



China's currency market finally shows signs of growing up

BUSINESS & FINANCE 17

U.K. budget will define nation's fortunes for years

NEWS 5

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Seven up as Portugal finally turns on the World Cup style



Portugal's Tiago, center, celebrates with teammates Cristiano Ronaldo, right, and Raul Meireles after scoring the fourth goal in their side's 7-0 World Cup win over North Korea at the North Point stadium in Cape Town on Monday. Ronaldo, who hadn't scored in the tournament, later added the sixth goal. **Articles on pages 3 and 28.**

Gangs in Osh were on a war footing

Interviews with witnesses in the few square blocks of Osh in Kyrgyzstan where Uzbek-Kyrgyz violence erupted June 10 indicate both sides were organized, armed and prepared for battle.

What began as a dispute two Uzbek men had over \$45 lost at a Kyrgyz-owned casino mushroomed into a rampage by Kyrgyz gangs on Uzbek neighborhoods in a four-day spree of burning, looting and gunfire. But, before that, about 1,500 Uzbeks were able to burn the casino, shoot up windows in a university dorm and set cars afire. The quick mobilization of both groups suggests that the struggle to fill a power vacuum left by the ouster of President Kurmanbek Bakiyev in April could keep this central Asian country destabilized for months to come.

—Full article on page 9

Pay policies get tougher

U.S. bank regulators aim to curb risk-taking as they expand scrutiny of compensation practices

By MICHAEL R. CRITTENDEN

WASHINGTON—U.S. banking regulators expanded their scrutiny of executive pay practices in the financial-services sector, pressuring firms to take more aggressive steps to discourage employees from taking imprudent risks.

The four federal banking regulators, led by the Federal Reserve, said banks of all sizes—not just major Wall Street firms—must ensure that pay packages for employees are “consistent with the safety and soundness of the organization.” While the new

guidance avoids any artificial caps on pay or specific formulas for calculating compensation, it stressed the need for firms to change the way they pay key employees.

“Many large banking organizations have already implemented some changes in their incentive compensation policies, but more work clearly needs to be done,” Fed Governor Daniel Tarullo said in a statement, warning banks that the central bank expects them to make “material progress this year” on any deficiencies.

Specifically, the guidance

issued Monday suggests firms should consider deferring payments for employees whose jobs can pose a risk to the firm, portioning out payments over longer time frames, and reducing the sensitivity of compensation to short-term gains by a firm.

The guidance expands on a review of executive pay packages started by the Fed last year and represents a shot across the bow for U.S. financial institutions. Regulators stressed that they expect to see banks address compensation issues for all employees who could pose a risk to a

firm's health, not just top executives, and that they will insist on changes if necessary.

“The agencies will take supervisory or enforcement action to ensure that material deficiencies that pose a threat ... are promptly addressed,” the guidance issued Monday said.

Regulators were quick to acknowledge that not all employees or banks will receive the same level of scrutiny on their pay practices. While no blanket exemption was included, the guidance notes that “tellers, bookkeepers, couriers, and data processing

personnel” are unlikely to pose any significant risk to a firm.

Still, officials also made a point to note that the need to attract and retain key staff isn't an excuse for poor compensation practices, effectively a rejection of concerns from critics of new compensation rules that banks won't be able to attract top employees.

“These goals do not override the requirement for banking organizations to have incentive compensation systems that are consistent with safe and sound operations,” the guidance said.

The Quirk



In football-mad Argentina, the national sport is a lame duck. **Page 29**

World Watch

A comprehensive rundown of news from around the world. **Pages 30-31**

Editorial & Opinion

Identifying Europe's zombie banks will help the healthy ones to prosper. **Page 13**





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PAGE TWO

Nul points for Luxembourg's rivals

[Agenda]

BY PATIENCE WHEATCROFT



Congratulations to Luxembourg. The Grand Duchy, to give it its official title, was relegated from the Eurovision Song Contest in 1993 and has yet to return but in the more important economic contest, Luxembourg is the outright winner. It is the only one of the 27 countries that make up the European Union that isn't flouting the rules and running a deficit of more than 3% of gross domestic product.

Last week Cyprus, Denmark and Finland were added to the European Union's list of offenders, each judged to be posing a potential threat to the wider European economy. Luxembourg, though, has been prudent. Once spurned by the song contest, it has refused to return without promises that its costs would be met. Now the European Union is intent on playing a more powerful role in ensuring that other member countries practise budgetary restraint. At last week's European Council meeting of leaders, an outline of a hefty new surveillance regime was agreed.

The European Commission intends that this would extend to giving it advance vetting of individual member's budgets. This should continue to be resisted by the U.K., where government plans have to be laid before Parliament before they are revealed anywhere else. The extensive media foreshadowing of what is contained in U.K. Chancellor George Osborne's first budget may indicate that this convention has been breached, as it regularly is, but that is no reason for allowing the commission to usurp the role of Parliament.

Mr. Osborne's drastic package of tax rises and spending cuts has been concocted with the short term intent of starting to rectify the country's precarious finances



Luxembourg's modern skyline overshadows its traditional buildings.

and the longer term aim of recalibrating the balance between the public and private sectors. The strictures of the European Union's Stability and Growth Pact are unlikely to have influenced his thinking one iota.

The U.K.'s position outside the single-currency zone should enable it to resist the insistent push from Brussels for more economic policing powers. For the

Luxembourg is the only EU country not flouting the rules and running a deficit of more than 3% of GDP.

euro-zone states, however, increased subservience to Europe seems inevitable. The president of the European Central Bank, Jean-Claude Trichet, is this week detailing plans for "a more ambitious approach" to economic governance. Not only would this demand the advance submission of draft budgets to the EU but there would be a single "EU fiscal framework which euro-area countries would be invited to follow..." For "invited", read "expected."

And the ECB wants there to be sanctions with real bite to punish states that do not comply with the budgetary rules. Given that only Luxembourg out of the 16 euro-

zone members has not flouted the terms of the Stability and Growth Pact, it is understandable that the ECB should advocate stronger incentives to comply. Among those it suggests are reduced access to EU funds, suspension of some voting rights and greater involvement in a naughty nation's affairs by the EU. The last might stretch to special missions from Brussels to take a look on the ground at what was going on. Such missions might even become "resident," an EU economic police force to oversee a member country's finances.

That there should be such a drive by European officials to increase their influence over the member states is not without irony. The commission itself isn't a model of financial rectitude. Its own accounts have failed to secure a clean bill of health from the European Court of Auditors for the past 15 years. There is little confidence that its budget, set at €142.6 billion for next year, will be well spent. Last year, the Court of Auditors' report into the 2008 accounts found that errors in economic and financial affairs cost between 2% and 5% of the budget and accounting errors in cohesion spending cost over 5% of the EU's total spending in this policy area.

Such failings are not, however, going to stop the move to bolster the power of the center in Europe. This has been the motivating

force of many of those who supported the European Union and, with the advent of a single currency, it became inevitable.

The euro's component economies still face huge potential problems but, on one level at least, that of the centralizers, they have provided a welcome opportunity.

Don't say you weren't warned

The lead-up to Tuesday's U.K. budget has been geared towards preparing the country for the worst. That, without draconian spending cuts and steep tax increases, the country was heading for total disaster was the message that became ever more strident as budget day approached.

The test now for David Cameron's government will be to see how quickly it can deliver on the rhetoric. Promises of cuts to come, after working parties have deliberated and commissions investigated, will not be enough to appease nervous ratings agencies. This is not a time when a scalpel can be used. Instead, a scythe will have to be taken to large fields of government activity. But such moves bring initial costs in the form of redundancy payments.

Hence tax rises are inevitable. Alistair Darling, when chancellor, cut VAT, at an estimated cost to the Exchequer of £12.5 billion. Restoring the cut didn't appear to diminish the public's appetite for spending. Now lifting the level again has to be on the agenda, yet this time the increase may come just as the public is feeling constrained, in part by other tax rises and also by growing nervousness encouraging saving.

A chairman's lot

As the chairmen of BP and Prudential face increasing criticism from investors, perhaps it is not surprising that headhunters say it is becoming extremely difficult to find people prepared to take on the role. Private equity is so much more inviting.

What's News

■ **The ECB's Trichet** called for "the equivalent of a single federation," that would substantially broaden the powers of the European Commission and member states to correct harmful developments in each country's budget position and competitiveness. 4

■ **The SEC sued** ICP Asset Management and its founder for allegedly defrauding clients who held pooled mortgage products. 17

■ **Stocks in Europe** gained as China's move to relax its exchange-rate regime lifted confidence in the global economic recovery. 23

■ **U.K.-based Resolution** and French insurer AXA are expected this week to announce a \$4.06 billion deal for AXA's U.K. life operations. 23

■ **Investments from Qatar** and Kuwait in a big Chinese share offering are the latest sign of financial and economic ties between China and the Middle East. 21

Inside



An office marriage: Meet the woman who bosses the CEO. 27



The real problem for Europe's World Cup football giants. 28

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NEWS

France has a bad case of Les Bleus

BY DAVID GAUTHIER-VILLARS

PARIS—France's squad went to the World Cup in South Africa with a bright motto: "All together for a new dream."

Since the competition began, "Les Bleus" have dragged their country into a national nightmare.

Striker Nicolas Anelka has been sent home, the captain has muttered about traitors in his midst and senior officials have had hissy fits.

On Tuesday France is facing a make-or-break game against the host team South Africa. Players made the team that much less likely to succeed by refusing on Sunday to participate in a training session in protest against their bosses.

At home, there are worries that the team's performance reflects something fundamentally wrong about France but also anger that the French team has desecrated the subtle art of the French protest.

"It's a caricature of France," Foreign Minister Bernard Kouchner said on French television. "A truly pathetic show."

The trouble started during France's 2-0 defeat on Thursday to Mexico, a result that makes it hard for the team to progress.

On Saturday, a French daily said that during the half-time break, striker Mr. Anelka had reacted to some advice by the coach, Raymond Domenech, by calling him a "dirty son of a whore." The Fédération Française de Football sent Mr. Anelka home.

Captain Patrice Evra decried the apparent breach of the code of *omertà* that governs football's dressing rooms. "The problem is the traitor who is among us and whom we need to eliminate," he told reporters. On Sunday, Jean-Louis Valentin, general manager of France's football federation, told reporters, "I'm going back to Paris. There's nothing for me to do here."

French newspapers have been scathing. "The deserters," said France Soir; "The appalling mutiny," said Le Parisien. Several sponsors, including French bank **Crédit Agricole SA** said they had decided to immediately withdraw advertising in which their names was associated to Les Bleus.

The fuss comes partly because of the elevated status enjoyed by France's football team since it won the World Cup in 1998. Les Bleus came to symbolize enlightened, multi-racial patriotism that celebrates the achievements of a team that usually contains more black players than white.

The uproar is also about a national culture of protest and defi-



Raymond Domenech conducts a training session in Knysna, near Cape Town on Monday.

ance—but a culture that also imposes limits on how far a protest should go.

Modern France was born in a bloody revolution in 1789 and in recent times, street protests have become a way of life. Last year saw a spate of "boss-nappings," when workers held bosses hostage in protest at proposed layoffs. In most instances, companies didn't file complaint for kidnapping and police tolerated what they saw as a "ritual" as long as managers were treated courteously.

There is even a precedent to French insurrection at the World Cup. Toward the end of the 2006 final, French star player Zinedine Zidane, known to his fans as "God," smashed his shaved head into the chest of an Italian defender, saying the Italian had insulted him. A few days later Jacques Chirac, then France's president, said he "understood" Mr. Zidane's behavior, even if he couldn't approve of it.

This year's revolt by Les Bleus has attracted little sympathy.

Football players have traditionally been spared the disdain that many French people hold for "les riches" in their country. But this time, even before arriving, the French team was criticized at home for staying in one of the in South Africa's most luxurious resorts.

On Monday some French politicians said they were a team of "bad-boy millionaires," mirroring a soci-

ety that has lost its moral compass.

"The decadence of the French team says something about France's weaknesses, a society where money is king," said François Bayrou, head of the center-right MoDem party.

French labor unions—which are preparing to demonstrate Thursday against a government plan to raise

the retirement age—weren't pleased that football players had borrowed unions' key weapon to convey their "stupid message." A strike was "the workers' main stick against oppression," said Eric Aubin, a national delegate with the CGT union. "I wonder if they will lose a day of pay for having done that."

Criticism has also been strong because football is promoted in France as a way to bring up bright, healthy children who can work together in teams. That idea dates back at least as far as French Nobel laureate Albert Camus, who in 1959 wrote: "The little ethics I know about, I learned on soccer fields and on the scenes of theater halls, which will remain my true universities."

Another accusation hurled at the French team - and run as a headline in the sports paper *L'Equipe* - was "Imposters!" During a qualifying game against Ireland then-France captain Thierry Henry illicitly controlled the ball with his hand before kicking it to another player, who scored a goal. The referee missed the infraction, and France had its ticket to South Africa while the Irish were eliminated. "Laughing stock of the world," the Irish Times said on Monday in a front-page banner headline, apparently enjoying the French team's difficulties.

Over the weekend, President Nicolas Sarkozy ordered France's Health and Sports Minister Roselyne Bachelot to prolong her stay in South Africa and help restore unity within the French team.

"My role isn't to stab them in the back," Ms. Bachelot said ahead of a meeting with Mr. Domenech and some players. On Monday evening, Mr. Domenech was asked how he would assemble a team to play. "First, I need to see who will be physically and mentally fit to play," he said.



The Quick burger chain is pulling ads from France featuring Nicolas Anelka.

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EUROPE NEWS

ECB's Trichet urges fiscal federation

By Geoffrey T. Smith

BRUSSELS—European Central Bank President Jean-Claude Trichet on Monday called for a big increase in the powers of the European Commission to restrict the ability of member states to destabilize the union.

Mr. Trichet told the European Parliament's economic and monetary-affairs committee that he was calling for "the equivalent of a fiscal federation" that would substantially broaden the powers of the commission and member states to correct harmful developments in each country's budget position and overall competitiveness.

However, he acknowledged the impossibility of transferring full budgetary responsibility to any centralized institution, and repeated that the ECB is opposed to any system that open-endedly transfers liabilities from one state to another through the issuance of bonds under a "joint and several" guarantee.

Mr. Trichet's comments, delivered in his routine quarterly testimony to the European Parliament, are the ECB's contribution to a fierce and divisive debate over how to reform the governance of the euro area in order to avoid debt crises such as Greece's.

The ECB is trying to balance the interests of Germany, which has emphasized the need for fiscal discipline and sanctions on deficit sinners, with those of much of the euro area's southern and western periphery, which is aggrieved at what it sees as German reluctance to stimulate national demand for their goods and services.



ECB President Jean-Claude Trichet addresses the European Parliament economic and monetary-affairs committee Monday.

Mr. Trichet fleshed out the call for a "quantum leap" in euro-zone governance that he has been making since markets started to fear for the long-term ability of member states such as Greece and Spain to service their debts in future. So far, countries that share the euro submit to a common monetary policy but manage their own fiscal affairs.

He said an independent agency, preferably to be housed within the European Commission, should have the powers to hand down a broad range of sanctions on countries whose budgetary and macroeco-

nom policies would lead to a sharp loss of competitiveness, whether or not those policies actually violated existing guidelines on excessive debt and deficits.

"Sanctions need to be applied earlier and must be broader in scope," Mr. Trichet said, noting that the power of sanction could extend to suspending member states' voting rights in financial affairs. However, he made no direct reference to the possibility of denying members access to the EU's structural and regional funds, as some have mooted.

"The commission should have

greater responsibility by making proposals which can only be modified with unanimity in the council rather than mere recommendations under the stability and growth pact," Mr. Trichet said.

He said the EU should first try to implement these reforms using "secondary legislation," that is, without resorting to a wholesale renegotiation of the EU treaty.

Mr. Trichet's comments come as the sharp volatility in euro-zone financial markets has appeared to ease. He said he saw a "progressive return to a normal functioning of

the money market," after turmoil in early May that forced it to start buying the bonds of some euro-zone governments on the open market. He repeated his pledge to withdraw "euro for euro" all the money injected through the so-called Securities Market Program, thus ensuring that it didn't lead to inflation.

He stressed that the ECB isn't embarking on a program of "quantitative easing" aimed at preventing a contraction of the money supply, and repeated that both this and all the other "nonstandard" policy measures used by the ECB over the past two years will be temporary.

He declined to say when he thought it will be possible to stop buying government bonds, a practice that has drawn heavy criticism from German officials, including those on the ECB's governing council.

In response to a question unrelated to the governance of the euro zone, Mr. Trichet said he welcomed the decision of the Chinese government to restore more flexibility to its currency regime. He said the decision "goes in the direction of more stability" and would benefit both China and its trading partners.

In response to another question, he acknowledged that the new framework for capital and liquidity in the banking sector, currently under development, "must not harm the economy" by making it harder for banks to lend. At the same time, however, he repeated his criticism of banks which he said had failed to appreciate how much risk taxpayers had assumed in bailouts that followed the 2008 financial crisis.

—Nina Koeppe and Matt Dalton contributed to this article.

U.S., Turkey deny intelligence rift

By Marc Champion

ISTANBUL—The U.S. and Turkey on Monday sought to squash speculation that the deaths of a dozen Turkish soldiers at the hands of Kurdish rebels over the weekend were caused by Washington's withdrawal of intelligence support.

Over the past two months, a renewed terrorist campaign by the Kurdish Workers Party, or PKK, has claimed the lives of more than 50 Turkish soldiers. This weekend, Kurdish rebels killed 11 Turkish soldiers in an attack on a post along Turkey's border with Iraq and another at a barracks, according to Anadolu Ajansi, Turkey's state news agency.

The attacks' scale led Turkish media to speculate that the killings were supported by Israel, or came because, they speculated, the U.S. had withdrawn intelligence support it has in recent years offered Turkey against the PKK. The trigger for such a U.S. withdrawal, these reports alleged, was Turkey's opposition earlier this month to sanctions against Iran in the United Nations Security Council.

"There has been no change in the level of U.S.-Turkey intelligence-sharing regarding the PKK in northern Iraq," U.S. Ambassador James F. Jeffrey said Monday. "We stand ready to review urgently any new requests from the Turkish military or government regarding the PKK."

On Monday, Turkey's Chief of the General Staff Ilker Basbug also appeared to damp speculation that the losses could be attributed to a U.S.-



Turkish Premier Erdogan visiting soldiers near the border with Iraq on Sunday.

Turkish rift, or to a Turkish-Israeli split following late May's deadly Israeli raid on a Gaza-bound aid ship.

Mr. Basbug told reporters after a speech that for the past 10 days, Turkey has been using Heron unmanned aerial vehicles recently delivered by Israel for surveillance in northern Iraq, Anadolu Ajansi reported. He said the unmanned vehicles were being used "in coordination with the United States" but said they "can't detect all terrorist activities second by second."

Turkey's national security council on Monday "discussed revising intelligence and the structure of personnel serving in [southeastern Turkey]," according to the office of President Abdullah Gül, who sum-

moned and chaired the council meeting. The office also called on neighboring countries to do more to combat terrorism.

Faik Bulut, a Kurdish former Palestinian Liberation Organization member who now writes on Turkish militant groups, said the latest PKK attacks were homegrown, and had been signaled by the group's leaders.

The relative quiet of recent years on the PKK front came as Turkey's government was pledging a new "democratic opening" to provide Kurds with greater political and cultural rights. But the government met with nationalist opposition and delivered little. Instead, some Kurds who returned to Turkey from northern Iraq through a kind of pilot am-

nesty program were put on trial; the Constitutional Court earlier this year shut down the main Kurdish political party in Turkey's parliament for having ties to the PKK.

On Friday, 151 Kurds—among them a dozen mayors including the prominent mayor of Diyarbakir in eastern Turkey—were charged with membership in the Kurdistan Associations Union, described by prosecutors as the PKK's urban wing.

Late last month, imprisoned PKK leader Abdullah Ocalan said he was withdrawing from efforts to bring the Turkish government and PKK together, citing lack of progress, and said he was leaving decisions to commanders in the field and Kurdish politicians. Days later, a PKK spokesman announced the end of a year-long cease-fire.

Turkey responded to the weekend attacks with strikes against suspected PKK bases inside northern Iraq on Saturday, triggering a complaint from Iraq's foreign ministry. Turkey's military said 12 PKK militants were killed.

Ethnic Kurds make up about 15% of Turkey's population. The PKK grew up in the 1970s, seeking a homeland that would include Kurds in Turkey, Iraq, Iran and Syria. Several tens of thousands of people—most of them ethnic Kurds—died in the guerrilla war that followed. The PKK has since moderated its demands to Kurdish-language schooling and regional autonomy, among others.

—Erkan Oz contributed to this article.

Russia cuts gas to Belarus over debts spat

MOSCOW—Russia cut natural-gas supplies to neighboring Belarus Monday after it said Minsk failed to pay off debts, though a European Union official said the dispute isn't expected to affect supplies flowing into the rest of the Continent.

By Jacob Gronholt-Pedersen and Alessandro Torello

Russian President Dmitry Medvedev told the head of gas giant OAO Gazprom to prepare to reduce gas supplies to Belarus by 85% from 6 a.m. GMT, the Kremlin said on its website. Early Monday afternoon, the gas monopoly said it had cut supplies to Belarus by 15% but could increase that to 85%.

Belarusian First Deputy Prime Minister Vladimir Semashko said Monday the country plans to repay debts to Russia in two weeks, Interfax news agency reported.

Still, the step marks renewed tensions between Moscow and Minsk—traditionally close allies—amid frequent energy and trade disputes. Belarus, whose fragile economy is largely dependent on trade relations with Russia, is the last of the ex-Soviet states still to pay a discount price for Russian gas deliveries.

The EU depends on Russia for around 25% of its gas needs, though the bulk of that transits through pipelines outside Belarus.

EUROPE NEWS



The government of Prime Minister David Cameron, shown second from left in London Monday, plans deep budget cuts.

U.K. government prepares deep cuts

BY ALISTAIR MACDONALD

LONDON—The U.K.'s new coalition government will deliver Britain's most important and painful budget in decades on Tuesday, with a spending plan that is likely to define the fortunes of both the government and the country for years to come.

Faced with one of the highest budget deficits in the world in terms of percentage of gross domestic product, Treasury chief George Osborne has warned of steep spending cuts and tax increases that economists say could ultimately be the equivalent of as much as 8% of GDP over the next five years, the sharpest pace of fiscal belt-tightening in the U.K.'s postwar history.

The government's program of dramatic cuts will put the U.K. on a different track from the one suggested by President Barack Obama, who has called for large economies to tread carefully and not risk the fragile global recovery.

The government knows that its credibility in financial markets and its triple-A credit rating are at stake at a time when countries across Europe are under severe scrutiny. Such tough fiscal medicine will set it up for a clash with unions and state workers, in a country where almost half the jobs depend directly or indirectly on the government.

"This budget's significance is immense, you have to maintain your triple-A rating," said Stuart Thomson, a government-debt investor at Ignis Asset Management. But, he said, "George Osborne faces a danger, caught between not cutting enough for the markets and cutting too much for the long-term health of the economy."

The government has already said it will take measures such as levying some kind of tax on banks, changing the structure of taxes on the airline industry to raise more revenue, and increasing the capital-gains tax to nearer the 50% highest income-tax level. Economists also expect it to raise the value added tax to 20% from 17.5% and expect news of aggressive cuts on the country's welfare and state pensions bill.

A scan of the budget

The government has already announced several measures, including:

- A bank levy, likely to be aimed at balance sheets
- Taxing airplanes rather than passengers could increase revenues to £5 billion from £2 billion
- Around £5.5 billion of efficiency savings
- Canceled or postponed around £2 billion of government projects
- Economists expect:
 - An increase in VAT to 20%, raising around £11 billion a year
 - An increase in capital-gains tax to move it closer to highest income-tax level, with exemptions.
 - Increases in alcohol duties

As it raises taxes elsewhere, the government also will exempt around 880,000 of the lowest-paid U.K. residents from having to pay income taxes while increasing the number of people—by some 650,000—for whom employers don't have to pay payroll taxes, according to a person familiar with the matter.

That reflects pressure on the government to not be seen as too hard on the poorest. It is also a nod to the coalition agreement Prime Minister David Cameron's Conservative Party accepted with the more left-leaning manifesto of its governing partner, the Liberal Democrats.

The government will pledge not to make further cuts to government capital spending, such as infrastructure projects, this person said, amid concern from businesses that this could undermine the productive capacity of the economy.

Governments around the world are faced with the same dilemma. As some announce aggressive cuts, others are pressured into following suit by the markets. But such mea-

asures add to governments withdrawing demand from the global economy.

On Friday, Mr. Obama wrote to the Group of 20 leading nations with a clear warning against cutting deficits too quickly. He suggested G-20 countries are ready to respond with pro-growth measures if the global economy starts to slide again.

Some countries have already complained, for example, that the German government's fiscal squeeze will hurt Europe's ability to bounce back. Germany has said it will shave €80 billion (\$99 billion) off its deficit between 2011 and 2014, or around 3.3% of GDP, with cuts of around €10 billion in 2011.

Among large economies, the U.K.'s cuts are expected to be among the biggest. Its structural deficit—the gap in the government's finances that won't be erased by an uptick in growth—is estimated at almost 9%, compared with 5% in the European Union, 7% in Japan and 7% in the U.S. But few other big economies are faced with ratings agencies making market-moving calls for greater details of cuts. At the other end of the scale, Greece has been forced to promise cuts to its deficit by 11% of GDP by 2013, and the U.K.'s growth and lending predictions are considerably rosier than Greece's.

In cutting so deeply, some economists and the Labour opposition worry that the U.K. may hurt its economic comeback.

Ross Walker, an economist at Royal Bank of Scotland, expects as a result of the cuts that the Office for Budget Responsibility's growth forecasts will be as much as 0.25 percentage point lower a year and the jobless rate will be lifted by 0.25 percentage point annually for 2010 through 2012. For many, that is a price worth paying. In addition to the market demands for more fiscal responsibility, the U.K.'s annual debt-interest bill jumped by 45% to £4.34 billion (\$6.43 billion) in May 2010, and the government expects it to hit £70 billion by 2015.

—Laurence Norman in London and Marcus Walker in Berlin contributed to this article.

Afghan deaths hit 300 for U.K.

Associated Press

LONDON—A British Marine wounded in Afghanistan has died, defense officials said Monday—the 300th British fatality of the nine-year campaign.

The Ministry of Defense said the member of 40 Commando Royal Marines was hurt in a June 12 explosion in Helmand province. He died Sunday in a hospital in England. The marine's name wasn't released, but the ministry said his family had been informed.

Prime Minister David Cameron said the milestone provided a moment "for the whole country to reflect on the incredible service and sacrifice and dedication that our armed services give on our behalf."

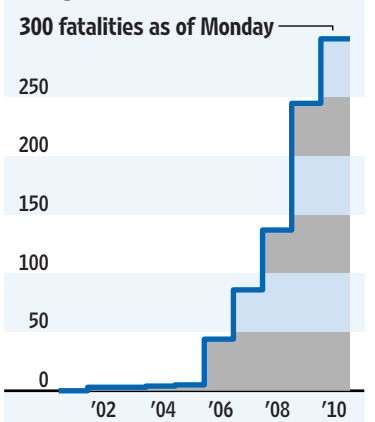
Britain has about 10,000 troops in Afghanistan, the largest international force after the U.S. Opposition to the conflict has grown as casualties have risen. Most of the British deaths have occurred since 2006, when troops were sent to Helmand, a southern province that is a center of the Taliban insurgency.

Defense Secretary Liam Fox paid tribute to the dead marine and said "our resolve and determination to see the mission through remains steadfast."

The Conservative-Liberal Democrat coalition government that took office last month has said Britain is

Tough command

Cumulative fatalities among the British military and U.K. civilians in Afghanistan since Oct. 7, 2001



Source: U.K. Ministry of Defense

committed to Afghanistan, but is also eager to offer Britons an exit strategy by speeding up the hand-over of control to Afghan forces.

"We are paying a high price for keeping our country safe, for making our world a safer place, and we should keep asking why we are there and how long we must be there," Mr. Cameron said. He said that as soon as Afghans "are able to take care and take security for their own country, that is when we can leave."

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EUROPE NEWS

Tapes to delay Bettencourt trial

Secret recordings by butler concern undeclared bank accounts and gift of private island

By CHRISTINA PASSARIELLO

PARIS—Secret recordings of L'Oréal SA heiress Liliane Bettencourt, one of France's richest and most private figures, could delay a trial over her fortune that is scheduled to start next week.

The tapes, recorded by Ms. Bettencourt's butler between May 2009 and May 2010, reveal conversations between the nearly deaf 87-year-old woman and her entourage. They concern undeclared bank accounts, fiscal fraud, political donations, and her gift of a private island to her photographer friend François-Marie Banier. The recordings were made illegally, but are still admissible as evidence in a criminal case.

Late Monday, Ms. Bettencourt

said she intends to declare all her assets abroad to French tax authorities. "Having one of France's large fortunes, I have always wanted to reside in France and pay my taxes here," Ms. Bettencourt said in the statement, adding that she had paid €400 million (\$495 million) in taxes over the last 10 years.

Ms. Bettencourt's only child, Françoise Bettencourt-Meyers, filed a lawsuit against Mr. Banier three years ago that accuses him of exploiting her mother's mental weakness. Ms. Bettencourt had allegedly given the 62-year-old celebrity photographer life-insurance policies, cash, and Matisse and Picasso paintings valued at €1 billion in recent years. In addition, the secret tapes reveal that she gave him the island of Arros in the

Seychelles and that her will designates him as her sole beneficiary.

Through her lawyer, Ms. Bettencourt has denied being taken advantage of. At a December hearing, Mr. Banier's lawyer, Hervé Témime, said his client wasn't afraid of prosecution. "He's in a hurry to be cleared of this defamation," he said.

The trial is scheduled to open July 1 in the Paris suburb of Nanterre. However, the assistant prosecutor and other people familiar with the case said Monday that the trial could be delayed to include the secret tapes as new evidence. In the taped exchanges with her financial adviser and a financial lawyer, Ms. Bettencourt has trouble recalling her gifts to Mr. Banier and his status as sole beneficiary.

The ownership of French cosmetics giant L'Oréal, founded by Ms. Bettencourt's father, doesn't appear to be in jeopardy. Ms. Bettencourt passed her 31% stake in L'Oréal on to her daughter, Ms. Bettencourt-Meyers, several years ago. Sixty percent of that stake is now in the name of Ms. Bettencourt-Meyers' two children, according to Ms. Bettencourt-Meyers' husband, Jean-Pierre Meyers. Ms. Bettencourt receives the dividends from her former stake.

Ms. Bettencourt-Meyers filed the lawsuit against Mr. Banier in order to prevent him from seeing her mother, Ms. Bettencourt-Meyers' lawyer Olivier Metzner said. "She's not making a claim on the art work," Mr. Metzner said.

Ms. Bettencourt's mental state has been difficult to establish. She has refused to submit to court-ordered psychiatric tests. "Enough of this. I'm not a vegetable!" she has said to past requests, according to her lawyer, Georges Kiejman.



Agence France-Presse

Liliane Bettencourt in 2007

New game plan.

Lawsuit ties Catholic order to sexual abuse

By STACY MEICHTRY

A man who claims to be the son of Rev. Marcial Maciel Degollado, founder of the Legion of Christ, filed a lawsuit against the powerful Roman Catholic order on Monday, alleging the group's support of the priest allowed Father Maciel to sexually abuse him for years.

A lawsuit filed in the Superior Court of New Haven, Conn., on behalf of José Raúl González Lara says Father Maciel led a double life, fathering Mr. Lara in 1980 and sexually abusing him from 1987 to 1998, according to a copy of the complaint seen by The Wall Street Journal.

The complaint accuses the Legion of battery and negligence for allowing Father Maciel to have contact with minors, including Mr. Lara, even though, the suit alleges, the group was aware that Father Maciel had faced allegations of sexual abuse decades earlier. Father Maciel, who died in 2008 at the age of 87, repeatedly denied the earlier sexual-abuse allegations. The Legion hasn't addressed the question of Mr. Lara's paternity.

Jim Fair, a U.S.-based spokesman for the Legion, declined to comment on the lawsuit or on Mr. Lara's alleged links to Father Maciel. "Our attorneys won't be able to talk about the suit at this point," Mr. Fair said in an email.

Joel Faxon, Mr. Lara's lawyer, said it was "premature" to say how much money his client was seeking in damages, adding that "historically, these types of cases have been resolved in excess of \$1 million." Mr. Faxon said he filed the suit in New Haven because Connecticut serves as an "operational center" for the Legion, which also has operations across Latin America and Europe.

The suit filed Monday alleges "the Legionaries were aware that Maciel was using the power and resources gained from the Legionaries to meet with children around the world, including Raul."

—Margherita Stancati contributed to this article.



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U.S. NEWS

BP blunts political hits from spill

Company won't be liable for costs related to drilling moratorium, restoration of coast beyond prespill conditions

By JONATHAN WEISMAN

BP PLC, despite being put under pressure by the U.S. government to pay for the oil-spill aftermath, has succeeded in pushing back on two White House proposals it considered unreasonable even as it made large concessions, according to officials familiar with the matter.

BP said costs related to its oil-spill response had reached \$2 billion as it continues work to contain the leak and to pay claims for damages.

To date, more than 65,000 claims have been submitted and more than 32,000 payments made, totaling about \$105 million, BP said. "It is too early to quantify other potential costs and liabilities associated with the incident," the company said in a statement.

BP last week agreed to hand over \$20 billion—to cover spill victims such as fishermen and hotel workers who lost wages, and to pay for the cleanup costs—a move some politicians dubbed a "shake down" by the White House. Others have portrayed it as a capitulation by an oil giant responsible for one of the worst environmental disasters in history. A truer picture falls somewhere between.

The fund is a big financial hit to BP. But behind the scenes, according to people on both sides of the negotiations, the company achieved victories that appear to have softened the blow.

BP successfully argued it shouldn't be liable for most of the broader economic distress caused by the president's six-month moratorium on deep-water drilling in the Gulf. And it fended off demands to pay for restoration of the Gulf coast beyond its prespill conditions.

After the high-profile meeting of administration and BP officials on Wednesday, it was in the interest of neither to discuss such details. BP wanted to look contrite and to make a grand gesture, and the White House wanted to look tough.

President Barack Obama came away touting how BP's money would be handed over quickly and impartially to those hurt by the spill. Not only did BP earmark the \$20 billion fund but it promised an additional \$100 million for Gulf workers idled by the drilling moratorium.

But BP didn't offer a blank check. The \$100 million—0.5% of the total—won't come close to covering collateral damage from the White House's moratorium.

The drilling industry estimates the moratorium will cost rig workers as much as \$330 million a month in direct wages, not counting businesses servicing those rigs like



BP CEO Tony Hayward appears before a House panel Thursday. BP successfully argued it shouldn't be liable for the fallout from the president's moratorium.

machine-shop workers.

BP and its defenders argue that the moratorium was a White House policy decision for which it shouldn't be responsible. The final deal was structured to limit the company's exposure to such claims.

BP negotiators also said the company won't pay for Mr. Obama's pledge to restore the Gulf of Mexico to a condition better than before the Deepwater Horizon exploded on April 20.

White House officials want to use the oil-spill disaster to implement long-developed plans to restore natural marshlands and waterways. Facing record budget deficits, that pledge could founder with BP balking.

Administration officials say the concessions extracted from BP are unprecedented. Negotiators were able to graft a deal onto the Oil Pollution Act of 1990, the main law dictating corporate responsibility in such a disaster, without having to ask Congress to change the law.

"A blank check was never in the cards," said an administration official at the talks. But, he added, the deal hammered out "went a very long way."

The Wednesday meeting at the

White House was designed to go smoothly, the latest in a string of administration showdowns with corporate titans from General Motors to Wall Street banks. By the time BP Chairman Carl-Henric Svanberg and Chief Executive Tony Hayward walked up the White House driveway just past 10 a.m., the company had agreed in principle to the fund. "The president knew when he walked in that we were amenable to the kind of proposal we had already agreed on in principle," a BP negotiator said.

Five days of preliminary talks between BP's hired lawyer, Jamie Gorelick, Associate Attorney General Thomas J. Perrelli, and White House counsel Robert Bauer had coalesced around the \$20 billion figure.

But the talks—with about a half-dozen people on either side—stretched longer than expected. "A lot of the work was done before, but there were a lot of details," said White House Chief of Staff Rahm Emanuel in an interview. "Details matter."

Twice, the two sides retreated from talks in the West Wing's Roosevelt Room to consult privately: On BP's ability to appeal decisions made by the \$20 billion

fund's independent administrator, Kenneth Feinberg; and on how far BP would go to meet Mr. Obama's request that it also aid workers hurt by the drilling moratorium.

Both sides described the negotiations as businesslike. BP hired Ms. Gorelick, a former deputy attorney general in the Clinton administration, from the white-shoe law firm Wilmer Cutler Pickering Hale and Dorr LLP, in part because of her ties to Democratic lawyers including Mr. Bauer.

But there was one item barely discussed ahead of the meeting: assistance for workers hurt by the moratorium, which has forced 33 deepwater rigs to pull anchor. To drive home the request, the president had Mr. Bauer relay the request to Ms. Gorelick the day before, negotiators for both sides said.

At the meeting's start, Mr. Obama told the group of his concerns about those workers, most of whom did not work for BP.

When the president and vice president left the room, Ms. Gorelick told White House negotiators their legal position mandating BP's assistance to displaced workers was weak. White House officials conceded such workers may not be able

to qualify for direct assistance under the \$20 billion fund, a White House official in the room said.

A BP negotiator said the White House position was "half-hearted" and its negotiators quickly gave up. "You won't find many lawyers who will say when the government imposes a moratorium, it's the company's obligation to help the workers impacted," the BP adviser said.

The BP side was so confident that Ms. Gorelick suggested the two sides let idled workers submit claims to Mr. Feinberg and allow a court to decide whether the company was liable.

A White House official said the administration believed it had grounds to push BP, but in the end, Mr. Bauer made an emotional appeal. He called BP's move cynical and asked why the company was "lawyering" after it told Congress and the administration it wouldn't duck its financial responsibility.

In response to that appeal, BP's negotiators agreed to voluntarily add \$100 million as "a goodwill gesture," one adviser said. The two sides didn't agree how that money would be distributed.

—Jeffrey Sparshott contributed to this article.

A New Orleans staple is latest victim

By PERRY STEIN

P&J Oyster Co. has shucked oysters every workday for the last 134 years. The fourth-generation, family-owned New Orleans company survived the 1927 flood off the Mississippi River, the Great Depression and Hurricane Katrina in 2005.

But the company has just hit a big hurdle: the Gulf spill. For the first time, P&J doesn't have enough oysters to shuck for use in po' boys and other dishes.

A major provider of the mollusks to many restaurants in New Orleans, P&J closed its shucking operations this past week and laid off 11 workers. Now, the company has become a symbol of how the oil spilling into the Gulf is beginning to hurt the city of New Orleans, not just the coast.

Al Sunseri, co-owner and president of P&J, said most of the company's profits come from shucking—removing the meaty bivalve from its shell. He plans to try to stay afloat by distributing pre-

shucked oysters from other areas.

When the Deepwater Horizon exploded, Mr. Sunseri didn't expect to lose his supply. Still, as a precaution, he purchased as many oysters as he could in advance. But all the Louisiana oyster beds that supplied P&J in the Barataria Basin now have been shut.

On Thursday, there were two community-outreach representatives from BP, as well as two claims adjusters, at the oyster house, according to BP spokesman John Curry.

"We have said all along that we are responsible for this, and we are going to do things to make it right," Mr. Curry said.

Mr. Sunseri said he wants to ensure his former employees—many of whom have worked at the company for more than 30 years—are taken care of in the face of unemployment.

"They are more than just my employees. They are my family," Mr. Sunseri said. "I hope that everyone does what they say, and that these people are made whole."

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U.S. NEWS



Steve Hebert for The Wall Street Journal

Mimi Foster, 37, a former dancer at Bazooka's in Kansas City, Mo., now works at the club training others.

Showdown over strippers

As Missouri weighs curbs, adults clubs say they offer jobs in tough times

BY JOE BARRETT

KANSAS CITY, Mo.—The Show Me state is headed for a showdown over a move to rein in the adult-entertainment industry at a time when every job counts—even those of strippers.

Last month, the Republican-controlled legislature passed one of the nation's toughest state laws aimed at strip clubs and other adult-entertainment venues. It would ban nude dancing and the serving of alcohol in adult cabarets, force strip clubs to close at midnight and forbid seminude dancers to touch patrons.

Missouri Gov. Jay Nixon, a Democrat who counts job creation among his top priorities, must decide whether to sign or veto the bill. His spokesman said Mr. Nixon was still studying the measure. After July 10, it would become law automatically, and opponents promise a legal battle if that happens.

Proponents say they aim to set minimum standards for an industry that they claim demeans women and contributes to prostitution and related social ills.

"You've got very vulnerable people who are being coerced into being the fodder for some of these places," said state Sen. Matt Bartle, the main champion of the bill, who has been pushing regulation of the industry for nearly a decade.

Club owners and dancers say that the venues rarely attract crime, and that the new rules would be so strict that hundreds of jobs and millions of dollars in state revenue could be lost at a time when Missouri's economy is struggling to re-

cover from the recession.

Mr. Nixon last week announced \$301 million of budget cuts because of falling revenue and proposed a special legislative session to discuss measures to support Missouri's auto industry.

The new legislation "was written to close us down," said Dick Snow, owner of an all-nude cabaret called Bazooka's Showgirls in a former warehouse district in Kansas City, Mo., that is now a popular arts area.

He said he and a partner have invested nearly \$2 million in the club since the mid-1990s and employ about 135 people.

With a three-story atrium at the entrance and state-of-the-art lighting and sound, Bazooka's does about 60% of its business after midnight, Mr. Snow said. His dancers earn most of their money not on stage but from socializing and providing customers with "booth dances" that would be illegal under the new law because they usually involve touching. During these tough economic times, Mr. Snow said, crimping a legal business that backers claim employs about 3,000 people and brings in some \$4.5 million of state sales taxes "makes no sense."

Dick Bryant, a Kansas City, Mo., lawyer who represents the industry, warned the governor to expect a vigorous legal challenge.

Scott Bergthold, a Chattanooga, Tenn., lawyer who developed model legislation that the Missouri bill drew from, said the bill's provisions have been tested in the courts.

"Missouri is on good ground," he said. The bill doesn't prohibit viewing erotic material but "does elimi-

nate the conditions that facilitate illicit sexual behavior and other secondary effects," such as the sale of drugs, Mr. Bergthold said.

Mr. Bartle, a Republican, said he became interested in regulating the industry about eight years ago, when he noticed a surge in sexually explicit signs popping up on Missouri highways. He pushed through a law targeting those signs only to have it struck down in federal court on free-speech grounds.

In 2005, Mr. Bartle attached a broader bill regulating the industry to an anti-drunk driving measure. The adult-entertainment section of the final bill was rejected in state court because it wasn't deemed relevant enough to the underlying legislation.

The lawmaker's efforts gained momentum in 2008. Still, the latest bill didn't pass until the final days of the legislative session last month.

Advocates for women say the adult-entertainment industry can be harmful to women, but also can help them stabilize their lives. Ashlie Sheets, who has been dancing at Bazooka's and other clubs for six years, is one such woman. The 24-year-old single mother of three said she suffered from bipolar disorder and received about \$900 a month in government disability checks. By dancing two to three weeks a month at the club, she earns another \$700—the maximum she can bring in while maintaining her benefits.

"I feel safe here," Ms. Sheets said. "It's really going to mess up a lot of people's lives if the law completely passes."

servatives and liberal Justice John Paul Stevens. Justice Stephen Breyer dissented, joined by two other liberals.

The case predated the Sept. 11, 2001 terrorist attacks and involved foreign organizations pressing causes unfamiliar to most Americans—the Kurdish separatist organization known as the PKK and the Liberation Tigers of Tamil Eelam.

The primary plaintiff in the case,

retired U.S. administrative-law judge Ralph Fertig, wanted to provide instruction to the PKK about how to advance its goals lawfully, but was worried that his actions could be construed as a crime.

Chief Justice Roberts wrote such activities amounted to "training" and "expert advice" that can be prohibited.

The case is *Holder v. Humanitarian Law Project*.

China's evolving global role brings benefits for the U.S.

[Capital Journal]

BY GERALD F. SEIB



President Barack Obama, badly in need of good news, got some over the weekend from the most unlikely of sources: China, which said it would allow the value of its currency to rise, thereby answering the single most fervent prayer U.S. officials utter when seeking divine intervention to help with America's big trade deficit.

In fact, this is the second time in a month that American prayers have been answered in Beijing. The first came when the Chinese agreed to a United Nations Security Council resolution imposing economic sanctions on Iran, then stuck to that agreement despite a diplomatic volley from Tehran designed to coax the Chinese into backing down.

Let's not get misty-eyed about a new age of Sino-American cooperation here. The Chinese moved on their currency as much for their own inflation-fighting self-interest as out of any concern for U.S. wishes, and they are moving slowly in any case. And one can argue that the Chinese did the minimum necessary, and belatedly, on Iran sanctions.

Still, the two moves show that the U.S.-Chinese relationship has a healthier glow than it did just a few months ago, when the two nations were arguing about global warming, a visit by the Dalai Lama to the White House and American arms sales to Taiwan.

More importantly, the steps suggest a certain maturing of China's view of its role in global affairs—and a more deft touch by the Obama administration in coaxing China into playing that role responsibly.

"In both cases there was a perception the Chinese had that they were in the danger of being isolated internationally," says Charles Freeman, a China watcher at the Center for Strategic and International Studies. "In both cases you can look at their moves as things the Chinese wanted to do in order not to be seen as troublemakers internationally."

The first thing to note here is that the Chinese actually cared that they not be isolated, or be seen as troublemakers. That wasn't always the case in years gone by.

Now, these recent events provide more evidence that China is slowly but steadily coming to see itself as a partner in world affairs, not just an observer and critic of them. As Mr. Freeman notes: "They are feeling both the joys of having achieved a certain global status, as well as the pressures."

A few years ago, the Chinese acted as if they could have the former, and not worry about the latter.

In the case of the currency revaluation, that meant the Chinese didn't want to be the subject of pressure and tongue-lashings at the summit meeting of



President Barack Obama, at a speech Monday in Washington, has benefited from decisions by China on its currency and Iran sanctions.

the Group of 20 major economies later this week. With China's artificially low currency widely seen as favoring its exports at the expense of economic recovery in the rest of the industrialized world, that was certainly going to be the case.

In that environment, the U.S. appears to have done two things right.

Mr. Obama, in a conversation with Chinese leader Hu Jintao, both assured him that China was headed for G-20 trouble, and used the threat of protectionist legislation from Congress, to underscore Beijing's political problems.

Then Treasury Secretary Timothy Geithner gave China breathing space to act by delaying an April report that would have branded the Chinese as currency manipulators—a report that likely would have produced an unhelpful nationalistic backlash.

Now Mr. Obama moves on to two more challenges. The first is to return the favor to the Chinese by cooling off a drive in Congress to impose trade penalties on China. Sen. Charles Schumer of New York, in particular, has been pushing such legislation, and already has signaled he'll continue to do so because the rise in the value of the Chinese yuan may be too gradual.

Yet it shouldn't be too hard for the president to deflect congressional action. Mr. Schumer knows by now that his role is to be the bad cop keeping up pressure on Beijing, while the White House gets to play the good cop. No reason to think that will change now. But the odds that legislation will actually pass just went way down.

The second challenge lies in North Korea. Exactly a year ago, China cooperated in passing economic sanctions on its friends in North Korea because of their nuclear-weapons program. But backsliding is underway. The Chinese refuse to blame North Korea for sinking a South Korea military vessel in March, and Beijing recently dis-invited Defense Secretary Robert Gates from visiting.

Meanwhile, a North Korean border guard shot three Chinese residents dead recently, in an incident that has Beijing fuming.

Maybe that also will be a wake-up call to China that, having been a stand-up player on Iran and economics, it should follow suit on North Korea.

WORLD NEWS



European Pressphoto Agency

Firefighters battled a blaze in the marketplace in Osh, Kyrgyzstan, on Monday. The situation remained tense in the area, with at least two Uzbeks killed by security forces in a nearby village.

Both sides blamed in Kyrgyz clashes

Witnesses in Osh, where violence erupted June 10, describe both sides as organized, armed and prepared for battle

By RICHARD BOUDREAU

OSH, Kyrgyzstan—It started as a routine scrape typical of this ancient city's ethnic divide: Two Uzbeks men lost \$45 at the 24 Hours Casino and picked a late-night quarrel with the Kyrgyz manager, claiming the slot machines were rigged.

What happened next, as they fled a hostile crowd and summoned ethnic kin by cellphone, was far more explosive.

Witnesses said an Uzbek crowd gathered—50 at first, then 500, eventually 1,500 or more—and went on a three-hour rampage in the Kyrgyz neighborhood, burning the casino, shooting up windows in a university dorm, pulling over motorists and setting cars afire.

Kyrgyz gangs, infuriated by a rumor that Kyrgyz women had been raped at the dorm, retaliated.

Led by masked men in luxury cars and in some cases armored personnel carriers, they stormed Uzbek neighborhoods across the city in a four-day spree of burning, looting and gunfire that left as many as 2,000 people dead.

Interviews with witnesses in the few square blocks where the violence erupted June 10 indicate that both sides were well organized, armed and prepared for battle.

The picture they describe suggests that the struggle to fill a power vacuum left by the ouster of President Kurmanbek Bakiyev in April could keep this Central Asian country, home to a U.S. air base that serves forces in Afghanistan, destabilized for months to come.

That struggle pits two longtime rivals from southern Kyrgyzstan, where ethnic animosity is most in-

tense: Mr. Bakiyev, who is Kyrgyz, against Kadyrjan Batyrov, a wealthy Uzbek businessman and champion of greater political autonomy for the country's Uzbek minority.

Mr. Batyrov has been quoted in local media as saying that Mr. Bakiyev and his relatives limited his business opportunities.

Seeking to bolster her own shaky authority, interim President Rosa Otumbayeva is asking voters Sunday to endorse a new constitution.

Many Uzbek community leaders oppose holding the referendum now, fearing it could serve as a flashpoint for new unrest.

Tensions flared again Monday, when at least two people were killed by security forces in an Uzbek village where the head of the local police precinct was killed last week when trying to persuade villagers to lower barricades.

Rights groups said forces bent on revenge attacked men and women with rifle butts; government authorities said the deaths occurred when security forces responded to "armed resistance," the Associated Press reported.

Meanwhile, 500,000 refugees remain displaced by the clashes, including 100,000 who have fled across the border to Uzbekistan, according to the United Nations.

The interim government initially asserted that thugs hired by Mr. Bakiyev and his family fomented the recent violence by escalating petty ethnic-based disputes in hope of returning to power in the chaos.

In a shift, prosecutors said Monday they were focusing a criminal probe on Mr. Batyrov as well as on the Bakiyev clan.

Mr. Bakiyev is in exile in Belarus,

and Mr. Batyrov's whereabouts are unknown. Both have denied stirring up violence.

By targeting Mr. Batyrov, the government appears to be acknowledging the strength of his movement.

Defense Minister Ismail Isakov calls him an extremist who provokes followers with pro-autonomy speeches. He already faces charges of inciting riots in the nearby southern city of Jalal-Abad in May.

"Today's situation is a result of a confrontation between Bakiyev, who wants to return to power at any expense, and Batyrov, who wants to dismantle the Kyrgyz state in the south," Mr. Isakov said in an interview, adding that dozens on both sides had been arrested. "It's not ethnic; it's purely political."

Yet there is little doubt that rival camps in southern Kyrgyzstan had been bruising for a confrontation in Osh, where Uzbeks make up nearly half the 250,000 population.

The violence unfolded swiftly along an unmarked divide between the mostly Kyrgyz neighborhood of Andizhanskaya and the predominantly Uzbek enclave of Shakhid-Tepe.

Tension had been in the air for weeks. In early May, Mr. Batyrov had gathered a large crowd of Uzbeks in Osh for a spirited rally. Kyrgyz border police had noticed a spike in illegal crossings into the city by Uzbeks from neighboring Uzbekistan.

A Kyrgyz-owned gun shop with clients in both adjacent neighborhoods said there had been brisk sales of hunting rifles to Uzbeks.

The Uzbeks' capacity to amass so large a large crowd so quickly after

the 11:30 p.m. casino quarrel was astonishing, witnesses said.

"Normally it's easy for the police in Osh to disperse a crowd of Uzbeks, but this crowd was different—very disciplined and determined," said Tallai Baigazyev, a 42-year-old Kyrgyz security guard who watched the fighting that night.

Police in two patrol cars fired red tracer bullets into the air, he said, but the Uzbek mob, then about 500 strong, continued to swell and the police retreated.

An Uzbek police colonel who appealed for calm was hit by a rock, suffering a serious head wound. Three police cars were burned, the prosecutor's office said.

"Uzbeks don't start fights like this without political leadership," said Tolekan Ismailova, an internationally respected Kyrgyz human-rights activist in Osh. "These actions appeared to be well coordinated."

In Shakhid-Tepe, many residents said they were simply defending the Uzbek neighborhood. But dozens of witnesses saw the Uzbeks, some of them armed, swarm over to the Kyrgyz side, chanting slogans such as "Osh is Ours!"

After hundreds of women in three four-story dormitories fled screaming to the rooftops, some in the crowd shouted "We raped your women!" according to Ziada Mamasaitova, a cook at a nearby restaurant.

In fact, the mob didn't enter the dorm complex or assault any students, three of its residents said.

But the tale of rape went viral, repeated unchallenged by ordinary Kyrgyz and senior officials as the trigger that set off the bloodletting.

Mr. Baigazyev, the Kyrgyz guard, who protects two casinos in the neighborhood that weren't hit, described the Kyrgyz gangs who struck back the next day as "something resembling a special paramilitary task force, organized in advance."

He said he saw masked men in a Toyota Land Cruiser and a Hummer distributing guns and cash to Kyrgyz marauders in Shakhid-Tepe. The men in the Land Cruiser didn't speak Kyrgyz or Uzbek, he said; officials claim Mr. Bakiyev's son hired thugs from other countries.

Alik Rakhimov, a 27-year-old Uzbek shopkeeper in Shakhid-Tepe, said an armored personnel carrier also attacked the neighborhood, accompanied by men in military uniform shouting "Kill all the Uzbeks!" "We ran away, and they set fire to the houses," he said. "When we came back to put out the fires, they shot at us."

Elders in the neighborhood said 15 people there were killed and 360 homes were destroyed.

The government has denied widespread reports of army involvement in attacks on Uzbek areas.

Pamirbek Asanov, a deputy head of the prosecutor's office in Osh, said investigators considered the violence "a provocation by third parties" who turned ordinary Uzbeks and Kyrgyz against each other. "Who represents these third parties? Of course, the Bakiyevs on the Kyrgyz side and Batyrov on the Uzbek side."

A senior prosecutor, Atai Shakir Uulu, said the government probe was stalled because most of the investigators are Kyrgyz and fearful of entering Uzbek neighborhoods to do their work.

WORLD NEWS

A new sumo scandal grips Japan

Athletes admit to betting on baseball, top sponsor considers walking away, and big tournament hangs in balance

BY MARIKO SANCHANTA
AND KOSAKU NARIOKA

TOKYO—The latest scandal to rock the sport of sumo wrestling involves gambling, reports of Japanese mafia involvement and a 29-year-old hairdresser who specializes in top-knots.

In the latest revelation—which has caused almost as much uproar in Japan as Tiger Woods's infidelities in the U.S.—65 of the sport's 700 active sumo wrestlers have admitted to gambling on baseball and other games, said a spokesman for Japan's sumo association.

The sumo association said Monday that the disclosure could force the cancellation of next month's grand tournament. The sport's largest sponsor, a maker of traditional Japanese soups, said it is considering pulling its advertising—displayed as banners paraded around the ring—from this and other tournaments.

Sumo wrestling, the iconic Japanese national sport steeped in hundreds of years of ancient rituals and discipline among its plump practitioners, has been shoved under a spotlight in recent months due to a plethora of scandals that have involved top wrestlers in drunken brawls and smoking marijuana.

The Japanese media have also reported that some of the gambling was through *yakuza*, the Japanese mafia.

The sumo association spokesman said he couldn't comment on whether gangsters were involved but added that the association is cooperating with a police investigation of the matter.

A hairdresser by the single name of Tokoike, who styles sumo wrestlers' samurai-style topknots, is the alleged middleman in the gambling operation, according to the Japanese media. He couldn't be reached for comment.

The reports threaten to derail a grand tournament, something that hasn't happened since 1946, when repairs at a hall were delayed.

"We are making preparations to hold the Nagoya meet, but we will



Sumo association chief Musashigawa, left, speaks to reporters in Tokyo on June 14. At right, ex-champion Asashoryu.



have another debate on the issue at an executive meeting on July 4, after we have received a report from the special investigative panel looking into illegal gambling," Musashigawa, the chairman of the Japan Sumo Association, told a news conference Monday.

Musashigawa himself has faced criticism, as one of his protégés was reported to have joined the betting ring.

In a move that underlines the level of obsession with the sport, national television channels featured former sumo wrestlers weighing in on the latest scandal on Monday evening, pushing aside the live news conference by the country's new prime minister, Naoto Kan.

The Japan Sumo Association, which governs the sport and is known for its strict adherence to hierarchy and ritual, said it has formed a special investigation committee composed of 10 outsiders. The association will decide whether

the Nagoya grand sumo tournament should be held as scheduled July 11, and if so, whether the 65 wrestlers who have admitted to gambling will be allowed to participate.

The sumo association spokesman said 29 admitted to betting on baseball. The rest gambled on cards, golf and mahjong, a Chinese tile game similar to cards.

Yuichi Sato, a spokesman for Japan's ministry of education, culture, sports, science and technology—which supervises the JSA—said the government was particularly concerned about the reported ties to *yakuza*, which could further undermine the sport's public reputation.

"As a public entity, it is inappropriate for the sumo association to have links with the organized-crime groups, even if those are at the level of individual wrestlers," Mr. Sato said in a telephone interview.

Nagatanien Co., the top corporate sponsor of the grand sumo tourna-

ments, is thinking about yanking its banners from the game, which are paraded between matches.

"We are considering ending our sponsorship due to the baseball betting scandal," said Yukiko Aizawa, a spokeswoman for the company, famous for its instant miso soup and mix for *ochazuke*, a green tea poured over rice.

The company, which started advertising at sumo matches a decade ago, spends 72 million yen a year, or about \$794,000, on advertisements at the six grand sumo tournaments a year. McDonald's Japan, which started advertising at sumo tournaments last year on a smaller scale, said it currently had no plans to stop showing its banners at matches.

Some sumo wrestlers, who were once considered to be near-deities in Japan and famed for their dignified—and discreet—manners, have been vilified over the past year for engaging in activities that reveal they are human after all: They drink,

smoke and gamble, like other young men their age.

In February, Asashoryu, the 29-year-old former Mongolian grand champion, announced tearfully that he would retire from the sport following a drunken brawl on a Tokyo street. He had just won his 25th national tournament in January. The JSA has also been plagued by the arrests of marijuana-smoking wrestlers and the death of a trainee at one of Japan's stables, or sumo training centers.

The moves come at a time when sumo in Japan has lost popularity to other sports such as football and baseball.

Fewer Japanese men find the sport alluring and the top ranks have been populated by foreigners—primarily Eastern Europeans and Mongolians. The last time a native Japanese wrestler won a sumo tournament was in 2006.

—Miho Inada
contributed to this article.

Japan tax increase years away, Kan says

BY TOMOYUKI TACHIKAWA

TOKYO—Japan's Prime Minister Naoto Kan said Monday that it may take two years or more before the government makes any increase in the nation's 5% consumption-tax rate, adding that he wants to start a discussion on tax issues after Upper House elections next month.

"It would be better for me to avoid mentioning the timing [of consumption-tax increases], but I personally think it may take two, three years or more" before the government raises the sales-tax rate, Mr. Kan said at a news conference.

The prime minister suggested last week he would raise the tax rate above 10% over time, drawing fire from several ruling-party lawmakers, because such taxes are unpopular with voters.

Clarifying his remarks Monday, Mr. Kan said several years would be needed to put in place a system to

reduce the burden of higher consumption taxes on lower-income households, who tend to suffer more from such levies because they spend a greater portion of their income on food and other essential items.

The government is considering providing tax refunds or lowering levies on the purchase of goods seen as necessities, Mr. Kan said. But he added that the move will likely require an invoice system to clarify taxes paid and that creating such a system would take time.

"If you think I sent the message that I will raise consumption taxes right after the Upper House elections, you are wrong," he said. "First I would like for cross-party discussions on consumption taxes to move into high gear after the elections," while drawing on the opposition Liberal Democratic Party's proposal for a 10% consumption tax rate, he added.

As Japan's public debt level approaches 200% of gross domestic

product, the highest among industrialized countries, tax increases are considered inevitable. Analysts say Mr. Kan's challenge is to explain why a 5% sales tax increase is needed and how he intends to spend new revenue. Failure to answer such fundamental questions could hurt his credibility and cost his party votes in the Upper House poll.

In February 1994, then-Prime Minister Morihiro Hosokawa suddenly announced plans to push the rate up to 7% from 3% at a midnight news conference. But the plan went nowhere. He dropped it the next day after a public backlash.

When former Prime Minister Ryutaro Hashimoto lifted the national sales tax to 5% from 3%, he was trounced in the July 1998 Upper House election and forced to step down, as criticism grew that the tax increase weakened consumer spending, dragging down economic growth.

Mr. Kan's public support rating



Japan's Prime Minister Naoto Kan speaking on tax issues Monday.

declined nine percentage points in a week after he signaled his willingness to consider raising the consumption tax, the Asahi Shimbun re-

ported Monday. The results of the survey conducted over the weekend showed his support rating fell to 50% from 59% in the previous poll.