decision we make about design, systems and procedures will be taken in close cooperation with the Federal Commission. Our project will be established with the active involvement of the Russian legal team that the Federal Commission entrusted with the drafting of the original mutual fund regulations. Second, we are likely to get a license before anyone else which will give a significant first mover advantage (discussed below). Third, our project will set the market standard. Given this project's relationship to the Federal Commission, any other attempts by definition will be in a catch up mode.

3.2 Management. We have the best management team. The ability of management is proven in Russia and has an exceptional reputation for honesty and competence which is unique in the Russian market place. The president, Julia Zagachin, is one of a few professionals who have successfully built large infrastructure operations, earned the confidence of the Federal Commission, every major western institutional investor active in the Russian equity markets, the Russian brokerage and banking community. She is completely bi-lingual and bi-cultural. The future head of operations, Nadezhda Masenkova is currently Chief Operating Officer of the DCC. She developed procedures and controls currently in use by the DCC. The strategic partner (discussed below) brings a first rate management team with similar western expertise that will be involved in the set up of the Specialised Depository.

3.3 First mover advantage. The economics of the Specialised Depository business give the advantage to the first group that gets established and attracts clients. In Russia, we are that group. In the early phase while no one else is set up we can be profitable with lower volumes of processing and high margins. As the business progresses, we can lower margins and maintain profitability with higher volumes of processing. Any other competitor that wishes to beat our prices must be able to immediately get the higher volumes that make it possible to live with the lower margins. The need for high volumes for profitability should be a significant barrier to entry for new competitors. This is also the case in the West where this business tends to be concentrated with a very few providers such as State Street/DST in the United States or Hexagon and Premier Trust in the United Kingdom. In the short to

medium term our advantage comes from the fact that the regulator wants us to be first. In the future we can keep our dominant position through a quality service at low prices where profitability is maintained by the fact that we built up higher volumes in the early years.

3.4 Assured client base. We have an assured client base for two reasons. First, we are establishing the Specialised Depository simultaneously with the establishment of a fund management company. The fund management company will be managed by Elizabeth Hebert who has managed the best performing fund publically traded Russia fund for the last two years. Her commitment to use the Specialised Depository will be an important signal to other potential clients. When Elizabeth chose to use the DCC as her custodian in Russia (at that time managed by Julia Zagachin), other market participants followed. We expect that the similar pattern will occur with the Specialised Depository. Second, the Federal Commission will direct potential fund managers to use the Specialised Depository that we are establishing. This is natural since the Federal Commission has an interest in ensuring that its flagship project sets the standard for the market place, and it has an interest in ensuring that fund managers that are licensed use the Specialised Depository that best meets regulatory standards.

3.5 Presence of strategic partner. Forum Financial is the strategic partner. The company is a Portland, Maine based fund administrator/distributor for commercial banks managing funds in the US but restricted by banking regulations from distributing funds directly to the public. Forum currently provides fund administration, transfer agency and valuation services to clients with \$14 billion under management. They also have a start-up operation in Poland. Forum won a tender conducted by the World Bank and the Russian Commission to establish the procedures and design the systems to be used by the model depository. Forum will contribute technical know-how of operations and systems. They will also contribute senior management expertise and systems specialists to shadow the local management team. The presence of a strategic partner should ensure that we are protected from making mistakes in the selection of systems and the development of procedures.

3.6 Subsidy from World Bank Funds. The Federal Commission has awarded Forum Financial \$2.5 million to develop systems and procedures for a model Specialised Depository. The Federal Commission has indicated that the Specialized Depository that we propose to create will be the Russian beneficiary of this work. This money will be used to pay consultancy fees, rent, translation of software, systems development, write procedures, and advise the Commission on regulatory issues. We also expect that the proposed Specialized Depository will be hired by Forum Financial as a sub-contractor, and that, as a result, the company will immediately generate revenue with should fund some of the start up costs. As a result the investment is significantly reduced, as operations of this type tend to require a high up front investment.

4.0 Assumptions About Profitability. The key variables that determine profitability of the Specialized Depository are a) the fixed cost of establishing the Specialized Depository, b) the marginal cost of processing a client account, c) the price that can be charged for processing a client account, and d) the number of client accounts that the Specialized Depository will process. The assumptions that we have made are illustrated in the table entitled "Administration Bureau."

While we believe that we have all the pieces in place to make the Specialized Depository successful, we never established such a business and do have some uncertainty about the precision of the numbers reflected in the business plan. For example, while we have the advantage that many of the fixed costs will be covered by the technical assistance funds, we are uncertain about the fixed costs associated with the establishment of a custodial service. Like many other issues, the issue of whether or not it is necessary to establish a custodial service (or whether for some assets we can or should use services provided by others) is one that will have to be addressed with our strategic partner in the implementation of this project.

Due to such uncertainties, we have used very conservative figures in the business plan. The business plan shows that the Specialized Depository will charge between \$15 and \$12 per year per client account per year (i.e. between 1% and 1.5% on an average investment of \$ 1000). We have been told that a comparative figure in the United States or the United Kingdom is \$30. The low price reflects i) our lack of knowledge about the number of transactions per account per year, and ii) sensible caution about the ability to charge monopoly prices. Even if we are the dominant player in the market, we think it is possible that there would be pressure from regulators to keep prices down. Our foreign ownership and management structure also makes us reluctant to assume that we can "charge through the nose" for our services. Our assumptions about price and cost are illustrated below:

Year of operation	1996	1997	1998	1999	2000
Price charged for processing a single client account	\$12	\$12	\$12	\$12	\$12

Cost of processing a single client account	\$9	\$8.8	\$6.5	\$5.5	\$5.0
Profit per account	\$3	\$3.2	\$5.5	\$6.5	\$7.0

The falling marginal cost relates primarily to the efficiency of operators in processing accounts. We assume that operators reach a western level of efficiency (2000 accounts per operator) only in the year 2000. In our assumptions, in the first 18 months of operation operators process accounts at only 40% the efficiency of their western counterparts.

The key variable that is likely to determine the success of the venture is the number of client accounts. Here again we want to be conservative in our representations to you and Nancy. We assume that we go from processing 31,000 accounts in the beginning of ~~1996~~ to 238,000 accounts in the beginning of the year 2000. Under these assumptions, the Specialized Depository becomes cash flow positive in the third quarter of its operation and gives profit net of Russian tax of about \$600,000 after 3.5 years of operation. Of course, if we were to assume that this Specialized Depository has a large market share and that it were to process millions of accounts, it would be an extremely profitable operation! We are certainly well positioned to achieve such success if Yeltsin wins the election and the mutual fund industry booms in Russia (and we expect both of these things to happen). However, the only scenario that we wish to present to you and Nancy is the conservative scenario that has been presented to you in the original business plan and that is summarized in the table above.

17 Aug
1996

5.0 Our competition. There are two potential sources of competition to this project. They are i) Russian banks and ii) Credit Suisse. We do not think that Russian banks are serious competitors because they are not trusted by the market place. Domestic banks, have a reputation for unbridled opportunism particularly where inside information is available. They also are extremely slow to develop anything new in the way of services. We think that they will watch and wait. Credit Suisse is a more serious threat since it has indicated that it would be interested in this fund administration business and because it is the furthest advanced in custody of any institution in Russia. We think our position is superior to that of Credit Suisse for the following reasons. First, Credit Suisse will not offer clients the registrar (transfer agent) service. Instead they will farm out their customers' register of unitholders to a Russian holder of corporate registers. The company that they have chosen has a dubious reputation in the market place and very Russian concept of client service and confidentiality.

Second, Credit Suisse has explicitly stated that they will not offer the service to clients until they have launched their own fund in order to create/maintain a barrier to entry (remember without a depository a fund can't be licensed). The Federal Commission will resist any attempt by a fund manager to block entry of competing funds in this way (Pioneer in Poland is a perfect example of what the Federal Commission intends not to happen in Russia). Finally, Credit Suisse will not have access to the technical assistance nor to the inside track afforded by the technical assistance to the Federal Commission.

6.0 Connection with the Fund Management Company. You have received a business plan from Elizabeth Hebert for investment in a fund management company. The Specialised Depository and the Fund Management Company are being offered to you as a package. We are not interested in your investment in the Specialised Depository unless this is helpful to raise the funds needed to start the Fund Management Company. This is for several reasons. First, the success of the Specialised Depository will be increased if we have a lead respected client to start things off. A fund managed by Elizabeth Hebert would have this effect as discussed above. Second, the Federal Commission will not license the Specialised Depository except as a package with its first client. For this reason we think that it is important to have control over the first client to ensure that there are no problems or friction in the set up stage. Third, we frankly want to start both of these things at the same time and are tying our futures to this strategy. We would like our backers to do the same with their investment.

7.0 I hope that this is a helpful summary of the Specialized Depository project. This work is on a short fuse. If you are interested in participating in the initial investment, it is important to block out some time to focus on this project. The Specialized Depository already has financing in place. If worse comes to worse it can be financed by the strategic partner. He has already indicated his willingness to do so (under this scenario we would still get 51% of it). If you are willing to participate in the financing of the Fund Management Company (even on a modest scale), we are ready to offer you an opportunity to invest in the Specialized Depository.

8.0 I look forward to talking with you about the proposal.

Annex 1: Functions of the Specialized Depository

Under the current regulations the Specialized Depository plays both a traditional custodial role and a compliance function.

Custody

As the custodian of the mutual fund the specialized depository's functions include:

- holding of assets and accompanying ownership records
- cash control accounting, where separate payment and disbursement accounts are maintained by the specialized depository on behalf of the fund and reconciled on a regular basis with fund accounting
- recording and accounting for capital and income received by the fund through investment of fund assets
- processing corporate actions notifications from investee issuers and acting on the instructions of the fund manager with regard to such actions
- documenting authorisations on fund transactions
- receipt of payments from subscriptions and payment for unit redemptions upon appropriate instructions
- payment for fund expenses at the direction of the fund manager
- settling all securities transactions with the market

Specialised Registrar and Unitholder administration

The specialised registrar function requires the specialised depository to control various aspects of the relationship between the unit holder and the fund manager including:

- maintaining the register of unitholders,
- processing unit purchases and redemptions, order verification and data entry, processing, verification and reconciliation of transactions of unit sales and redemptions as reported,
- documenting all changes to the register unrelated to creation or cancellation of units (i.e. change of address),
- responding to customer service inquiries,
- mailing informational materials upon instruction of the fund manager.

Fund Accounting and Valuation

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The Specialized Depository would also hope to offer the following (in fact this requires certain modification to existing regs, but we expect this to be achievable):

- securities valuation, which must be conducted daily using price quotes obtained from reputable sources (e.g., The Russian Trading System),
- processing of corporate actions, including stock splits and dividend payments, which can effect the total value of the funds assets,
- accounting and accruing of Fund expenses and income in compliance with the applicable regulations,
- calculation of the net asset value (NAV) of the fund based on daily reports received.

In addition to the traditional role of a fund administrator the current regulations require that the the specialised depository assumes a regulatory function on behalf of the Commission and is responsible for reporting all improprieties of the fund manager to the Commission.

① Real Estate License

② 5% of ~~assets~~ assets based fee.

③ 5% of ~~assets~~ Depository
Revenues.

Want Real Estate

① Nancy

② Jonathon

③ Real Estate License

100 for 5%.

Revs negotiate first or
internal mutual fund

transfer license to keep
full interest

Am diluted share.

CASH CUSTODY AGREEMENT

CASH CUSTODY AGREEMENT dated July 5th, 1996 between Forum Financial Group Russia, Limited Liability Company, a Delaware limited liability company, ("Party A") and Citibank T/O., a Russian commercial bank with its legal address at ul. Gashoka 6-10, 125047 Moscow, Russian Federation (the "Agent").

Preliminary Statement

WHEREAS Party A is a founding shareholder of The First Russian Specialized Depository, a Russian limited liability company organized for registration in the Russian Federation ("Party B"); and

WHEREAS pursuant to the Charter of Party B, Party A is obligated to contribute USD 400,000 as part of its obligation to the charter capital of Party B; and

WHEREAS Party B has applied for a Central Bank of Russia license in order to receive contributions of charter capital in hard currency pursuant to the laws of the Russian Federation; and

WHEREAS Party A desires for Agent to hold USD 400,000 as charter contribution until Party B receives the requisite Central Bank license;

NOW, THEREFORE, the parties hereto agree as follows:

Section 1. Establishment of Account. Party A will deliver to the Agent at Citibank T/O Moscow A/C 36067478 at Citibank New York Four Hundred Thousand US Dollars (\$400,000) as the "Property". The Property shall be held, administered and disposed of by the Agent in accordance with the terms and conditions hereinafter set forth.

Section 2. Interest on Account Fund; Distribution of Interest. (a) The Agent shall act as custodian of the Property and Property shall earn interest at 0% p.a.

(b) Any interest accrued on the Property shall become part of the Property.

Section 3. Release of the Property. (a) The Agent shall release the Property or any portion thereof to

(1) Party B upon presentation of the Central Bank license issued in the name of Party B to receive charter capital in hard currency and deliver to

• the USD account opened in the name of Party B on the Books of the Agent; or

(2) Party A upon presentation of a Central Bank letter rejecting the application for a license to receive charter capital in hard currency to Party's A bank account opened at:

• Atlantic Bank N.A.
100 Foden Road
South Portland
Maine 04106

at 466-02-4500-12

to effect payment to Party B by conversion of funds and remittance through T account opened in a name of Party A.

NR

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ID: 7 581 251 6582

PAGE 2

(iii) the terms of an order, judgment or decree ordering the release of the Property or any portion thereof, accompanied by a legal opinion of counsel of the party requesting such release satisfactory to the Agent to the effect that such order, judgment or decree represents a final adjudication of the rights of the parties by a court of competent jurisdiction, and that the time for appeal from such order, judgment or decree has expired without an appeal having been perfected.

(b) Promptly upon receipt of the original license or letter referred to in Section 3(a)(i) and 3(a)(ii) above, or the order, judgment or decree and opinion of counsel referred to in Section 3(a)(iii) above (and in no event later than two business days following any such receipt), the Agent shall release the Property in accordance therewith.

(c) This Agreement will terminate upon the release of the entire Property pursuant to this Section 3.

Section 4. Language Concerning the Agent. To induce the Agent to act hereunder, it is further agreed by the Undersigned that:

- (a) The Agent shall not be under any duty to give the Property held by it thereunder any greater degree of care than it gives its own similar property and shall not be required to invest any funds held hereunder except as directed in this Cash Custody Agreement.
- (b) This Cash Custody Agreement expressly sets forth all the duties of the Agent with respect to any and all matters hereto. No implied duties or obligations shall be read onto this agreement against the Agent. The Agent shall not be bound by the provisions of any agreement among the other parties hereto except this Cash Custody Agreement.
- (c) The Agent shall not be liable, except for its own gross negligence or willful misconduct that are successfully asserted against the Agent, the other parties hereto shall jointly and severally indemnify and hold harmless the Agent (and a its successor Agent) from and against any and all losses, liabilities, claims, actions, damages and expenses, including reasonable attorney's fees and disbursements arising out of and in connection with this Cash Custody Agreement. Without limiting the foregoing, the Agent shall in no event be liable in connection with its investment or reinvestment of any cash held by it hereunder in good faith, in accordance with the terms hereof, including without limitation any liability for any delays (no resulting from its gross negligence or willful misconduct) in the investment or reinvestment of the Property, or any loss of interest incident to any such delays.
- (d) The Agent shall be entitled to rely upon any order, judgment, certification, demand, notice, instrument or other writing delivered to it hereunder without being required to determine the authenticity or the correctness of any fact stated therein or the property or validity or the service thereof. The Agent may act in reliance upon any instrument or signature believed by it to be genuine and may assume that any person purporting to give receipt or advice or make any statement or execute any document in connection with the provisions hereof has been duly authorized to do so.
- (e) The Agent may act pursuant to the advice of counsel with respect to any matter relating to this Cash Custody Agreement and shall not be liable for any action taken or omitted in accordance with such advice.
- (f) The Agent does not have any interest in the Property deposited hereunder but is serving as escrow holder only and having only possession thereof. Party A shall pay or reimburse the Agent upon request for any transfer taxes or other taxes relating to the Property incurred in connection herewith and shall indemnify and hold harmless the Agent from any amounts that it is obligated to pay in the way of such taxes. Any payments of income from this Account shall be subject to withholding regulations then in force with respect to Russian Federation taxes. The parties hereto will provide the Agent with appropriate tax registration certificates for residents. It is understood that the Agent shall be responsible for income reporting only with respect to interest earned on the Deposits and is not responsible for any other reporting. This agreement and

paragraph (c) shall survive notwithstanding any termination of this Cash Custody Agreement or the resignation of the Agent.

- (g) The Agent makes no representation as to the validity, value, genuineness or the collectability of any security or other document or instrument held by or delivered to it.
- (h) The Agent shall not be called upon to advise any party to the wisdom on selling or retaining or taking or refraining from any action with respect to any securities or other property deposited hereunder.
- (i) The Agent (and any successor Agent) may at any time resign as such by delivering the Property to any successor Agent jointly designated by the other parties hereto in writing, or to any court of competent jurisdiction, whereupon the Agent shall be discharged of and from any and all further obligations arising in connection with this Cash Custody Agreement. The resignation of the Agent will take effect on the earlier of (a) the appointment of a successor (including a court of competent jurisdiction, whereupon the Agent will take effect on the earlier of a) the appointment of a successor jurisdiction) or (b) the day which is 30 days after the date of delivery of its written notice of resignation to the other parties hereto. If at that time the Agent has not received a designation of a successor Agent, the Agent's sole responsibility after that time shall be to safekeep the Property until receipt of a designation of successor Agent or a joint written disposition instruction by the other parties hereto or a Final Order of a Court of competent jurisdiction.
- (j) The Agent shall have no responsibility for the contents of any writing of the arbitrators or any third party contemplated herein as a means to resolve disputes and may rely without any liability upon the contents thereof.
- (k) In the event of any disagreement between the other parties hereto resulting in adverse claims or demands being made in connection with the Property, or in the event that the Agent in good faith is in doubt as to what action it should take hereunder, the Agent shall be entitled to retain the Property until the Agent shall have received (i) final non-appealable order of a Court of competent jurisdiction directing delivery of the Property or (ii) a written agreement executed by the other parties hereto directing delivery of the Property, in which event the Agent shall disburse the Property in accordance with such order or agreement. Any court order shall be accompanied by a legal opinion by counsel for the presenting party satisfactory to the Agent to the effect that said order is final and non-appealable. The Agent shall act on such court order and legal opinions without further question.
- (l) Agent shall be compensated for the services to be rendered by the Agent hereunder through free use of Property while held in custody, however, Party A agrees to reimburse the Agent for all reasonable expenses, disbursements and advances incurred or made by the Agent on performance of its duties hereunder (including reasonable fees, expenses of the Agent or its counsel which are not paid as provided for herein) may be taken from any property held by the Agent hereunder. It is understood that the Agent's fee may be adjusted from time to time to conform to its then current guidelines.
- (m) The parties agree that all disputes arising from and in connection with this Agreement shall be resolved by the Parties by way of negotiations. If the parties fail to reach an agreement within 15 days of receipt of notice from one party to another regarding a dispute or controversy, then all such disputes and controversies arising out of or in connection with this Agreement shall be considered, without recourse to the common courts, by the International Court for Commercial Arbitration at the RF Chamber of Commerce and Industry in accordance with the Rules of Procedure of that Court.
- (n) Any communication, notice, request, inquiry or other information in connection with this Agreement shall be sent to the Parties at the following address:

The Agent:	Custody Account Administration, ul. Gashchik 8-10, 125047, Russian Federation
Party A:	Forum Financial Group Russia, Two Portland Square, Portland, Maine 04101:

21-AUG-86 11:07 FROM: CITIBANK T/O MOSCOW

ID: 7 501 251 5682

PAGE 4

Party B: The First Russian Specialized Depository, 8 26, ul.Chayanova,
Moscow, 125047, Russian Federation

- (o) No printed or other matter in any language (including without limitation prospectuses, notices, reports and promotional material) which mentions the Bank's name or the rights, powers, or duties of the Agent shall be issued by the other parties hereto or on such parties' behalf unless the Bank shall first have given its specific written consent thereto.
- (p) This Cash Custody Agreement shall be binding upon and inure solely to the benefit of the parties hereto and their respective successors and assigns, heirs, administrators and representatives and shall not be enforceable by or inure to the benefit of any third party except as provided in paragraph (l) with respect to a resignation by the Agent. No party may assign any of its rights or obligations under this Cash Custody Agreement without the written consent of the other parties. This Cash Custody Agreement shall be constructed in accordance with and governed by the laws of the Russian Federation (without reference to its rules as to conflicts of law).
- (q) This Cash Custody Agreement may only be modified by a writing signed by all of the parties hereto, and no waiver hereunder shall be effective unless in a writing signed by the party to be charged.
- (r) This Agreement shall be executed in both Russian and English versions and shall be governed by, and construed in accordance with, the laws of the Russian Federation. In case of doubt as to the proper interpretation or construction thereof, the English version shall prevail.



Name: John J. Miller Asst. Mgr.
Title: Manager 11/24/96

Agreed and Accepted:

Date: 8th July 96

CITIBANK T/O
AGENT

Name: Christophen Elias
Title: Vice President

.M/

August 19, 1998
To: Jon Keffer
Fax: 931-9704

Mike's Proposal

1. Control of Forum Consulting and Forum Russia transfers to a company designated by e.g. Julia Zagachin. Name of Forum Russia is changed immediately. The name of Forum consulting will remain only for the nominal purpose of submitting invoices to the Federal Commission for the duration of the contract. A way would be found to ensure the full protection of the Forum name.
2. Jon Keffer and all associated persons and entities would be indemnified in writing for any harm done and would be released from all obligations or promises made to ILBE, the Federal Commission or any other party related to the transaction. At the end of this transaction, Forum should be protected from all liabilities that might have arisen from its relationship with ILBE and the Federal Commission.
3. Forum receives \$400,000 in cash (for investment in First Russian Specialized Depository) plus an amount in cash to be equal to out-of-pocket expenses incurred on this project to date. Federal Commission will also consider compensating immediately for expenses incurred for the salaries of outside consultants —such as Gennadi from Seward & Kissel. Forum will prepare records of these expenses as soon as possible. Other legitimate expenses will be agreed and paid over the duration of the contract.
4. Each party pays their own closing costs.
5. As a consultant or sub-contractor Forum will continue to perform services to be precisely defined. In particular, Forum will process for the first fund to go live on September 2. Forum will continue to process until the First Specialized Depository has moved to new programming for the purposes of processing. Forum will advise on selection of software and procedures to be used going forward. It will probably be difficult to pay in advance for work, but we could work out procedures so that the delay between work done and payment is very short. The idea of advance payment is being discussed with the World Bank.

Dmitry Valerievich Vasiliev
Chairman
Federal Commission on the Capital Market
Gazetny Pereulok 5
Moscow, Russia

August 23, 1996

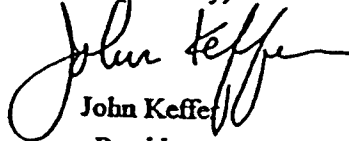
Dear Dmitry Valerievich,

As you are probably aware, there have been some developments recently in connection with the Specialized Depository Project which have caused some concern among all the interested parties. In light of those developments I believe it would be very useful to meet with you, together with your advisors if you so wish, to clarify our respective positions on some key project issues at your earliest convenience.

In anticipation of such a meeting, I have attached a memorandum which outlines our understanding of the current situation and some of the questions which have arisen from our side. We will also present at the meeting a proposed scope of services and work plan, which we believe will address the Commission's most immediate concerns. I understand that there may be some differing points of view with regard to these issues and I would welcome your perspective on them.

I will call your office later today to confirm your availability and to make arrangements. Please feel free to contact me at any time at the Tverskaya Hotel at 258-30-00.

Respectfully,



John Keffer

President

Forum Financial Group

CC: A. Sokin

J. Hay ✓

Specialized Depository Project Issues

1. Commercial Viability

The scheduled September 2, 1996 public demonstration, as we understood it from our original discussions, was to be a non-commercial pilot project conducted for demonstration purposes only. Presently, however, it has developed into a launching ceremony for a fully operational business venture; an undertaking which, in our view, is both commercially premature and damaging to the prospects of long term development of a stable mutual fund industry.

2. Implementation of the World Bank Contract

The high priority and visibility assigned to the demonstration by ILBE/FCCM have deflected attention and scarce resources from implementation of other crucial components of the World Bank Contract. Forum has been asked to concentrate solely on the SD demonstration and to delay implementation of deliverables whose stable, efficient and predictable functioning must underpin any commercially viable SD. The reversal of priorities between these two crucial elements has added to the confusion on all sides regarding the scope of this project, has required a shift in its timetable and has created profound misunderstandings and even disputes among the parties.

3. Resulting Difficulties

As a result of the above, Forum now finds itself faced with the following uncomfortable realities:

- A) Our investment in the SD (\$400,000) has been placed in jeopardy due to the extraordinarily high risk associated with operating a full-fledged commercial specialized depository in an underdeveloped, sometimes contradictory regulatory environment and in the absence of critical legal and institutional infrastructure.
- B) Our out-of-pocket outlays (approximately \$300,000) have gone un-reimbursed due to delays and disputes over disbursement of an advance payment stipulated in the World Bank Contract.
- C) Cooperative spirit and communications among the parties have deteriorated, making negotiation and problem-solving extremely difficult and casting grave doubts on the viability of future working relations.

4. Need for Revision of Scope of Services and Work Plan

Given the qualitative change in priorities, the FCCM's representatives from the ILBE have instructed Forum, and Forum has agreed, to prepare a revised scope of services and work plan. Toward that end, Forum has discussed the issues with representatives of the ILBE and has created a proposed plan which redefines Forum's role and assists the Commission in carrying out its agenda. Key issues include:

- ownership of the SD;
- liability;
- scope of work;
- basic services;
- supplementary services;
- reporting structure; and
- tax liability.

K.

Dmitry Valerievich Vasiliev
Chairman
Federal Commission on the Capital Market
Gazetny Pereulok 5
Moscow, Russia

August 23, 1996

Dear Dmitry Valerievich,

Thank you for your fax which I received earlier today. I understand that the Russian language version of our memorandum may have improperly conveyed the intended meaning of paragraph 2, which described perceived problems in implementing the World Bank Contract. Hence, I would like to take this opportunity to reiterate my strong personal and professional support for your vision for building an international standard capital market in Russia. Specialized depositories can play a significant role in guarding against fraud and the Specialized Depository Project clearly demonstrates your commitment to protect the individual shareholder in an uncertain economic environment. If these sentiments have not been adequately conveyed up to now, please allow me to correct that oversight with this letter.

With regard to some of the other issues raised by my memorandum of August 23, 1996, please consider the following:

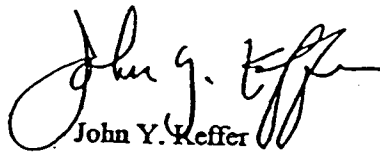
1. Having reviewed the World Bank Contract referred to in your fax, it is my understanding that a work plan is not required beyond what is already set forth within the Description of Services section, a view that has been previously communicated to Jonathan Hay of ILBE.
2. The Forum team has been instructed by your representatives to focus all resources on the September 2 demonstration to the exclusion of all other World Bank Contract deliverables, thereby requiring, at the very least, an adjustment to the timetable.
3. Forum has continued to perform work along the lines instructed by your representatives, i.e., preparing for and facilitating an SD demonstration with a "live" fund on September 2. I am proud to say that we have made great strides in this area, particularly given the tightness of the timetable. Specifically, our efforts have included the following:
 - Forum's chief technical experts are working in Moscow full time installing specialized registrar and fund accounting systems in English and Russian. We would be pleased to provide you and your colleagues with a preliminary demonstration of our installations at any time.

- Forum's senior mutual fund accountant and head of training is also working in Moscow adapting U.S. fund accounting operations to the Russian environment.
- We have purchased computer hardware, and have provided temporary office space since mid-June pending ILBE's selection of a permanent facility.
- Forum's legal and operations experts have produced a substantial body of operational rules and procedures which have been submitted to the ILBE for review.

Given the new set of circumstances described in our previous memorandum, Forum believes that a high-level discussion and agreement regarding the scope of services to be performed by Forum must take place before a meaningful work plan can be prepared.

We have attached a proposed scope of services, which reflects the position we have communicated to ILBE and your representatives. We have offered to discuss this at the highest levels, with a view toward continuing to assist the Federal Commission on the Capital Market in meeting its objectives.

Sincerely,



John Y. Keffer

President

Forum Financial Group

CC: A. Sokin
J. Hay

Proposed Scope of Services

- Facilitate the September 2nd demonstration, to be performed with a "live" fund, provided Forum no longer owns the SD. In case the sale of the SD does not take place prior to September 2, 1996, Forum will facilitate a demonstration but will not enter into commercial contracts required for a fund to be "live" because such contracts will expose Forum to an unacceptably high level of business risk and liability.
- Re-work the World Bank Contract such that Forum will continue to provide certain services to the SD for a specified time after the September 2nd demonstration. The most basic of these services will include oversight of the SD's systems processing (i.e. processing the inputs and producing the necessary outputs), surveying and proposing alternative systems from among those currently available in the marketplace and overseeing implementation of the selected systems, including installation, training and conversion from the systems and software initially installed by Forum. Forum agrees to provide these services for a fixed period of time during which the replacement systems are selected and implemented.
- Payment/performance terms of the contract, as re-worked, will be as follows: it will be strictly a "time and materials/best efforts" contract. Billing and payment will be made in short intervals and termination clauses will enable each party to end the contract with 10 days' notice.
- Re-worked contract will contain changes in the personnel assigned, sub-consultants used and the reporting structure. The reporting structure change will require that the project manager be a third party (Bert Lewis has been proposed) and that the SD management agree to cooperate and not interfere with the work of Forum's consultants. In addition, the ILBE will continue to provide resource support and the project team will continue to have direct access to D. Vasiliev.
- Should Forum be asked to perform certain services beyond overseeing the SD's current systems processing, recommending alternative software and arranging for a smooth transition between the two, Forum is prepared to negotiate the provision of a broader range of services, which may include rules development, procedure writing and other deliverables from the original World Bank Contract.

Proposed Terms Under Which Forum Will Perform Services

- (i) The SD will be purchased from Forum for the price of capital invested (\$400,000) plus cost of formation and cost of sale (appr. \$10,000-15,000) for cash or cash equivalent.
- (ii) Forum will be paid the \$450,000 advance due under the World Bank Contract.
- (iii) Forum will be absolved of any past liabilities (in writing) and agreements will be signed indemnifying and holding John Keffer and his affiliates harmless for everything that has transpired to date. Such agreements will be executed by the FCCM, ILBE and the buyer(s) of the SD.
- (iv) The World Bank Contract will be re-worked, as agreed between the parties, to provide for a change in:
 - deliverables
 - dates
 - third party administration
 - freedom to use sub-contractors as needed and approved by the third party administrator
 - freedom to substitute personnel as needed and approved by the third party administrator
 - termination clauses
 - time and materials/best efforts basis
- (v) FCCM agrees to accept responsibility and pay at the time of billing for any Russian tax liability or withholdings.



ФЕДЕРАЛЬНАЯ КОМИССИЯ
ПО РЫНКУ ЦЕННЫХ БУМАГ
(ФКЦБ РОССИИ)

117939, ГСП-1, Москва В-49, Ленинский проспект, 8
Тел. 236-12-84, факс: 236-12-20

28.08.96. № 1116-149

На № _____ от _____

August 27, 1996

Mr. John Keffer
President
Forum Financial

Dear Mr. Keffer,

I am writing in response to your letter of August 23, 1996. Thank you for making clear your position on a number of matters. Allow me to respond to several of the issues raised in your letter.

The World Bank contract which you signed on July 25, 1996 calls for the creation of a specialized depository. Section 6 of the contract requires that you provide a plan for the implementation of the specialized depository to ILBE and the Federal Commission. OKA

This plan forms the basis of an agreed strategy for implementing the specialized depository. Although there have been many discussions to date no final plan has been provided. Your idea of a demonstration project is not consistent with the contract nor acceptable to the Federal Commission as a result of this project.

The Federal Commission has asked you to focus your resources on the implementation of a specialized depository within the aggressive timeline required by the contract. This is consistent with the letter and spirit of the contract between Forum Financial and Federal Commission. The Federal Commission needs a working specialized depository to launch the Russian mutual fund industry in a fashion that protects the rights of investors.

L

I understand from your letter and our previous conversation that you are prepared to meet the Federal Commission's timeline on the condition that you are not owner of the specialized depository. As a result, I request that you immediately present to the Federal Commission a concrete proposal for altering the ownership structure of the First Russian Specialized Depository. We must stabilize the ownership situation immediately to ensure the viability of the project and move forward with confidence.

Once the ownership has been stabilized, my representatives and I are committed to work with you to structure the resources available under the contract between Forum Financial and the Federal Commission in order to implement the objectives of the contract smoothly and without further interruption. I hope that we share this goal.

Sincerely,



Dimitri Vasiliev

Chairman

M.

+75839561888

FLEMINGS (CIS) LTD

T-433 P-001

28.08.96 14:54

To : John Keffer
Guest in room 419 or in 4th floor Lobby Bar
Tverskaya Hotel

CC : Julia Zagachin

From : Beth Hebert

Date : 28th August 1996

Re : SD

I understand you are interested to no longer hold an interest in the First Russian Specialised Depository ("SD"). I have attempted to identify a source of financing to take you out of the SD and a structure which, to the best of my knowledge, is acceptable to the relevant parties.

The Transaction.

The transaction is the sale of Forum Financial Group Russia (FFR), a Delaware limited liability company which owns the First Russian Specialised Depository, a company registered in Russia, to another Delaware limited liability company, Oasis Financial Services.

The sale will not affect the ownership of the SD - only ownership of FFR, although I assume parties to the transaction would intend to change the name of the Delaware Company.

The Seller.

FFR is owned by Forum Financial and John Keffer. It is understood that FFR is a special purpose company which was formed for the sole purpose of holding the shares of the First Russian Specialised Depository and that it has no undisclosed liabilities. The only liability which the new owner has agreed in principle to assume is the legal bill for set up and closing costs of the SD (estimated to be approximately \$11,000). These costs should be clearly outlined and agreed prior to execution of the transaction.

The Buyer.

Initially, the new owner of FFR would be Oasis Financial Services, a company owned 99% by Julia Zagachin and 1% by Sage Capital, a Delaware Company formed by Julia Zagachin. Oasis has obtained a loan of \$400,000 and the funding of the loan is in process (I am told that the proceeds can be moved today if the banking details can be worked out).

+78239561800

FLEMINGS (CIS) LTD

T-435 P-002

28.08.96 14:55

The Structure.

I propose that you consider one of the two structures:

1) a new cash custody account under the control of Oasis is opened for the purpose of making the contribution to the charter capital of the SD. Forum withdraws the \$400,000 from the original cash custody account. Forum sells the company to Oasis. I assume that this structure is simpler as the company can then be transferred for 2 kopek and legal costs will be minimised. Citibank has not come back to me yet with feedback on this structure.

2) an escrow account is open by Citibank and an escrow agreement is signed between Oasis, Citibank and FF. The \$400,000 is deposited in the escrow account and is transferred to FF as soon as shares are transferred to Oasis. This structure is likely to be more costly, time consuming and complicated.

Next Steps.

- Oasis to meet with Citibank to work out details of cash custody account, etc.; JZagachin
- I understand we need to complete the registration of the SD in order to facilitate the transaction from Citibank's point of view; Sergey Shishkin and Gennady Khareyn.
- draft a purchase-sale agreement for the shell company FFR:Gennady
- sign purchase-sale agreement and change of ownership
- John Keffer to withdraw funds from the Citibank account.



N.



United States Agency for International Development

Local USAID/Moscow
Address: 19/23 Novinsky Bulvar
Moscow 121099, Russia

U.S. Mailing
Address:

USAID/Moscow
PSC 77
APO, AE 09721

22

May 20, 1997

Mr. Jeffrey Sachs
Director
Harvard Institute for International Development
One Elliot Street
Cambridge, MA 02138

Sent to fax no. 617-495-0527

Subject: Cooperative Agreement Nos. CCN-0005-A-00-3023-10 and EPE-A-00-95-00122-02

Dear Mr. Sachs:

The program description of Agreement No. CCN-005-A-00-3023-10 includes a component to develop "the legal and regulatory framework that sets out the procedures for ... institutions to ensure competition, transparency and fair play," including "the development of a Securities and Exchange Commission and its early regulatory and enforcement activities ... and private sector self-regulatory initiatives." HIID used funds provided under this agreement for several activities; including to establish the Institute for a Law Based Economy (ILBE) and to finance equipment as well as American and Russian staff for ILBE. USAID also has provided assistance directly to ILBE.

The program description for Agreement EPE-A-00-95-00122-02 is entitled "Impartial Oversight and Strategic Guidance for Privatization and Market Reform Programs in Russia in support of the Russian Privatization Center and states: "The recipient [HIID] shall provide unbiased input to, and overall day-to-day management, review and evaluation of, the privatization and market reform programs. The recipient must develop the complete confidence and trust of the host government and also the array of donor agencies and implementing organizations." A Conflict of Interest Statement included as part of HIID's technical proposal for this program states HIID's commitment "to maintaining an objective and unbiased role in advising the officials of foreign governments."

USAID funded these programs through HIID in order to engage the expertise and stature of HIID and the resources available to it in a crucial undertaking to which the United States attaches major importance. The subject agreements require HIID to use USAID-funded assets solely for authorized purposes. These agreements also state with respect to non-Russian employees, "Other than work to be performed under this grant for which an employee is assigned by the grantee, no employee shall engage directly or indirectly, either in the individual's own name or in the name or through the agency of another person, in any business, profession, or occupation in the foreign countries to which the individual is assigned, nor shall the individual make loans or investments to or in any business, profession or occupation in the foreign countries to which the individual is assigned." Article XVI, entitled "Conflict of Interest and Illegal Transactions", of HIID's own ADMINISTRATIVE MANUAL: OVERSEAS ACTIVITIES, dated 1 July 1992, contains even more restrictive limitations on the activity of HIID employees and members of their families within the project country.

As you know, USAID's Office of the Inspector General (OIG) has been investigating the activities of certain key HIID personnel associated with the subject USAID-financed cooperative agreements. While the investigation is not complete and may continue for some time, the OIG was sufficiently concerned about the activities of two HIID officials that the investigators have shared with USAID/Russia certain serious findings about activities of those officials in Russia.

The investigation has revealed that HIID's General Director in Moscow has used resources financed by USAID to support the private investment activities of the spouse of the HIID Project Director in Cambridge, with the knowledge and participation of the Project Director. More specifically, the investigators have documentary evidence or statements of HIID staff in Moscow to confirm that the General Director in Moscow directed HIID and ILBE staff to take certain actions on behalf of the Project Director's spouse concerning various investments the spouse has made in Russia. Those actions included buying and selling Russian bonds, tracking deposits and withdrawals from the investments' Russian bank accounts, consulting about tax aspects of the investments and possible additional investment opportunities. The resources financed by USAID used for these purposes include office equipment and valuable staff time of Russian and American personnel of HIID and ILBE. The investigators also have evidence, recently confirmed by the General Director in Moscow, that his personal funds were invested in Russian Government bonds during his assignment in Moscow, and benefited from those investments.


Activities for individual gain by personnel placed in a position of trust in Russia and financed under these USAID cooperative agreements is not in the national interest of the United States. Through these cooperative agreements, the General Director in Moscow and the Project Director have gained influence over nascent Russian capital markets. They have abused the trust of the United States Government by using personal relationships, on occasion, for private gain. USAID has been trying to explain to key Russian Government counterparts the value of open and transparent processes, and the importance of avoiding conflicts of interest, as ways to increase investor confidence in the Russian capital markets. These were some of the key

objectives of the subject cooperative agreements. The private activity of the General Director in Moscow and the Project Director, supported by staff and equipment paid for with U. S. Government funds, conveys exactly the wrong message to the Russians.

In view of the foregoing and pursuant to 22 CFR 226.61(a)(3), which gives USAID the authority to suspend awards when further assistance would not be in the national interest, I am hereby notifying HIID that USAID is suspending further payments under the subject cooperative agreements, with immediate effect, until further notice. At a minimum, I would expect staff changes in accordance with HIID's policies and greater day-to-day oversight responsibility for USAID/Russia, to reduce the risk that such private activities might occur in the future. The damage to the United States in Russia caused by HIID's General Director in Moscow and Project Director is serious, and we cannot allow this to happen again. I urge you to act swiftly to minimize damage to the program. You can reach me in Moscow by fax at 7-095-956-7091 or by phone at 7-095-956-4121.

As you know, the OIG investigation is ongoing, and you will be notified if there are additional matters that require resolution under the terms of USAID's agreements with HIID.

Sincerely,



Orion Yeandel
Agreement Officer

cc: Douglas Arnold, Controller, USAID/Russia
Randall Draper, HIID

0.

HARVARD INSTITUTE FOR INTERNATIONAL DEVELOPMENT
One Eliot Street, Cambridge, Massachusetts 02138
Jeffrey D. Sachs, Director

Tel: (617) 495-4112
FAX: (617) 495-8885
jsachs@huid.harvard.edu

May 23, 1997

Mr. Orion Yeandel
Agreement Officer
USAID/Moscow

Subject: Cooperative Agreements Nos. CCN-0005-A-00-3023-10 and EPE-0005-A-00-5122-00

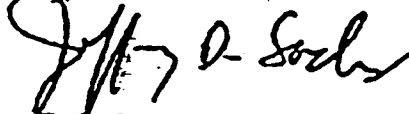
Dear Mr. Yeandel:

In response to your letter of May 20, I would like to inform you that, effective immediately, Andrei Shleifer and Jonathan Hay have been removed from their positions as Principal Investigator and General Director, respectively, of the projects funded by the cooperative agreements referenced above. These personnel changes do not represent an endorsement of the allegations noted in your letter. Rather, they reflect HIID's zero tolerance for conflicts of interest, whether actual or perceived, as well as our rigorous enforcement of the Institute's well-established internal policy in these areas. HIID will continue to cooperate fully with USAID in the ongoing investigation.

With respect to the projects in question, I propose that HIID Institute Fellow Glenn Jenkins serve as Acting Principal Investigator and that former HIID Director Lester Gordon assume, also on an acting basis, oversight of the field operations of these two projects. Both are senior, long-term HIID professionals with many years of field experience in the areas most relevant to these projects. I will follow up next week by sending materials outlining their qualifications and experience.

I am eager to discuss the status of these projects with you and your colleagues. We are grateful for your support and look forward to the resumption of a fruitful collaboration.

Sincerely,



Jeffrey D. Sachs

cc: Ms. Janet Ballantyne
cc: Mr. Donald Pressley

HARVARD UNIVERSITY

TOTAL P.22

P.



Local USAID/Moscow
Address: 19/23 Novinsky Bulvar
Moscow 121099, Russia

U.S. Mailing USAID/Moscow
Address: PSC 77
APO, AL 09721

June 6, 1997

Mr. Jeffrey Sachs
Director
Harvard Institute for International Development
One Elliot Street
Cambridge, MA 02138

Sent to fax no. 617-495-0527

Subject: Cooperative Agreement Nos. CCN-0005-A-00-3023-10 and EPI-A-00-95-00122-02

Dear Mr. Sachs

Thank you for your letter of May 23, 1997. USAID appreciates the effort and commitment represented by your decision. USAID subsequently has consulted with the Government of the Russian Federation and with you concerning continuation of assistance under the subject agreements. During these discussions, USAID and Harvard Institute for International Development (HIID) have agreed to terminate these agreements pursuant to 22 CFR 226.61(a)(2). Accordingly, USAID will terminate the assistance under the subject cooperative agreements according to the following schedule:

1. CCN-0005-A-00-3023-10 This cooperative agreement will terminate as of August 1, 1997. In the interim, HIID is to take immediate and reasonable steps to close out all ongoing activities. Please submit a comprehensive close out plan for this cooperative agreement no later than July 1, 1997. The close out plan must include, among other items, schedules for disposition of property financed under the cooperative agreement and releasing employees. No further costs should be incurred under this agreement after July 31, 1997.

2. EPI-A-00-95-00122-02 This cooperative agreement is partially terminated as of August 1, 1997. All activities except tax reform are included in this termination. In the interim, for all activities except tax reform, HIID is to take immediate and reasonable

Mr. Jeffrey Sachs
June 6, 1997

Page 2

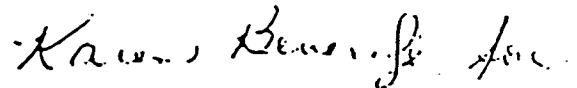
steps to close out all ongoing activities. Please submit a comprehensive close out plan for all activities except tax reform activities under this cooperative agreement no later than July 1, 1997. The close out plan must include, among other items, schedules for disposition of property financed under the cooperative agreement and releasing employees. Except for tax reform activities, no further costs should be incurred under this agreement after July 31, 1997.

Tax reform activities will be terminated as of January 1, 1998, to allow USAID time to conduct full and open competition for an organization to manage the overall tax reform program. The suspension is lifted for tax reform activities with immediate effect. A comprehensive close out plan for the tax reform activities will be requested at a later date.

HIID's cooperative agreements in the environment sector are not affected by these terminations.

Please feel free to contact the undersigned for further clarification of these instructions. Thank you for your continued cooperation.

Sincerely,



Orion Yeandel
Agreement Officer