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**RUSSIAN AND AMERICAN COOPERATION IN
POWER SECTOR RESTRUCTURING AND
PRIVATIZATION
WORK PLAN**

**NIS Institutional Based Services Under the Energy
Efficiency and Market Reform Project
Contract No CCN-Q-00-93-00152-00**

Electric Power Sector Restructuring and Privatization

Delivery Order No 1

Prepared for

U S Agency for International Development
Bureau for Europe and NIS
Office of Environment, Energy and Urban Development
Energy and Infrastructure Division

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Work Plan for Working Group 1 Restructuring and Privatisation

The objective of Working Group 1 is to review and recommend changes to the existing plans for reorganising and privatising the Russian power sector to enable it to function efficiently and effectively in a market economy. These recommendations must be consistent with Russia's general market reform and privatisation policies.

SCOPE OF WORK

To accomplish its objective, Working Group 1 must perform the following activities:

1. Become familiar with the mandates of all other working groups and ensure that their work plans are consistent with and supportive of the work plan for Working Group 1.
2. Develop a solid working knowledge of the overall market reform and privatisation policies and plans of Russia.
3. Undertake a comprehensive review of the current and planned organisation of the power sector and of the existing plans for its privatisation.
4. Organise and sponsor a workshop on "The Russian Power Sector Organisation and Privatisation Plans," to provide members of all working groups an overview of the alternatives and key decisions that must precede privatisation of the power sector.
5. Organise and sponsor a seminar on "The Power Sector in a Modern Market Economy," to provide senior Russian officials with a common base of information on this subject.
6. Describe and assess the alternative structural models and ownership forms for organising the Russian power sector, and make recommendations regarding which should be adopted.
7. Describe and assess both the regulatory and market-based alternatives for pricing electricity at the wholesale level, including the development of a competitive wholesale power market, and make recommendations regarding which should be adopted.
8. Describe and assess the alternative regulatory methodologies for pricing electricity at retail level, and make recommendations regarding which should be adopted.
9. Organise site visits for key Russian officials and consultants to familiarize them with electric power system planning and operation in Western countries.

- 10 Participate in workshops and seminars with RAO and other Russian officials to assist them in making decisions regarding modifications to the existing proposal for power sector reorganisation and privatisation
- 11 Assist RAO officials with producing and revising a comprehensive description of the desired long-term structure and organisation of the power sector and an implementation plan for managing the transition from its current state to the long-term objective
- 12 Provide analytical support and policy guidance to Working Group 2 in its efforts to draft legislation required to put in place the legal framework needed to make possible implementation of the final privatisation proposal

The initial activities of the US members of the working group will be to familiarize themselves with Russia's overall program for converting to a market economy and privatising its enterprises. In addition, they will thoroughly review the Russian power sector and existing plans for its privatisation.

The first task directed at modifying existing privatisation plans will be to develop and screen a comprehensive set of structural models to choose a small subset of structures that are most suitable for adoption in Russia. This analysis will evaluate the options on the basis of their effect on the efficiency and effectiveness of both the day-to-day operation of the power system as well as the planning and procurement of the physical plant needed to meet future electricity demand.

A closely related issue will be that of ownership forms, i.e., which component enterprises are to be privately-owned and which (if any) are to remain wholly- or majority-owned by the State. By mid-December the working group will produce a report examining these two issues and recommending one or two structural models and complementary ownership schemes for further consideration.

In mid-January the working group will sponsor a workshop to provide the other working groups with an overview of the basic alternatives for reorganising the power sector and of the key decisions that must precede its privatisation. The latter half of the workshop will be committed to discussing the working group's report on structural models and ownership. We anticipate that the Coordinating Committee will decide these two issues the end of January.

From February through June, Working Group 1 will examine and assess alternative ways of organising Russia's wholesale power market. Parallel efforts will be undertaken to focus on the establishment of a competitive wholesale market and on alternative ways of establishing a regulated wholesale power market which bases prices on generation cost of service. These two efforts will produce competing reports addressing wholesale pricing by early April. Each report will assess the incentives for economic efficiency that its respective approach

offers and will apply other selection criteria. It is anticipated that the Coordinating Committee will choose, by the end of April, one of these wholesale market forms as the long-term solution to be adopted in Russia. In addition, it will choose some combination of regulation and market-based pricing for adoption during the transition period from the current situation to the long-term goal. Following these decisions, the pricing approaches chosen will be further refined.

Retail pricing is the final issue addressed. The Working Group will produce a report describing alternative retail pricing methodologies by mid-May. The report will recommend the adoption of one retail pricing methodology that is consistent with and supportive of the wholesale pricing approach adopted and also with the overall goals of privatisation. We anticipate that the Coordinating Committee will select a retail pricing methodology by the end of May.

During the month of June Working Groups 1 and 5 will organise and sponsor a seminar in Moscow on "The Power Sector in a Modern Market Economy." Its purpose will be to make senior Russian officials aware of the important economic role the power sector plays and the value of privatising it in a market economy. This seminar will be held prior to the release of RAO's proposal for privatising the sector (discussed next).

By the end of June Working Group 1, with the assistance of Working Groups 2 and 6, will prepare a complete proposal for reorganising Russia's power sector. The proposal will combine and integrate the earlier decisions made regarding structure, ownership, wholesale and retail price regulation. After reviewing and approving the proposal, the Coordinating Committee will circulate the proposal for comment to those governmental bodies and other entities selected by RAO. Based on the comments received, Working Group 1 will revise the proposal, with the assistance of Working Groups 2 and 6, by the end of July.

Working Groups 1 and 2 will prepare an implementation plan for managing the transition from Russia's current power sector organisation to its final form. The initial draft of the plan will be completed by the end of September.

During the last quarter of 1994 Working Group 1 will provide assistance in revising and refining the proposal, including its implementation plan, assessing its impacts on various groups within the Russian economy, and promoting its adoption. It will also provide inputs to Working Group 2 so that legislation can be drafted to create the legal framework needed to implement the finalized proposal for privatising the power sector.

The specific tasks, responsibilities and schedule of deliveries is described in the next section.

TASKS, RESPONSIBILITIES AND DELIVERY SCHEDULE

The scope of work for Working Group 1 will be subdivided into 6 basic tasks and a number

of supporting subtasks. These are described in the following table, along with responsibilities and the approximate dates for deliverables.

Table 1
Schedule of Tasks for Working Group 1

Task & Sub-tasks	Description	Responsible Parties	Completion Date
1	Background research		24 Jan 1994
1 1	Review materials and interview Russian officials to develop a working knowledge of Russia's market reform and privatisation program	US	12 Dec 1993
1 2	Review documents describing the Russian power sector, including both its physical characteristics and its organisational, regulatory and managerial aspects	US	12 Dec 1993
1 3	Review existing plans for privatising the Russian power sector	RAO & US	12 Dec 1993
1 4	Visit a remote regional utility	US	21 Jan 1994
1 5	Visit Mosenergo	US	24 Jan 1994
1 6	Visit the Central Dispatch Center	US	24 Jan 1994
2	Assist RAO in choosing one or two structural models and complementary ownership forms for further development		15 Jan 1994
2 1	Prepare a report describing the advantages and disadvantages of alternative structural models and ownership forms	US	24 Dec 1993
2 2	All working group co-chairmen and all Russian consultants review structure/ownership report	RAO & US	28 Jan 1994
2 3	Conduct a work shop for all working groups to provide an overview of the basic options available to prepare the power sector for privatisation	US	28 Jan 1994

Table 1
Schedule of Tasks for Working Group 1

Task & Sub-tasks	Description	Responsible Parties	Completion Date
2 4	Workshop in Moscow to discuss the report on structure and to choose the structural models to be further developed	RAO & US	28 Jan 1994
3	Assist RAO in choosing an approach to organising and regulating Russia's wholesale power market		29 Apr 1994
3 1	Senior working group members visit the National Grid Company and a distribution utility in the UK	RAO & US	18 Mar 1994
3 2	Senior working group members visit two interconnected power pools in the US	RAO & US	15 Apr 1994
3 3	Prepare a report describing the alternatives for creating a competitive generation market in Russia	US	22 Apr 1994
3 4	Prepare a report describing the regulatory alternatives for setting wholesale power prices in Russia based on generation cost of service	US	22 Apr 1994
3 5	All working group co-chairmen and all Russian consultants review the wholesale market reports	US & RAO	29 Apr 1994
3 6	Workshop in Moscow to discuss the alternatives for organising the wholesale power market in Russia and to choose one of the alternatives for further development	RAO & US	29 Apr 1994
4	Assist RAO in choosing a retail pricing methodology		31 May 1994
4 1	Produce a report on retail pricing options	US	15 May 1994

Table 1
Schedule of Tasks for Working Group 1

Task & Sub-tasks	Description	Responsible Parties	Completion Date
4 2	All working group co-chairmen and all Russian consultants review the retail pricing report	RAO & US	31 May 1994
4 3	Workshop in Moscow to discuss retail pricing and to choose one or more regulatory methodologies for further development	RAO & US	31 May 1994
5	Produce an comprehensive plan for reorganising and privatising the Russian power sector		30 Dec 1994
5 1	Conduct a seminar in Russia for senior Russian officials regarding the key role of the power sector in a privatised market economy	US	3 Jun 1994
5 2	Produce a comprehensive description of the long-term organisation with support from other work groups	RAO & US	15 Jun 1994
5 3	Distribute the proposal to outside government agencies for comment	RAO	30 Jun 1994
5 4	Workshop in Moscow to modify the proposal in response to comments received	RAO & US	30 Jul 1994
5 5	Prepare an implementation plan for managing the transition to the long-term organisation with support from Working Group 2	RAO & US	15 Sep 1994
5 6	Distribute proposed implementation plan to outside government agencies for comment	RAO	30 Sep 1994
5 7	Workshop in Moscow to modify the proposed implementation plan in response to comments received	RAO & US	30 Oct 1994

Table 1
Schedule of Tasks for Working Group 1

Task & Sub-tasks	Description	Responsible Parties	Completion Date
6	Provide analytical support as needed to further revise the privatisation proposal, estimate its impacts on various parties and support the drafting of legislation	RAO & US	30 Dec 1994

GROUP TWO IS MISSING

SECURITIES (FINANCIAL MARKET) WORKING GROUP
1993 - 1994

OBJECTIVES

The basic function and objectives of this group will be to recommend specific actions required to prepare and effectively integrate the power sector of Russia into national and international securities markets. An important complementary responsibility of this group will be to influence the formation of financial markets in Russia to assure that they serve the needs of the power sector.

The members of the working group recognize that two of the keys to attracting and maintaining capital will be improved accounting standards and improved management of the existing capital of the power sector. Therefore the scope of work has been expanded to specifically address these issues early in phase 1b of this project.

SCOPE OF WORK

- (A) Become familiar with the mandates and work plans of all other working groups and maintain effective horizontal communications with them as required to harmonize conclusions and recommendations.
- (B) Drawing on information gathered and developed by the privatization plan working group, develop a solid working knowledge of overall market reform and privatization policies and plans of Russia. This shall include participation in two or more seminars and presentations that will be organized by the Privatization Plan Working Group.
- (C) Undertake a comprehensive review of current accounting standards for the Russian and Western power sectors and recommend new accounting standards for the Russian power sector.
- (D) Undertake a comprehensive review of current financial management practices and recommend an appropriate financial management organization and procedures for RAO.
- (E) Undertake a comprehensive review of present and planned securities (financial) markets in Russia and Russian plans to access/join international markets. These reviews shall include reviews of present and planned legal and regulatory frameworks for national financial markets and Russian power sector participation in international markets.
- (F) Taking into account recommendations received from other working groups and the unique circumstances and economic policies of Russia, recommend the most appropriate legal and regulatory framework required to assure the sector's ability to attract and

maintain an adequate supply of capital

(G) Develop a program for the early integration of Russia's power sector into both national and international financial markets

(H) Identify the need for and assist in the planning and organization of the travel of Russian executives, managers and specialists to the United States and other countries to become familiar with and gain experience in financial operations and financial market aspects of the electric power sector in market economies

(I) Draft reports and other documents and organize special meetings and two or more seminars at appropriate times as required to achieve the objectives and disseminate the results of the working group's efforts

KEY TASKS, RESPONSIBILITY AND SCHEDULE

KEY TASK	RESPONSIBLE	DUE DATE
1 Accounting and Financial Disclosure Tasks		
1 1 Prepare a summary of Russian accounting standards for the power sector in response to a questionnaire to be prepared by the American side	RAO	Dec 15
1 2 Convert RAO Sept 30 1993 financial statements to conform with Western standards	US	Jan 31
1 3 Prepare a summary of differences between Russian and international accounting standards for the power sector	US	Jan 31
1 4 Recommend new accounting standards for the Russian power sector	US/RAO	March 31
1 5 Recommend financial disclosure standards for dealing with outside parties	US/RAO	March 31

2. Asset Management Tasks

- 2 1 Review current capital structure, financing arrangements and cash management policies and procedures for RAO US/RAO Feb 28
- 2 2 Recommend appropriate cash management policies, procedures and organization structures for RAO, considering the constraints of the Russian banking system inc, including steps, a schedule and budget for implementation for consideration by the coordinating committee US/RAO March 31
- 2 3 In an effort to resolve the current liquidity problems, gain a thorough understanding of the proposed Russian debt swap for bonds and recommend a strategy for RAO RAO/US Feb 1
- 2 4 Prepare an overview of the use of internal and external auditors for use by RAO in determining appropriate policies for the Russian power sector US Feb 28

3. Securities Market Tasks

- 3 1 Drawing upon the above work and the work of other working groups prepare an overview of RAO including financial, organizational structure and legal and regulatory environment for discussion with domestic and foreign sources of debt and equity, both private and public US/RAO April 30
- 3 2 Undertake a comprehensive review of the present and planned financial markets in Russia US/RAO March 31
- 3 3 Prepare an overview of Western capital markets and their operations vis a vis the power sector including a review of key analytical factors used by investors and analysts US March 31

- | | | |
|--|--------|----------|
| 3 4 Visit with key financial intermediaries and power sector investors in Moscow, New York, London, Paris and Frankfurt to present and discuss review of RAO and solicit input as to legal, regulatory and financial changes required to elicit investor interest and to familiarize Russian executives, managers and specialists in financial operations and financial market aspects in market economics | US/RAO | June 30 |
| 3 5 Recommend a strategy for securities management in a market economy | US/RAO | Aug 31 |
| 3 6 Based upon all of the above make recommendations to Working Group 2 on the legal and regulatory framework required to attract and maintain an adequate supply of capital | US/RAO | Sept 30 |
| 3 7 Recommend a program for integration of Russia's power sector into both national and international financial markets, including steps, a schedule and budget for implementation | US/RAO | Sept 30 |
| 4 Training Tasks. | | |
| 4 1 Prepare and present a seminar on recommended accounting and financial disclosure standards for 25 to 30 senior power sector financial managers in conjunction with Working Group 5 | US/RAO | June 15 |
| 4 2 Prepare and present a seminar based upon the summary of the operations of Western debt and equity markets for 25 to 30 senior power sector executives in conjunction with Working Group 5 | US/RAO | April 15 |
| 4 3 In conjunction with Working Group 5, prepare and present a seminar in shareholder relations /corporate governance issues for 50 senior power sector executives | US | May 15 |
| 4 4 Develop a library of appropriate financial | US | on going |

literature for RAO

5. Coordination and Reporting Tasks

- | | | | |
|-----|--|--------|-----------|
| 5 1 | Prepare monthly progress reports in the format required by USAID | US/RAO | Monthly |
| | | US/RAO | Quarterly |
| 5 2 | Hold Quarterly progress meetings of the entire working group alternating between Moscow and Washington | | |
| 5 3 | Prepare final report on activities, recommendations and lessons learned and dissolve | US/RAO | Dec 15 |

STAFFING

US Staff		Man-months
David Reed		4
Tim O'Neill		8
Senior Power Sector Accountant		4
Power Sector Corporate Finance Specialist		6
Corporate Finance Consultant		10
Cash Management Specialist	4	
Western Trained Russian Accountant	4	
Total		38
USAID Financed Russian Staff		
Russian Banking Specialist		4
Russian Corporate Finance Assistants		10

Russian Accountant	4
Total	18
Grand Total Man-Months	56

RAO Designated Staff

Borisov, Yevgeny As Required

Senior Specialists As Required

WORK PLAN WORKING GROUP ON INVESTMENT PROMOTION

OBJECTIVES

To recommend actions and strategies to achieve an early in-flow of private national and international investment in the power sector. An emphasis will be placed on the use of private power as a mechanism for attracting investment. The working group will also work to develop investment planning and policy procedures that will be useful in the development of corporate strategies for attracting investment.

SCOPE OF WORK:

The basic function and responsibility of this group will be to recommend specific actions required to achieve an early in-flow of private national and international investment in the power sector. It is recognized that independent power plants may likely offer the most attractive mechanism for attracting early private investments in the sector, however, the group will not limit itself to this option. The work of this group must be carefully sequenced and closely coordinated with the work of the legislation and regulatory and financial markets working groups.

In June, the Russian side asked that the American side take the lead in preparing draft documents required of this group.

Specific functions of the working group include the following:

- (A) Develop and recommend a final work plan for the working group.
- (B) Recommend any changes that might be needed in the pre-approved Terms of Reference, make-up, and staffing of the work group.
- (C) Become familiar with the mandates and work plans of all the other working groups and maintain effective horizontal communications with them as required to harmonize conclusions and recommendations.
- (D) Drawing on information gathered and developed by the first working group, develop a solid working knowledge of overall market reform and privatization policies and plans of Russia. This shall include participation in the two seminars that will be organized and sponsored by the privatization plan working group.
- (E) Undertake a comprehensive review of the present assets, present and planned legal and financial structures and projected investment needs of the sector.

- (F) Identify the various short, medium and long-term options available for raising capital expected to be required for the improvement and expansion of the power sector and its conversion to a market economy This shall include national and international investments in independent power generation plants as well as in RAO EES Rossi and the 72 regional electric power companies being established
- (G) Recommend the options that should be considered
- (H) Draft reports and other documents and organize special meetings and additional seminars as required to achieve the objectives and disseminate the results of the working groups efforts
- (I) Identify the need for and assist in the planning and organization of the travel of Russian executives, managers and specialists to the United States and other countries to become familiar with and gain experience in the ownership, organization and operation of the electric power sector in market economies
- (J) Recommend the strategies, steps, schedule and budget required to implement relevant decisions taken

KEY TASKS, ACTIVITIES, PERSONNEL REQUIREMENTS AND SCHEDULE

TASK 1 To recommend legal and regulatory approaches to providing for investment in the power sector, with an emphasis on foreign investment This activity will be conducted in coordination with the working group on legislation

Activity Collect and submit appropriate reference materials regarding existing and proposed legislation and laws on foreign investments

Responsibility	Rao EES Rossi and Latham & Watkins
Deliverable	Package of reference documents
Date	November 30, 1993

Activity Collect and submit reference materials and examples of investment incentives that have been used in recent power sector project investments This will include examples from the United States and selected other countries

Responsibility	Hagler, Bailly and K&M Engineering
Deliverable	Briefing book with reference materials translated into Russian
Date	November 30, 1993

Activity Develop recommendations and options regarding changes and modifications of existing laws regarding foreign investments in the power sector

Responsibility Rao EES Rossi, Hagler, Bailly, K&M Engineering and Latham & Watkins

Deliverable Preparation of materials for a Working Group Meeting on "Investment Options in the Power Sector"

Date January 1993

Responsibility Hagler, Bailly, K&M Engineering and Latham & Watkins

Deliverable Concept Paper on Recommended Options on Investment in the Power Sector

Date March 31, 1993

Responsibility RAO EES Rossi

Deliverable Submission of legislative recommendations to relevant Russian authorities

Date No later than October 31, 1994

TASK 2 Procedures and policies for planning and evaluating investment projects and capital expenditures

Activity Transfer available materials on methodologies, guidelines and techniques for evaluating and appraising investment proposals. Be certain to include methodologies that account for inflation

Responsibility Hagler, Bailly and K&M Engineering

Deliverable Reference materials, briefing books, computer models, and manuals translated into Russian

Date January 31, 1994

Activity Provide an overview of state-of-the-art methodologies and techniques on policies and planning for investment and capital expenditures

Responsibility Hagler, Bailly

Deliverable Briefing book and Discussion Paper

Date March 31, 1994

Activity Provide reference materials on existing investment policies and planning techniques currently used by RAO EES Rossi

Responsibility RAO EES Rossi

Deliverable Reference materials in Russian

Date March 31, 1994

Activity Development and recommendations for modifications to RAO EES Rossi investment planning procedures and policies

Responsibility RAO EES Rossi and Hagler Bailly
Deliverable Memorandum on Options and Recommendations
Date July 31, 1994

Seminar Topic Evaluation of Power Sector Investment Projects

Responsibility RAO EES Rossi and IIE with contractor assistance as necessary
Deliverable Two - three day seminar session to be held in Russia
Date Second Quarter 1994

Seminar Topic Investment Policy and Planning

Responsibility RAO EES Rossi and IIE with contractor assistance as necessary
Deliverable Two-three day seminar session to be held in the United States
Date Second or Third Quarter 1994

TASK 3 Begin the development of four investment projects including a new thermal power plant, the Beloporogeskaya Hydro Power Plant, the rehabilitation of an existing thermal power plant and an inter-utility transmission power line project

Activity Selection of projects and submission of existing technical and economic data on the projects

Responsibility RAO EES Rossi
Deliverable Reference materials on four projects
Date February 28, 1994

Activity Review of existing information on four projects and identification of additional work that will be required to complete a pre-appraisal of each project

Responsibility K&M Engineering and Joseph Technology Corporation Inc
Deliverable Workplan and Budget for Pre-Feasibility Studies
Date July 31, 1994

Activity Conduct technical, economic, financial and management evaluation of four investment projects Develop a strategy for attracting foreign investment in each project

Responsibility RAO EES Rossi and affiliated institutes, K&M Engineering, Joseph Technology Corporation Inc , Hagler Bailly and Bankers Trust

Deliverable Four pre-feasibility studies and Memorandums on Strategy for Attracting Investment Capital

Date September 1994 - December 1994

TASK 4 Development of relationships with investor groups This will be done in coordination with the Working Group on Finance and Securities

Activity Develop a network of potential investors

Responsibility RAO EES Rossi, Hagler Bailly

Deliverable Monthly Reports of Contacts Made

Date Ongoing

Activity Prepare RAO EES Rossi to present itself and its projects to investor groups

Responsibility RAO EES Rossi, Hagler Bailly, Bankers Trust, Price Waterhouse

Deliverable Briefing materials and meetings

Date November - December 1994

Activity Facilitate introductions to investor groups

Responsibility RAO EES Rossi, Hagler Bailly, Bankers Trust, Price Waterhouse

Deliverable Conference on Investment in the Electric Power Sector or a series of individual meetings with investors, to be determined

Date January 1995

STAFFING PLAN

Co-chairman	116 days
Private Power Specialist	61
Sr Legal Specialist	6
Jr Legal	6
Utility Planning	45
Technical Engineers	250
Financial Analyst	80
Sr Investment Banker	30
Jr Investment Banker	56
Conference Planners	40
 Total Level of Efforts	 690

TRAVEL SCHEDULE

<u>Trip and Sub-Task Number</u>	<u>Persons and Destinations</u>	<u>Dates</u>
Task 1 and planning for Task 2 and 3	Smith, K&M Engineering Moscow, Russia	January
Task 2 and planning for	Smith, K&M Engineering Moscow, Russia	March
Task 2 workshop and seminar	Smith, K&M Engineering Moscow, Russia	2 Q 94
Task 2 workshop and seminar	15 people selected by working group co-chair United States	3 Q 94
Task 3 - pre-feasibilities	Two teams of three persons will travel to Moscow and conduct site visits Smith will go on one site visit Investment banker will	July, August September