

MEMORANDUM OF DETERMINATIONS

Claim of St. Michael Enterprises d.o.o for Wrongful Calling of a Bid Bond
Republic of Serbia
Contract of Insurance No. F360

Public Version

I. Claim

St. Michael Enterprises d.o.o., a company organized under the laws of the Federal Republic of Yugoslavia and the Republic of Serbia and existing under the laws of the Republic of Serbia (“SME”), purchased a policy of bid guaranty insurance against the wrongful calling of its bid bond in connection with the privatization of 70% of the shares of Jelen Do (“Jelen Do”), a producer of lime and stone aggregates located in Jelen Do, Serbia.

SME participated in the privatization auction process (the “Tender”) and posted the required bid guaranty in the amount of US\$150,000 (the “Bid Bond”). SME was selected as the winner of the Tender, and entered into an Agreement for Sale and Purchase of the Jelen Do shares (the “SPA”) that required, among other things, payment of the purchase price and the posting of performance bonds within 20 days of the execution of the agreement. Before the termination of the 20-day period, SME sought a time extension to make the payment and post the performance bonds; essentially, an amendment to the SPA. The request was refused, SME failed to make the payment and post the performance bond, and the Privatization Agency administering the Tender called SME’s bid bond in accordance with the Tender rules and the terms of the Bid Bond itself.

SME claims that the Privatization Agency’s denial of its request to amend the SPA to extend the period for paying the purchase price and posting the performance bonds was the product of corruption and that, therefore, the Bid Bond was wrongfully called. Despite repeated requests from OPIC to do so, SME has never articulated a theory as to how the Privatization Agency’s refusal, for whatever reason, to amend an SPA freely and knowingly entered into by SME, and its subsequent actions in accordance with existing agreements, constitutes a wrongful calling under the terms of its OPIC insurance.

II. Factual Background

. . . SME [was formed] in 1991 to participate in the privatization opportunities becoming available in the Republic of Serbia that, at that time, continued to exist with the Republic of Montenegro as what remained of the Federal Republic of Yugoslavia. Jelen Do was one of a number of socially owned – that is, state owned – enterprises to be wholly or partially privatized.

Tender Process

The Privatization Agency of the Republic of Serbia issued its Public Invitation for the Participation in a Tender Process for the Acquisition of a Controlling Interest in Jelen Do, including, among other things, its “Instructions to Bidders – Tender Rules” (the “Tender Rules”) on September 16, 2002. In response, SME teamed with the Montenegrin entity Luka Bar, the “Port of Bar”, with which SME had a consulting relationship, to submit a bid to purchase Jelen Do. The bid provided for, among other things: (a) a 97% - 3% split between SME and Luka Bar of the 70% of the Jelen Do shares to be purchased in the privatization; (b) a purchase price of US\$3,700,000 for the Jelen Do shares; (c) covenants to make certain investments in the infrastructure of the Jelen Do project (the “Investment Commitment”); (d) covenants to enact a defined social program of worker benefits, including housing (the “Social Program”); and (e) the posting of performance bonds to guaranty the performance of the Investment Commitment and the Social Program, in amounts to be agreed upon at the time of execution of the SPA.

Bid Bond

Simultaneously with the submission of its bid, and in accordance with the Tender Rules, SME submitted the Bid Bond. The Bid Bond was issued by Raiffeisen Bank Jugoslavija a.d. on March 24, 2003. In keeping with the Tender Rules, the Bid Bond provided that Raiffeisen would pay the Privatization Authority under the guaranty upon written request for payment and its written confirmation stating that:

- (i) [SME] has withdrawn its bid after the deadline for submission of bids and during the specified period of bid validity; or
- (ii) [SME] is liable under the Confidentiality Undertaking which it signed as a condition of receiving the Tender Documents and participating in the Tender; or
- (iii) [SME] refuses to proceed with the Tender procedure, if selected by the [Privatization Agency] to proceed in negotiations[; or]
- (iv) [SME], after having been notified of acceptance of its Bid during the period of bid validity:
 - a) has failed, or has refused to execute the [SPA], if required[;] or
 - b) has failed to vote its share capital at a general assembly of [Jelen Do] as required for closing of the [SPA]; or
 - c) has failed, or refuses to furnish the performance security in accordance with the tender conditions; or

- d) has failed to pay the purchase price for the share capital in accordance with the [SPA].

For the winner of the Tender, the Bid Bond would remain in force until the earlier of either (a) the consummation of the Tender, including the closing of the SPA and the presentation of a performance guaranty in accordance therewith; or (b) the termination of the unconsummated SPA.

Winning Bid; Calling the Bid Bond

The Privatization Agency selected the SME-Luka Bar consortium as the winner of the Tender. The parties entered into the SPA as of June 9, 2003, pursuant to which SME was required to post performance bonds in the amounts of US\$10,500,000 for the Investment Commitment, and US\$800,000 for the Social Program. The SPA provided that SME was to pay the full purchase price of US\$3.7 million and post performance bonds totaling US\$11.3 million not later than July 7, 2003.

[SME] has suggested that it was inappropriate, at least, for the Privatization Agency to have insisted on performance bonds covering the full amount of the proposed Investment Commitment and Social Program in negotiating the SPA. [It] asserted that no other winning bidder in a privatization had been required to do so. That said, SME has presented no evidence that this was any more than a matter of the Privatization Agency driving a hard bargain and SME accepting it. SME knowingly entered into the SPA with those provisions, and there has been no suggestion that the SPA itself is invalid.

On July 1, SME requested a 20-business day extension of the deadline for payment of the purchase price and posting of the performance bonds. On July 7, the Privatization Agency rejected the request for an extension. SME did not deliver either the purchase price or the performance bonds on July 7 or at any time thereafter. On July 11, the Privatization Agency called the Bid Bond.

Allegations of Corruption and Other Illegality

SME has asserted from the beginning that the decision to deny its request for an extension was the result of corruption and other illegal maneuvering on the part of the Privatization Agency officials tasked with responding to the request. The details of the corruption allegations have changed over time. . . .

On July 22, 2005, SME's counsel produced to OPIC a package that included more specific allegations. The package included a written statement by the general manager of Jelen Do, who was a member of the committee responsible for choosing the Tender winner (the "Tender Committee"). The general manager asserted that the procedure for voting on SME's extension request was irregular and illegal and that, despite pressure exerted on him by the director of the Privatization Agency, he did not vote on the matter. Nevertheless, the record of the Tender Committee reflected that he had voted to oppose the requested extension, and his

requests to have the record corrected were ignored. SME's counsel refers to additional information in support of the proposition that the Tender Commission did not deny the extension request by a legal vote, and that the denial of the request was fraudulent and illegal.

For the purposes of its analysis of the SME claim, and regardless of the evolution of the claimant's assertions, OPIC may assume that the facts as set forth in the July 22, 2005 package are true.¹

No Demonstration of Ability to Pay

. . . SME [informed OPIC that it had] requested the extension to purchase the Jelen Do assets and post the performance bonds because [it] had not yet obtained the financing to fulfill those obligations. There has been no subsequent communication to OPIC suggesting that SME could have met those obligations either at that time or at any time thereafter.

SME Self Help

In communications between August 2003 and June 2005, SME informed OPIC that it was taking various actions in Serbia, ranging from litigation to negotiation with government authorities, to be made whole. Only in late 2006 did SME, through its counsel, inform OPIC that SME's self help efforts had been unsuccessful and were terminated, and that it was finalizing its claim under the insurance contract.

III. The Contract

SME and OPIC entered into OPIC Contract of Insurance No. F360, a policy of bid guaranty insurance against wrongful calling (the "OPIC Contract"), as of March 24, 2003.

Scope of Coverage

The Scope of Coverage set forth in Section 2.01 of the OPIC Contract, as modified in Section 6.01, provides that:

Compensation is payable, subject to the exclusion..., limitations..., and adjustment..., if the bid guaranty or any portion thereof is called by the buyer: 1) in violation of the terms and conditions governing the posting and calling of the bid bond as set forth in the tender rules...; and 2) the Insured is not in default of its obligations under the tender.

¹ As will be made clear in Section IV, Determinations Under the Contract, OPIC may also assume that the original allegations of corruption are true. Neither set of facts leads to the conclusion that SME has a valid claim under the insurance contract.

Exclusion for Inability to Pay

The following exclusion, set forth at Section 6.09 of the OPIC Contract, is of particular relevance:

Notwithstanding any other provision in this policy to the contrary, no compensation shall be payable under this policy if the bid guaranty or any portion thereof is called by the buyer due to the Insured's inability to obtain financing for the project in the form or amount represented in the offer at the date of submission.

Coverage Amount

The OPIC Contract provides for 90% coverage of the US\$150,000 Bid Bond, with a coverage amount of US\$135,000.

IV. Determinations Under the Contract

A plain reading of the OPIC Contract demonstrates that SME is not entitled to compensation from OPIC. The Privatization Agency was within its rights to call the Bid Bond and, in any event, SME's reason for seeking extension to close the SPA and post the performance bonds – that it did not have the funds to do so – falls within the exclusion at Section 6.09 of the OPIC Contract.

No Wrongful Calling

SME knowingly and voluntarily executed an SPA that required it to pay a purchase price of US\$3.7 million and post performance bonds totaling an additional US\$11.3 million by July 7, 2003. As the closing date approached, SME asked the Privatization Authority to amend the SPA to postpone the closing date. The Privatization Authority refused to do so. After the passage of the July 7 closing date without SME having made the required payments, the Privatization Authority called the Bid Bond in accordance with Section 21 of the Tender Rules² and corresponding provisions of the Bid Bond.

In its communications with OPIC, SME has suggested that the alleged corruption that resulted in the Privatization Authority's refusal of SME's request to amend the SPA and extend the closing date is the source of a valid claim. That does not appear to be the case. The Privatization Authority was under no obligation to amend a valid contract merely because SME asked that it do so. It could have denied SME's request for any reason or for no reason, so the character of the Privatization Authority's internal deliberations is irrelevant. Accordingly, even

² Section 21 of the Tender Rules reads, in pertinent part, "The Bid Bond shall be cashed on behalf of the [Privatization Authority] according to the following conditions:... the Bidder, after having been notified of acceptance of its Bid during the period of bid validity:... has failed to pay the purchase price for the share capital in accordance with the [SPA]."

if we assume that the allegations of corruption are true, the Privatization Authority was not exceeding its rights or authority to call the Bid Bond upon SME's default. The presence or absence of corruption has no bearing on the analysis of this case.

It is worth noting here OPIC counsel has repeatedly asked both SME and its outside counsel to address the specific argument that, since the Privatization Agency had no obligation to amend the SPA or to justify its decision to SME, the alleged corruption is irrelevant to SME's claim. Neither SME nor its counsel has ever responded directly to the request. It may be appropriate to infer from those indirect responses that neither SME nor its counsel could identify an answer that was helpful to its claim.

SME's Claim is Excluded

The OPIC Contract explicitly excludes compensation in situations where the Bid Bond is called as a result of the insured's inability to pay the amounts required under the SPA. SME failed to pay and was unable to obtain financing for the purchase price and the performance bonds required under the SPA on or before July 7, 2003. SME has failed to demonstrate, or even allege, that it has been able to post those amounts at any time since then. The OPIC contract does not require or permit compensation to SME under these circumstances.

V. Conclusion

The Privatization Authority's calling of the Bid Bond upon SME's failure to pay the purchase price and post the performance bonds, as required by the contract SME knowingly and willingly entered into, was appropriate. SME's claim under the OPIC Contract is invalid, and the request for compensation under the OPIC Contract is denied.

OVERSEAS PRIVATE INVESTMENT CORPORATION

[The original memorandum of determinations, executed by OPIC's president and chief executive officer and dated April 24, 2007, is on file at OPIC.]