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WEEKEND JOURNAL

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BUSINESS & FINANCE 17

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Hayward faces lawmakers' fire

Bloomberg News

BP CEO Tony Hayward said he wasn't involved in critical decisions about the deep-water well that caused the massive U.S. oil spill. Articles on pages 7, 14-15 and 32. Video at WSJ.com/US

Medvedev sees risks for BP, euro

ST. PETERSBURG, Russia—Russian President Dmitry Medvedev voiced concern about the fate of Europe's common currency and said the Gulf of Mexico oil spill could threaten the survival of BP PLC.

By Rebecca Blumenstein, Robert Thomson and *Gregory L. White*

Asked whether Europe's debt turmoil could threaten the euro, Mr. Medvedev said, "I don't exaggerate the threat, but it can't be underestimated."

The Russian president didn't rule out financial assistance to struggling European nations, but said the European Union should bear the burden of any major "financial injections."

"Russia's prosperity, to a large extent, depends on how well things are going on the European continent," Mr. Medvedev said in an exclusive interview with The Wall Street Journal. "We are not a member of the EU, but we are a European country."

On the eve of his first state visit to the U.S. next week, Mr. Medvedev also questioned whether the Gulf oil spill might lead to the "annihilation" or breakup of BP, as the company faces billions of dollars in losses from the disaster.

He stopped short of saying Russia would re-evaluate BP's lucrative partnership in Russia, which represents almost a quarter of its oil production, but predicted that the spill will prompt a fundamental rethinking of oil exploration around the world.

"This is a wake-up call," Mr. Medvedev said. Of BP's fate, he added: "Certainly, we are not indifferent to their future. ... Hopefully, they can absorb the losses."

Mr. Medvedev, who succeeded Vladimir Putin as president in 2008, was candid in his remarks on a range of subjects.

He voiced optimism that he could continue to widen cooperation between the two superpowers and continue a "dialogue" he has started with U.S. President Barack Obama.

His representatives said the interview, given at the president's residence outside Russia's former capital, was the first he has given to a U.S. newspaper since he took office.

On the subject of Iran, Mr. Medvedev condemned the government in Tehran for failing to abide by an agreement crafted by Moscow, but expressed concern that additional sanctions imposed by the EU and the U.S. could hurt the people of Iran rather than the government.

He also said he was worried that the situation in the strategic central Asia republic of Kyrgyzstan, where ethnic conflict broke out last week, could deteriorate further, warning that a Taliban-style extremist regime could arise in that country.

Mr. Medvedev said Russia was closely watching the fallout from "tragic" ethnic violence in southern Kyrgyzstan, where at least 187 people died in attacks that sent 200,000 Uzbeks fleeing into Uzbekistan. He said that wounded had been killed by attackers and ambulances had been burned.

In the past, Russia has objected to the U.S. military base in Kyrgyzstan, established in 2001 as a linchpin of its operation in Afghanistan. "The future of this base is in the hands of the Kyrgyzstan government," Mr. Medvedev said.

But he said, in his personal opinion, the base in Kyrgyzstan shouldn't become "permanent."

The Russian president warned that if Iran developed a nuclear bomb, other countries in the Middle East and North Africa could also seek to follow suit.

He complained that the U.S. and the EU have imposed additional sanctions against Iran, just after Russia backed a carefully negotiated package of United Nations sanctions last week.

"A couple of years ago, that would have been impossible," Mr. Medvedev said of Russia's support of the U.N. sanctions aimed to deter Iran from building a nuclear bomb.

He said the U.S. has nothing to lose by imposing additional sanctions, as it has no ties with Iran, unlike Russia and China. He said he was concerned that the added sanctions will harm people in Iran.

"We didn't agree to this when we discussed the joint resolution at the U.N.," Mr. Medvedev said. "We should act collectively. If we do, we will have the desired result."

Associated Press

■ Interview: Medvedev struck a sobering note on a nuclear Iran, risks to global security and dangers for the euro zone. 11

EU stress-test results slated for July

BY CHARLES FORELLE AND MARCUS WALKER

BRUSSELS—European governments agreed Thursday to submit their banks to public tests of their soundness, in the Continent's biggest step yet to allay global worries that its financial system is hiding masses of risky loans that are putting the region's economy at risk.

The decision from European Union leaders at a summit in Brussels overcomes longstanding resistance to the disclosure of the results of the "stress tests," which are aimed at demonstrating how well banks would stand up to serious economic shocks.

The agreement wagers that instilling market confidence in Europe's banking system would outweigh long-held concerns that the publication of results could torpedo weak institutions and require expensive rescues.

"There is nothing better than transparency to demonstrate solvency, to give confidence and to leave behind us all these unfounded rumors," Spanish Prime Minister José Luis Rodríguez Zapatero said Thursday. Spain's announcement Wednesday that it would publish results of its own banking stress tests appeared to open the door to the wider effort.

Banking jitters have been rising all week, sparked in part by vigorously denied speculation that Spain would seek an international bailout for its burdened banking system.

The leaders agreed unanimously that each country would publish the results of national stress tests on all its banks as soon as it felt ready to, said Cristina Gallach, a spokeswoman for the Spanish government. Some officials said, however, that about 25 big, cross-border banks would have their test results published.

All the test results should be published by the end of next month, the leaders concluded.

The resistance to disclosing the results of the tests had been strong, particularly from Germany, the region's strongest economy but one seen as having a host of banks with weak finances.

Even at the summit, a European official said, Angela Merkel, the German chancellor, was reluctant to agree and argued in favor of a coordinated release of information by governments.

The official said European Central Bank President Jean-Claude Trichet strongly backed rapid disclosure of all

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PAGE TWO

All euroland's eyes are on Germany and Merkel's wobbling coalition

[Agenda]

By Terence Roth

European governments are scything spending and raising taxes to close dangerous budget gaps, only it's not going down particularly well.

Mass German protests against government welfare cuts over the weekend featured scuffles with police and sharp anticapitalism rhetoric. Church leaders and charities have made common cause with the protests.

Greece remains incendiary after austerity protests led to street clashes, with top unions saying their rolling strikes will continue.

Romanian protesters outside their parliament last week hurled abuse at arriving lawmakers and demanded they vote against deep cuts in public wages and pensions.

Spanish public-sector workers walked out for a day last week and trade unions promise a nationwide general strike soon to protest government spending cuts.

The scenes depict the age of budget tightening colliding with decades of European welfare largess as governments cut back outlays to close budget gaps.

The stage is set for what a senior German trade union leader predicts will be a "societal struggle."

Governments have to work hard selling the currency franchise as being worth the price. In the 16 euro-zone, countries, people are told that the euro project itself is at stake if investors aren't reassured that European governments won't go broke.

European Union leaders will take leave of their domestic battlegrounds to seek mutual moral support at their summit in Brussels beginning Friday. There they can give themselves mutual reassurance before going back and

European Pressphoto Agency

German doctors in Cologne demand better wages and working conditions.

bracing for struggles to get all their spending cuts on budgets in the autumn.

And the outcry at home is building. What has become clear is that a principal threat to the future of the euro zone and

> **The stage is set for what a senior German trade union leader predicts will be a 'societal struggle.'**

neighboring economies lies not in financial markets, but on how successful governments are at controlling their streets.

Europe's left is mobilizing to defend against what they perceive as becoming the biggest onslaught on the postwar social model.

Governments are acknowledging that they've been living above their means. The more these mea culpas translate into real cuts into welfare and social services, the more they are likely to feel the backlash at the ballot box and in town squares.

In most cases, governments so far have just chiseled around the fringes, trimming some jobs benefits, taking some child care here and boosting retirement ages there. But trade unions and social groups also see the regular demands for more and faster cuts from Washington and Brussels.

And the next ratings downgrade looms right behind any signs of government mistakes.

The Fitch ratings agency gave poor grades to British Prime Minister David Cameron's savings plan, claiming his government needed to chip out an additional 1% of national output to overcome its debt problems.

Although not in the euro zone, the U.K. will show it is right in trend with austerity elsewhere when it presents details of its new emergency budget on June 22.

The postrecession European savings drive is fragmenting national politics as special interests fight to defend their stakes. Recent elections have failed to bring in one-party rule, leaving often incompatible parties to water down their programs enough for a coalition that can secure a parliamentary majority.

Over the past year Germany, the U.K., the Czech Republic, Slovakia and the Netherlands have all been landed with patchwork governments. Belgium's vote on June 13 likely will yield the same result.

In Germany, which is expected to set an example for Europe, Chancellor Angela Merkel is having trouble even with her own Christian Democrats over axed welfare programs in her €80 billion budget-savings plan.

The Netherlands, which has been warned to fixed a top-heavy pension system, saw chances for a stable government dashed when its election result last weekend was fragmented by a major swing behind a far-right anti-immigration party.

This won't be a reprise of Europe 1968, a time of generational upheaval. But governments will face a tough test of strength as they try to cut into state spending without opposition from broad swaths of the population normally not prone to street protests.

In the words of Germany's Ms. Merkel, Europe is now at a cross-roads. Backing down now could spell the end of the euro, she has warned. In Germany lies the key. The rest of Europe, and world financial markets, will be watching how successfully her wobbly coalition can force its controversial budget cuts through German parliament this autumn.

What's News

■ **U.K. bankers reacted** calmly to the regulatory overhaul plan announced Wednesday, believing that the newly empowered Bank of England governor, Mervyn King, won't prove as hostile as once feared. 17, 32

■ **EU leaders authorized** a significant widening of the bloc's sanctions against Iran because of concerns over its nuclear-weapons program. 5

■ **Center-left parties** in Germany's most-populous state aim to form a minority government to replace a center-right coalition led by Merkel's Christian Democrats. 5

■ **Swiss legislators** approved a law that clears the way for the government to hand over the names of alleged U.S. tax evaders to the IRS. 6

■ **Four senior executives** are expected to resign at Shinsei Bank, the first major casualties of a new Japanese rule forcing greater disclosure of executive pay. 17

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Roberta B. Cowan on TomTom's global deal with Twitter to geomap tweets

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Vote and discuss: Should Europe publicly disclose bank stress-test results?

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Q: At what age do you want to retire?

55-60	35%
60-65	24%
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NEWS

London calling | The city's prime real estate has attracted a slew of deals from Qatar in recent years

Harrods flagship store

ACQUIRER
Qatari Holding

PRICE
£1.5 billion ($2.2 billion)

ANNOUNCED
May 2010

The holding company of Qatar's royal family bought Harrods from Egyptian-born Mohamed al-Fayed and plans to upgrade the iconic department store.

Park House

Rendering

ACQUIRER
Barwa Real Estate

PRICE
£250 million ($369 million)

ANNOUNCED
June 2010

Barwa—which is 45% owned by Qatari Diar, the property unit of the country's sovereign wealth fund—is buying the Mayfair development, which is to comprise offices, stores and apartments, from U.K. developer Land Securities.

Songbird Estates

ACQUIRER
Qatari Holding

PRICE
$555.4 million

ANNOUNCED
October 2009

Qatar increased its stake in Songbird, which owns much of Canary Wharf, London's second financial district, to 24%, becoming the biggest shareholder.

Source: Jones Lang LaSalle, Real Capital Analytics, WSJ research

Chelsea Barracks

ACQUIRER
Qatari Holding

PRICE
£959 million ($1.4 billion)

ANNOUNCED
January 2008

Qatar bought the former military camp on the banks of the Thames from the U.K. government, planning to turn it into luxury housing. It later bought Nick and Christian Candy's stake. The brothers are now fighting a legal battle with Qatar because the project was shelved.

U.S. embassy

ACQUIRER
Qatari Diar

PRICE
$665 million

ANNOUNCED
November 2009

Qatari Diar bought the building in Grosvenor Square from the U.S. government and plans to eventually redevelop it into a luxury hotel and apartments.

Photo credits: Associated Press (Chelsea Barracks, Harrods); European Presphoto Agency (Songbird); Agence France-Presse/Getty Images (U.S. embassy); Land Securities (Park House)

Qatari investors on the hunt for prime London properties

By Anita Likus

LONDON—Developer and investor **Barwa Real Estate** Co. will buy the Park House development in London's fashionable West End district for £250 million ($369 million), as Qatari investors continue to snap up prime real estate in the city.

"Qatar has emerged as a new global powerhouse and is expected to be the largest source of cross-border real-estate capital during 2010," said property adviser Jones Lang LaSalle.

Qatar's wealth is based on the rapid expansion of its gas industry over the past 10 years and, in response to a windfall of revenue, the government has created a number of major investment vehicles including Qatar Investment Authority, Qatar Holding, Qatari Diar and Barwa, which have been buying prime London properties and stakes in companies.

Recent purchases of property in central London by Qatari investors suggest that they have called the bottom of the market and are still benefiting from the weakness of the pound.

Qatar, which operates some of the world's largest sovereign-wealth funds, last month paid £1.5 billion for Harrods, one of the world's most famous department stores.

Late last year, Qatari investors reached a deal to buy the U.S. Embassy building in Mayfair for $664 million, and they also paid almost £1 billion in 2007 for the 13-acre Chelsea Barracks site in the heart of London.

Qatar also has a 24% holding in **Songbird Estates** PLC, which owns most of London's second financial district, Canary Wharf.

Jones Lang La Salle expects more deals. Qatari investors are preparing to make an offer on London hotel the Grosvenor House, said a person familiar with the matter. The property is expected command a price tag of about £500 million.

According to media reports, Qatari investors also are looking to buy a share in the landmark Savoy Hotel.

Barwa, which is 45%-owned by Qatari Diar, the property unit of the country's sovereign-wealth fund, said Thursday that it will pay **Land Securities Group** PLC £225 million immediately for Park House and £25 million when building work is completed, due in November 2012.

It will also meet all of the construction costs.

> Qatar, which operates some of the world's largest sovereign-wealth funds, last month acquired Harrods, one of the world's most famous department stores.

On top of that, Barwa will pay a share of the profit to Land Securities, the U.K.'s largest landlord and developer. Based on current expectations for office and retail rental values, Land Securities' profit share is estimated at £33 million and is capped at £50 million.

Land Securities started developing Park House, at 453/497 Oxford Street, in May and acted directly on the sale. According a person close to the company, Barwa started looking at the Mayfair site six months ago.

The project, which covers an entire city block of just over an acre on a prime Mayfair site, with frontage onto Park Street, North Row and Oxford Street, would have cost Land Securities £412 million, of which the remaining capital expenditure to complete the plan was £179 million.

Park House is a development of 330,000 square feet comprising offices, retail space and residential accommodation.

Land Securities will still complete the development, acting as manager responsible for delivery of the project.

"The investment demonstrates our commitment to Europe as part of our growth strategy and signals our interest in strengthening our portfolio interests in London," said Ghanim bin Saad Al Saad, the chairman and managing director of Barwa.

The acquisition is the first major wholly owned investment made by Barwa in the U.K. Barwa also has a minority investment in The Shard building in London and is in the process of taking over Qatar Real Estate Investment Co.

Barwa is looking for other mixed-use opportunities of a similar size in London, which it will finance with debt and cash, depending on how much cash banks are willing to lend, according to a person close to the company.

"Park House is the largest speculative development in Mayfair for a generation, and this sale enables us to realize the majority of our profit ahead of schedule, with significantly reduced risk and with no capital employed," said Robert Noel, managing director of Land Securities' London portfolio.

Land Securities plans to invest the capital into its speculative development pipeline.

WSJ.com

ONLINE TODAY: See expanded coverage of residential and commercial property deals, at **WSJ.com/RealEstate.**

EUROPE NEWS

Tide turns for 'stress-testing' of banks

[Brussels Beat]

By Stephen Fidler

The tide has turned on the question of whether European governments should publish the results of bank stress tests.

Following Spain's announcement that it will go ahead with publishing the results of bank-by-bank stress tests, Germany and France indicated they would follow suit.

Publication of the results of U.S. stress tests in May 2009 marked, more or less, a turning point in the crisis, despite criticisms at the time that they weren't tough enough. Since then, the U.S. has been encouraging European governments to follow suit. The U.K., which stress tested its banks last year and published results, has also urged the euro zone to do the same.

Continental European governments rarely like to be seen yielding to pressure from their Anglo-American counterparts. But evidence has been growing that, since euro-zone governments and the International Monetary Fund put in place packages to rescue Greece and any other euro-zone governments that hit financial troubles, uncertainty over the health of the euro zone's banks has been the biggest obstacle to riding out the crisis.

That recognition seems to have overcome once strong objections to publishing stress test results. Those objections have been on two fundamental lines.

The first set of objections related to the answers that stress tests would provide. In some countries, the authorities were clearly worried that credible stress tests would show some banks needed to raise significant amounts of capital and some might be revealed as so weak that it would frighten the markets.

For banks whose shares trade on stock exchanges, this would force them to the market at a less-than-optimal moment—many have seen their share prices weaken in recent months. But for another group, without publicly traded shares, raising capital would be more problematic. While those that are government-owned have an obvious source of capital, those that are mutually or cooperatively owned—many of Spain's savings banks or cajas are examples—do not.

According to European officials, however, developments over the last year raised to the fore a second set of objections against stress-testing. They worry what about the banks would be stress-tested for.

The questions in last year's U.S. stress tests were related to the impact on balance sheets of a serious downturn in the economy, and the consequent increase in unemployment and mortgage default rates and the like.

However, to be credible, European bank stress tests would now need to test for eventualities that European governments don't want to admit are possible, such as a default on Greek, Portuguese and even Spanish debt. The worry is that testing for such an eventuality—even on a worst-case basis—would diminish the credibility of government claims that a euro-zone sovereign-debt default is out of the question.

In fact, bond prices betray that the markets are already questioning—to a greater extent, in the case of Greece, or a lesser extent, Portugal and Spain—those government assertions claiming default is not an option

It is hardly credible now to argue that worst-case testing for sovereign-bond defaults would raise doubts in the minds of investors that aren't already there.

Nonetheless, Europe's banking authorities are surely ruing their failure last year to bolster confidence in the banks with a set of scenarios that would have been less politically sensitive.

There is no doubt that last year's U.S. stress test happened upon a lucky combination: It provided a credible outcome—showing that banks needed to raise significant sums to boost capital—but not one that showed the banks to be so weak that the markets were spooked.

In Europe too, there will be some stress-test choreography, with perhaps a discreet dry run or two, before publication of the outcomes.

The initial response to this week's stress-test announcements have been greeted positively by the financial markets, where the euro rallied, and among analysts.

In a research note, Marco Annunziata of UniCredit said that the Spanish announcement "raised the stakes and markets' expectations—now it will need to show that it is up to the challenge."

French and Spanish bank regulators claim they know a lot about the banks they look after because they park officials inside the organizations. But until now, that has been something that the markets have had to take on trust.

Spain is presumably also confident that its program to encourage savings-bank mergers and recapitalizations is robust enough to cope with what the stress tests will disclose. Other governments may have to set up similar mechanisms.

Perhaps the biggest question marks are over the health of Germany's banks, particularly its Landesanks and savings banks. But if there is one country in the euro zone that could afford a major bank recapitalization exercise without setting the sovereign-debt markets alight, that is probably Germany.

Mr. Annunziata suggests Europe's publication of stress tests could, if things go right mark a turning point, just as the publication of U.S. stress-test results did last year.

"If [Spain's] transparency effort is successful, it could provide the crucial incentive for other countries to follow suit, allowing Europe to finally clear the air on the health of its financial system," he said.

Reuters

EU leaders pose at the state summit in Brussels, the first for the U.K.'s David Cameron, middle row, second from left

EU reverses course, to publish bank-test results

Continued from first page

the results, saying each country followed common European guidelines for stress tests and as a result they would be broadly comparable.

The exposure of Europe's big banks to public and private debt in countries such as Greece, Portugal and Spain remains murky, and European policy makers have for months been battling fears that sovereign-debt troubles in those countries could infect the banking system and cause broad damage.

They settled on disclosure to keep the infection at bay. The more-detailed stress tests would go far beyond the last round of Europe tests, released in October 2009. Then, regulators gave only a vague assurance that Europe's banks passed—without even saying which banks were tested or what the precise questions were.

Disclosure of stress tests in the U.S. last year was a signal moment in the financial crisis that helped dispel lingering market doubts about the health of the American banking sector.

The spring 2009 tests led 10 large institutions to raise tens of billions of dollars to plug capital shortfalls identified by regulators.

Mr. Zapatero said he pushed his European counterparts over lunch Thursday to agree on public tests, and all 27 European Union countries fell into line.

"This is an important step to stress to markets that we are pursuing full transparency," Ms. Merkel said after the meeting.

Still, much remains to be worked out, most particularly how detailed the disclosure of results should be.

Agreeing on the parameters is "not going to be as quick and simple as in the U.S., because authorities from so many different countries are involved," says Nicolas Véron of the Bruegel think tank in Brussels and the Peterson Institute for International Economics in Washington.

But the announcement is still welcome, he says: "The deadlock has been broken."

Germany, whose Landesbanken share the spotlight of market worry with Spain's regional savings banks, or cajas, remained the key hurdle.

Germany's main banking associations have expressed vehement opposition to publishing stress tests, claiming markets might "misinterpret" the results, and arguing that German law requires banks' consent before disclosing stress-test results. The German government said Thursday it plans to seek banks' consent, but a finance-ministry official said a change in the law is also possible if banks don't cooperate.

Spain's intention to publish its own results left Germany with little choice but to also show its cards, one European official said, lest it be seen as having something to hide.

While the stress tests may shore up confidence, they come with their own costs. The heaviest: What to do with banks that fail the exam. Most European countries are now racing to embrace a newfound philosophy of fiscal prudence to ward off concerns about their own deficit and debt levels. Shelling out for pricey bank rescues would imperil those efforts.

German Bundesbank President Axel Weber told a conference in Frankfurt on Thursday that if stress tests show the need for extra support for banks, then governments must be prepared to give it.

He warned that the publication of stress test results could backfire if governments don't then have the money available to address the issues they expose.

"Any stress test only makes sense if it is accompanied by a corresponding commitment by the respective government to drive forward the process of recapitalization and the guarantee of liquidity," Mr. Weber said.

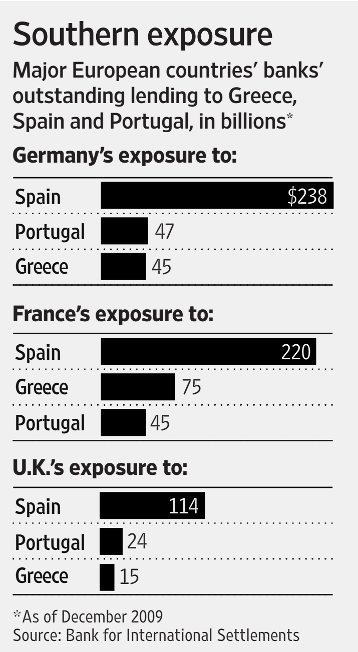
German officials say the growing nervousness in financial markets about the state of European banks has tipped the balance of the argument in favor of doing stress tests in public, overcoming Germany's previous doubts about the value and necessity of publishing the results.

German policy makers have been frustrated at the fact that few German banks have so far used the country's financial-sector bailout fund, known as Soffin, to bolster their capital.

Most of Soffin's €500 billion ($615 billion) in capital and guarantees remain available. Making the true state of banks' balance sheets public could force many banks to use the fund.

In other business at the summit Thursday, European leaders endorsed the idea of a bank tax to pay for the financial crisis, and pledged to argue for a global financial-transaction tax at the Group of 20 meetings in Toronto.

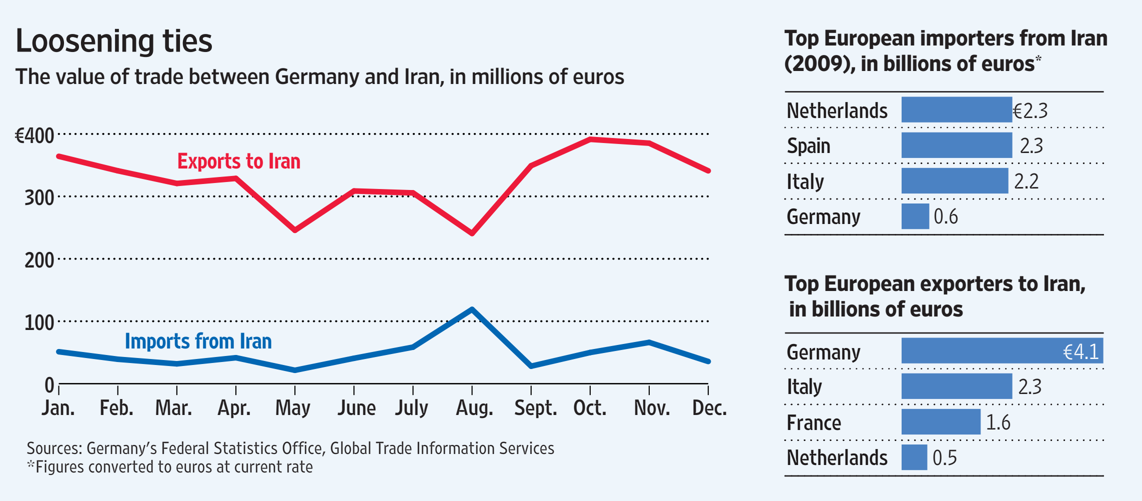
—Stephen Fidler, Geoffrey T. Smith, David Enrich —and Patrick McGroarty contributed to this article.



EUROPE NEWS

EU widens sanctions on Iran to target gas and oil sectors

By Stephen Fidler And Laura Stevens



BRUSSELS—European Union leaders on Thursday authorized a significant widening of the 27-nation bloc's sanctions against Iran because of concerns over Tehran's nuclear-weapons program, in a move that will likely reinforce a slow but steady trend toward weakening economic relations between Europe and Iran.

The new European measures aim explicitly for the first time at parts of the economy unconnected to Tehran's nuclear program and go well beyond curbs agreed in a more narrowly focused United Nations sanctions resolution this month. Pressure from the U.S., a much more important market than Iran, has already persuaded a growing band of big firms to curb business ties with the country.

EU President Herman Van Rompuy said after a summit in Brussels that European leaders "remain deeply concerned about Iran's nuclear program, and new restrictive measures have become necessary."

The leaders decided the measures, to be settled in detail next month, would target Iran's oil and gas industry.

They would impose a freeze on additional Iranian banks and target the Islamic Republic of Iran Shipping Line and air cargo. Like new measures that have been announced by the U.S., they would include new visa bans and asset freezes on individuals, especially on members of the elite Islamic Revolutionary Guard Corps.

The measures, which brought threats of retaliation from Iran, will most affect Germany and Italy, traditionally Iran's largest trading partners in Europe as well as the biggest European investors in the Iranian economy.

Germany is Iran's second-largest trade partner, after China. However, because Germany is the second-largest exporter in the world, that is true with many countries. German exports to Iran fell 5% in 2009 and are off 15% from their peak in 2005. Although exports to Iran for the first four months in 2010 increased 13% to €1.24 billion ($1.53 billion) from the year-earlier period, for unexplained reasons, it was still less than the €1.44 billion exported five years ago.

Iranian business is still important for many German firms, said Michael Tockuss, one of the chief executives of the German-Iran Chamber of Commerce based in Hamburg. "We don't think sanctions, generally, are helpful," he said, "at least not to achieve political goals."

Current sanctions don't affect any German firms right now, he said, because the sanctions focus on, for example, nuclear and military technology that hasn't been exported to Iran in years.

But the expected EU curbs could hit more firms, Mr. Tockuss said. Some of the sanctions on banks or transport could restrict the ability of companies to finance or deliver products. "This, right now, is what the businesses are concerned with," he said.

> The sanctions represent Europe's latest effort to weaken economic relations with Tehran.

Many well-known German firms have already abandoned business in Iran.

In January, **Siemens** AG said it would halt any new business with Iran. **Daimler** AG decided to sell off its Iranian holdings, and insurance providers **Allianz** SE and **Munich Re** AG also announced they were cutting ties. **Deutsche Bank** AG cut off its business in Iran under political pressure in 2007.

Hamburg-based **HHLA Hamburger Hafen & Logistik** AG, a port-terminal company owned primarily by the city in which it is based, halted its plans to work with an Iranian firm in the modernization of port terminals.

A wide range of Italian companies, from car markers to fashion companies, operate in Iran, but the bulk of Italy's exports to Iran is machinery that could come under heightened scrutiny. Over the decades, Tehran has also given Italian oil companies access to developing some of its largest oil fields.

Italian oil company **Edison** SpA operates the Dayyer offshore block in the Persian Gulf. Under a contract with the National Iranian Oil Co., Edison is expected to invest about €30 million over four years to find and develop potential oil reserves around Dayyer. An Edison spokesman declined to comment on the EU's plans.

Over the past year, the Italian government has begun to put pressure on Italian energy companies to scale back their operations. Italian oil giant **Eni** SpA, which has operated in Iran since the 1950s, has reined in its activity there amid pressure from Rome and the U.S. The company operates Darkhovin, one of Iran's biggest oil fields, but plans to hand over management of the field "at some point" this year, according to its 2009 annual report. Eni declined to comment.

Total SA, France's largest oil company and the world's fourth-largest, once was active in Iran through buyback contracts where it financed and developed operations, then sold them to the national oil company. It has entered into such buyback contracts for four Iranian fields, but for each development operations have been completed.

However, Total says it is still waiting for reimbursement related to some of these fields.

In refining and marketing, Total has a 50% share in Beh Total, with the other half belonging to **Behran Oil**. The company produces and markets lubricants to Iranian consumers, and in 2009 generated revenue of €27.4 million.

Renault SA has had operations in Iran since 2004, and now makes cars through two joint ventures, a Renault spokeswoman said. But production is modest, and fell last year to 37,000 vehicles from 56,000 in 2008, due to production difficulties related to suppliers' financing problems.

PSA Peugeot-Citroën sells car parts in kit form for assembly, but has no manufacturing facility there. It sold 337,700 cars worth of these in 2009, a Peugeot-Citroën spokesman said.

One area where Iran is considered vulnerable is on imports of gasoline, where Iran suffers shortages.

According to a European official, the EU considered imposing explicit sanctions on gasoline imports to Iran but backed off after the Netherlands and Germany voiced opposition.

However, several European oil-trading companies, including **Royal Dutch Shell** PLC, **Vitol** and **Trafigura**, already announced this year that they wouldn't sell gasoline to Iran—though oil traders say some gasoline from such companies still finds its way to Iran via third parties.

—Stacy Meichtry, Spencer Swartz and Sebastian Moffett contributed to this article.

Iceland starts talks to be EU member

Associated Press

BRUSSELS—European Union leaders were set to open negotiations Thursday on bringing Iceland into the EU, but only if it settles a €3.8 billion ($4.7 billion) dispute with Britain and the Netherlands, a legacy of the 2008 meltdown of Icelandic banks.

A draft statement, to be firmed up at the close of the one-day summit, said "accession negotiations should be opened" with Iceland. The 27 EU leaders added they are counting on Iceland to "actively pursue its efforts to resolve all outstanding issues"—a reference to the financial dispute.

In March, Icelandic voters rejected a deal to repay the British and Dutch governments €3.8 billion as compensation to customers of Iceland's Icesave bank, which collapsed in 2008.

"We will not block the start of membership negotiations," Dutch Prime Minister Jan Peter Balkenende said when he arrived at the EU summit in Brussels. "But if and when it gets to [joining], Iceland must meet its obligation" and compensate Dutch nationals who saw their savings evaporate overnight. "Iceland must face its responsibility. We shall see to that," Mr. Balkenende said.

He said beginning entry talks is no guarantee that Iceland will become a member. The process may take a year or more. "The negotiations will be based on Iceland's commitment to address" that issue, the draft summit statement said.

Any European country can apply for EU membership. Candidates must be democracies, be ready to adopt the euro, have market economies and no border disputes.

Iceland has mixed feelings about ditching its independence. It decided to try to enter the EU only after a devastating financial crisis almost wiped out its banking sector, forced its currency to plunge and saw the government bailed out by the International Monetary Fund and Nordic nations.

Four out of the country's five parties are urging Parliament to withdraw the EU bid. For decades, Iceland avoided seeking EU membership over concerns that it would be forced to share its rich North Atlantic fishing grounds with boats from other European nations.

In blow to Merkel, center-left parties plan alliance in key German state

By Andrea Thomas

BERLIN—Center-left parties in North Rhine-Westphalia, Germany's most populous state, said Thursday they aim to form a minority government to replace a center-right coalition led by Chancellor Angela Merkel's Christian Democrats.

The plan means Ms. Merkel will likely lose her majority in the upper house of Parliament, which represents Germany's 16 states, making it more difficult for the central government to implement key reforms.

May 9 state elections in North Rhine-Westphalia left conservative Gov. Jürgen Rüttgers short of a majority with his Free Democratic Party coalition partner. The election had been influenced by the Greek bailout package, which is highly unpopular in Germany.

Negotiations among all parties about a majority government collapsed over the past few days.

The Social Democratic Party's Hannelore Kraft said she will form a minority government with the Greens. They have a combined 90 seats in the state Parliament, 10 more than the CDU and FDP.

To be elected as the state's next governor, Ms. Kraft would need an absolute majority of 91 votes in the first three votes, but a simple majority will be sufficient in the fourth. The vote is planned for July 13 or 14.

Reuters

The Swiss People's Party, shown in the National Council in Bern on Thursday, had wanted a referendum on the UBS deal.

UBS tax deal clears Swiss parliament

By Deborah Ball

ZURICH—Swiss legislators approved a law that clears the way for the government to hand over the names of thousands of alleged U.S. tax evaders to the Internal Revenue Service, dodging the risk that the U.S. would reopen a bruising tax case against Swiss bank **UBS** AG.

Final passage of the law had been hung earlier this week when the lower house of Switzerland's parliament included a provision that would have subjected the bill to a popular referendum—a process that would have prevented the handover of the names until after an August deadline set by the U.S.

After tough negotiations in recent days, the lower house dropped the referendum provision.

The vote allows Bern to fulfill its obligations under a deal Switzerland reached last August with the U.S. to resolve a tax case brought against UBS, Switzerland's largest bank by assets. The U.S. Department of Justice charged that UBS helped thousands of Americans evade taxes on as much as $20 billion of income by setting up secret offshore bank accounts. As part of the settlement, UBS admitted wrongdoing and agreed to provide the IRS with the names of 4,450 account holders. Swiss tax authorities must give those names to the U.S. by August.

That settlement hit a snag in January when a Swiss court ruled the agreement violated domestic law. In April, the Swiss government presented a bill aimed at laying the legal groundwork to follow through on the settlement. However, the bill soon became the subject of rancorous debate, with some parties accusing the government of capitulating to U.S. demands and compromising the country's cherished bank secrecy.

Last week, Switzerland's lower house rejected the bill. Earlier this week, it reversed that decision and approved it, but attached the condition that the law be subject to a referendum. Because citizens are allowed 100 days to gather the necessary signatures to launch a referendum in Switzerland, the government would have missed the August deadline to hand over the names.

After heated negotiations among the nation's leading parties, the lower house approved the bill Thursday without the referendum. The Swiss Senate had already approved the legislation without a referendum. As a result, the new law can't be subject to a popular vote.

If Switzerland had failed to fulfill its obligations under the settlement, the IRS was prepared to reopen the case, a spokesman said this week.

In a statement Thursday, UBS welcomed the vote. The conclusion of the tax battle with the U.S. has been critical to restoring the banking giant's image and helping it repair its large private-banking business. UBS shares closed 1.4% higher in Zurich.

UBS's private bank, with 1.7 trillion Swiss francs ($1.505 trillion) under management, is the second-largest in the world but has hemorrhaged bankers and clients in the wake of the scandal.

The U.S. case also emboldened other governments to pressure Switzerland into watering down its bank-secrecy laws, thus weakening its status as a leading tax haven. As a result, many clients who used Swiss bank accounts to hide from the taxman at home have come clean over the last two years.

With the passage of the law, Swiss tax officials, who had suspended processing the 4,450 names, are ready to hand over data on 1,200 accounts, according to a government spokeswoman. So far, the Swiss have sent 500 names of clients who consented to the immediate transfer of their details to the IRS.

Cup boosts U.K. sales

By Ilona Billington And Joe Parkinson

LONDON—U.K. retail sales rose more than expected in May as food and electrical-goods sales picked up ahead of the soccer World Cup, data from the Office for National Statistics showed Thursday.

The volume of retail sales rose 0.6% from a month earlier and 2.2% on a year-to-year basis in May. The year-to-year increase was the strongest since November 2009. Economists surveyed by Dow Jones Newswires last week were expecting a 0.3% monthly gain and a 2.1% year-to-year increase.

The underlying three-month pace of food store sales declined in May, highlighting consumer's concerns ahead of the government's June 22 emergency budget.

In April, sales were revised down sharply to show an unchanged reading on the month. The ONS originally reported retail sales rose 0.3% on the month.

French remember de Gaulle on day of historic address

[Letter from Paris]

By Max Colchester

PARIS—A Eurostar train emblazoned with General Charles de Gaulle's image was scheduled Friday to carry 700 French World War II veterans to London.

Accompanied by President Nicolas Sarkozy, they will commemorate the 70th anniversary of what has been elevated to a defining moment of French defiance: The general's London radio message to rally his compatriots against Nazi Germany.

In June 1940, Hitler's armies had conquered most of France, and the official French government was preparing to surrender.

But de Gaulle headed to London, where he asked the French people: "Is it all over? Must hope disappear? Is defeat certain? Non!"

Very few French people actually tuned in to the June 18 address. The now-famous broadcast—made over BBC airwaves—was never even recorded, and few overseas French joined the resistance at first.

But the subsequent battles fought by the Free French who rallied around Gen. de Gaulle are prized for having saved national honor—while some other French people collaborated with the German occupiers.

After World War II, de Gaulle became the defining image of French pride. A 2007 study found that 3,634 French communes had at least one road named after the general, putting him well ahead of runners-up Louis Pasteur, the scientist, and Victor Hugo, the novelist. France's mint is stamping out two-euro pieces featuring de Gaulle.

A de Gaulle application for iPhones that features the history of the Free French has also been created.

"Today we need to show young people that there are people to look up to," says Sharon Elbaz, the deputy head of the Charles De Gaulle Foundation. The June 18 address showed "that one man was not willing to capitulate."

One reason for the late general's popularity is that France has lost many wars over the past two centuries.

That has left it with few military heroes to look up to—in a country with one of the world's most bellicose histories.

"Since the second republic [which ended in 1852] military commanders haven't been up to scratch," says Sylvain Cornil-Frerrot, a historian at Foundation of the Free French. "They have been treated with some suspicion."

As a result, many of the war heroes France celebrates today were members of the resistance. Jean Moulin, one of its leaders, died after being captured by the Germans and was interred in Paris's Pantheon for national heroes in 1964.

Mr. Sarkozy has publicly praised Guy Moquet, a young communist French resistance fighter who was executed by German forces in 1941.

Associated Press

A giant de Gaulle poster in Paris

The president proposed that French schoolchildren read a moving letter Mr. Moquet wrote before his death.

Throughout the rest of World War II, Gen. de Gaulle referred to his initial broadcast every June 18. "He promoted his own myth," says Mr. Cornil-Frerrot.

After the war, Gen. de Gaulle pushed the idea of a strong, centralized state and national independence.

One reason for Gen. de Gaulle's popularity is that France has lost many wars over the past 200 years, leaving it with few military heroes to look up to.

He was elected president in 1958, after which he pulled out of the North Atlantic Treaty Organization's common military command. He resigned as president in 1969 and died the following year.

The doctrine called *Gaullisme* was taken up after his death by a range of political groupings but has become less significant over time.

In 2006, former French President Jacques Chirac declared June 18 a national commemorative day.

By then Gen. de Gaulle had evolved into a politically neutral figure.

Today the June 18 date is used to thank people outside France for their efforts.

That's part of the point of Friday's events, when some French veterans will meet British Prime Minister David Cameron along with Mr. Sarkozy.

In October, members of the Charles De Gaulle Foundation plan to travel to Brazzaville in the Republic of Congo. That's where the first group of Free French—a mixture of French colonialists and Africans—hoisted a tricolor featuring a two-barred cross and rallied to the general.

"We may decorate the town," says Mr. Elbaz. "We want to show our appreciation to all who helped Gen. de Gaulle."

U.S. NEWS

BP chief denies role in key decisions

BY SIOBHAN HUGHES AND TENNILLE TRACY

WASHINGTON—**BP** PLC Chief Executive Tony Hayward on Thursday told hostile U.S. lawmakers he wasn't involved in critical decisions about the deep-water well that exploded April 20 and caused the worst offshore oil spill in U.S. history.

Mr. Hayward, appearing on Capitol Hill one day after BP agreed to put $20 billion into a compensation fund for people harmed by the nearly two-month-old spill, was seated alone at a table while lawmakers charged that the British oil giant sacrificed safety to cut costs.

During a daylong appearance, Mr. Hayward answered questions in a subdued monotone. He apologized for the accident, deferred many responses until an internal investigation is done and distanced himself from decisions made in the final days before the rig exploded.

Getty Images

BP Chief Executive Tony Hayward looked in the direction of protesters before his testimony in the U.S. on Thursday.

"There is not a single email or document that shows you paid even the slightest attention to the dangers at this well," U.S. House Energy and Commerce Committee Chairman Henry Waxman (D., Calif.) told Mr. Hayward at one point.

Over and over, lawmakers asked Mr. Hayward whether the company had taken shortcuts to save time and money in capping the well. Mr. Hayward repeatedly declined to answer, saying he wasn't part of the decisions that led to the explosion and that it was premature to draw conclusions until multiple investigations have determined the cause of the explosion.

"With respect, sir, we drill hundreds of wells a year around the world," Mr. Hayward said, when asked to comment on some of the decisions his employees had made.

"That's what's scaring me," Rep. Michael Burgess (R., Texas) said.

BP's agreement to contribute $20 billion to the spill-damage fund did little to quell anger. The company faces multiple probes, including civil and criminal U.S. Justice Department investigations. Oil is gushing out of the well at a rate of 35,000 to 60,000 barrels a day, a government-led team of scientists said this week. Mr. Hayward said 20,000 barrels a day are being captured. By the end of June, the company will have in place equipment to handle between 40,000 and 50,000 barrels a day, Mr. Hayward said. "We will pay all necessary cleanup costs," he added.

Investors' initial enthusiasm about BP's deal with the White House gave way to doubts Thursday that it will remove the uncertainty still hanging over the company.

BP's shares rose 7% in London, but there was still dismay that the agreement on the $20 billion fund didn't cap BP's liabilities, raising fears the company will face litigation risks for years to come.

"[The deal] draws a line in the sand for the time being, but there might be another wave coming that could wash it out," said Ivor Pether, a fund manager at Royal London Asset Management.

The deal not only abolishes BP's next two dividend payments but cancels a first-quarter payout that was already declared and due to be transferred to shareholders' accounts next week.

That cancellation, Mr. Pether said, was an "unexpected blow, particularly for income funds." He said losing three BP dividends, worth $7.8 billion, chops 9% off total U.K. market income.

However there was some consolation. BP will make staggered payments into the escrow account over more than three years. Fears that it might have to pay the full $20 billion up front prompted Fitch Ratings to downgrade the company by six notches earlier in the week.

"It put an end to the doomsday scenario that many investors were worried about," said Will Riley, a fund manager at Guinness Atkinson Asset Management. "It gives the market comfort that the U.S. doesn't want to bankrupt BP."

During Thursday's hearing. Mr. Waxman and other lawmakers grew frustrated with Mr. Hayward's polite refusal to answer certain questions, saying he wasn't involved or needed to get the results of an investigation before responding.

"Are you failing to cooperate with other investigators, as well?" Mr. Waxman said. "Because they're going to have a hard time reaching conclusions if you stonewall them, which is what we seem to be getting today."

"I'm not stonewalling," Mr. Hayward said. "I simply was not involved in the decision-making process" that led to the explosion.

Mr. Hayward declined to say precisely when his company will respond to a list of questions the committee's top members sent him on Monday about the accident, saying "you'll get it as soon as we can make it available to you."

The oil spill has fouled marshes and beaches and forced the shutdown of rich fisheries along the Gulf Coast. Democrats and many Republicans on the panel expressed frustration and anger with the company.

"You said safety was your No. 1 priority," said Mr. Burgess. "Safety was traded off; in fact, it was not the priority."

Rep. Marsha Blackburn (R., Tenn.) said "the appearance is, Mr. Hayward, that BP has not learned from previous mistakes."

BP did get some support from Texas Republican Rep. Joe Barton, the senior Republican on the committee, who attacked the $20 billion escrow fund.

"I think that it is a tragedy of the first proportion that a private corporation is subjected to what I would characterize as a shakedown, in this case a $20 billion shakedown," said Mr. Barton. While "there is no question that BP is liable," he complained about the participation of U.S. Attorney General Eric Holder, who is overseeing a criminal probe of BP, in White House talks on the escrow fund.

"I apologize. I do not want to live in a country where any time a citizen or a corporation does something that is legitimately wrong it is subject to some sort of political pressure," Mr. Barton said.

Elsewhere in Washington, Mr. Holder said: "I don't apologize for the Justice Department's role in this matter." He said that "what we have done has been entirely appropriate." The White House issued a statement calling on lawmakers to "repudiate" Mr. Barton's comments, while Vice President Joe Biden called the remarks "outrageous."

House Republican Leader John Boehner also distanced himself from Mr. Barton's comment. "BP agreed to fund the cost of this cleanup from the beginning, and I'm glad they are being held accountable," he said.

Later Thursday, Mr. Barton sought to revise his remarks.

"I think BP is responsible for this accident, should be held responsible and should, in every way, do everything possible to make good on the consequences that have resulted from this accident," he said. "And if anything I said this morning has been misconstrued to the opposite effect, I want to apologize for that misconstruction."

Meanwhile, the Associated Press reported that a rig drilling a relief well meant to stanch a the oil flow is ahead of schedule and could reach its target over the next three to four weeks, according to Coast Guard Adm. Thad Allen.

Mr. Allen, the government's point man for the spill, said Thursday that a drill from a rig near the ruptured well is nearly 10,000 feet below the seafloor. He said it should come within 10 feet of the existing well within the next few weeks.

Then the drill will bore down about 1,000 feet and intersect with the damaged well farther underground. Mr. Allen said the final push of drilling is the most difficult. The drilling was originally slated for completion in mid-August. Once the drill reaches its target, BP will pump heavy "mud" down the relief well in an attempt to stop the flow.

—Stephen Power and Guy Chazan contributed to this article.

David McNew for The Wall Street Journal

A man walks past a vacant Texaco gas station last week in Brawley, Calif.

Blighted hopes haunt California's old outposts

By Tamara Audi

BRAWLEY, Calif.—Signs of economic recovery are sprouting across the U.S., but the most visible bright spot in town is a plan to open a Burger King.

Cities here in Imperial County, a vast swath of desert wedged against the borders of Arizona and Mexico, are stuck in a deep malaise. A few years ago, California's housing boom promised to transform the largely agricultural region. But now, the county's unemployment rate is 28%, making Imperial the metropolitan area with the highest unemployment rate in the nation, according to the Bureau of Labor Statistics.

Food banks are overwhelmed. Families splinter as members leave to find work in San Diego or Los Angeles, more than 100 miles away.

The struggles waged by places like Brawley indicate how hard it will be for some quarters of the country to hitch themselves to a broader economic recovery. While job creation across the U.S. has been anemic, in places that have entrenched economic woes and an overhang from the collapse of the construction boom, the prospects of generating significant new employment are even grimmer.

"These places will come back, but they'll be last in line," said John Husing, an economist studying California's eastern regions.

For decades, such fringe communities as Brawley, hardy outposts clinging to the edges of big urban centers, survived on agriculture and cattle. The town, founded in 1908, started as a tent city and sprang to life when canals turned desert into farmland growing everything from cauliflower to alfalfa. In the past decade, Imperial County began to bustle as families priced out of nearby San Diego County pushed eastward.

New neighborhoods bloomed in the desert. In 1999, home builders invested $37 million in Imperial County, according to the Construction Industry Research Board. In 2005, home-building in Imperial County was valued at $442 million.

"Here's an area that was suddenly seeing, finally, this surge in activity ... Then the recession comes in and stops it cold," said Mr. Husing, the economist. "We're seeing this all along California's spine. These places saw what they could be, and now they're back to being what they were."

When Brawley's Wal-Mart supercenter opened in 2008, 10,000 people applied for 200 jobs.

Business boosters here say the region's cheap land is beginning to attract businesses such as geothermal-energy firms and algae farms, which could provide a big boost to the local economy.

For now, though, there is the prospect of a new Burger King in Brawley. That may seem like a small thing, said Brawley city councilman Sam Couchman, "but to us, every little thing counts."

Driving through his hometown, Mr. Couchman focused on Brawley's potential. "Look, see? Those two guys with orange vests? Working. Those two at the auto-parts store? Working," he said. "We haven't rolled up and gone away."

Many families are grappling with eviction notices and unpaid utility bills. As summer approaches and temperatures reach 120 degrees, social-service workers fret that families will shut off the air conditioning on dangerously hot days to save money. The Imperial Valley Food Bank now serves about 13,000 people a month—a 40% rise in demand over the past two years.

Unemployment checks sustain many families here, but some are still trying to find work. In Brawley's modern job center, residents tap out resumes and search for jobs on a bank of computers. Teenagers take classes on interview skills. Many wonder, though, where they can put those skills to use.

"There aren't really choices here," said Melissa Cruz, a 17-year-old who signed up for the center's youth program, which places her in temporary jobs around town. "It's either this or the fields."

Mike Neciuk, pastor of Brawley's Assembly of God Church, said about a quarter of his 300 congregants have lost jobs. Drug and alcohol abuse in the town has skyrocketed as neighbors and friends lose homes, then spouses, then hope, he said.

Walking through the little stucco building that houses the church's offices, Mr. Neciuk stopped in front of a stack of boxes outside the back door. "Oh, look! Someone left us onions," he said. "That happens a lot. Sometimes the worst times bring out the best in people."

WORLD NEWS

Associated Press

Women take a break from digging for diamonds in Marange, Zimbabwe, in this November 2006 photo before Zimbabwe was directed to clean up the lawless field.

Diamond problems resurface

Illegal panners are said to have returned to Zimbabwe's controversial Marange field

Illegal panners have returned to a disputed diamond field in eastern Zimbabwe, say miners in the area and human-rights groups, just days before the international diamond-monitoring body is expected to weigh whether to approve sales of diamonds from that area.

*By **Farai Mutsaka** in Harare, Zimbabwe and **Sarah Childress** in Nairobi, Kenya*

The Kimberley Process, the international diamond body established to eliminate the trade in conflict diamonds, has been investigating Zimbabwe for alleged violations of the body's rules. Those rules rules prohibit the military from entering the controversial Marange field, permitting illegal panners to work there and smuggling diamonds out of Zimbabwe.

But those who live in the area and have visited recently say little in Marange has changed, even as a Kimberley Process inspector has praised progress cleaning up mining practices and recently recommended that the stones be reapproved for export. "The government of Zimbabwe has demonstrated its commitment to meet the minimum requirements of the [Kimberley Process]. A great deal of hard work has gone into their efforts to do just that," the Kimberley Process monitor assigned to Zimbabwe, Abbey Chikane, said in a report after his visit in May. The report, which hasn't yet been made public, was seen by The Wall Street Journal.

Reached by phone in South Africa, Mr. Chikane declined to comment on the report or Zimbabwe's case. He said that the Kimberley Process members have agreed not to speak to the media until the report is made public.

The Kimberley Process's 49 members, which represent different countries, meet early next week in Tel Aviv to discuss the report. Following Mr. Chikane's recommendation, it would be an unusual move if the organization's members didn't approve diamonds from Zimbabwe's Marange field for export.

Zimbabwe, which was facing suspension from the Kimberley Process late last year, had agreed to implement some changes to operations in Marange. It has argued that it needs soldiers in the fields to keep out illegal panners and provide security. The government plans to sell concessions in the Marange fields to private investors, who would then secure the area themselves, allowing for the troops to be dismissed.

In his report, Mr. Chikane argued against "immediate demilitarization" that could worsen the security situation. "Based on this indication, the army may have to remain in [Marange] until conditions are conducive for the withdrawal," he said in the report.

The diamond body has been investigating Zimbabwe for more than a year. An earlier Kimberley Process investigation found that soldiers forced illegal miners into syndicates and pushed them to mine diamonds on their behalf. The diamonds also benefited top government officials, according to the earlier Kimberley Process report. The report cited beatings, rapes and other abuses, which the government denied had taken place.

In interviews with The Wall Street Journal, miners—who are typically people from nearby communities—say they work in syndicates for armed soldiers, and surrender all or part of their cache of diamonds to the troops. They said security had been tightened during Mr. Chikane's visit in May, keeping some out of the field. But in recent weeks, the panners had returned to work under armed guard.

Zimbabwe's Minister of Mines, Obert Mpofu, said the criticism of the country's diamond industry is racially motivated. "These are statements by whites who don't want to see Zimbabwe benefit from its resources. We have been checking, and illegal activities are to a bare minimum," he said.

But in an interview with The Wall Street Journal shortly after he met with Mr. Chikane, human-rights activist Farai Maguwu said that he had given Mr. Chikane a document from Zimbabwe's internal-security forces that he had obtained that proved that soldiers were involved in the illegal mining, and that some had been arrested. Mr. Maguwu said some of the diamonds smuggled into Mozambique are mined on a disputed plot in Marange and smuggled out by miners working for one of the private companies with links to the government.

In Mr. Chikane's report, the monitor noted that Mr. Maguwu had given him a document, but the monitor didn't discuss its contents. Mr. Chikane said that he turned it over to authorities out of concern he might be violating Zimbabwean law.

He added that Mr. Maguwu's conduct in passing him the document had been "unlawful" and urged the matter to be viewed "in a legal context."

After their meeting with Mr. Chikane, Mr. Maguwu was arrested and charged with publishing and communicating falsehoods. A court has ordered that he receive medical treatment for wounds incurred after spending 13 days in prison, where his lawyers allege he was beaten. A police spokesman said he wouldn't comment on a case that was before the courts.

China vice president to visit Australia

In a sign of the deepening ties between Canberra and Beijing despite a series of diplomatic dust-ups last year, China Vice President Xi Jinping has made Australia the focus of a four-nation tour that could strengthen his nation's standing in a region closely aligned with the U.S.

*By **Rachel Pannett** in Canberra and **Brian Spegele** in Beijing*

The tour could also burnish the international profile of Mr. Xi, who is seen as the probable successor to China President Hu Jintao. The Australian visit caps an 11-day swing through the Asian-Pacific region.

Mr. Xi arrives in Melbourne on Saturday with a retinue of more than 200 executives from about 80 Chinese companies, underscoring China's status as Australia's largest trading partner. Australian Prime Minister Kevin Rudd said Thursday that Mr. Xi's visit is a "welcome opportunity to discuss ways to maintain momentum in the strong economic and trade relationship between Australia and China."

China's government views such high-profile visits as a chance to demonstrate its status as a friendly and potentially helpful player in a region where its rapid rise as an economic and political power has fueled anxiety.

Mr. Xi on Thursday visited New Zealand.

Dutch sentence five Somalis for ship attack

By Spencer Swartz

A Netherlands court sentenced five Somali men Thursday to five years each in prison for trying to hijack a Dutch Antilles-flagged ship last year, the first ruling of its kind in Europe as the continent moves to crack down on East African offshore piracy.

The men were the first to go to trial in a European court on charges of piracy in the waters off East Africa, which has been a beehive in recent years for hijacking-for-ransom incidents against oil tankers and other cargo vessels.

The ships traveling through that region often hail from European states, whose governments have come under pressure from the shipping industry to do more to combat the piracy, which is almost always committed by men from the poor and lawless state of Somalia.

Thursday's ruling comes after another Dutch court earlier this month approved the extradition to Hamburg, Germany, of 10 other Somali men suspected of piracy. Prosecutors there are expected to charge them with hijacking a German container ship in April. Somali men accused of piracy are also awaiting trial in France and Spain.

In the ruling Thursday in a Rotterdam court, the Dutch prosecution had sought seven years in prison for each of the men, who were found guilty of trying to take over the Samanyolu, a cargo ship, in January 2009. The men were tried under a sea robbery law that has been in the Dutch legal system since the 17th century. It was the first time the law has been used, according to the prosecution.

The convictions and prison sentences are the first of their kind in Europe as countries attempt to crack down on piracy off the East African coast.

The Somali men, who range age from the mid-20s to mid-40s, claimed they were out on a fishing trip and had sought help from the Samanyolu after having boat problems.

A three-judge panel in Rotterdam said that defense was bogus because the men were armed with assault rifles and a rocket-propelled grenade launcher.

"We're very pleased the court agreed with us that this defense had no credibility," said Wim de Bruin, a spokesman for the Dutch national prosecutor's office in Rotterdam.

Intertanko, which represents more than 200 independent tanker operators, said it hoped the Rotterdam case "will lead to successful prosecutions becoming the norm for both actual and attempted hijackings," according to Bill Box, a spokesman for the group.

The Somali men have two weeks to decide whether to seek an appeal. The men and their lawyers could not be reached for comment.

Until now, nearly all of the legal prosecutions against Somali men arrested in international waters have taken place in Kenya and the Seychelles islands, where courts are overloaded with pending cases.

DPJ prepares Japan for tax hikes

Japan's new prime minister told voters to brace themselves for a major tax increase to avoid Greek-style problems

By Yuka Hayashi

TOKYO—Japan's new prime minister told voters to brace themselves for the pain of a major tax increase as a way to avoid a Greek-style debt crisis, adopting a higher sales tax as the centerpiece of his economic and political platforms.

Only nine days after taking the helm of the center-left Democratic Party of Japan, Naoto Kan delivered a bombshell announcement that the government will aim for doubling the nation's broad sales tax from the current 5% over the next few years, and backed away from the party's earlier promise that such an increase won't take place at least until 2013.

Mr. Kan made the vow at a news conference called to unveil a package of campaign pledges ahead of elections scheduled for July 11, a key event for the new ruling party to solidify its hold on power. Under a new slogan "Reviving a Healthy Japan," the party said it will expand the economy by an average nominal rate of 3% over the next decade, a level Japan hasn't seen since the early 1990s.

But stepping away from previous growth strategies that focused on big spending, Mr. Kan said the first step to lifting Japan's economy is to cut national debts that already amount to 180% of gross domestic product. To do so, the DPJ plans to cap next year's debt issuance at the current fiscal year's level and aim to balance its main budget within 10 years.

"We can't be an idle spectator of the turmoil in Europe started by the fiscal collapse in Greece," said Mr. Kan, who has repeatedly mentioned the Greek crisis as a warning to Japan in his previous capacity as finance minister.

The Japanese government's new embrace of debt reduction mirrors similar moves in the U.S. and Europe, where the Greek crisis appears to have rippled through politics around the world, making fiscal rectitude a popular political slogan.

With his aggressive campaign to rein in runaway borrowing, Mr. Kan is pitching the DPJ to the voters as a responsible ruling party with solutions to the nation's deep economic problems. Despite its historic victory in general elections in August, popular support for the party had sunk to perilously low levels in recent months before bouncing back with Mr. Kan's appointment.

The party was hurt by campaign-funds scandals involving top leaders and inconsistent handling of the relocation of U.S. military bases. Following the surprise resignation by Yukio Hatoyama, his predecessor, Mr. Kan took over the challenge of mending the party's reputation in time for the July 11 elections.

Polls have shown that the Japanese public, perhaps spooked by scenarios of potential fiscal crises, are warming up to the idea of eventual tax pains. Still, running an election campaign on a platform of a big tax increase is a gamble for Mr. Kan.

Despite Japan's deteriorating fiscal conditions, the country's political leaders have avoided touching the consumption tax since 1997, afraid of losing popular support. Even Mr. Hatoyama had promised last year the current tax rate would be maintained at least until 2013 and that the DPJ would instead focus on eliminating wasteful government spending.

Some opposition parties are already ready for an attack. "Boosting the economy with a tax hike? That's an obscene stretch," Yoshimi Watanabe, leader of Your Party, a popular startup party seeking a small government, said in an interview.

The prime minister said the government will decide on the details of the tax increase, such as the exact size of the increase and the measures to ease the pain for lower-income earners, by the end of March. To implement the step swiftly, the DPJ plans to initiate negotiations with opposition parties, with the hopes of getting cooperation from the Liberal Democratic Party, the former ruling party that has unveiled its own economic rehabilitation blueprint—a program that also includes raising the controversial tax to 10%. Mr. Kan said that level is a "reference point for the time being."

If agreement with opposition parties is reached smoothly, the tax could be raised as soon as the fall of 2012, said Koichiro Genba, chief of the DPJ's policy research council.

Many economists have argued that raising the sales tax is the most effective way to reduce Japan's mounting national debt and secure a steady stream of funds for caring for the nation's growing elderly population. The rate of the tax in Japan is far lower than in most other developed nations, they say, and it's so broad-based that a small increase will quickly boost tax revenues.

Naoki Tsuchiyama, a market economist for Mizuho Securities Co., said a rise in the consumption tax to 10% would increase the tax revenue annually by 10 trillion yen ($110 billion). "That's a substantial amount and definitely positive for the debt market," he said.

But others worry that raising the sales tax will discourage consumption and push Japan's economy back into a double-dip recession.

"What I am afraid of is the return of the 1997 experience," said Masazumi Wakatabe, an economics professor at Tokyo's Waseda University, referring to the previous consumption tax increase, which often is blamed for triggering a recession that has led to a long stretch of deflation. "The economy may seem to be doing fine right now but it still has weak spots and the recovery is propped up by government stimulus plans," he said.

Rather than cutting government borrowing, Mr. Wakatabe said, the priority for Japan now is eliminating deflation by setting an inflation target and loosening monetary policy further.

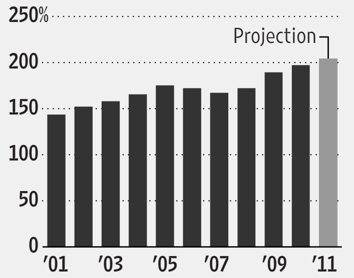
—Takashi Nakamichi contributed to this article.

Associated Press

Naoto Kan shows a leaflet of the ruling Democratic Party of Japan's pledges for the Upper house elections in July

Massive IOUs

Japan's financial liabilities as a percentage of nominal GDP



Source: OECD Economic Outlook

■ Four foreign senior Shinsei executives plan to resign 17

Israel agrees to loosen its blockade of Gaza

By Charles Levinson

JERUSALEM—Israel agreed to ease its land blockade of the Gaza Strip, amid international outrage over its deadly response to an aid flotilla heading to the territory, but offered few details on the new policy.

The government said in a short statement Thursday that the seven-member security cabinet had decided to "liberalize the system by which civilian goods enter Gaza." Israeli officials said greater quantities of building supplies such as cement and steel would also be allowed to reach the territory's 1.5 million inhabitants, provided they were intended for one of the approximately dozen building projects being overseen by international organizations.

Separately, Israeli officials announced that food would be allowed into Gaza, as would other formerly prohibited items such as kitchen utensils, office supplies, children's toys, bedding and towels. A senior Israeli military official and an official in Prime Minister Benjamin Netanyahu's office both said that those changes had been in the works for a while as part of Israel's months-old policy of slowly easing the blockade.

The government emphasized that, despite the easing measures, the sea and land blockade of Gaza would continue. Israel says the blockade is necessary to prevent weapons from reaching Hamas, the militant group that controls Gaza. Israeli officials also say that many restrictions on Gaza are there to keep pressure on Hamas, especially while the group continues to hold Israeli soldier Gilad Shalit, who was captured in 2006.

Israeli officials said further measures to ease the blockade would likely be announced in coming days.

"In the next few days we're going to be much more forthcoming on civilian goods reaching the civilian population," said a senior official in Mr. Netanyahu's office. "We're moving toward a process where items that there were restrictions on in the past will be able to go in unfettered."

Some Western governments and aid groups say that in coming days they hope Israel will announce a final list of banned items, instead of a constantly evolving roster of items that are allowed.

The Obama administration has called Israel's blockade of Gaza "unsustainable" and has been pressuring the Netanyahu government to find a new policy, though it has stopped short of calling for the blockade to be lifted altogether. A U.S. official offered tempered praise for the Israeli decision, but said the full scope of that decision was still unclear.

"It's a positive step," the official said. "They appear to be trying to do the right thing."

Human rights groups said the changes fall far short of what is required by international law, noting that Gazans are still denied the freedom to travel and that bans, such as the one on imports of raw materials needed to produce or package food, such as wrappers, remain in place.

European Pressphoto Agency

A supply truck about to enter the Gaza Strip at a crossing earlier this month.

Neither of the eased restrictions Israel announced Thursday heralds a significant policy shift. Israel has been allowing small quantities of cement and steel in to Gaza under the supervision of the United Nations and other international aid organizations for several months now.

Israel had also been quietly and gradually easing the restrictions on some civilian goods long before its naval commandoes killed nine passengers aboard the Mavi Marmara aid ship on May 31.