The Impact of the International Investment Bank in the Czech Republic

PSSI 2021 Report

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Introduction

The debate over Czech membership in the Russia-controlled International Investment Bank (IIB) was sparked off in 2014, when Andrej Babiš became the Minister of Finance. It intensified when the IIB moved its headquarters to Budapest in 2019. Although the Czech Senate and many experts have been calling for an exit from the bank for over two years, and the Security Information Service has issued warnings about the bank's operations, no apparent progress towards leaving the bank has been made. PSSI believes the newly formed Czech government should open this debate once more and take the necessary steps to withdraw from the IIB.

First established in 1970 and then dormant between 1991 and 2012, the IIB is nominally a United Nations-registered intergovernmental organization but is primarily controlled by the Russian government (which contributes 47% of the bank's paid-in capital). The institution ostensibly exists to promote development and cooperation among its predominantly Central and Eastern European members (i.e., former Comecon member states). PSSI has **previously argued** that the IIB is, at best, a vehicle for Russian evasion of European Union sanctions and, at worst, an instrument of Russian economic and financial warfare.

Prague Security Studies Institute's review of the International Investment Bank's 2020 Annual Report indicates that none of the bank's activity in the Czech Republic appears to have had a significant positive impact on the country's economic growth or trade ties to other IIB member states, either in the national aggregate or within any particular industry.

The only discernible economic impact of IIB activity in the country has been negative, particularly in the scandalous case of a loan to Pilsen Toll. These findings show that Czech IIB membership is currently, at best, passively tolerated by the Czech Government, despite being widely criticized by the Czech media.

According to IIB's 2020 Annual Report, the Czech Republic was the Bank's fourth-largest contributor of paid-in capital after Russia, Hungary, and Bulgaria, accounting for 9.87% of total capital, approximately EUR 37.4 million. The IIB has issued one loan to a Czech Republic-based company, the now-bankrupt Pilsen Toll, in the amount of some EUR 50 million, in addition to making a second loan to Russia-based "Private Joint Stock Company State Transport Leasing Company" in order for it to lease aircraft from Czech Republic-based Aircraft Industries.

IIB has also provided guarantees for smaller loans to a number of Czech manufacturing companies, which export to Eurasian Union countries, primarily Belarus. The bank has also issued several debt offerings on the Czech bond market, totaling approximately EUR 57.3 million.

All of IIB's limited investment activity in the Czech Republic has been directed toward Russian nationals with interests in marginal, outdated components of the country's manufacturing sector. Our case study on the company concludes that a significant portion of IIB funds directed to the country through the Pilsen Toll loan may have been embezzled by its recipients.

Czech Officials Connected to IIB

In the Czech Republic, representatives to IIB are all high-ranking officials in the Czech Ministry of Finance. There is limited information available about these officials, who are mostly career public servants with low profiles. There is little evidence connecting them to other IIB representatives, or Russian interests more broadly. IIB affairs are primarily handled by the International Relations Department of the Ministry of Finance.

The Minister of Finance is usually appointed as the Czech governor at IIB. Alena Schillerová, the last Minister of Finance, is one of the Czech officials to ever speak positively about the IIB, calling membership in IIB **"beneficial and profitable"** for the Czech Republic.[1] She also stated that the bank's move to Budapest is a useful step to manage the bank's compliance with EU sanctions on Russia.

IIB Activity in the Czech Republic

The IIB has focused its support on small or medium-sized enterprises in the manufacturing sector, most of which are dependent on exports to Eurasian Union states. Until the case of Pilsen Toll, the bank had acted as a guarantor of other banks' loans, rather than providing direct loans to Czech companies. Usually, one bank in the targeted country and Ceskoslovenska Obchodni Banka, a. s. **(CSOB)** on the Czech side would cooperate on a given project, with the IIB agreeing to cover the loan(s) in the event of default. CSOB has often been selected to arrange guarantees through IIB, rather than the Export Guarantee and Insurance Corporation, a state-owned firm with a nearly identical function in the Czech Republic. When Czech anti-corruption journalists at Investigace.cz asked CSOB to explain this process, the bank refused to comment.[2]

- The first Czech recipients of IIB export loan guarantees were POLIMAX Group and ENERGO CHOCEN, which jointly exported an industrial cooling system to Belarus.
- The IIB guaranteed a loan for MONTS s.r.o., exporting animal waste processing machinery to Belarus, as well as Vychodoceske Plynarny, a company exporting technologies related to Liquid Petroleum Gas (LPG) to Belarus.
- Loan guarantees were also extended to CINK Hydro-Energy, exporting small-scale hydroelectrical equipment to Armenia.
- Investigace.cz found that the companies were offered cooperation with IIB by CSOB when negotiating a loan.[3]
- Directing CSOB clients to IIB with the knowledge that it was the only bank willing to guarantee high-risk loans to businesses dependent on exports of specialized industrial goods to weak, unstable post-Soviet economies could represent a legally actionable abandonment of CSOB's fiduciary duty.

Although the overall aim of IIB is to ensure sustainable development and competitiveness of member states' economies, the overall trend in the Czech Republic shows exclusive support for small and medium-sized manufacturing enterprises exporting to Eurasian Union markets despite the elevated business and political risks. The contribution to the Czech economy is also negligible, with Czech exports to Eurasian Union countries accounting for less than 2.5% of Czech exports in recent years, while roughly 85% of its exports are directed to EU countries.[4]

[1] "Parliamentary Meeting, 5 March 2020", Parliament of the Czech Republic, accessed 12 March 2021, https://www.psp.cz/eknih/2017ps/stenprot/041schuz/s041121.htm
[2] Hana Capova, "'Ruska banka' v Budapesti: Permanentní stret zajmu, Investigace.cz, 16 July 2019, Accessed 10 March, 2021, https://www.investigace.cz/ruska-banka-v-budapesti-permanentni-stret-zajmu/
[3] Ibid.

IIB Membership Considerations in the Czech Republic

Notwithstanding the Senate's repeated calls to leave IIB[5] and the Czech Government's stated decision to leave the similarly Russia-dominated International Bank for Economic Cooperation (IBEC) in 2017, no concrete steps have been taken to end Czech IIB membership.[6]

In 2017, former Minister of Finance Ivan Pilny proposed leaving IIB[7] due to the reputational and security risks connected with the Bank.[8] However, the Ministry of Finance opted to remain a member, although former Prime Minister Sobotka confirmed that the government was prepared to leave IIB should the ministry ask for such a motion.[9]

The main reason for this hesitancy appears to be worry among Czech officials about not receiving compensation for the Czech Republic's shares in the Bank. This concern stems from Poland's experience, which left the IIB in 2000 and, as of this writing, has not received any financial compensation for its shares. The debate over exiting the IIB revolves around several arguments. According to Senator Pavel Fischer, a member of the Senate committee calling for such an exit, the Bank mainly serves Russian interests[10], a position that this report's findings tend to support. Membership also means that Czech investment capital (provided by taxpayers) is being used – either directly or indirectly – to finance internationally-sanctioned companies such as Rosatom and Sberbank.

U.S. Government representatives and the Czech intelligence service have issued warnings to the Czech Republic regarding the security-related risks associated with IIB, particularly regarding its activities in the nuclear energy sector. IIB and Rosatom, Russia's state-owned nuclear power company, signed a Memorandum of Understanding for general cooperation in 2017.[11] According to the agreement, the IIB will help implement Rosatom projects, such as the construction and maintenance of nuclear power plants in IIB member states.

[4] "Where did the Czech Republic Export to in 2018?", Atlas of Economic Complexity, accessed 17 March 2021, https://atlas.cid.harvard.edu/explore?country=59&product=undefined&year=2018&productClass=HS&target=Partner&partner=undefined&startYear=undefined
[5] Lukas Prchal, "Sef hradniho odboru odmitl jednat o odchodu z postsovetskych bank. Nejde pry o zasadni vec", Denik N, 5 March 2021, https://denikn.cz/575488/sef-hradniho-odboru-odmitl-jednat-o-odchodu-z-postsovetskych-bank-nejde-pry-o-zasadni-vec/
[6] "Schuze bezpecnostniho vyboru: Senatori chtejí vystoupeni CR z Mezinarodni investicni banky (18.09.2019)" Senate of the Czech Republic, accessed 10 March 2021, https://www.senat.cz/zpravodajstvi/zprava.php?id=2808
[7] Lukas Prchal, Jakub Zelenka, Jan Pavec, "Neverejne dokumenty odhaluji ceske pusobeni v Ruskem ovladane bance. Penize tecou firmam, ktere sleduji tajne sluzby", Denik N, 9 July 2020, https://denikn.cz/395320/neverejne-dokumenty-odhaluji-ceske-pusobeni-v-ruskem-ovladane-bance-financujeobchody-rosatomu-s-uranem/

Rosatom's reported interest in constructing a nuclear power plant in the Czech town of Dukovany sparked a years-long, intense debate within the Czech Parliament over whether to exclude Russia from the planned construction tender.[12] This debate has shifted only because of the events in Vrbetice.[13]
According to Czech intelligence, there is a danger that Russia could be interfering in the decision-making process, as a similar scenario occurred in Finland, where Rosatom is currently building a nuclear power plant.[14]

The debate over Czech membership in both IIB and IBEC has recently resurfaced. Last year, during parliamentary interpellation (the formal issuance of parliamentary requests to the government), Finance Minister Alena Schillerova was asked to explain why the Czech Republic is a member of IIB, and what steps the Ministry is taking in order to leave IBEC. Her justification was that IIB is a well-reformed institution that serves its purpose and actively helps Czech companies, whereas IBEC is not effective enough.

Accordingly, the Ministry is taking steps to end Czech membership in IBEC. Alena Schillerova reiterated that the government is not currently considering leaving IIB, arguing that the bank has been restructured and moved to an EU member state, and that the Senate's calls to leave the IIB were **"politicized."**[15]

At the end of 2020, Ministry of Finance representatives suggested putting a possible exit from both banks on the agenda of bilateral talks scheduled with Russia, but the request was declined supposedly to prioritize more pressing topics.[16] Members of the opposition parties have been vocally critical of IIB, with the Pirate Party explicitly labeling it a national security risk.[17] Civic Democratic Party (ODS) MP Petr Beitl repeatedly brings the matter to parliamentary interpellation.[18] With both parties currently participating in the new Czech government, more decisive action might be anticipated.

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[8] Hana Capová, et al., "Budapest – Welcoming Gateway to Europe for Russian Bank", Investigace.cz, 18 July 2019, https://www.investigace.eu/budapest-welcoming-gateway-to-europe-for-russian-bank/
[9] Lukas Prchal, Jakub Zelenka, Jan Pavec, "Neverejne dokumenty odhaluji ceske pusobeni v Ruskem ovladane bance. Penize tecou firmam, ktere sleduji tajne sluzby", Denik N, 9 July 2020, https://denikn.cz/395320/neverejne-dokumenty-odhaluji-ceske-pusobeni-v-ruskem-ovladane-bance-financuje obchody-rosatomu-s-uranem/
[10] "Schuze bezpecnostniho vyboru: Senatori chteji vystoupeni CR z Mezinarodni investicní banky (18.09.2019)", Pavel Fisher.cz, 18 September 2019, https://www.pavelfischer.cz/11192-schuze-bezpecnostniho-vyboru-senatori-chteji-vystoupeni-z-mezinarodni-i nvesticni-banky
[11] "IIB and Rusatom – International Network sign a memorandum of understanding for cooperation", International Investment Bank, 19 June 2017, https://iib.int/en/articles/mib-i-rusatom-mezhdunarodnaya-set-i-podpisali-memorandum-o-vzaimoponimanii-i -sotrudnichestve

Key Russian IIB-linked actors in the Czech Republic

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Igor Shamis

Igor Shamis was born in St. Petersburg, and eventually gained Israeli citizenship. Little information about his career is available until 2004, when he appeared in a memorandum as a partner in “Midland Group”, a Canadian-Russian-Ukrainian investment firm.[19] He then became the majority owner of Bummash, a large manufacturer of lumber-processing machinery based in Russia’s South Ural region in 2008.[20] He is alleged to have close connections to Russian President Vladimir Putin[21], but there is no clear evidence that this is the case. He does not appear on the Forbes top 200 wealthiest Russians list, suggesting that he has a net worth below $400 million.[22]

While Shamis’s connection with the IIB is tied to his purchase of Pilsen Steel in 2011, the creation of Pilsen Toll in 2012 and IIB’s loans to Pilsen Toll in 2015 and 2017, the Pilsen Toll case may be part of a broader pattern in his business activities.

In 2015, Shamis purchased TLM, a Croatian aluminum producer, for an undisclosed price. TLM then went bankrupt later the same year after Shamis was unable to obtain a loan to save it. The company was eventually resold to the Slovenian firm Impol in 2017. Shamis also attempted to purchase metallurgical factories on the brink of bankruptcy in Serbia[23] and Latvia in 2014[24], both of which ultimately fell through for reasons difficult to determine. Shamis was apparently later arrested in France in 2020 on the authority of a Croatian warrant on embezzlement charges related to his tenure as owner of TLM, although there is only one Croatian source available confirming his arrest but providing no further details of the proceedings.[25] He was expected to face trial in Sidenik, the town in which TLM is domiciled, but it is unclear whether he has yet been brought to trial.

Shamis’ business strategy of targeting distressed metallurgical companies in post-communist countries seems to consist of temporarily stalling the bankruptcy and closure of the production facilities by securing new loans. Little to nothing is changed, followed by bankruptcy and Shamis’s quick resale of the company. Though Shamis has not been convicted of embezzlement, these business practices are more suggestive of a predatory corruption scheme than of a streak of bad business luck.

[12] Lukas Prchal, Jakub Zelenka, Jan Pavec, “Neverejne dokumenty odhaluji ceske pusobeni v Ruskem ovladane bance. Penize tecou firmam, ktere sleduji tajne sluzby”, Denik N, 9 July 2020, https://denikn.cz/395320/neverejne-dokumenty-odhaluji-ceske-pusobeni-v-ruskem-ovladane-bance-financuje obchody-rosatomu-s-uranem/

[13] Petr Tuma, "Czechmate? What’s behind the downward spiral in Czech-Russian relations", New Atlanticist, May 14, 2021, https://www.atlanticcouncil.org/blogs/new-atlanticist/czechmate-whats-behind-the-downward-spiral-in-czech-russian-relations/

14 Lukas Prchal, Jakub Zelenka, Jan Pavec, “Neverejne dokumenty odhaluji ceske pusobeni v Ruskem ovladane bance. Penize tecou firmam, ktere sleduji tajne sluzby”, Denik N, 9 July 2020, https://denikn.cz/395320/neverejne-dokumenty-odhaluji-ceske-pusobeni-v-ruskem-ovladane-bance-financuje obchody-rosatomu-s-uranem/

[15] Ibid.

Andrey Kozitsyn

Andrey Kozitsyn is a Yekaterinburg-based Russian businessman and owner of Ural Metallurgical and Mining Company (UMMC), a large conglomerate primarily focused on the copper industry. UMMC is also the owner of Aircraft Industries (AI), a Czech Republic-based manufacturer of light propeller aircraft. AI has benefitted from an IIB loan to one of its major customers, a transport leasing company in Russia, AI's primary market.

Compared to Igor Shamis, Kozitsyn is a more typical Russian oligarch. With a reported fortune of $4.8 billion, he ranks among the top 25 wealthiest Russians. He was appointed by the Austrian Government as their honorary consul in Yekaterinburg and has invested significant money in building Orthodox churches there. He is also the president of the local hockey team, Avtomobilist,[26] and has received several national awards from President Putin, including recently for his financial support for local anti-COVID-19 efforts.[27] These activities are all indicative of a businessman interested in obtaining a significant degree of support from the government, which is the norm in Russia at this level of wealth. Kozitsyn is on a U.S. Treasury Department Office of Foreign Assets Control List, along with other figures characterized as "close to Putin" according to Reuters.[28]

There is nothing to suggest that Kozitsyn has a particularly strong interest in Aircraft Industries or in the Czech Republic in general. He made a single comment about the potential for more light aircraft usage in the South Ural region after UMMC bought a majority stake in AI.[29] That said, Kozitsyn is a fairly major player in Putin's circle, which needs to be taken into account when examining IIB's relationship with Aircraft Industries.

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[16] Lukas Prchal, "Sef hradniho odboru odmitl jednat o odchodu z postsovetskych bank. Nejde pry o zasadni vec", Denik N, 5 March, 2021, https://denikn.cz/575488/sef-hradniho-odboru-odmitl-jednat-o-odchodu-z-postsovetskych-bank-nejde-pry-o-z asadni-vec/
[17] "Resortni Tym Evropska Unie, Zahranici, Obrana: Prvni Podzimni Newsletter 2019", Czech Pirate Party, accessed 18 March 2021, https://nalodeni.pirati.cz/news/msg/133/
[18] "Petr Beitl: Interpelace na ministra zahranicnich veci ve veci Mezinarodni investicni banka - zruseni naseho clenstvi", Civic Democratic Party, 23 January 2020, https://www.ods.cz/clanek/18663-interpelace-na-ministra-zahranicnich-veci-ve-veci-mezinarodni-investicni-ba nka-zruseni-naseho-clenstv
[19] "Informatsionyy Memorandum k debyutnomu vypusku obligatsiy", Midland Group, accessed 13 March 2021, http://st.finam.ru/ipo/memorandum%5C1089_memomcm.pdf i
[20] "Igor Shamis: Na 'Bummash' my prishli s chetkim ponimaniyem, kakim zavod stanet v blizhayshem budushchem", Svoedelo, 16 August 2008, https://svdelo.ru/igor-shamis-na-bummash-my-prishli-s-chetkim-ponimaniem-kakim-zavod-stanet-v-blizhajshe m-budushhem/
[21] Lucie Sykorova, "Pilsen Steel? To je nestastny pripad, takovy vred kraje", Neovlivní.cz, 29 March 2016, https://neovlivni.cz/pilsen-steel-to-je-nestastny-pripad-takovy-vred-kraje/
[22] "200 Bogateyshikh biznesmenov Rossii 2020", Forbes, accessed 14 March 2021, https://www.forbes.ru/rating/397799-200-bogateyshih-biznesmenov-rossii-2020-reyting-forbes
[23] "Ukrainian, Russian, Chinese, Indian, West European firms eye Serbian steel mill", bne IntelliNews, 17 April 2012, https://www.intellinews.com/ukrainian-russian-chinese-indian-west-european-firms-eye-serbian-steel-mill-367 671175/?archive=intellinews
[24] "Investors from Russia and Ukraine may become buyers of Liepajas metalurgs", Baltic News Network, 27 August 2014, https://bnn-news.com/investors-russia-ukraine-buyers-liepajas-metalurgs-118438
[25] "Bivsi vlasnik sibenskog TLM-a uhicen u Francuskoj", Jutarnji HR, 29 January 2020, https://www.jutarnji.hr/vijesti/hrvatska/bivsi-vlasnik-sibenskog-tlm-a-uhicen-u-francuskoj-9910756
[26] "Andrei Kozitsyn", Forbes, Accessed 14 March, 2021, https://www.forbes.ru/profile/andrei-kozitsyn>
[27] Nina Kalina, "Putin nagradil gendirektora UGMK Andreya Kozitsyna", ura.ru, 12 February, 2021, Accessed 14 March, 2021, https://ura.news/news/1052471622
[28] "FACTBOX-Russian individuals named on U.S. 'Oligarch List'", Reuters, 30 January 2018, https://www.reuters.com/article/usa-russia-sanctions-list-idUKL8N1PP0SH
[29] "Russian miner UMMC buys 51 pct of Czech plane maker" Finance.cz, 2 June 2008, https://www.finance.cz/zpravy/reuters/MTFH41497nL02531220-russian-miner-ummc-buys-51-pct-of-czech-pla ne-maker/

Case study: Pilsen Toll

Given the IIB's mission of funding **"projects aimed at supporting the economic development of its member states and that would have a significant positive social, economic and environmental impact",** the case of Pilsen Toll, its sole direct investment in the Czech Republic to date, appears to be an unmitigated failure in each of these categories. The Pilsen Toll loan involves four interrelated companies: Pilsen Steel, Pilsen Estates, United Pilsen, and Pilsen Toll itself.

Pilsen Steel is a metallurgical factory in Pilsen, Czech Republic, that at its peak employed roughly 1,000 workers in the production of steel, cast iron, crankshafts, rotors, and turbine components.[30] It began as part of the local Skoda Works in the 19th century, but was spun off in 2003 as a separate entity, at which time it was purchased by Moscow-based United Heavy Machinery (OMZ). Pilsen Estates was established in 2007 as a separate legal entity that owns the land surrounding the factory, which it rents to Pilsen Steel. During this period, the company continued production but fell into significant debt, particularly after the 2008-2009 financial crisis.

Russian-Israeli businessman Igor Shamis created United Pilsen, a Luxembourg-registered corporate entity, and purchased Pilsen Steel and Pilsen Estates from OMZ through United Pilsen in 2011 for EUR 126 million, using a EUR 110 million loan from Russian state-owned Vneshekonombank (VEB; Bank for Development and Foreign Economic Affairs), to which Shamis pledged 100% of the shares in Pilsen Steel as loan collateral.[31] IIB head Nikolay Kosov was at the time the first deputy chairman of Vneshekonombank, however this does not imply that he is linked to the case, either directly or indirectly.

The loan proceeds, however, were not made directly available to Pilsen Steel. In 2012, Igor Shamis created Pilsen Toll, a **"tolling company"** operating as the financial arm of Pilsen Steel, loaning Pilsen Steel money from the Vneshekonombank loan pool at additional interest, selling the company raw materials and then buying back the finished products for sale to customers.[32] But by the end of 2012, Pilsen Steel was in bankruptcy proceedings, and production had ceased.

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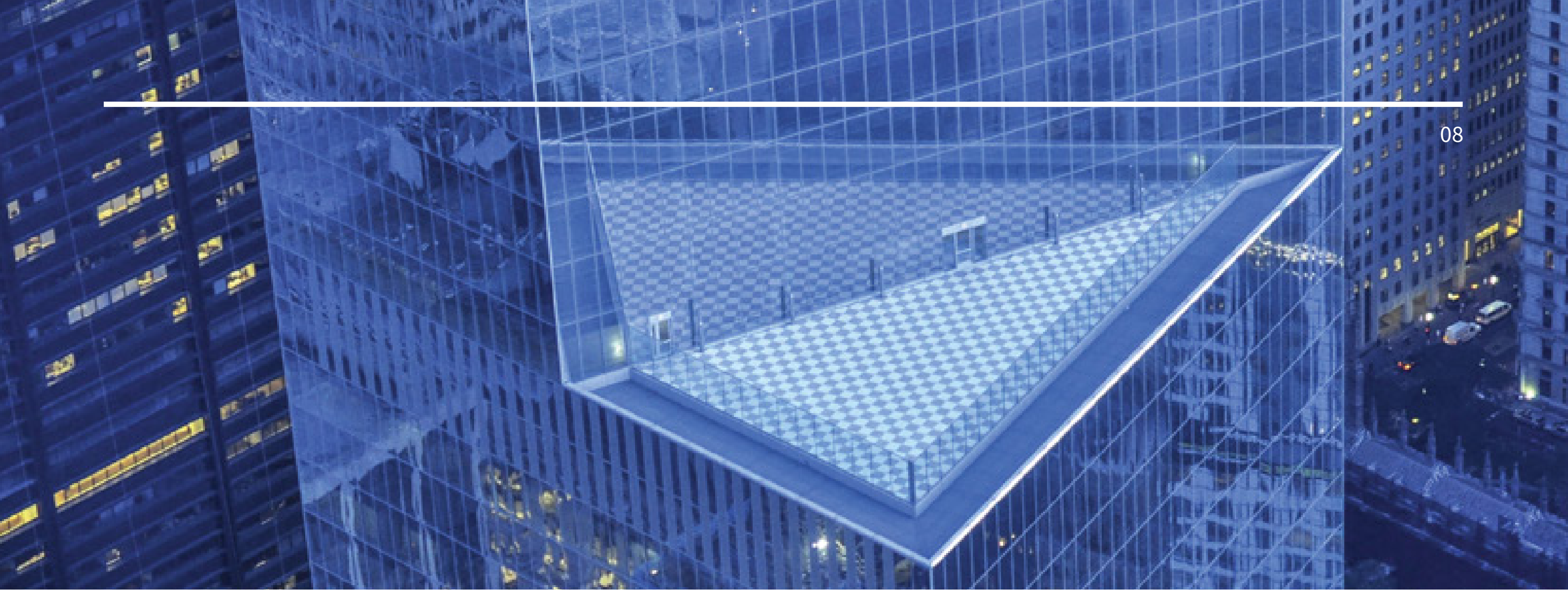
[30] "Dolgovaya yama metallurgicheskogo giganta", Radio Prague International, 21 February, 2019, https://ruski.radio.cz/dolgovaya-yama-metallurgicheskogo-giganta-8137985

[31] Hana Capova, "OpenLux: Rusove a Pilsen Steel", Investigate.cz, 1 March, 2021, https://www.investigace.cz/openlux-rusove-a-pilsen-steel/

[32] This "tolling" structure is not in itself an unusual or inherently problematic business practice in heavy industry, but creates the potential for distortionary business practices and tax evasion.



Shamis resigned as managing director later that year, and in 2013 VEB apparently took full control of Pilsen Toll.

Pilsen Steel received a new injection of capital and partially resumed operations until the summer of 2015, when the company was fined by the Czech Government for failing two environmental tests.[33] It is not clear what degree of control over either Pilsen Steel or Pilsen Toll Igor Shamis maintained after this point, nor the extent of his relationship with VEB. In a 2015 Kommersant interview, Shamis denied that ownership of Pilsen Steel had been transferred to VEB, while VEB declared that they still have "unresolved issues" with Mr. Shamis, possibly related to VEB's initial EUR 110 million loan to him through United Pilsen.

In a 2016 interview with the Czech magazine Neovlivni, Vaclav Slajs, then-governor of the Pilsen Region, stated "We do not know what is going on in that company [Pilsen Steel]. We only have information that the employees are afraid, they are not allowed to say anything about their work and some of them prefer to leave."[34]

Enter IIB

It was at this deeply dysfunctional point in the company's history, in late 2015, that the International Investment Bank granted Pilsen Toll the largest IIB loan to date. Meanwhile, Shamis' other metals factory, TLM in Croatia, went bankrupt in late 2015 after less than six months of ownership by Shamis, and was resold to a Slovenian firm.
In December 2015, an agreement was signed to loan Pilsen Toll EUR 35 million. This money was nominally intended to support Pilsen Toll's activities managing financial affairs in support of Pilsen Steel's operations.

It is unclear, however, how much of this money was ever directed to these purposes, or how much control Igor Shamis might have exercised over the management of the loan relative to VEB. A March 2021 article from Investigace.cz describes how, between 2015 and 2017, Pilsen Steel continued to report net losses on its activities ranging from EUR 3 to 10 million annually.

Pilsen Toll continued to be profitable, taking in roughly EUR 5 million over this same period, apparently through a combination of interest charged on loans made available to Pilsen Steel and a pattern of Pilsen Toll overcharging Pilsen Steel for raw materials and/or underpaying for finished goods. This was apparently a deliberate effort to deny profitability to Pilsen Steel, while guaranteeing it at Pilsen Toll.[35]

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[33] Lucie Sykorova, "Pilsen Steel? To je nestastny pripad, takovy vred kraje", Neovlivní.cz, 29 March 2016, https://neovlivni.cz/pilsen-steel-to-je-nestastny-pripad-takovy-vred-kraje/
[34] Ibid.
[35] Hana Capova, "OpenLux: Rusove a Pilsen Steel", Investigate.cz, 1 March 2021, https://www.investigace.cz/openlux-rusove-a-pilsen-steel/

- As head of the Pilsen Steel workers union, Ivanka Smolkova adds, these profits were supplemented by the rent income extracted by Pilsen Estates, which she described as exorbitantly high, the **“largest boulder and burden we have been carrying with us for years.”** She also notes that, despite having worked at the company for years, she was still uncertain whether VEB or Shamis was the company’s owner, what the relationship was between them, or why VEB had been willing to loan Shamis the money to buy the company in the first place.[36] It is not clear whether Pilsen Toll’s profits were being directed to VEB or to Shamis, or both.

- Despite the continued floundering of Pilsen Steel, the IIB announced that it would loan Pilsen Toll another EUR 15 million in September 2017. It is at this point that IIB’s activity goes from highly suspicious to an unequivocal breach of fiduciary duty. Given the continued losses at Pilsen Steel (notwithstanding bankruptcy and multiple reorganizations), the deteriorating state of relations between Pilsen Steel/Pilsen Toll and the local government,[37] and the openly predatory relationship between Pilsen Toll and Pilsen Steel, it would have been abundantly clear to any financial analyst or accountant that the collapse of the entire group of companies was imminent.

- Nonetheless, the loan was approved, though with less publicity from IIB than had accompanied the first loan. Business continued to follow the same pattern, and in January 2019, Pilsen Steel closed down again. By summer 2019, Pilsen Steel, Pilsen Estates, and Pilsen Toll had all filed for bankruptcy after VEB and other creditors finally cut off access to further credit.

- There was some initial suggestion that VEB’s debt would be declared void and rendered unrecoverable, and a protracted legal battle between Pilsen Steel and its creditors appears inevitable.[38] In January, 2020, Pilsen Steel laid off its roughly 500 remaining production workers, with some 50 administrative employees staying on, presumably engaged in unwinding the company’s remaining assets and dealing with the claims of its many creditors, including IIB and VEB.[39] The factory was purchased for an undisclosed (likely token) price by the German metallurgical company Max Aicher, though it remains uncertain whether it will ever be reopened or merely stripped for assets and permanently dissolved.[40] Investigace.cz finds that United Pilsen remains intact and is apparently now legally under the ownership of a Denis Kotlyar, who had also acted as the head of Pilsen Toll in its late stages.

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[36] Jan Bukovsky, “Ke dnu nas stahly platby sesterske firme, rika sefka odboru Pilsen Steel Ivanka Smolkova”, E15.cz, 23 January 2019, https://www.e15.cz/rozhovory/ke-dnu-nas-stahly-platby-sesterske-firme-rika-sefka-odboru-pilsen-steel-ivanka smolkova-1355609
[37] Lucie Sykorova, “Pilsen Steel? To je nestastny pripad, takovy vred kraje”, Neovlivní.cz, 29 March 2016, https://neovlivni.cz/pilsen-steel-to-je-nestastny-pripad-takovy-vred-kraje/
[38] Jaroslav Bukovsky, “Insolvencni spravce Pilsen Steel poprel vetsinu pohledavek”, E15.cz, 21 January, 2019, https://www.e15.cz/byznys/prumysl-a-energetika/insolvencni-spravce-pilsen-steel-poprel-vetsinu-pohledavek 1359869
[39] “Zavod Pilsen Steel uvolit 500 sotrudnikov”, 420ON.cz, 6 January 2021, https://420on.cz/news/economics/58281-zavod-pilsen-steel-uvolit-500-sotrudnikov
[40] Lenka Proksova, “Novym majitelem zkrachovalych huti Pilsen Steel je Max Aicher”, Denik.cz, 7 January 2021, https://plzensky.denik.cz/zpravy_region/novym-majitelem-zkrachovalych-huti-pilsen-steel-je-max-aicher-2020 0701.html

Pilsen Toll: Cui bono?

It is unclear how much IIB, VEB, Igor Shamis, Denis Kotlyar, or any of the other actors involved in the past ten years of Pilsen Steel's operations profited from the venture, but it appears that several individuals involved were able to successfully compartmentalize areas of risk via separate related entities; Pilsen Steel was set up to take on virtually all of the business risk, and debt, and to incur the highest operating costs and smallest share of revenues possible in order to keep income moving through the other companies. Pilsen Estates was a profit sanctuary that could reliably bring in several million euros annually with virtually no overhead expenses, regardless of the unprofitability and debt burden of Pilsen Steel.

- Pilsen Toll realized a rent of its own in the form of overcharging Pilsen Steel for raw materials and underpaying it for finished goods. Pilsen Toll was also the designated recipient of the IIB loan, likely to prevent fresh capital from being consumed by Pilsen Steel's growing "debt sinkhole." It is not clear how much (if any) of this money actually reached Pilsen Steel at any point. The fact that both VEB and IIB were willing to loan substantial amounts of money to the enterprise, knowing its underlying weaknesses, rather speaks for itself. The owners were careful to direct their loans towards the insulated profit sanctuary of the business (from which the profits seem to have evaporated), only to have the entire family of businesses collapse a short time later. It suggests that both banks never expected repayment of their outstanding loans, especially the IIB, as it arrived later than VEB, when the situation was even more dire.

  This would indicate that they instead intended to use IIB and VEB's access to state funds to temporarily keep activity at Pilsen Steel alive, while siphoning off steady profits from the enterprise, possibly through Igor Shamis and United Pilsen, an arrangement that officials at IIB and VEB were likely aware of and personally benefitting from as well. Investigace.cz finds that in 2017, some 100 million Euros in assets were moved off the books at United Pilsen without explanation, possibly a combination of the pay-out from Pilsen Toll and Pilsen Estates profits and VEB/IIB loan money.

- It may take years before the public really knows what happened to this money, and how much of it ended up with Igor Shamis, Denis Kotlyar, and/or kicked back to officials at IIB and VEB. Curiously, despite its utter collapse just a few years after the IIB's involvement, the Pilsen Toll loans remain on the IIB website under the "Implemented Projects" tab, still the only such project for the Czech Republic. The facts of this case are a testimonial to the obfuscation, manipulation, and corruption that has plagued Russian business activity in Central and Eastern Europe for decades.

Case study: Aircraft Industries

The second loan from the IIB that supported Czech industry happened indirectly. IIB approved a USD 33 million credit line to the Russian entity Public Joint Stock Company "State Transport Leasing Company" (PJSC "GTLK") to finance the purchase of 11 L-410 turboprop planes from the Czech firm Aircraft Industries. This loan was considered by the bank as "fully consistent" with their mandate. It was said to promote connections and integration among its member state economies, while utilizing established historical ties between Russia and the Czech Republic in this sector.[41]

At the time of the loan, September 2017, the company Aircraft Industries was 100% owned by the Russian Ural Mining and Metallurgy Company (UMMC), and selling most of its aircraft to Russia, and had plans to relocate production there as well.

Aircraft Industries

The company, which has gone through several ownership and name changes, is best known for the L-410 Turbolet, which was initially produced in Soviet-era Czechoslovakia.[42] During that time, the company was known as Let Kunovice. After privatization in 1991, the company passed to two different owners, without much commercial success. In 2005, the company was bought by the Czech company Pamco and became Aircraft Industries. In 2008, Russian UMMC bought 51% of the shares, and then in 2013 acquired the remaining 49%. The company has faced significant financial problems, with an insolvency suit in 2016, but managed to pay off its debts before filing for bankruptcy.[43]

Controversy

The company faced a scandal in 2016 over the shift of its aircraft production to Russia. The Czech Government had supported the modernization of production with nearly EUR 20 million under an agreement that production would remain domestic.[44] However, Russian media reported that production was going to move almost completely to their new owner's facility in Russia.

The AI worker's union went on strike over missing compensation and the potential loss of jobs.[45] At this point, the plant in Kunovice employed just over 1,000 workers. In response, the owners settled with the workers and production remained mostly in the Czech Republic. This was not the only scandal involving Aircraft Industries.

On 10 November 2011, Karel Musela broke onto company property, shot, and killed two board members and then himself.[46] While the exact motive is not known, it is believed to be related to the accident that permanently disabled his brother Pavel Musela – the owner of Pamco and formerly of Aircraft Industries. Karel believed that his brother's accident, in which he fell from a hunting stand, had been an attempted murder.[47] Pavel Musela and his company had also been part of a highly scrutinized arms deal.[48] Pamco had acted as a pseudo-arms lobbyist for Steyr, an Austrian arms manufacturer, which sold Pandur armored vehicles at highly inflated prices to the Czech Government. While the suspicions over his attempted murder and corrupt military deals have no direct connection to IIB, his case is helpful in understanding the type of management Aircraft Industries was under and tensions at the company.

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[41] "Lizing i kredity: sinergiya partnerstva GTLK i MIB", GTLK.ru, 25 September 2017, https://gtlk.ru/press_room/news/lizing-i-kredity-sinergiya-partnerstva-gtlk-i-mib/
[42] "Aircraft Industries a.s. History", Let.cz, accessed 17 March 2021, http://www.let.cz/en/history.php
[43] "Aircraft Industries Doplatila 363 Korun, Insolvencni Rizeni Skoncilo", iDNES.cz, 14 July 2016, https://www.idnes.cz/zlin/zpravy/soud-ukoncil-insolvencni-rizeni-s-firmou-aircraft-industries-z-kunovic.A16071 4_123511_zlin-zpravy_ras
[44] "Tradicni Ceska Letadla L-410 Budou Vyrabet Rusove. Odborari z Kunovic Se Bouri", Aktualne.cz, 17 June 2017, https://zpravy.aktualne.cz/ekonomika/tradicni-ceska-letadla-l-410-budou-vyrabet-rusove-odborari-z/r~d2bf7b 16527311e7b65b0025900fea04/

IIB Involvement

In 2017, an IIB loan was extended to State Transport Leasing Company PJSC/STLK “GLTK” in order to purchase 11 L-410 planes. This transport company, a state-owned enterprise which was created in 2009, buys transport vehicles to be leased across Russia, but especially in more remote areas of the country. STLK became the largest buyer of the L-410. Notably, the company is the only large leasing company in Russia not sanctioned by Western countries.[49] The company, although nominally public, is 100% owned by the Ministry of Transport.

Unusual Investment

When Ural Mining and Metallurgical Company UMMC/UGMK originally invested in Aircraft Industries, the move was criticized. AI was failing financially, the L-410 airplane they were manufacturing, and the company’s production infrastructure were badly outdated. The aircraft needed improvements in their seating capacity, weight, and flight range in order to make them competitive with modern aircraft. This modernization had been underway since 2010.[50] Production of the New Generation model L-410 NG, however, was only started in 2018, long after UMMC’s investment.[51]

UMMC is a strategic partner of Ural Works of Civil Aviation/Ural Civil Aviation Plant (UWCA/UZGA).[52] This makes it possible to speculate that the original plan for investing in AI was to take a stake in the company and then move all production to Russia, to be taken over by UWCA. This likely failed to happen for two reasons, the first being that the Czech Government demanded repayment for their investment in the company if production was to be moved.[53] The second is that Russia was unable to make or find a replacement engine for the L-410.

It was announced in Russian media in 2015 that by 2020 there would be a Russian-made replacement for the L-410 engine, meaning that although the aircraft could be assembled in Russia, and they have access to the L-410 licenses, they remain dependent on foreign imports. This theory is reinforced by the fact the UWCA has been working on finding a Russian-made replacement engine for another of AI’s models, the L-610, in an effort to manufacture it completely within Russia.[54]

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[45] “Vyroba Letadel v Kunovicich Zustane, Ujistuje Vedeni Aircraft Industries” Aktualne.cz, 15 September 2016, https://zpravy.aktualne.cz/ekonomika/vyroba-letadel-v-kunovicich-zustane-ujistuje-vedeni-aircraft/r~3fd5423c 7b2211e6bc7c0025900fea04/

[46] “Klicovy Svedek o Pandurech Nic Nepovi, Ochrnul Pri Podivne Nehode Na Lovu” IDNES.Cz, 22 February 2010, https://www.idnes.cz/zpravy/domaci/klicovy-svedek-o-pandurech-nic-nepovi-ochrnul-pri-podivne-nehode-na-l ovu.A100222_081334_domaci_jw

[47] “Strelec z Kunovic Vedel, Koho Zabije. Ostatni Vyzyval k Odchodu”, iDNES.cz, 11 November, 2011, https://www.idnes.cz/zpravy/cerna-kronika/strelec-z-kunovic-vedel-koho-zabije-ostatni-vyzyval-k-odchodu.A11 1111_103103_zlin-zpravy_sot

[48] “Secret Pandur Agreement: Bring the Politicians, We’ll Pay”, iDNES.cz, 21 February 2010, https://www.idnes.cz/zpravy/domaci/secret-pandur-agreement-bring-the-politicians-we-ll-pay.A100221_142541_domaci_abr

[49] “Lizing i kredity: sinergiya partnerstva GTLK i MIB”, GTLK.ru, accessed 16 March 2021, https://gtlk.ru/press_room/news/lizing-i-kredity-sinergiya-partnerstva-gtlk-i-mib/

[50] “Vyroba Letadel v Kunovicich Zustane, Ujistuje Vedeni Aircraft Industries” Aktualne.cz, 15 September 2016, https://zpravy.aktualne.cz/ekonomika/vyroba-letadel-v-kunovicich-zustane-ujistuje-vedeni-aircraft/r~3fd5423c 7b2211e6bc7c0025900fea04/

[51] “Aircraft Industries a.s. History”, Let.cz, accessed 17 March 2021, http://www.let.cz/en/history.php.

[52] Vladimir Karnozov, “Kremlin Considers Relaunching L-610 Production”, Aviation International News, 24 October 2010, https://www.ainonline.com/aviation-news/air-transport/2019-10-24/kremlin-considers-relaunching-l-610-production

[53] “Tradicni Ceska Letadla L-410 Budou Vyrabet Rusove. Odborari z Kunovic Se Bouri”, Aktualne.cz, 17 June 2017, https://zpravy.aktualne.cz/ekonomika/tradicni-ceska-letadla-l-410-budou-vyrabet-rusove-odborari-z/r~d2bf7b 16527311e7b65b0025900fea04/

[54] Vladimir Karnozov, “Kremlin Considers Relaunching L-610 Production”, Aviation International News, 24 October 2010, https://www.ainonline.com/aviation-news/air-transport/2019-10-24/kremlin-considers-relaunching-l-610-prod uction

Motivations for the IIB's Involvement with Aircraft Industries

Based on the timing and facts of this case, it appears highly likely that the IIB loan was made in AI solely to keep manufacturing in the Czech Republic alive long enough to be modernized so that it could be moved completely to Russia, in line with Putin's public plan to have new, domestically produced transit. The initial investment from UMMC also fits this hypothesis, as it allowed the corporation to be completely controlled by Russian interests. Both the AI and the Pilsen Toll cases demonstrate that in the Czech Republic, IIB loans were directed to well-connected Russian nationals and their foreign business ventures rather than local partners.

Reading IIB's Aspirations in the Czech Republic

From what we have researched and observed, IIB's key objectives in the Czech Republic include:

- Directing IIB resources to Russian business interests in the country, even if IIB may have reason to believe such loans will be unrecoverable, or even embezzled.
- Ensuring the continued supply of specialized industrial components needed by companies in Russia and Russian-allied countries (e.g. aircraft engine exports to Russia, machinery exports to Belarus); these Czech export companies are generally weak businesses facing bankruptcy, producing outdated products at low prices.
- Raising funds on the Czech bond market from Czech retail investors to bolster the IIB's capital.
- Using the prestige of the Czech Republic's membership to legitimate IIB as a desirable, relevant, European institution.
- Using IIB as a vehicle for championing the continued "economic ties" between Russia and the Czech Republic, despite their virtual irrelevance in terms of aggregate economic impact on either country.

IIB may be further motivated by the privileged, private access it gives IIB's Russian principals to top officials in the Czech Ministry of Finance, as well as by the right it conveys to Russian nationals on "IIB business" to enter the Schengen Zone freely. The Pilsen Toll case also suggests that IIB officials themselves may be benefitting from kickbacks from their reckless loan activities in the Czech Republic, but hard evidence is not available.

As the IIB member state with the highest per capita income level, the most robust manufacturing sector in Central Europe, and a strong foreign trade position deeply embedded within stable EU networks, there appears no economic rationale for the Czech Republic to pursue enhanced trade ties to Russia and other Eurasian Union countries. The likely effect of continued membership of the Czech Republic in IIB will be more experiences of corruption and manipulation. It is an international embarrassment and major step backward for the Czech Government, especially the Ministry of Finance, to continue this perilous charade with the Russian security services and a lending arm it appears to ultimately control.

It is PSSI's studied view that there is no compelling reason for the Czech Republic's continued membership in IIB, and that its Czech investors, and those of other European member states, face material, reputational, and national security risks by prolonging their membership in what appears to be little more than a Moscow-controlled vehicle for directing state funds to corrupt private Russian interests, using its new headquarters in Budapest to circumvent EU sanctions on Russia.

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