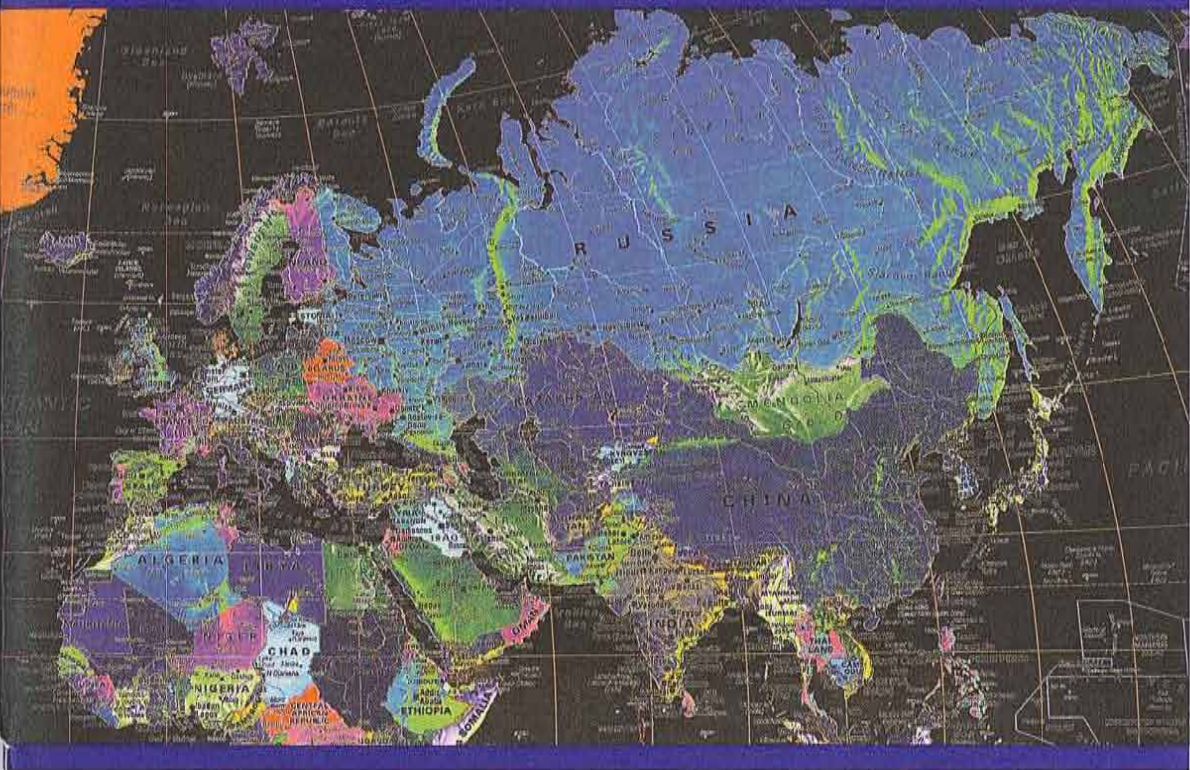


# TOWARD THE COMMON GOOD: Building a New U.S.-Russian Relationship

EWI BIPARTISAN TASK FORCE  
HOW SHOULD THE UNITED STATES DEAL WITH  
PUTIN'S RUSSIA?



Chairmen: David L. Boren, John C. Danforth & Alan K. Simpson

EASTWEST INSTITUTE



## ABOUT THE TASK FORCE

Opinion in the West regarding the current and future direction of the Russian Federation under President Vladimir Putin covers a wide spectrum, and the US policy debate includes choices ranging from active engagement to benign neglect. To meet this challenge, the EastWest Institute decided to launch a Bipartisan Task Force to examine the Putin administration's record over the last 18 months. The presidential administration in Russia agreed to cooperate with this study and to provide unprecedented access to top Russian officials, including President Putin himself.

The study began in April 2001 and has included a number of Task Force visits to the Russian Federation, as well as two meetings of the Task Force in Washington, DC. Through systematic analysis of recent events in Russia and President Putin's reforms, the Task Force hopes to inform the current policy debate and explore the opportunities created by changes in Russia to build a fundamentally new and better relationship for our two countries and the world.

The Task Force is co-chaired by former Senators David L. Boren (D-OK), John C. Danforth (R-MO), and Alan K. Simpson (R-WY), who have a combined 52 years of leadership in the United States Senate. The Project Co-Directors are John Mroz, EastWest Institute; John Tedstrom, RAND; and Sherman Garnett, Michigan State University. The Task Force members are listed in Appendix A. Signatories of the report may be found in the attached insert.

## ABOUT THE CHAIRMEN

**David L. Boren** (D-Oklahoma) is the first person to serve as Governor of Oklahoma, US Senator from Oklahoma, and President of the University of Oklahoma. During his Senate career, he was the longest-serving chairman of the US Senate Select Committee on Intelligence, from 1987 to 1993. He authored the National Security Education Act, which established international study fellowships for undergraduate and graduate students for language and cultural studies in areas where US expertise is insufficient. In November 1994, two years before the end of his senate term, he resigned to become president of the University of Oklahoma. Boren has degrees from Yale University, the University of Oklahoma College of Law, and Oxford University, where he was a Rhodes Scholar. He and his wife Molly have two children, Dan and Carrie. Senator Boren currently resides in Norman, Oklahoma.

**John C. Danforth** (R-Missouri) is a partner in Bryan Cave LLP law firm. He served as a Republican Senator from Missouri in the US Senate from 1976 to 1995. He was Chairman of the US Senate Committee on Commerce, Science, and Transportation. He served for two terms as Attorney General of Missouri and as a member of the US Commission on Presidential Debates. Senator Danforth was born and raised in St. Louis and has degrees from Princeton University, Yale Law School, and Yale Divinity School. He was ordained in 1964 as a priest in the Episcopal Church. He is chairman of the Danforth Foundation. He and his wife Sally have five children: Eleanor, Mary, Dorothy, Johanna, and Thomas. Senator Danforth currently resides in St. Louis, Missouri.

**Alan K. Simpson** (R-Wyoming) is a partner in the firm of Burg, Simpson, Eldridge, Hersh, and Jardine of Denver, Colorado and Cody, Wyoming. He served for 18 years in the US Senate, from 1979 to 1997. For ten of those years, he was the Assistant Republican Leader to Senator Bob Dole. He is currently a visiting professor at the University of Wyoming. He was a visiting lecturer and former Director of the Institute of Politics at Harvard University and serves as a member of the US Commission on Presidential Debates. He was a member of the Wyoming State Legislature for 13 years. Senator Simpson holds a BS and a JD degree from the University of Wyoming, and holds seven honorary Doctorate degrees. He and his wife Ann have three children: Bill, Colin, and Susan. Senator Simpson currently resides in Cody, Wyoming.

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TOWARD THE COMMON GOOD

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## PREFACE

This report is not about improving our existing policy agenda toward Russia. Instead, the report addresses the dramatic possibility that exists at this particular time in history for the United States and Russia to change their relationship in a way that enhances global peace, stability, freedom and prosperity.

If the United States and Russia can move to a new kind of relationship, beyond deterrence and toward strong and positive collaboration in order to reduce security threats of mutual concern, the two countries have the potential to change far more than the bilateral relationship. A new relationship might begin between the two presidents, focusing on areas of immediate bilateral concern and leading to broader multilateral cooperation among the world's leading nations. Such cooperation could be the impetus behind the creation of new multilateral mechanisms that more effectively address the problems posed by terrorism, infectious diseases, drugs, the instability of failed states and the proliferation of nuclear materials and weapons of mass destruction.

Obviously, this kind of new relationship depends on a democratic Russia, and one that continues to integrate with the global economy. Such a Russia would be an important part of addressing almost any significant regional or global security issue. Almost no one disagrees with this fact, though U.S. opinion is divided over whether Russia has progressed enough over the last ten years to be on track for both democracy and global integration.

Our view is that we are at a dramatic turning point, one that could support the transformation of the U.S.-Russian relationship with wider implications for the world at large. This turning point is supported by trends within Russia, by the energy and visions of Presidents Vladimir Putin and George W. Bush, and by the basic fact that the United States, from its position of prosperity and strength, can afford to make a bet on a much broader and more positive change.

Although it is too early to reach a final judgment on the thrust of President Putin's leadership, there have surely been enough positive initiatives at this point to create the basis for exploring further ways to build a new relationship with Russia. These positive steps are not generally understood today in the United States. It is important to state explicitly here that what occurs inside Russia matters to us. The United States, and the West in general, will not wish to pursue the type of relationship that

we envision with any country that does not adhere to basic and internationally accepted principles of democracy, human rights, market economics and transparency. Although every country will adapt these principles to its own specific context, the community of leading nations embraces a common set of fundamental norms and expects all its members to do so.

If we do not seize this moment, we may well miss a historic opportunity to change the nature of U.S.-Russian relations. Although this approach entails some risks, the failure to take these risks will certainly lead to a world that is less safe and secure. Acting on positive assumptions should not, however, mean any reduced diligence in observing the actions of President Putin and his administration. It should fairly be expected that the Russian side would take the same approach of “trust but verify”.

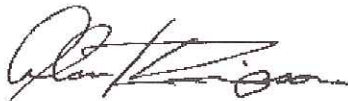
Shifting the basis of U.S.-Russian relations will not be easy, and it will not occur overnight. Both sides need to avoid the misplaced euphoria of the early 1990s and approach the relationship with candid, hard-headed realism. Both countries—and their partners in the international community—must approach the relationship with a shared vision of a fundamentally better future, a wisdom based on sound principles and lessons learned and a renewed mutual trust and respect shorn of all vestiges of Cold War mentalities.



David L. Boren



John C. Danforth



Alan K. Simpson

CHAPTER ONE

# TOWARD A NEW RELATIONSHIP

The Bush administration faces a Russia that is at a critical and perhaps defining juncture in its history. The country's leadership has launched a reform agenda that, if carried through, will take Russia further down the path toward becoming a modern, market-oriented democracy. The resistance to change in Russia is significant, and the ultimate success of these reforms is far from assured. Yet the reform initiative gives the United States and Russia an opportunity to set their relationship on a new foundation that will enhance international peace, stability, freedom and prosperity in an increasingly interdependent world.

Attaining this goal will not be easy and will not occur overnight. Both countries must decide whether they care to make the investment of presidential vision, leadership, commitment and other resources necessary to reach this goal. Even with this investment, success is not guaranteed; both countries will need to make tough, deep changes. Russia must press forward on a path toward becoming a "normal" market democracy that fits into the international system better than it does today. It is a simple truth that neither the United States nor other leading members of the international community will pursue the type of new relationship that we envision with Russia—or with any other country for that matter—unless it meets basic norms of behavior, both at home and abroad.

For its part, the United States must accept that Russia is a sovereign country with its own legitimate interests and must shed its fixation for judging and micromanaging every twist and turn in Russia's reforms. The United States must also work better to understand the impact on Russia of the events of the last decade and the enormous new challenges that they have left for the current Russian leadership and its civil society. It is necessary to understand these challenges, such as the fight against the widespread corruption that hinders small- and medium-sized firms from entering market competition, in order to make fair and objective judgments about the policies and actions of President Putin and his administration.

## U.S. INTEREST IN RUSSIA

Although Russia should not command the defining place in U.S. foreign policy that the Soviet Union once did, its transformation into a successful, market-oriented democracy that is effectively integrated into the global community remains very important to the broader, strategic interests of the United States. Achieving this goal therefore warrants systematic, sustained engagement at the highest levels of government in the two countries. Although Russia is still economically weak, its large landmass, multiple borders, human and natural resources and nuclear arsenal all combine to make it an important player in the twenty-first century.

If Moscow makes the necessary transition, it will not only acquire greater legitimacy in the eyes of its citizens, but it can become an important exporter of prosperity, stability and security across Eurasia. President Putin and his most senior aides have repeatedly told this Task Force that Russia has turned its back on a policy of confrontation with the West and has decided once and for all to become a democratic, open-market state. If such a Russia emerged, it would share many more international interests with the United States and the democratic West than it does today. Cooperation on issues ranging from regional conflicts, nuclear security and non-proliferation to international trade and the environment will be more likely to occur; when such cooperation occurs, results will be more predictable and more successful. A strong, integrated Russia operating on the basis of mutual interests could also exert a positive influence on its neighbors both in Europe and in the broader Eurasian region. The prospects for regional as well as global stability and peace would be enhanced.

If Russia falls short of these goals, it will fall into a trap of playing catch-up economics and will be a net importer of international economic, political and security resources. It will define its interests in opposition to ours and pursue zero-sum strategies. It will find its economy dependent on the vagaries of international energy markets and debt traders, and will be driven by the need for cash to sell weapons and technologies to states that the international community views with suspicion. Unable to invest in its physical or human capital, Russia will fall even further behind the more dynamic and prosperous European and Asian nations and find it increasingly difficult to live in peace with others or with itself. Such an outcome is in no one's interest. Certainly not Russia's. Certainly not America's.

How the United States approaches Russia will have an important impact on Russia's internal development. In Warsaw in June, President Bush said, "we have a stake in Russia's success, and we look for the day when Russia is fully reformed." He went on to add that the United States and Europe "can and should build partnerships



with Russia and with all the countries that have emerged from the wreckage of the former Soviet Union.” Yet the past decade has been filled with strong words and expressions of good intentions. For Bush and Putin’s positive June 16th meeting in Ljubliana, Slovenia<sup>1</sup>, to be the start of a new momentum, deeds must now follow from both sides.

How to build on the presidents’ forward-looking sentiments is the subject of this report. Although subsequent chapters will discuss specific policy proposals in detail, several important themes are worth highlighting here.

Although Russia no longer dominates U.S. national security concerns, its successful integration into the global community is squarely in our long-term regional and global interests.

- A lack of understanding and trust currently hampers relations between the two countries. The United States should listen more closely to Russian concerns and judge the progress of reforms against the standards imposed on other countries in the world.
- Russia must also understand the need to show the world community that it is sensitive to ensuring that its transition preserves and broadens fundamental freedoms of speech and press, while also creating clear and effective restraints on arbitrary state power.

We must develop the patience to endure Russia’s transition, which will be protracted and difficult, by recognizing the positive potential for developing a new international security paradigm with a new Russia. During the first ten years of Russia’s emergence from the ashes of the Soviet Union, the major vestiges of the Soviet communist system were eliminated and the basic—and still fragile—pillars of a market democracy were set in place.

- What happens within Russia matters to the United States. Russia’s foreign policy and international orientation will be shaped by the strength and scope of its democratic and market institutions.
- President Putin has initiated a set of reforms that, if successfully implemented, will take Russia further on its path toward being a normal, market-oriented democracy.
- The United States should refrain from hasty judgments about apparent short-term successes or failures in Russia’s reforms. Real progress will be the result of cumulative change over time.

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<sup>1</sup> The June 16 summit in Ljubliana, Slovenia, was the first meeting between Presidents Bush and Putin.

We should encourage Russia to assume important responsibilities within its region. Its regional diplomacy should emulate western and global institutional frameworks, standards and engagement.

- Joint work on the ground in Bosnia, Kosovo and perhaps eventually Macedonia and collaboration on Nagorno-Karabakh are good examples of how the two sides can work together to pursue common interests.
- The United States and the West should continue and enlarge its support for the development of Russia's still emerging civil society.

U.S. policy toward Russia should be couched in our broader European policy framework. We should support close and active political and economic relationships between Moscow and European capitals as well as European and Euro-Atlantic institutions.

- U.S. policy to support the independence of Russia's neighbors, particularly countries such as Ukraine and Georgia, can help promote a secure, stable and increasingly "European" region that will be advantageous to Russia and the entire region. Developing better relations between these former Soviet states and the West and Russia is in everyone's best interests.

The United States and Russia should jointly lead the rest of the world in an effort to move to a post-deterrence security structure.

- Presidents Bush and Putin should explore ways of accelerating our dialogue on strategic nuclear issues so as to replace the fatalistic logic of mutually assured destruction as quickly and responsibly as possible.
- Progress on strategic nuclear issues should open the way for a fuller dialogue on a host of other important security problems ranging from arms proliferation to NATO enlargement to drug trafficking and terrorism.

Recently launched economic reforms and other reforms working their way through parliament hold real promise for the expansion of Russia's international economic relationships to everyone's advantage.

- Russia's work toward quick accession to the World Trade Organization (WTO) has motivated the most promising set of reforms in this regard. The United States should engage Russia in ways that support these reforms and accelerate the accession process. Engagement by the United States should come from both the public and private sectors.

CHAPTER TWO

BEYOND DETERRENCE:  
CONSTRUCTING A NEW  
STRATEGIC ARCHITECTURE

As the cornerstone of their new relationship, the United States and Russia should aim at nothing less than creating a post-deterrence relationship that abandons mutually assured destruction as its defining reality. Progress in this area is key to creating the type of trust and understanding that will allow the new U.S.-Russian relationship to develop. At its full potential, this new relationship could serve as a catalyst for new multilateral initiatives and institutions to address global security problems from nuclear proliferation to drugs to failed states. It could also draw in other participants such as Japan, China, India and the European states in an expanded and creative dialogue. Indeed, as Russia's internal reforms allow for broader and deeper integration, Russia's interests will increasingly coincide with those of the West, creating additional opportunities for collaboration on issues of mutual concern.

The U.S.-Russian security relationship encompasses much more than just the issues of missile defense and the 1972 Anti-Ballistic Missile (ABM) Treaty. As Russia works to overcome a disadvantageous international environment, it has successfully begun to initiate new relationships with the West; these relationships can now be strengthened if Russia's efforts to reach out to other countries are accompanied by real reforms at home.

Russia has forged new but sometimes rocky ties with the United States and Europe, as well as what appears to be a new strategic partnership with an old and possibly future rival, China. Russian authorities have claimed they do not want this partnership to compete with the West, but both countries have made clear their unease with the United States being the only global superpower and have said that counterbalance is necessary.

Meanwhile, the leaders and citizens of neighboring countries formerly part of the Soviet Union still feel a real sense of unease about Russian intentions vis-à-vis their states and are sensitive to any economic, political or military pressure exerted from Moscow. At the same time, however, it is Russian military support that is countering

Taliban aggressions against Tajikistan and Uzbekistan. And the worry about fundamentalist Islamic forces does not stop with the Taliban—fundamentalist Islamic gains throughout Eurasia are a major concern for both the United States and Russia. Finally, the addition of Pakistan and India to the nuclear club adds to the concerns for Moscow and Washington.

Russia must now back up with policy and action the Putin team's repeated rhetorical assurances to the Task Force that the Russian Federation has no desire to dominate its neighbors imperially but only to pursue its interests within a normal framework of close, friendly and mutually beneficial bilateral and multilateral relationships. For its part, the West must acknowledge that Russia has legitimate political, economic and security interests in its own backyard. Strong mutual dependencies still exist in all sorts of areas, for example with Ukraine in energy supplies. How Russia conducts these relationships will send an important signal about its intentions to its Western partners, one that will in turn influence their policies and actions toward Moscow.

The profound changes that have occurred both in the U.S. and Russian nuclear postures, and in the threat environments that Moscow and Washington face, offer an opportunity to forge such change in our strategic nuclear relationship. Moreover, if the challenges posed by the new threat environments are not properly managed, they could become sources of uncertainty and potential friction. Creating a post-deterrence relationship is a long-term commitment, but the first steps toward such an outcome are already within our grasp.

We believe Presidents Bush and Putin ought to take the opportunity afforded by their upcoming meetings at the G-8 summit in Italy and at the next bilateral summit in Crawford, Texas, to explore their personal visions of the future security environment and, on the basis of these visions, to search for ways to put in place the first building blocks of a new strategic nuclear relationship. Specifically, the two should share their perceptions of threats and explore whether they have common security goals and whether, on the basis of these mutual objectives, a more efficient way of reaching and implementing agreements could be found, including a more robust sharing of information about threats of mutual concern. Each side has expertise and knowledge to share with the other.

Such an approach is based on good common sense. The global U.S.-Russian rivalry has profoundly diminished, even as important differences of view remain on other critical issues such as arms sales or individual states of concern. Indeed, the global strategic environment is intriguing and worrying precisely because the most important sources of security concern lie outside the Washington-Moscow axis for the first time since World War II. These issues include the emergence of China, India and

Pakistan's public demonstrations of their nuclear capabilities and the ongoing efforts of Iran, Iraq, other states of concern and even terrorist groups to acquire nuclear and other weapons of mass destruction and their means of delivery. Though the United States and Russia look quite differently at some of these trends, it is our belief that frank and honest dialogue could narrow the gap on at least some of our threat perceptions and reveal important common objectives. Ultimately, U.S.-Russian cooperation could be a catalyst (and U.S.-Russian friction an impediment) to new or reinvigorated multilateral efforts on these issues.

## THE U.S.-RUSSIAN BILATERAL NUCLEAR AGENDA

As a first step, Presidents Bush and Putin should explore the creation of a special high-level channel on security questions, regularly reviewed by both, as a key element to making progress. Such a channel would not be bound to a particular negotiation (i.e., START III or ABM Treaty revision). Rather, it would be empowered to look at the breadth of security issues, beginning with the bilateral nuclear agenda, to identify common interests and serve as a regular, reliable conduit between the two presidents.

The two sides should make an up-front commitment to an interim nuclear relationship that features a mix of dramatically lower levels of offensive weapons and defensive systems. Frankly, there can be no progress unless both sides accept this vision, however much they may differ on the actual size or particular mix of residual arsenals or the scope and architecture of missile defenses. As senior U.S. officials have suggested, Russia should also be made a part of the research and development effort on ballistic missile defense, ensuring that Moscow derives real benefits from any alteration to the ABM Treaty.

Beyond the questions of offensive and defensive systems, the two sides should explore ways of making the joint early warning agreement more effective. They should also explore further measures to reduce alert status for strategic forces, and thus the danger of hair-trigger responses.

An important but often neglected aspect of Russian nuclear policy is defense reform. It was, after all, the crisis in Russian conventional forces and the country's various budgetary constraints that led to greater reliance on nuclear weapons. Many observers fear that the combination of this increased reliance on nuclear weapons and gaps in the early warning system have in fact created a potentially dangerous "launch on warning" posture for Russia's nuclear forces. Russia has for a decade talked of defense reform and done little. Putin's new team and particularly his

minister of defense, Sergei Ivanov, have now initiated a controversial and serious defense reform that would simultaneously reduce and upgrade Russia's conventional forces. If the defense ministry seeks Western advice or assistance, the West should indeed be prepared to respond.

## NON-PROLIFERATION

One of the most important mutual interests of the United States and Russia is to stem the proliferation of nuclear and other weapons of mass destruction and their means of delivery. A world of many small nuclear (or chemical or biological) powers is not in the interests of either the United States or Russia. Both sides need to look past the issue of particular clients or irritants to the unfolding security trends beneath. These trends do not favor long-term stability in Eurasia. On the contrary, they cry out for a new level of collaboration between Moscow and Washington (as well as for the two countries to reach out to other key states in the emerging global security environment).

To make broader progress on non-proliferation, Russia and the United States must reinvigorate efforts to address the leakage of nuclear materials and know-how from Russia itself. The two sides must acknowledge and address the crisis of cooperative (also called "Nunn-Lugar") assistance. The notion of a cooperative effort to address the safety and secure storage of nuclear materials and to keep nuclear technology and skills within Russia is sound. The United States believes that Russian cooperation, however, has been missing or suspect on key projects. Budget shortfalls and more pressing domestic concerns have often made Russia appear uninterested in cooperative efforts. Moscow in turn complains about red tape and about too much of Washington's aid money flowing to U.S. consultants. Whatever successes the program has achieved, large amounts of fissile material, important storage sites and other crucial nuclear facilities still lie outside its scope.

Only the efforts of the two leaders can help restore both momentum and effectiveness to this program. Specific efforts are needed to resolve such difficult issues as further reducing the number of facilities where nuclear weapons and material are stored, comprehensively upgrading Russian security and accounting procedures and accelerating programs to identify, tag and seal nuclear materials. A key to this latter initiative's success is Russian and U.S. willingness to see it encompass a significantly larger share of the estimated amount of highly enriched uranium now in Russia, as well as to work toward excluding the usage of enriched uranium and plutonium in world atomic energy production.

In the context of building a safer world, Russia's management of its long-term storage of spent nuclear fuel has global significance. Given Russia's indigenous capabilities for the production of fissile materials, it is folly to see long-term storage as adding anything to Russia's nuclear capabilities. However, the Russian government must show that it can in fact store the additional materials safely and use the profits to address its own nuclear safety and infrastructure issues.

Addressing the problem of new nuclear states is an important area for bilateral coordination and cooperation. The United States and Russia may both have a role to play in minimizing the risk of accident, misunderstanding or unauthorized use of weapons by countries such as India or Pakistan through data-sharing and other measures.

### BROADER ISSUES OF MUTUAL CONCERN

At various times in the last fifteen years, Washington and Moscow have committed to an expanded strategic dialogue. The hope of each attempt has been to shift the focus from bilateral nuclear matters to global issues on which the two countries may share mutual interests. We believe it is still important for both sides to have such a dialogue.

As with the other aspects of the strategic relationship, it is crucial that such a dialogue begin at the top and spread throughout the leadership of key ministries and agencies. The best place to start is with an extended discussion of the global security environment. Russia and the United States see the world quite differently, given their respective geographies, histories and current political, economic and military capabilities. Yet their interests potentially overlap in Eurasia, particularly in attempting to minimize the risks from weak or failing states, growing advanced military capabilities throughout Eurasia, new pressures on energy, water and other natural resources, immigration, regional and ethnic conflicts and international terrorism and drug trafficking.

We realize that progress on this ambitious agenda will be influenced by the steps both countries take on important bilateral issues such as missile defense. An important first step here requires dealing with important differences on arms sales to Iran, Russia's relations with its new neighbors, Caspian oil and gas and Iraqi sanctions. The world already presents serious security challenges to both Russia and the United States. Two new presidents and new players at senior levels are an additional reason to try to forge a new security relationship. Modest steps in this direction, whether on ballistic and cruise-missile threats or intelligence sharing, could be a sound basis for testing whether the basis for a broader strategic dialogue is in place.

CHAPTER THREE

RUSSIA AND AN EXPANDING  
EUROPE

Europe is undergoing a historic transformation. The deep and sweeping changes that began nearly two decades ago—with the rise of Mikhail Gorbachev, freedom for Poland and other Soviet satellites, and the end of the Soviet Union itself—made a free and united Europe a real possibility. Of course divisions and differences still remain, not least between the European Union (EU) and non-member states, but a united Europe ought still to be the strategic aim of the countries of east and west. Any new division of Europe, with its corresponding risks of military confrontation, is simply not in U.S. interests. Both sides need to work to avoid the emergence of a stark division and instead encourage further progress in European integration, through both the EU and wider cooperation between east and west.

**RUSSIA AND THE EUROPEAN UNION: A NEW FOCUS**

Over the past 18 months, Russia's relationship with Europe has developed in important new directions. The most strategically important of these developments is the shift from a series of uncoordinated bilateral relationships (in several cases based largely on personal relationships between European leaders and their Russian counterparts) to a greater emphasis on the relationship between Moscow and the European Union. This relationship was codified in the EU's Common Strategy for Russia, which the EU member states and Russia agreed to in June 1999, but more recently it was symbolically highlighted when Vladimir Putin became the first Russian president to attend an EU Summit (Stockholm, March 2001).

Several important developments lead us to believe that Russian-EU relations will expand in the coming years, as long as the Putin team's domestic reforms continue apace:

- First, the EU enlargement process continues, and the accession of Estonia, Latvia, Lithuania and Poland will significantly extend the EU's border with Russia. This will accentuate Russia's potential role in a number of important policy issues for Europeans, including environmental management, nuclear-waste management and nuclear-reactor safety.



- Second, it is clear that Moscow is now assigning greater priority to international commercial and economic integration than during the Yeltsin era. The EU is Russia's largest trade partner, accounting for 36.7 percent of Russia's imports and 33.2 percent of its export trade. Russia provides over 15 percent of the EU's needs in imported fuel. If Moscow is able to implement reforms to improve the country's investment climate, we should see a substantial rise in European investment in Russia as well. The political impact, as well as the economic results, of that investment will be profound.
- Third, EU enlargement will bring new border regimes. A serious commitment to make Kaliningrad successful as a pilot project within EU-Russian relations is particularly important. Enlargement to Poland and the Baltic states should bring greater stability and prosperity to the whole region. However, serious efforts need to be undertaken now to avoid a new dividing line that could adversely affect Russian and other neighboring states' trade and interaction with these new EU members.
- Finally, the current flux in the European security environment could open up new areas for intra-European and European-U.S. cooperation in regional security. Although creating a common European security policy is for many people a more controversial issue than the expansion of economic ties, the important opportunities for enhancing European security should not be ignored. The EU's 1999 Common Strategy for Russia explicitly mentions the need for cooperation to strengthen stability and security in Europe and beyond—at the October 2000 EU-Russia Summit in Paris, the Europeans effectively gave Russia a stake in this cooperation when they acknowledged that Moscow should have some role in the development of the European Security and Defense Policy.

Energy is also a key element of the broader Russian-European relationship. Already, energy supplies represent 45 percent of Russia's exports to the EU, which account for 42 percent of the EU's needs in imported natural gas and 17 percent of oil imports. As Europe's demand for energy (especially gas) grows in the coming years, Russia's overall presence in Europe will inevitably increase. The issue of Caspian energy development, long in the developmental stages, will also take on more immediate importance. Russia, Europe and the United States will need to redouble efforts to work toward sustainable, win-win solutions in energy trade in general and cooperation in the Caspian region specifically.

## NATO'S ENLARGEMENT AND TRANSFORMATION

A key irritation in U.S.-Russian relations is NATO enlargement, or what the Russians prefer to call NATO expansion. NATO's leaders have agreed to allow a further round of enlargement at their 2002 summit. No countries have yet been invited for 2002,

but Bulgaria, Estonia, Latvia, Lithuania, Romania, Slovakia and Slovenia are among those mentioned as possible candidates.

NATO officials and the leaders of NATO countries see enlargement as an essential process of consolidating democratic and economic reforms in central and eastern Europe. But they are also aware that expansion poses serious political and security concerns to Russia and the non-NATO states that neighbor the organization's new entrants, so they have tried to provide security guarantees by expanding cooperative structures with non-members and agreeing to limit military deployments (especially stationed nuclear weapons and NATO forces) on the territory of new members. Such security cushions, however, do not address the concerns of senior Russian officials. Although they acknowledge that NATO is not a military threat today, their opposition stems from the fact that they do not understand the logic—consolidating market democracy—behind the organization's desire to expand. Moreover, they see NATO enlargement as a political tool for influencing Russia and areas of Russian interest. They are not happy with enlargement anywhere, but they strongly oppose the accession of the Baltic countries or any other nation formerly part of the Soviet Union. Whether or not a Baltic state is part of the 2002 enlargement, NATO has made it plain that the states of this region are eligible. Enlargement is thus an issue about which Russia and NATO will likely continue to disagree. At the heart of Russian leaders' concerns about NATO is the example of NATO's circumvention of the United Nations Security Council in its decision to intervene militarily in Kosovo.

We believe that regardless of the decision on enlargement—and our group is divided on its merits—the two sides have an important and unfulfilled agenda. The NATO-Russian Permanent Joint Council needs to be made to work. Unrest in Macedonia and the potential for instability elsewhere in the Balkans make a viable process of political and military consultation a priority, whether within this council or in another structure. The overall success in Bosnia and Kosovo of Russian military integration with NATO forces is a daily reminder of what the two sides can do together, but it did not occur automatically. First, NATO and the Russians had to overcome problems, differences of views and misunderstandings. The basis for an effective arrangement does exist, however, provided that both sides are sufficiently flexible in their positions: Russia must acknowledge the likelihood of NATO's continued intervention in the Balkans, and NATO must recognize Russia's interest in shaping that intervention, both as part of the political preparations and then as a contributor on the ground.

Beyond practical efforts to enhance cooperation, a larger project looms. It is nothing less than the transformation of NATO itself. The two strands of NATO's current policy toward non-members—enlargement toward some and cooperation with others—

ply an important and enduring change in the military environment and thus ultimately in the organization itself. Now that it no longer faces the Cold War-era task of containing the Soviet Union, NATO has made fostering political and operational cooperation in peacekeeping and disaster relief, whether in the Balkans or elsewhere, its major day-to-day business. If this trend continues, the current tension between NATO's territorial enlargement eastward, and its transformation away from a posture designed to counterbalance the east, could well be resolved by an enlargement of the organization to include Russia, Ukraine and the other states of the former Soviet Union coupled with the embrace of a broader collective security mission. It is not too early to begin to discuss such a transformation and enlargement of NATO, including the role the organization would consequently play as a collective security mechanism. Not all supporters of enlargement will find this kind of NATO to their liking, yet the logic that drives enlargement to the east now will ultimately have to apply to even such states as Russia and Ukraine. Indeed, to argue that NATO has helped to consolidate Polish, Czech and Hungarian reforms and should soon act in the same way with regard to candidate countries, and at the same time reject the idea that it should take the same role in Ukraine or Russia, is actually to declare a *de facto* permanent dividing line in Europe. This, obviously, is not in the interest of any of the countries involved.

## OTHER OPPORTUNITIES AND CHALLENGES

Russia's relationship with Europe is and must continue to be wider than its relationship with NATO or the European Union. Even if the two key institutions and Russia begin to consider seriously the prospect of eventual membership, Russia still faces many years as a non-member. It thus has an interest in seeing the institutions to which it does belong, such as the Organization of Security and Cooperation in Europe (OSCE) and the Council of Europe, become more effective. Russia also has to face up to its own ambivalence about the role such institutions will inevitably play in or around Russia. Its recent decision to allow the return of OSCE and Council of Europe observer missions to Chechnya is a good start, but Russia must now consistently concede an expanded role for Europe and its institutions in other issues regarding Russia's immediate neighborhood. Just like NATO carving out its own portion of Europe to the exclusion of Russia and other eastern states, a separate Russian zone of special interests outside the reach of Western institutions would also contribute to a permanent European dividing line.

In the near term, however, Moscow and the Europeans are diverging in many areas. Russian leaders simply view problems and events inside and immediately around their country through a different historical, cultural and political lens than do their

counterparts in the West. Even so, these differences pale in comparison to the overtly dangerous antagonisms that the two sides successfully managed during the Cold War. So there is every reason to believe that Russia's national interests could be made compatible with an increasing multilateral approach to its surrounding region as well.

Ukraine, Georgia and the other countries of eastern Europe and the Caucasus that border Russia significantly influence Europe's view of itself and of its relationship with Russia. Ever since these states achieved independence, support for their sovereignty has been a cornerstone of European and U.S. policy in the region. That support should not be seen as anti-Russian. Indeed, having stable and prosperous neighbors would remove an enormous security challenge from Russia's list of priorities. Countries such as Ukraine must see—and help Russia understand—that reform and improved ties with the West need not come at the expense of strong ties with Russia. In the current diplomatic and security environment, Ukraine, Moldova, Georgia and other states of the region do not face a stark choice between Russia or the West. On the contrary, they need good political and economic ties with both in order to address their own internal challenges. Thus, as EU, Canada and the United States intensify their relationships with Russia, they must take steps to strengthen ties with other states in the region as well. The stability and security of this part of the world depends in no small part on the successful development of all the countries in Europe's "near abroad," including Russia. Similarly, the West needs to develop a more subtle view of Russian policy, one that can distinguish the ordinary and legitimate pursuit of interests and advantages from a direct threat to the sovereignty and independence of its neighbors.

CHAPTER FOUR

A CHANGING RUSSIA:  
POLITICAL AND ECONOMIC  
REFORMS IN CONTEXT

The Task Force believes that the seeds of a potentially fruitful reform agenda, as planted by the Putin team, have created a historic opportunity for the United States fundamentally to change our relationship with Russia. Moreover, it is important to note the obvious truth that, although presidential leadership is critical, Russia is changing from the bottom up in powerful ways. Its people are more exposed to and connected with the West, especially Europe, than ever before, and this grassroots factor has tremendous potential to shape Russia's future for the better. It is worth stressing, however, that the political environment in Russia is complex and Putin's reforms are only now taking shape. We see many contradictory patterns, especially in terms of reform implementation and of apparent abuses of official powers. Unless these deficiencies are corrected, our relationship with Russia will not evolve as we wish, even if the two presidents establish a good personal rapport.

The following analysis of Putin's priorities and basic approach to domestic reform is based on our conversations with senior Russian officials and independent experts from Russia and the West and careful examination of official documents and unofficial studies.

THE CONTEXT OF THE PUTIN REFORM AGENDA

Observers inside and outside Russia have historically posed large questions about that country's destiny. Where does Russia's future lie? How will it define its greatness? Will Russia seek to integrate into the European and global economic, political and security systems or will it pursue its own path, perhaps even in opposition to these systems? That Russia is still in the early years of a protracted, historic transition is clear. What is not well understood, however, is how much progress Russia has already made since the collapse of the Soviet Union and the dissolution of the Communist Party, and what direction the country is taking today.

After 70 years of Communist Party rule, Mikhail Gorbachev's reforms combined with internal economic decline to bring the Soviet Union to an end on December 25, 1991.

Launched in 1985, *glasnost* and *perestroika* unleashed powerful forces that led to greater human rights and the promise of new economic opportunities for millions of people in the Soviet Union and East-Central Europe. But the end of communism was just the beginning of Russia's rebirth. Over the last decade, Russia has gone through a difficult, wrenching transformation, with mixed results.

When Boris Yeltsin assumed the reins of power in the Kremlin, he faced daunting challenges. The Soviet-communist system, although legally terminated, still dominated Russia's political and economic landscape and exerted a psychological hold over many Russians, especially those of the older generation. The country's leadership faced the historic burden of simultaneously dismantling old structures (e.g. the command-administrative economic system) and building new institutions (e.g. representative political structures, a market economy) that were entirely alien to those who had grown up under the Soviet system. Although it seems preposterous today, the original strategy for transforming the Soviet economy into a modern market economy was a 500-day plan. Western euphoria over the collapse of the U.S.S.R. contributed to Russians' inflated expectations of a swift transition.

Although the early Yeltsin reforms made substantial progress toward dismantling the command economic structures and breaking the grip of communism, they failed to create new, modern market institutions and practices in their place. For most of Yeltsin's second term, Russian domestic and foreign policies seemed either erratic or adrift. Therefore, in the absence of new legal, economic and political frameworks, what had emerged by the time Yeltsin left office in December 1999 was an environment that allowed those with access and influence to abuse their power and amass great wealth. Indeed, politics, business and government became one. Corruption and economic crime were rampant. By 1992, inflation destroyed what savings the average Russian citizen had accumulated, and the contraction of large segments of the economy greatly increased unemployment rates. As a result, the aim of creating a robust middle class went unfulfilled.

Moreover, the devolution of power outward from Moscow, which the Yeltsin administration encouraged in the early 1990s, exacerbated disparities in living standards and civil-political rights protection among different regions of Russia. As the authority and legitimacy of federal power structures waned, some regions prospered while others turned into impoverished totalitarian fiefdoms, in which all authority resided in the governor and the regional political and economic elites associated with him.

Adding to this political and social disintegration, Russia's demographic situation declined precipitously in the 1990s. Birth rates fell dramatically, as did life expectancy, especially for men. And the problems have not been arrested: the incidence of infec

tious disease (especially HIV/AIDS and multi-drug resistant tuberculosis), alcohol and drug addiction, and cancer and heart disease are on the rise. In many cases these afflictions claim the lives of the most productive segments of society. Some outside experts estimate that HIV/AIDS is growing at a faster rate in Russia than in any other country in the world. In 2000 alone, Russia's population of 146 million declined by some 768,000 people, and prominent demographers forecast that by 2005 it will fall an additional 2.8 million.

Despite the severity of these problems, most pressing was the protracted and severe economic decline that began well before the disintegration of the Soviet Union and continued through 1998. Official statistics put Russia's economic decline from 1992-98 at about 40 percent of gross domestic product (GDP). Even adjusting for the fact that much of Soviet production did not add value or contribute to social welfare, and the upsurge in black market or other unreported activity which compensated for some of the decline in official statistics, the economic crisis in Russia was real and was felt by virtually every Russian family. Some experts compare the socioeconomic impact of the decline to that of the Great Depression.

Since the financial crisis of August 1998, Russia has—thanks largely to skillful management of fiscal and monetary policy, on the one hand and a weak ruble and advantageous trends in world energy prices, on the other—enjoyed a notable economic rebound. Russian official statistics put GDP growth at about 5.4 percent in 1999 and 8.3 percent in 2000. Foreign direct investment in 2000 totaled less than \$5 billion, a tiny sum given Russia's enormous potential. The positive impacts of import substitution and high energy prices will diminish over time, however, and a surge in demand for other Russian exports is unlikely in the near term. Russia's ruble is likely to appreciate in the coming months, making exports less competitive. The yet-to-be-determined outcome of Russia's reforms, therefore, stands as the single most important factor in determining whether Russia's economy becomes compatible and competitive with global markets and generates the kind of growth that can bring renewal to Russia.

Considering Russia's multifaceted domestic crisis, coupled with significant international challenges ranging from U.S. intentions to pursue a national missile defense program to pending NATO enlargement to a strong and growing China, any new Russian president would feel a sense of urgency. By all accounts, the new Putin administration has brought new focus and energy to the executive branch. President Putin appears both to his supporters and to his critics as someone with a strong sense of strategic purpose. In domestic affairs, Putin has articulated and begun to put in motion an impressive reform agenda centered on reversing the deterioration of the federal authority, improving the economy, and attacking corruption and criminality

## POLITICAL REFORMS

When Putin came to office in early 2000, halting and reversing the disintegration of the state by rebuilding a strong, cohesive federal government (so-called “vertical power”) was at the top of his list of priorities. As prime minister, Putin persuaded the government to pursue an aggressive campaign against Chechen separatists, earning him high approval ratings in Russia and much criticism from the West. Upon assuming the office of president several months later, his first step was to consolidate federal power by creating seven new federal districts, each headed by a presidential representative. He faced no easy task in reasserting central control over regional authorities—indeed, the legacy of Yeltsin’s program of enhancing regional autonomy was that no less than 70 percent of laws at the local and regional levels contradicted federal laws.

Putin had recognized that he could not implement the far-reaching political and economic reforms that he envisioned for Russia without some rebuilding of central authority. But many Western critics saw this quest for “vertical power” simply as an attempt to reassert KGB-style control over the country and stifle the freedoms that *oblasts* and localities had wrestled away from the center during the turmoil and transition of the 1990s. The results of the first year, however, show some promise. Many, if not most, legal inconsistencies have been resolved, and new forms of regional cooperation are underway. But there is a legitimate concern, however, that the “super-governors” sent from Moscow to the federal districts should not be given budgetary and other powers which would make them accountable only to the executive branch.

Putin also identified battling corruption and criminality as a major early priority. And in this area, the reviews of his effectiveness and prognostications about his true intentions have been mixed. Early efforts to tackle corruption were widely dismissed as ineffective, until the president began to sack senior officials. Putin also began to unleash the machinery of the state to break the dominance of oligarchs, who had acquired valuable state property at bargain prices during the privatization process. But then many observers looked at the uncanny way that prominent “anti-Putin” oligarchs were the first to come under investigation. Some concluded that the new president was out to replace the old “family” with one loyal to himself. Others were concerned that the government might be cutting corners on due process or jeopardizing important democratic principles, citing the persecution of NTV as a prime example. The president refuted some of these worries by sacking Rem Viakhirev, the head of Gazprom, which signaled to many observers that Putin was indeed serious about attacking corruption on a broad scale. Indeed, Viakhirev’s successor, Alexei Miller, has already taken steps to increase transparency, including agreeing to meet



personally with minority shareholders to hear their views. At the same time, however, Viakhirev's appointment as Gazprom's board chairman only sends more mixed signals, although it is considered a position of limited power. President Putin will give great assurance to domestic and international audiences alike if he continues to broaden his battle against corruption.

## DEMOCRACY AND CIVIL SOCIETY

The Western media's focus on the negative elements of Russia's transition does not adequately represent the magnitude of positive change that is occurring even outside of leading cities. When measured against modern, mature democracies in the West, Russia and all the transition states fall short. When measured against where it was in 1990, however, Russia's progress is impressive. Russia today boasts a constitutional democracy: the judiciary functions (if not fully independently) and the national legislature is growing increasingly effective; free (if not always fair) elections have become commonplace; public opinion matters; widespread (if not universal) protection of civil liberties such as freedom of religion and assembly is generally assured; and both state-controlled and independent media outlets present a diverse accounting of the news. Russian citizens' constitutional rights are largely protected, although certain segments of the population—notably Chechen refugees, prison inmates and military conscripts—continue to encounter severe human-rights violations. More than 35,000 non-governmental organizations operate in Russia today, whereas virtually none existed just ten years ago; they form the foundation, yet delicate, of an emerging civil society. Most important from the perspective of U.S.-Russian relations going forward, however, is not what Russia has achieved, but the direction it is heading and the future it will create for itself.

Some in Russia and many in the West, even while acknowledging recent signs of progress such as changes to the tax code, judicial reform and anti-money-laundering initiatives—are concerned that such reform comes at too high a price. These observers point to a variety of worrying clouds in Russia's new landscape: the protracted war in Chechnya, especially its high toll in civilian lives; government pressure on the media, especially NTV; new limits on political parties; a reported rise in "self-censorship"; and restrictions on academic contacts with foreigners. Although due credit should be given to Putin for taking on an ambitious and politically difficult agenda, critics wonder whether Putin's reforms, even if well intentioned, are not headed down a slippery slope toward a newly centralized and authoritarian state. The FSB raid on Ekho Moskvyy radio station the day before French President Jacques Chirac was to speak has again raised concerns, both inside Russia and in the West. Going forward, the attitudes of many Western policymakers and observers will be determined by how Russia constructs an effective yet democratic state and resolves

other equally complex challenges. It will be important for President Putin and his colleagues to be sensitive to the concern of both friends and critics that his administration is following a policy where the ends justify any means. Domestic and foreign audiences will carefully study his words and actions for signs of this sensitivity or the lack of it. For example, a successful resolution leading to a spin-off of Gazprom's media properties, like the radio station Ekho Moskvy, into independent hands would reassure potential critics about the Putin administration's response to concerns about freedom of the media in Russia.

## ECONOMIC REFORMS

After more than a decade of economic decline, Russia's economy is showing signs of life; with good management, the recent improvements in economic performance can be sustained and even accelerated. President Putin and his economics team have articulated a reform agenda that, finally, appears to take on many of the vested interests that prevented reforms from moving forward during the Yeltsin era. These vested interests—oligarchs, corrupt senior officials and other opponents of reform—will still mount a vigorous challenge to serious attempts to create a transparent and efficient economy that is open to and competitive in global markets.

Putin came to office in early 2000 with a clear diagnosis of the main challenges facing the Russian economy and a clear set of strategic objectives. Importantly, he publicly rejected the organizing principles of the Soviet period:

Communism and the power of Soviets did not make Russia a prosperous country with a dynamically developing society of free people. Communism vividly demonstrated its ineptitude for sound self-development, dooming our country to a steady lag behind economically advanced countries. It was a road down a blind alley, which is far away from the mainstream of civilization.<sup>2</sup>

But Putin also took office without a strong power base or a clear mandate from the electorate to pursue difficult market reforms. It is widely accepted that Putin did not seek this job—indeed, Russians had been just as surprised as the international community when Yeltsin selected the former St. Petersburg city administrator and KGB officer as his prime minister and, later, successor. But unlike their Western counterparts, the Russian electorate reacted favorably to a young, articulate and energetic leader who held a law degree, had gained experience managing international investment matters under St. Petersburg's reformist mayor Anatolii Sobchak and had enjoyed a meteoric rise within Russia's federal bureaucracy since 1996.

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<sup>2</sup> Vladimir Putin, *Russia at the Turn of the Millennium*, December 13, 1999.

But although Putin enjoyed high public opinion ratings, he was attempting to effect change in a Russia where the vast majority of the public had grown deeply skeptical and even cynical of further reforms from above. Neither he nor the Russian public was ready to tackle controversial and painful reforms immediately. Solid economic growth in 1999 and 2000 gave Putin some political breathing room with both the Duma and the public, and allowed his team a chance to plan and organize its reform strategy.

The economic agenda conceived during Putin's first year in office included major overhauls of the tax code and the budget and reforms of the banking system and the capital and securities markets, as well as bureaucratic administrative reform.

A major theme throughout the reform agenda is the need to impose transparency in economic and business activities and in government operations. This is a response to the conviction that economic crime and corruption are the key brakes on Russia's economic development. Indeed, in our conversations with senior officials, virtually all stressed the importance of increasing transparency in order to hold officials—public and private—accountable before shareholders, citizens and the international community.

Another theme we heard often was the priority Putin and his team attach to WTO accession. The Russian government is currently making serious efforts to implement the reforms required for WTO accession. Moscow has already reformed its customs code and cut tariff rates significantly. The related package of new laws for this year, some already approved by the Duma, includes:

- A new land code allowing for purchase and sale of non-agricultural land;
- A new commercial code including intellectual property rights;
- A deregulation and licensing package simplifying licensing procedures for new firms, eliminating red tape and removing restrictions on private-sector activity;
- A new corporate profit tax law reducing the rate from 35 percent to some 25 percent;
- A new customs code simplifying tariff schedules and reducing rates; and
- New laws to improve corporate governance and bankruptcy procedures.

Despite these encouraging reforms, meeting the requirements of the international trade regime will pose serious challenges. Liberalizing the service and agricultural sectors are the two main challenges ahead. Steady progress in the coming months and a receptive, encouraging posture from the international community will help sustain the necessary political will to move forward on these and other difficult measures. We strongly endorse this initiative.

## ECONOMIC REFORMS: THE LEGISLATIVE AGENDA

We are impressed with the legislative agenda that is going forward; if implemented, the reforms under review by the Duma should give a significant boost to economic performance and facilitate integration into the global economy.

ISSUE	GOALS	STATUS
<b>Tax Reform</b>	Enact in 2001 rest of new code to ease burden, simplify rates, and limit exemptions; to take effect for 2002.	Remaining chapters of Part II of new code to be considered separately in 2001; Part I amendments to be redrafted, fixes for newly enacted Part II chapters in Duma.
<b>2002 budget</b>	Set realistic revenue and expenditure targets.	Government already working on draft 2002 budget, plan to send to Duma in August.
<b>Pension and social welfare reform</b>	Reduce high payroll taxes that fund benefits but encourage evasion; target social aid to needy.	Social welfare tax rates reduced for 2001; new draft pension reform program to be finalized in the summer of 2001.
<b>Housing and utility subsidies</b>	Shift to unsubsidized housing and utility fees for all but those below poverty line by 2008.	Government to complete new reform proposal by July; new bills due in late 2001.
<b>Regulation of "natural" monopolies</b>	Force dominant firms in gas and electric power sectors to open to competition; restructure railroad system.	United Energy Systems, telecom, railroad, restructuring plans to be approved by mid-2001, Gazprom by late 2001.
<b>Property rights</b>	Assure right to own, sell, or mortgage land; key to spurring long-term investment.	State land registry law in effect; federal framework of land code approved by Duma in June, farmland sales bill by end of July.
<b>Bankruptcy legislation</b>	Apply new bankruptcy laws to allow restructuring, sale, or closure of insolvent firms, banks.	Amendments to enterprise, credit firm bills in Duma, farm bankruptcy bill redrafted; draft bank reforms in Duma.
<b>Privatization</b>	Continue sell-off and improve management of state-owned shares and enterprises.	New privatization bill approved in first reading by Duma in June; sales of state shares continuing.
<b>Production-sharing agreement (PSA) legislation</b>	Open way for multibillion dollar energy and mineral development projects.	Amendments to modernize PSA law on spring Duma agenda; government action needed, normative acts stalled; controversial PSA tax bill due in July.

Recent developments in Russia's political environment, especially the consolidation of numerous political factions into a smaller number of stronger, generally pro-reform parties, may give Putin the political foundation he needs to press ahead with the reform agenda advocated by liberals such as Economics Minister German Gref, Presidential Economic Adviser Andrei Illarionov and Finance Minister Alexei Kudrin.

Given recent trends in economic policy, there is reason for cautious optimism that the Russian leadership has both the right ideas and the political will to push forward on reform. Potential investors await implementation of long-promised structural reforms, in particular a land code, a new labor code and important changes to the tax code. Current (Brezhnev-era) labor rules do not cover private workers, who represent some 80 percent of the workforce. The new labor code that is working its way through parliament gives employers the legal right to hire and fire workers. Protection of minority shareholders and steps to remove state interference in developing small and medium enterprises must be augmented as well. A European and North American posture of openness and readiness for inclusion and integration will be key to providing critical political support for Russian reforms.

### **U.S.-RUSSIAN ECONOMIC RELATIONS: FROM TECHNICAL ASSISTANCE TO COMMERCE AND BUSINESS**

In the 1990s, U.S.-Russian economic relations were dominated by U.S. efforts to render technical assistance to Russia in hopes of accelerating economic reform. The other main dimension of Russia's international economic engagement was multilateral, conducted through the International Monetary Fund and the World Bank. As we enter a new phase of Russian reforms, it is time drastically to restructure those channels of engagement, to move from Russian dependence on foreign assistance to institutional collaboration. As Russia continues its economic transformation, it will rely increasingly on its growing domestic savings supplemented by private external capital in the form of increased direct investment and borrowing on international capital markets. Indeed Russia's performance, supported by high prices for its energy exports, has eliminated the need of any balance of payments support from the IMF for the foreseeable future. Project financing from the World Bank, EBRD and European Investment Bank may continue, in support of further reforms and strengthening of institutions supporting the private sector, but such financing will continue to shrink as a share of external capital. The issue of debt relief from the Paris Club is now moot. Minister of Finance Alexei Kudrin has expressed Russia's ability and intent to meet its debt obligations in full through 2003 without such relief.

We can do much to encourage Russia's economic reforms, primarily through working to expand opportunities for commercial relations, support for integration in

international and multilateral institutions and cooperation on scientific and technological advancement. U.S. support for the WTO is very important, as we noted above. In this context, we advocate graduating Russia (as well as Ukraine) from Jackson-Vanik. Also, the European Union can and should do more to encourage Russia to meet the terms of its Partnership and Cooperation Agreement, the “road map” that leads to associate membership in the EU.

Foreign investment, which will be a key catalyst to Russia’s economic growth, is picking up again after the financial crisis of August 1998, which drove foreign investors out of the country. Despite the great potential and recent steady growth of investments in the Russian economy, the amount of foreign investment in Russia today is very small compared to that in China and the former communist countries of central and eastern Europe. As of January 2001, cumulative foreign direct investments (FDI) in Russia amounted to \$16.1 billion. In comparison, Poland, as the most successful transition economy in central Europe, attracted an estimated \$35.5 billion in FDI from 1991 through the end of 2000. Last year Poland enjoyed a record FDI of \$9.3 billion, whereas the equivalent figure for Russia was \$4.4 billion. The prospects for further increases in what foreign investors are willing to put into Russia will depend on whether the proposed reforms are implemented.

In our bilateral economic, commercial and scientific relationships as well, much remains to be done. A large investment today in improving mutual understanding between the next generation of leaders and citizens in our countries will pay important returns over the longer term. Such investments might include encouraging programs that expose Russians to U.S. and Western businesses. In addition to traditional projects that bring business people together, other means of cooperation would involve:

- Exchanges that introduce Russian lawmakers, journalists and educators to U.S. businesses, and vice-versa;
- Expansion of educational exchanges of Russians studying in U.S. business schools;
- Instead of sending highly paid consultants to lecture on economic reforms, exploring “twinning” programs that match government officials in the U.S. with their Russian counterparts in a collaborative/mentoring way. This was successfully done in Central Europe by West European civil servants;
- Considering the expansion of micro-credit programs to support small and micro businesses;
- Looking for ways to expand scientific and technological collaboration; and
- Addressing global issues such as HIV/AIDS.

## CONCLUSION

We present our analysis and recommendations fully mindful of the unkind fate that befalls most reports of this type. We are equally aware of the skeptics, both in Russia and in the United States, who believe they have seen this kind of call for change before and remain more comfortable with their view either of an unfriendly and rus-sophobic United States or an authoritarian and unchanging Russia. Those who hold these views deny any hope for fundamental change in the relationship.

But there is good reason for hope, and good reason for continuing to engage Russia. The past fifteen years of remarkable and unpredictable change have erased nearly half a century of division and fear in Europe, eliminating the military confrontation at the heart of Europe and opening up the prospect of an undivided continent. And a key ingredient in the final outcome is Russia. Almost no one disagrees with this. However, deep differences of opinion remain as to where Russia stands and where President Putin is taking it. Some believe he represents renewed hope; others fear a reversion to the strong and centralized state power that has dominated so much of Russian history. As we initiated our study, we shared these same uncertainties.

This report makes a clear and consistent argument that we are at a dramatic turning point in history, one that could support the transformation of the U.S.-Russian relationship. It further argues that we should take advantage of this turning point, and for several reasons: the hopefully positive trends within Russia, the energy and vision of the Russian and U.S. presidents and the simple fact that the United States, from its position of prosperity and strength, should place a bet on change.

As we stated at the outset, although it is still too early to reach a final judgment on the thrust of President Putin's leadership, there have now been enough positive initiatives to create the basis for attempting to move forward in cooperation with his administration. What occurs inside Russia does matter to us. We repeat, a new relationship simply cannot take shape between the United States, and the West more generally, with any country that does not adhere to basic and internationally accepted principles of democracy, human rights, market economics and transparency. Yet Russia's struggles over the past ten years have yielded positive changes. Moreover, though the burden falls ultimately and centrally on Russia to make the changes it needs, the United States and the West must provide support. In our view, support no longer means endless advice or limitless doses of foreign aid. It means sustained and pragmatic engagement between our citizens, our societies, our businesses and our governments.

We believe it is imperative to seize this moment. This proactive approach entails some risks—indeed, the failure to take such risks in turn implies a fatalism regarding Russia's future, hardly an incentive for Russia to continue with its reforms. Acting on positive assumptions should not, however, mean any reduced diligence in observing the actions of President Putin and his administration. The basic outlines of a new relationship are clear, but its emergence can only be supported by real and substantial progress in ways that must be visible to all. We should measure ourselves and our potential partners by clear standards, as we expect them to do with us. First, regarding security matters, Russia will be held up to standards that include concrete steps toward a more stable, post-deterrent security relationship, new efforts at stemming the spread of weapons and materials of mass destruction and real cooperation on fundamental global security challenges. On the economic side, international business requires a market that is free and transparent, is actively integrating into the global economy and is not content with corruption and crony capitalism. If such a Russian market emerges, U.S. and other international businesses will indeed seize the opportunity presented. And finally, in the political sphere, Russia's membership in the global community will require steady progress on democratic reforms.

In our own lifetimes we have all experienced the tensions and rivalries of U.S.-Soviet competition. This competition has cost our taxpayers a great deal. With the goal of a united and free Europe still unmet, with the clear potential for continued change in Russia, and with a world in some ways more fragmented and dangerous today even than it was during the Cold War, the United States and Russia, together with the European Union and other members of the international community, can make all the difference.



## ACKNOWLEDGEMENTS

Fifteen years ago, U.S. and European opinion about Soviet leader Mikhail Gorbachev was largely skeptical. Few believed that *glasnost* and *perestroika* might succeed. In response to the potential that Gorbachev's reforms represented, the EastWest Institute assembled a bipartisan Task Force of prominent Americans to study the situation and make recommendations on how the United States should respond. That report, *How Should America Respond to Gorbachev's Challenge? A Report of the Task Force on Soviet New Thinking*, challenged conventional wisdom and was credited by officials in Washington and Moscow with having played a major role in affecting the way Americans thought about the Soviet Union at that time.

This Task Force Report on U.S.-Russian relations enjoys important advantages over the earlier study. First, our Task Force has been given unprecedented access to the top leadership in Russia, including President Putin himself. We have listened carefully and asked many questions of senior Russian officials as well as many independent experts and observers in Russia, Europe and the United States. Our report has taken into account a wide spectrum of views and experiences, which lead, we believe, to new insights and perspectives on what is really happening in Russia today.

The second advantage is that we have been able to deal with a leader who has in place an 18-month track record by which we can compare actions to words. Thankfully for this study, Putin has been an activist president right from the starting gate.

A third advantage is that the two presidents met for the first time on June 16<sup>th</sup> in Slovenia. Their meeting focused on building trust and laying out an understanding of where they share goals and concerns and where legitimate differences exist. The meeting was welcomed in many quarters as a sign that these two powers might be able to deal with one another in a new and constructive way. But the encounter also raised many questions in both countries about trust. In the days following the summit, both countries found themselves asking, "How can we trust after two hours?" In response, many skeptics have proposed the "trust but verify" formula.

This report starts from the understanding that the Bush and Putin administrations are engaged in assessing their respective policies, coming to grips with new realities and trying to determine whether their relations can be conducted in a more

constructive, reliable way that enhances global security and maximizes opportunity for their citizens and the citizens of the world.

A special feature of this project has been the important contributions of three distinguished American statesmen, David L. Boren, John C. Danforth and Alan K. Simpson, who served as our Co-Chairmen. Previously, they served for a combined total of 52 years in leadership positions in the U.S. Senate while representing their states of Oklahoma, Missouri and Wyoming, respectively. Representing both major political parties, they have been a source of sound guidance, keen insight and policy savvy.

The Task Force members themselves have generously shared their views, attended meetings and sent a stream of concerns, questions and information for which we are most grateful. We also appreciate the helpful contribution of our numerous European colleagues on earlier drafts of this report. It is clear that the transatlantic interests of the United States and Europe play heavily in any consideration of the bilateral U.S.-Russian relationship, especially at a time when a new security arrangement seems to be on the horizon. The EastWest Institute intends to pursue this theme further by creating, as a follow-up to this project, a European-U.S.-Russian Task Force.

We are also grateful for our dialogue with the administrations both in Washington and in Moscow. In Russia, we are grateful to President Putin and his administration, especially Defense Minister Sergei Ivanov, First Deputy Head of the Presidential Administration Dmitrii Medvedev and Deputy Head of the Security Council Oleg Chernov, whose support and time were generously given from the very beginning of this project. We are particularly grateful for the role Peter Castenfelt played in helping us in Russia. The trust with which he is held by officials at the highest level in Moscow and his knowledge of Russian politics and economics made our Moscow visits especially productive.

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We would also like to extend a special thank you to our commissioned policy paper writers, Jonathan Elkind, Eugene Rumer and Andrew Weiss. We are indebted to them, as we are to many members of the EWI staff for their support. At our Moscow Centre, we would like to thank Russia Country Director Alexei Makushkin, Moscow Centre Director Alexei Boudnitskiy and Moscow Centre staff Alexander Kupriyanov and Vladimir Ivanov. At our New York Center, we would like to thank Project Manager Marisa Robertson-Textor, Head of the Executive Office Kristin Strohmeier and Research Associate Trond Gabrielsen.

The opinions expressed herein represent a consensus of those who have agreed to sign this Task Force Report. They do not necessarily represent the views of the EastWest Institute, the Rand Corporation, Michigan State University, their trustees or the Task Force's funding parties or any of the organizations with which the signators are affiliated. As in any group exercise on a controversial policy topic, not every signator agrees with each point in the text, but rather accepts its general thrust. We trust that this report will advance the cause of peace and stability to which every American and Russian aspires. Finally, we welcome the comments of those reading this study. Any comments sent to the Institute will be shared with the authors and subsequently with the Chairmen and Task Force members.

Sincerely,

John Edwin Mroz  
John Tedstrom  
Sherman Garnett

July 2001

## APPENDIX A: LIST OF TASK FORCE MEMBERS

The following is a list of the Bipartisan Task Force Members. These individuals participated in Task Force meetings and contributed to the findings of the report.

*This is not a list of signatories of the report. For an official list of signatories, please see the insert.*

### CHAIRMEN

**David L. Boren**

Former U.S. Senator (D-OK)  
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**John C. Danforth**

Former U.S. Senator (R-MO)

**Alan K. Simpson**

Former U.S. Senator (R-WY)

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**John Edwin Mroz**

President and Founder  
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**John E. Tedstrom**

Senior Economist  
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Former Chairman  
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**Patricia Cloherty**

Chairman of the Board  
U.S.-Russia Investment Fund

**Timothy Colton**

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Professor of History and International Studies  
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**John Fitzgibbons**

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**Gary Hart**

Former US Senator (D-CO)  
Of Counsel  
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**Stephen Heintz**

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Merrill Lynch Europe, Middle East and Africa

**Carla Hills**

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Hills and Company

**James Hoge**

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**Heyward Isham**

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**George Russell**

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Frank Russell Company and Russell 20-20

**John Shalikashvili**

Center for International Security Cooperation  
Stanford University

**Ernest Stern**

Managing Director  
JP Morgan

**Donald Straszheim**

President  
The Milken Institute

**Stuart Subotnick**

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**John C. Whitehead**

Chairman  
AEA Investors

**Frank Wisner**

Vice-Chairman  
American International Group

**William White**

President  
Charles Stewart Mott Foundation

\*Special thanks are extended to James Billington, Librarian of Congress,  
for his contributions to the Task Force.

**APPENDIX B:  
LIST OF PEOPLE INTERVIEWED IN RUSSIA**

**The Steering Group of the Task Force met with the following people  
on a series of trips to Moscow, Russia in April-July 2001:**

**Aleksandr Arofikin**

Director, Credit Suisse First Boston

**Aleksandr Bessmertnykh**

President, Foreign Policy Association

**Oleg Chernov**

Deputy Head, National Security Council of the  
Russian Federation

**James Collins**

U.S. Ambassador to Russia

**Oleg Dobrodeev**

Chief of VGTRK (All-Russian State Television  
and Radio Company)

**Aleksandr Dzasokhov**

President, Republic of Northern  
Ossetiya-Alaniya

**Robert Foresman**

Executive Director, Dresdner Bank Group,  
Head of Investment Banking in Russia

**Andrei Illarionov**

Economic Adviser to the President

**Sergei Ivanov**

Minister of Defense

**Masha Lipman**

Former Deputy Editor-in-Chief, Itogi Magazine

**Vladimir Lukin**

Vice Speaker, State Duma

**Irina Khakamada**

Vice Speaker, State Duma

**Mikhail Khodorkovsky**

Chairman and Chief Executive Officer, YUKOS

**Yuri Komarov**

Head of the Department of Foreign Relations,  
Gazprom

**Igor Kostikov**

Chairman of the Federal Securities  
Commission of the Russian Federation

**Yevgeny Kozhokin**

Director, Institute for Strategic Studies

**Aleksei Kudrin**

Minister of Finance, Deputy Prime Minister

**Col. Gen. Valeri Manilov**

First Deputy Chief of the General Staff

**Vladimir Mau**

Director, Russian Center for Economic Reforms

**Dmitrii Medvedev**

First Deputy Head of the Presidential  
Administration

**Aleksei Miller**

Chief Executive Officer, Gazprom

**Georgii Poltavchenko**

Presidential Representative to the Central  
Federal District

**Vladimir Putin**

President of the Russian Federation

**Andrei Richter**

President, Media Law and Policy Center

**Julian Schweitzer**

Director, World Bank Russia

**Anton Siluanov**

Director of the Department of Macroeconomic Policy, Finance Ministry

**Vladislav Surkov**

Deputy Head of the Presidential Administration

**Pavel Teplukhin**

President and CEO, Troika-Dialog

**Sergei Vorobyev**

President, Club 2015

**Mattias Warnig**

Geographic Head of the Dresdner Bank Group in the Russian Federation

**Sergei Yastrzhembsky**

Presidential Advisor for Coordination of Information and Analytical Activities

**Mikhail Zadornov**

Head of the Central Bank Subcommittee State Duma

**Aleksandr Zhukov**

Head of the Budgetary Committee, State Duma





## ABOUT THE AUTHORS

**John E. Tedstrom** is a Senior Economist at RAND, which he joined in 1992. He took leave from RAND in 1999-2000 to serve as Director of Russian, Ukrainian, and Eurasian Affairs at the National Security Council. Dr. Tedstrom has a B.A. from DePauw University, an M.A. from Indiana University, and a Ph.D. in Economics and Russian Studies from the University of Birmingham, England. He serves on the Board of Trustees of the International Center for Policies in Kyiv, Ukraine. Dr. Tedstrom's publications include: *Socialism, Perestroika, and the Dilemmas of Soviet Economic Reform* (Westview Press, 1991) and *Planning America's Defense* (RAND, 1998). He currently resides in Washington, DC.

**Sherman W. Garnett** is Dean of the James Madison College of International Affairs at Michigan State University. From 1994 to 1999, Dr. Garnett was a Senior Associate at the Carnegie Endowment for International Peace. From 1983 to 1994, Dr. Garnett spent eleven years in the US Government, most recently as the Deputy Assistant Secretary of Defense for Russia, Ukraine and Eurasia. During his nearly ten years in the Office of the Secretary of Defense, Dr. Garnett worked on a wide variety of security and arms control issues. He served as Director for the Offices of Russia, Ukraine and Eurasia (1992-1993) and European Security Negotiations (1989-1992). Dr. Garnett has published widely in such national and international publications as *Foreign Affairs*, *Foreign Policy*, and the *Washington Post*. His most recent book is a co-authored study for the Trilateral Commission on Central Asia. He is married to Jill and has three children: Sara, Anna, and Patrick. He currently resides in East Lansing, Michigan.

**John Edwin Mroz** is President and CEO of the EastWest Institute, which he founded in 1981. Over 20 years, EWI has grown into a major European-American public policy, action-oriented institute. Mr. Mroz has served as an advisor to more than 30 governments, as well as to the European Commission and Council of Europe. He has received numerous awards for his work, including the Federal Republic of Germany and Romania's highest awards to non-citizens. Mr. Mroz is a graduate of the Fletcher School of Law and Diplomacy, Tufts University and of Notre Dame University. His publications include *Beyond Security* (Pergamon Press, 1980), as well as articles in *Foreign Affairs* and numerous media sources, including in the Russian Federation. He is married to Karen and has three children: Jonathan, Jessica, and Jeffrey. Mr. Mroz currently resides in New York City.

The authors welcome comments and inquiries on this report and may be contacted at [RussiaTaskForce@IEWS.org](mailto:RussiaTaskForce@IEWS.org), or via the addresses listed on the back cover.

## ABOUT EWI

The EastWest Institute (EWI) is an independent European-American non-profit organization, founded in 1981, that works to promote stability, freedom, and prosperity in the transitional countries of Central and Eastern Europe and Eurasia. Its goals are to:

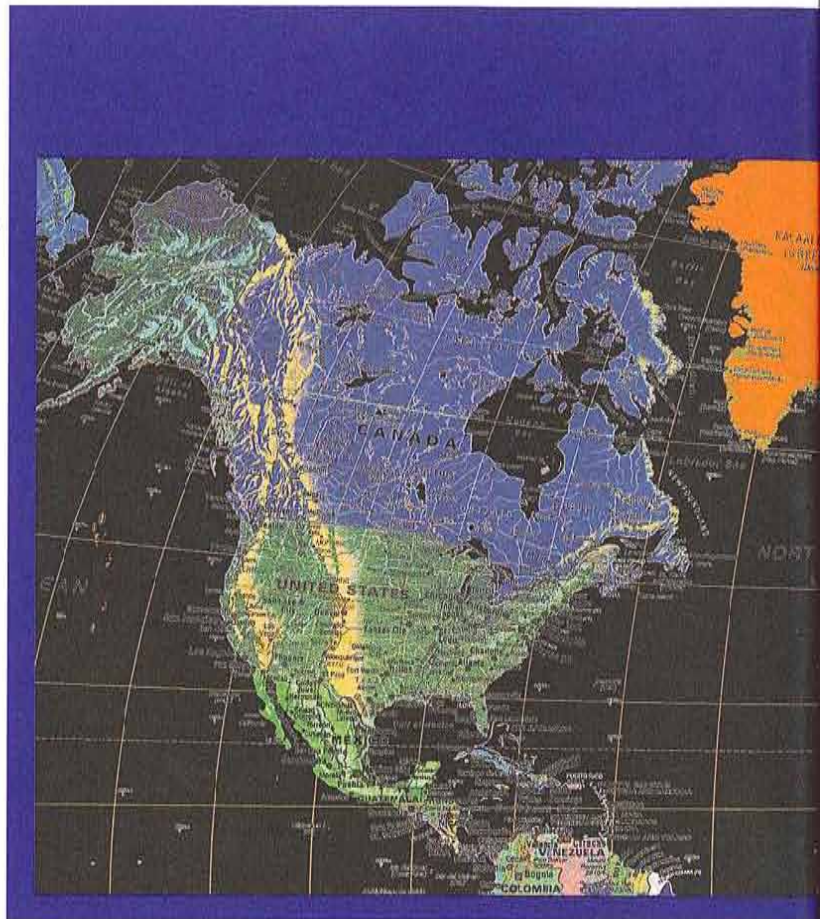
- Defuse tensions that threaten stability and peace
- Strengthen democracy and the rule of law
- Promote market economies in emerging-market nations
- Create new forms of cooperation across borders

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**TOWARD THE COMMON GOOD:  
Building a New U.S.-Russian  
Relationship**

A REPORT OF THE EWI BIPARTISAN TASK FORCE

Chairmen: David L. Boren, John C. Danforth & Alan K. Simpson

**EXECUTIVE  
SUMMARY**

**EASTWEST INSTITUTE**



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## MAJOR FINDINGS:

The Task Force has identified a historic opportunity to put in place a fundamentally new approach to U.S.-Russian relations—one that is not grounded in Cold War thinking or the euphoria and disappointments of the 1990s. Instead, it envisions a new relationship based on principles of mutual respect and shared values. Such a relationship depends on Russia's continuing progress toward democracy and market economics and its further integration into global economic, political, and security institutions.

The Task Force believes that U.S.-Russia relations could be at a dramatic turning point, if both sides choose to seize this opportunity. President Putin's ambitious reform agenda, and the vision and energy of both President Bush and President Putin form the basis of this opportunity.

While there will always be imperfections in transitions as complex and profound as the one Russia is experiencing today, the basic signals from Russia are encouraging over the longer term. The United States, from its position of prosperity and strength, can afford to make a bet on continued positive change in Russia. How Russia manages issues such as human rights, free speech, and the sovereignty of its neighbors will have a strong influence on America's ability to adopt this new approach.

President Putin's reform agenda, if implemented in ways consistent with democratic principles, has the potential to accelerate Russia's market and democratic development, attract foreign capital, broaden the range of mutual interests between Russia and the West and promote Russia's integration into global institutions, including the WTO.

A new relationship between the U.S. and Russia could provide the basis for creating new multilateral mechanisms that more effectively address the problems posed by traditional as well as new threats, such as terrorism, the proliferation of nuclear materials and weapons of mass destruction, the spread of infectious diseases and narcotics trafficking.

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## POLICY RECOMMENDATIONS:

Presidents Bush and Putin should explore ways of accelerating the dialogue on our security relationship with a focus on strategic nuclear issues in order to replace the fatalistic logic of mutual assured destruction. An early, frank dialogue on threat perceptions is essential to broader success in this area. The presidents ought to take the opportunity afforded by their upcoming meetings at the G-8 in Italy and at the Bush ranch in Crawford, Texas, to explore their visions of the future security environment.

The U.S. and Russia should make an up-front commitment to an interim nuclear relationship that features a mix of dramatically lower levels of offensive weapons and defensive systems.

The U.S. should encourage Russian participation in international efforts to stabilize difficult regions, such as the Balkans. The overall success in Bosnia and Kosovo of Russian military cooperation with NATO forces, as well as collaboration on Nagorno-Karabakh, is a reminder of what the two sides can do together, and opens up the possibility of further collaboration in places such as Macedonia.

Russia's work toward quick accession to the WTO has encouraged the most promising set of reforms. The U.S. should engage Russia in ways that support these reforms and accelerate the accession process.

U.S. policy toward Russia should be couched within our broader European policy framework. We should support close and active political and economic relationships between Moscow and the European Union (together with the EU accession states), as well as European and Euro-Atlantic institutions.

The U.S. and Russia should pursue a policy to support the independence of Russia's neighbors, including Ukraine, Georgia and the other countries of eastern Europe and the Caucasus, which can help promote a secure, stable and increasingly "European" region that will be advantageous to Russia and the entire region.

The U.S. should significantly expand investments in programs that expose Russians to US and Western businesses, including an expansion of exchanges of Russians studying in U.S. business schools and exchanges that introduce Russian lawmakers, journalists and educators to U.S. businesses.

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## SIGNATORIES OF THE REPORT

### CHAIRMEN

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**Gary Hart**

Former US Senator (D-CO)  
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