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State Weakness in Perspective: Trans-territorial Energy Networks in Georgia, 1993-2003

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AUTHOR DECLARATION

I certify that all material in this thesis which is not my own work has been identified and that no material has previously been submitted and approved for the award of a degree by this or any other University.

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Abstract

This thesis is concerned with the persistent weakness of the post-Soviet states and it examines the implications of state weakness for inter-state relations. Applying concepts from the trans-national and globalisation literatures, this thesis determines that it is in the synergy between global and local forces, state and non-state actors, and informal and formal economies where the dynamics affecting the post-Soviet state are located. The weak state is reconceptualised as an arena for the operations of stakeholders locked in a struggle for resources.

The principles of network analysis are used to develop a political network model of socio-economic relations in a weak state. The network model is used to assess the role and implications of the trans-territorial networks operating in Georgia's energy sector. Numerous examples illustrate how the monopolisation of transactions by networks was a major contributing factor in the decline of Georgia, deterring it from engaging in collaborative arrangements to rectify weakness. The decline of the state occurred despite the fact that Georgia's geo-strategic location along a lucrative hydrocarbon transit corridor meant that it received significant levels of foreign assistance and investment.

Empirically, the network model offers a different analytical lens, through which it is clear that a weak state's inter-state relations are best viewed within the dynamics of trans-territorial networks. Theoretically, the reordering of state-societal relations within the networks, as well as the interdependence of these networks with external actors, exposes a complex web of relations that disperses authority and legitimacy across a spectrum of entities. While not contesting the juridical sovereignty of a state, this thesis argues that a weak state's domestic sovereignty is neither a given ontological entity, nor is it located within the traditional polis, but it is rather simulated by various stakeholders traversing the state.

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The Georgians have a saying: 'A guest is a gift from God.' I certainly felt welcome in Georgia, and it changed my perspective on many things, including myself. I dedicate this thesis to the future of a thriving Georgia and to a peaceful South Caucasus region.
SRC

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Acronyms and Abbreviations

ACG	Azeri-Chirag-Guneshli fields
AES	American Enterprise Services Corporation
AIDs	Acquired Immune Deficiency Syndrome
AIOC	Azerbaijan International Operating Company
AmCham	American Chamber of Commerce
ANM	Armenian National Movement
BP	British Petroleum
BTC	Baku-Tbilisi-Ceyhan oil pipeline
BTE	Baku-Tbilisi-Ezerum gas pipeline
BSEC	Black Sea Economic Cooperation
CIS	Commonwealth of Independent States
CISPFK	CIS Peacekeeping Force
CIPDD	Caucasus Institute for Peace Democracy and Development
CPSU	Communist Party of the Soviet Union
CUG	Citizens' Union of Georgia
DIFD	Department for International Development
E7	International Group of Emerging Economies composed of China, Brazil, India, Indonesia, Mexico, Russia, and Turkey
EBRD	European Bank for Reconstruction and Development
EU	European Union
DFID	Department for International Development (UK)
GAOR	Georgian American Oil Refinery
GDP	Gross Domestic Product
GEL	Georgian lari (currency)
GFSIS	Georgia Foundation for Strategic and International Studies
GIC	Georgian Gas International Corporation
GIOC	Georgian International Oil Corporation
GNERC	Georgian National Energy Regulatory Commission
GNI	Gross National Income
GRECO	Group of States Against Corruption

GUAM	Regional organisation of Georgia, Ukraine, Azerbaijan, and Moldova
GUEU	Georgia-Ukraine-EU gas pipeline
GWEM	Georgian Wholesale Electricity Market
HES	Hydroelectric Station
IDP	Internally Displaced Person
IFC	International Financial Corporation
IFIs	International Financial Institutions
IMF	International Monetary Fund
INOGATE	Interstate Oil and Gas Transport
JCC	Joint Control Commission
KATB	Kars-Akhalkalaki-Tbilisi-Baku railroad
LICUS	Low Income Countries Under Stress
LLC	Limited Liability Company
MFA	Ministry of Foreign Affairs
NATO	North Atlantic Treaty Organisation
NGO	Non-governmental Organisation
ODIHR	Office for Democratic Institutions and Human Rights
OPIC	Overseas Private Investment Corporation
OSCE	Organisation for Security and Cooperation in Europe
ROA-UES	Unified Energy Systems of Russia
SCP	South Caucasus pipeline (another name for BTE)
SOCAR	State Oil Company of Azerbaijan
STO	State Trade Organisations
TACIS	Programme of Technical Assistance to the Commonwealth of Independent States (EU)
TRACCC	Transnational Crime and Corruption Center
TRACECA	Transport Corridor Europe–Caucasus–Asia (EU TACIS)
UDC	United Distribution Company of Georgia
UES	Unified Energy Systems
UN	United Nations
UNDP	UN Development Programme
UNESCO	UN Education, Scientific and Cultural Organisation
UNHCR	UN High Commissioner for Refugees

UNOMIG	UN Observer Mission in Georgia
UK	United Kingdom of Great Britain and Northern Ireland
US	United States of America
USAID	US Agency for International Development
WB	World Bank

Map of the South Caucasus

Source: (Relief Web 2000)

Map of Georgia's Major Cities and Town

Source: (United Nations Cartographic Section 2005)

Chapter 1: Introduction

> I think that if we look at Georgia before Saakashvili, if we look at Georgia under Shevardnadze, it was the only place in post-Soviet space that we could not consider to be a state. Georgia was little more than a territory, a land we could say. Or a very, very weak state. Shevardnadze never reached his main goal. He didn't consolidate, he didn't construct a Georgian state (Aleksei Malashenko in Karumidze and Wertsch 2005: 88).

1.1 Introduction

In conjunction with the collapse of the Soviet Union, the integrated energy system throughout the republics ceased to function. The previous system was directed from Moscow and reliant on the inter-dependence of the republics in sharing various aspects of production and supply. Replacing this were new arrangements based on revised ownership, as well as the inclusion of new sources of energy and payment systems. However, these new arrangements were caught up in several simultaneous events reshaping regional relations. These included wars in the North and South Caucasus and Tajikistan, privatisation of state assets, and the exploration for new sources of hydrocarbons within Eurasia. Russia and some of the Central Asian nations benefited from an influx of funds, new technologies, and alternative export routes for hydrocarbons. However, energy dependent states embroiled in internal conflicts, including Armenia, Georgia, Moldova, and Tajikistan experienced severe energy deficits. The governments were preoccupied by the tasks associated with recovering from war-torn years, navigating the responsibilities required of a state in the international system, and operating within new regional arrangements, in which Russia was still a dominant player. As a result, a new system appeared, one that mostly operated in the shadows for the majority, as the governments were unable to provide goods and services for the citizens.

For a newly independent resource deficient state such as Georgia, securing a regular supply of energy was paramount to strengthening the state in multiple sectors. A sufficient energy supply would be central to the socio-economic development of the state. In addition to rehabilitating national electricity generation facilities and transport systems, financial revenues from taxing the import and transit of hydrocarbons would bolster development budgets. This would be particularly relevant to Georgia, which imported all of its natural gas supply, most of its electricity in the winter months, and virtually all of its petroleum products, as well as serving as the major transit corridor from Azerbaijan and Armenia to Europe. A regular supply of energy to operate state facilities, such as schools, hospitals, and transport systems would also be critical to the welfare of the population. A reliable source of energy would help to bolster the new state's national security by supporting the training and equipping of forces to protect the territory from external threats. Ultimately, a state that diversified its supply of energy sources would be able to more easily pursue multiple geo-strategic orientations and alliances. It is for these reasons that those individuals and institutions that control access to the sources, transportation, and distribution of energy hold significant power, and how they conduct business directly impacts on the development of the state (Ruth 2002).

During the three different periods of President Shevardnadze's reign over Georgia, an adequate level of energy security was never obtained. The first period saw the destruction and dilapidation of the energy sector during the war years (1991-1994). Shortly after independence, Georgia suffered a civil war and two separatist wars, resulting in the loss by 1995 of two key energy transport corridors (via South Ossetia and Abkhazia). This was compounded by wars between Armenia and Azerbaijan over Nagorno-Karabakh, and between Russians and Chechens in Chechnya. A hopeful period followed, in which there was some deregulation and privatisation, including the sale of Tbilisi's electricity distribution centre to an American company (1995-1998). Improvements in legal structures facilitated the reconstruction of an oil pipeline from the Caspian to the Black Sea (Baku-Supsa) and a small oil production industry. However, the 1998 Russian rouble crash led to a period of instability marked by disinvestment and perpetual energy shortages (1999-2003). The only positive development was the commitment by an international consortium to build the Baku-Tbilisi-Ceyhan oil pipeline and a parallel gas pipeline.

Thus, the 'dramatic turnaround' that began after 1995, when Georgia was no longer 'failing' in comparison to the other post-Soviet states, was short-lived (Nodia 2002: 413). By the early 2000s, Georgia's leading scholars concluded that, 'basically the most appropriate notion for describing Georgia is as a weak state, although one might legitimately consider using the term failed' (Darchiashvili and Tevzadze 2003: 108). Georgia's extreme weakness was all the more perplexing given that it received disproportional amounts of foreign assistance when compared to other post-Soviet states. Starting in the late 1990s, Georgia was the third largest recipient of US foreign assistance in the world per capita. Georgia received more than US$ 778 million in aid for the fiscal years between 1992 and 2000, a level roughly five times that of US aid to Azerbaijan for the same period (Giragosian 2001). In 2000, the Clinton administration, partly in an effort to bolster the country's ability to act as a transit state for Caspian hydrocarbon export to Europe, spent US$ 200 per Georgian. This amount was 6 times higher than the amount spent on Ukraine and roughly 160 times more per capita than aid received by Russia (Christophe 2003). Between 1995 and 2003, Georgia received approximately US$ 3 billion towards redeveloping its energy sector in combined international assistance, private investment, and gas and electricity loans.[1]

This thesis is concerned with Georgia's decline during its first decade of independence despite disproportionately high levels of foreign assistance and asks: ***why did the Georgian state remain persistently weak, and what impact did Georgia's weakness have on its inter-state relations?*** Examining the disjuncture between the levels of assistance and a persistently weak energy sector should provide an obvious case study of the factors causing state weakness. This is particularly evident when considering that the path of Georgia's decline can be traced through events related to the absence of energy security. There were the protests across Georgia in 2000 and 2001 as a result of the persistent blackouts and gas shortages in the coldest months, which marked the beginning of the decline of Shevardnadze's political party. There were two major western private investors, whose efforts would have strengthened Georgia's energy independence, but who failed due to newly imposed government regulations. There was Georgia's sale of its strategic energy

[1] Author's estimate.

assets to Russia at the height of disputes between the two governments regarding Georgia's alleged harbouring of Chechen fighters. There was the crippling energy debt Georgia owed to its neighbours, which played a part in the international financial institutions (IFIs) suspending loans. Finally, there were concerns among the international community as to the impact Georgia's weakness would have on securing the hydrocarbon transit corridor from Central Asia to Europe. By 2003, President Shevardnadze's liberalisation programme, so generously funded partly as a result of his role as the Soviet foreign minister who had helped bring down the Berlin Wall and end the Cold War, was deemed impotent both by a majority of Georgians, as well as much of the donor community.

Georgia's weakening paralleled the western governments' heightened concern about weak states beginning in the mid-1990s. Examinations of weak states were made as both a guiding tool for the obstacles to state development, as well as an 'early warning' method to determine future hot points in the world. Weak states were viewed as an epidemic in the global arena – a kind of disease, the symptoms of which were born of a variety of factors and, if left untreated, could contribute to an outbreak of instability across a region of such a scale as to cause an epidemic of insecurity. At that time, the most likely scenario envisioned was the spill-over of violence across borders, which would necessitate intervention by the international community. Addressing state weakness became an even more urgent task for the international community after al-Qaida created a base for its operation in Taliban–controlled Afghanistan and subsequently launched attacks on American facilities, the most devastating being the attack on the World Trade Center in 2001. The 2002 US National Security Strategy placed priority on development assistance for weak states, stating that, 'poverty, weak institutions, and corruption can make weak states vulnerable to terrorist networks and drug cartels within their borders' (The White House 2002). The 2003 European Security Strategy maintained that 'state failure is an alarming phenomenon that undermines global governance, and adds to regional instability' (European Union 2003). Thus, by the early 2000s western security discourse named the weak state among the key threats to international security.

However, qualifying the weak state, quantifying its impact on international security, and devising effective counter measures to address the causes of weakness have proven to be challenging exercises. There have been empirical efforts by governmental and international organisations, such as the UK Government's *Contribution to Millennium Development Goals,* the US Government's *Fragile States Strategy,* and the World Bank's *Low Income Countries Under Stress* project (Department for International Development 2005; US Agency for International Development 2005; World Bank 2002). There have also been three main avenues of academic investigation into weak states, most of which are either subjective and tautological, blaming weak institutions for weak states, or objective taxonomical accounts which measure states according to the idealised Weberian model. The third main approach to weak states has been ideational, whereby the state is perceived to constitute an arena of conflict between the government and its citizens. However, none of the empirical or theoretical approaches have adequately delved into the complexity of causal factors of state weakness. Nor have they addressed the notion of problematic sovereignty in weak states, that is, where empirical (domestic) sovereignty is a simulated phenomenon, the act of which exists for something else (Krasner 1999; Weber 1995).

One key to understanding the causes of state weakness is to re-examine the actors operating within the state, the system in which they operate, and to what ends the state serves their objectives (Smith, et al. 1996). In order to do this, this thesis reconceptualises weak states as a medium for the operations of networks composed of a spectrum of state and non-state actors locked in a struggle for resources, in which the networks have replaced legitimate channels of communication (Holsti 1996; Linz and Stepan 1996). These networks are referred to as 'trans-territorial' in order to capture the fact that they traverse recognised and unrecognised territories moving beyond the 'national' boundaries of the state, both in terms of physical borders and global financial markets (Latham 2001). Alongside a weak state is another ordering of actors, a second if not substitute economy, and an unwritten but understood set of rules that serves the interests of those in power and sustains the livelihoods of the rest. Thus the weakness of a state is not necessarily about a failure to develop, as it is a tool to strengthen certain actors operating within an alternative system of trans-territorial networks. This system challenges the state, which suggests that sovereignty of a weak state may actually exist beyond the authority designated as the state.

This study seeks to make a three-fold contribution. First, it reconceptualises the state as an arena of conflict among stakeholders locked in a struggle for resources. Applying concepts from the trans-national and globalisation literatures, this thesis concludes that it is in the synergy between global and local forces, state and non-state actors, and informal and formal economies where the dynamics affecting the post-Soviet state are located. Second, at the empirical level, a political network model of socio-economic relations is developed to map the dynamics of a compilation of actors. The network model offers a different analytical lens through which to analyse a weak state, concluding that the impact of a weak state on inter-state relations is best viewed within the dynamics of an alternate force of trans-territorial networks traversing the state. Third, at the theoretical level, the reordering of state-societal relations within the trans-territorial networks, as well as the interdependence of these networks with external actors exposes a complex web of relations that disperses authority and legitimacy across a spectrum of entities. While not contesting the juridical sovereignty of a territorially bound state, this thesis offers a new conceptual space for the examination of activities affecting weak states. This leads to the conclusion that a weak state's domestic sovereignty is neither a given ontological entity, nor is it located within the traditional concept of the polis, but it is rather simulated by various stakeholders within and beyond the state.

This chapter begins with a rationale for studying the weak state and presents the primary argument. The second section reviews the published literature on Georgia as a weak state and the transition literature's approach to networks, and discusses the limitations of both for addressing persistent state weakness. The third section provides a conceptual framework for analysing the weak state, which applies concepts from the trans-national literature as a bridging mechanism between the theoretical perspectives of internationalists and globalists. The utility of network analysis will be discussed as a tool for analysing trans-national relations. The fourth section addresses the methodological approaches applied in this research, focusing on the single case study and techniques used in fieldwork to overcome challenges associated with conducting research on sensitive topics. The chapter concludes with an outline of the remainder of the thesis.

1.2 Rationale and Argument

In the supposed era of international terrorism, a new genre of literature is emerging, which claims to dispel two previously held truisms in International Relations literature. First, it claims to have shattered once and for all the idea that domestic affairs can be separated from international studies (Bunker 2003). Second, states are no longer supposed to be conceptualised as they were in the twentieth century, that is, through the Westphalian lens (Krasner 2001). Instead, the literature has developed a host of definitions across the spectrum of degrees of negative sovereignty, from collapsed, failed, shadow, and criminal, to weak and quasi. Clapham (1996: 271-274) has urged the study of international relations to be concerned with political relationships within states, as well as between them. However, there remain at least two obstacles in the literature to truly embracing these challenges. First, the state is most often viewed as a holistic entity; a coherent unit, acting with common purpose and existing as something more than the sum of its parts, or its individual people (Waltz 1979). Second, there is a behavioural assumption that politics within states are significantly different from politics between states. That is, people's loyalty to their state, in particular to the idea of strengthening the institutions within, is more intense than other relationships, such as those with actors outside of the state.

For the most part, the state debate in International Relations remains framed by three ideas, within which there are juxtaposing theories. First of all, the state is either a rational unitary actor or it is being subsumed by globalising forces. Second, state institutions conduct business in the formal sector, while non-state actors operate in the informal sector. Yet a third idea is that state institutions adhere to the rule of law, while illicit activity is, for the most part, the conduct of less savoury actors in the shadows. The so-called 'third debate' in International Relations solidified these dichotomies in the coalescence of the neo-realism/neo-liberalism paradigms. They maintained the assumption of a rational actor - *the state.* However, the policies pursued by weak states do not quite fit into these theoretical explanations. How those residing in weak states perceive the role of the state, treat matters concerning the state, and operate within and beyond the state are different from the strong state.

Defining the state in International Relations and locating state sovereignty are perhaps the two most fundamental debates in the literature. And yet, the assumption of a state, its sovereignty, and the functioning of a specific kind of state sovereignty are often taken for granted in the literature regarding weak states. This not only places certain restrictions on the possible variations on stateness that can occur among stronger and weaker states, but it also limits the debate about the causes of persistent weakness. The post-positivist theories provide some space for seeing the state as a problematised entity, and for conceiving of stateness as a continuous process, utilising empirical analysis to go beyond the rational actor (Ashley 1987; Ashley 1998). Hence, when discussing the weak state in International Relations, this study will treat these two terms – state and sovereignty - as problematic and will attempt to explore alternative conceptualisations of the weak state and its sovereignty.

As a result of extensive fieldwork in Georgia, I conclude that weak states are mediums for the interaction of a variety of state and non-state actors operating in web-like formations traversing the state in the pursuit of resources. I conceptualise these relationships through a political network model of socio-economic relations. The network model is composed of stakeholders from the following four groups: *elite* (ruling family, key power ministers, and international partners), *bureaucracy* (state and local), *business groups* (peacekeepers, paramilitary groups, and criminals), and *consumers* (the marginalised majority). Most transactions among the stakeholders are made with the *sponsorship* of someone working in the state apparatus. Transactions take place between official and unofficial markets, or in the *grey market*. Stakeholders form *trans-territorial* networks, traversing recognised and unrecognised territories, taking advantage of global markets. The networks are *semi-permanent,* forming for a specific task with a *unique* assemblage *conditioned* by socio-political and economic factors. Some of the networks operate as a substitute for the state, in the absence of a reliable and undiscriminating supply of goods and services. Others take advantage of the deficiency in enforced regulatory mechanisms to enhance their personal earnings. The networks eventually create an *alternate force*, which, for the most part, works counter to strengthening the state.[2]

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[2] I chose deliberately not to use the term 'corruption' in this thesis when describing Georgia's persistent weakness unless it is used by authors in their descriptions, or in the names of organisations. It is because corruption is rather like 'weak', in that it increasingly means everything, and therefore

Applying the network model to several trans-territorial networks traversing Georgia in the energy sector allows for a much more nuanced understanding of interactions in a weak state. I conclude that the weak state is an internationally recognised state in which networks have replaced legitimate channels of communication. Flows of information, finances, directives, and implementation of directives do not occur in a recognisable, transparent, and logical manner. These networks infiltrate every aspect of the state to such a significant degree that decisions are taken based on the directives of the actors within the networks. Their decisions often subvert the transparent laws and procedures of enforcement, purposefully keeping the state weak. Authority rests on the accumulation of assets through the state apparatus, which validates the basis for the patron's power over clients within networks. This authority, however, is undermined by a lack of legitimacy among the population, which results in overlapping networks of marginalised members of society with non-state entities.

International recognition of a state and relations of the regime with international actors, including other states and organisations, is crucial to the regime's survival. However, the actors within the state have a contrived notion of the territorial and institutional state. Territory is simply something in which to move about and beyond in the pursuit of resources. Statehood can assist (through international legitimisation) but does not prevent the network's activities. Moreover, while the government is too weak to govern effectively, individual members of the government are strong enough to grab scarce resources, to push economic activity into the shadows, and to suppress political and economic opposition questioning the legitimacy of the regime. Juridical sovereignty is an asset; a valued prize fought over by contending groups for the right to use the shell of the state in pursuit of personal power and profit. Thus, weakness is not necessarily about the failure to develop state institutions, nor is it about measuring the relationship between the state and society, but it is rather a deliberately designed condition to strengthen certain actors within and beyond the state.

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retains little value. Therefore, it deserves a thorough review in and of itself. Corruption more often refers to elite abuse of privilege, and this thesis obviously moves well beyond that to a group of actors whose actions contribute to undermining the state. Further, corruption has attached to it a necessarily negative connotation, while this thesis argues for a more neutral selection of terminology in order to avoid the pejorative and agenda-setting analyses of weak states that tends to dominate the literature.

1.3 Literature and its Limitations

The lack of International Relations literature on Georgia is unsurprising, and is worth noting as a literary reflection of the less than central position given to Georgia after its independence. The events during and after the November 2003 parliamentary election leading to the Rose Revolution and the resignation of President Shevardnadze increased Georgia's coverage. One of the leading revolutionaries, Mikheil Saakashvili, won the January 2004 presidential election with an overwhelming majority of 96 percent. This led to the publication of several books and articles on socio-political aspects of Georgia's revolutionary experience (Broers 2005; Coppieters and Legvold 2005; Fairbanks Jr 2004; Jones 2005; Karumidze and Wertsch 2005; King 2004; Morozova 2005; Wheatley 2005a). Despite this, there remain so few works on Georgia that the spectrum of the literature review will be broadened to cover political science literature on transition more broadly. The literature provides three explanations for Georgia's weakness: ethno-territoriality versus nationalism, Russian encroachment, and failed transition. The concept of networks was employed in the latter explanation by scholars studying Central and Eastern European transition. It provided some insights into the legacies of network formation in the political, economic, and social realms of former communist states that hindered post-independence transition. Georgia's weakness, and the broader coverage of networks in the transition literature, will be discussed, including the limitations of its application in this thesis.

1.3.1 Reasons for Georgia's Weakness

Georgia's independence was followed shortly by three conflicts, social dislocation and instability, ethnic divisions, and politics characterised by factional battles (Garnett 2000). A leading Georgian political scientist, Gia Nodia, explained that the disintegration of the state went further in Georgia than anywhere else in the former Soviet Union with the exception of Tajikistan (Beissinger and Young 2002: 412). The literature is unanimous that at least until 1994, Georgia was a failing state, if not virtually collapsed (Demetriou 2004). According to one analyst, 'In the winter of 1993-94, the Georgian government could not manage to defend the country, keep order on the streets of the capital, pay state workers, collect taxes, or print the currency in common use' (Fairbanks Jr 2001). There was a fear that Georgia might not survive as a state, but rather that it would 'disintegrate into a collection of ethnic enclaves and warlord fiefdoms' (Aves 1996: 3). A collection of works attributed Georgia's weakness to the conflict between the unitary nationalist ambitions of the Georgian population and the ethnic diversity within Georgia (Broers 2003; Losaberidze and Kikabidze 1998; Nanava 2005; Panossian and Schwartz 1994; Suny 1994). Georgia's weakness was linked to the problem of ethno-territoriality, in particular the clash between Georgians and ethnic minority groups in South Ossetia and Abkhazia (Duffy Toft 2001b; Lynch 1998). Cornell showed how autonomy, by empowering ethnic elites with control of state-like institutions played a crucial role in the escalation of the conflicts in Abkhazia and South Ossetia. Conversely, the absence of autonomy mitigated separatist and secessionist sentiments among two of Georgia's other minority groups - Javakheti's Armenian and Kvemo Kartli's Azeri populations (Cornell 2002a).

In the post-war malaise, the problems of ethno-territoriality persisted, but it was now complicated by the after effects of 'frozen conflicts' in Abkhazia and South Ossetia. One effect was the high levels of anti-politics sentiment after ethnic conflict (Tamasz 1994; Fairbanks 1997). The second effect was the transformation of the chaos of war into networks of profit, which supported the institutions of the separatist states (Demetriou 2002a; King 2001). Related to this was Keen's reference to Georgia when discussing the role post-conflict economies of violence played in keeping the state weak (Keen 1998). Snyder argued that individual security was threatened as a result of the rise of war-time semi-private militias in the Caucasus (Rubin and Snyder 1998). Questions of how to overcome the post-Soviet frozen conflicts between the newly constituted state and minority-populated regions resulted in various solutions proposed by analysts, including federalism, autonomy, or independence (Aves 1996; Bertsch 1999; Coppieters 1996; Coppieters 2001; Cornell 2002b; Dawisha and Parrott 1994; Dawisha and Parrott 1997; Goldenberg 1999; Lynch 1998).

A second approach in the literature examined whether Russia was a source of Georgia's weakness. The Russian armed forces' support for the separatist fighters during the conflicts, and their role as the post-conflict peacekeeping force in Abkhazia, was assessed to be a challenge to Georgia's sovereignty (Baev 1997;

Cornell 2001a; Light 1996; Lynch 1998). This tension was heightened by the continued presence of Russian military bases in Georgia despite requests to leave (Antonenko 2001b). According to a Georgian expert, Russian government officials used their position of relative strength as a strategic bargaining tool to counter Georgia's Euro-Atlantic orientation (Rondeli 2003). As Duffy Toft explained, a 'large, powerful, imperialist neighbour, made it impossible for Georgia to establish stable institutions capable of moving it towards its goal of a strong, multinational and democratic state' (Duffy Toft 2001b). Another Georgian expert took the position that Georgia had not gone far enough in its western orientation, while at the same time rejecting Russia as a development model (Nodia 2001).

A third approach recognised Georgia's failure to meet democratic and economic transition goals. Cornell explained,

> Transition is over and what is left are a poorly institutionalised form of politics, endemic levels of corruption, deeply impoverished populations, low levels of economic interaction with international markets, declining production bases and subsistence agricultural sectors - all within a climate characterised by growing popular disenchantment and a deepening gap between the ruled and ruling (Cornell 2003: 12).

A common theme was the interweaving of 'politics, crime, and clans', which normalised the diversion of state assets for private means (Darchiashvili 2003). Fairbanks explained that this intertwining of business and politics meant that the 'weak state' would be hard to overcome because it fed on itself (Fairbanks Jr 2001). Experts in the Georgian Parliamentary Budget Office explained that slow rates of growth and disparity in income levels in Georgia were caused by the fact that political-economic power was held by personnel who had not changed since Soviet times (Gotsiridze 2001). Lengthy academic studies focussed on entrenched corruption in Georgia, the result of the monopolisation of the political system through such practices as clientelism, criminal activity, a weak law enforcement, and the manipulation of state resources to provide economic benefits for a privileged few (Huber 2004; Stefes 2005).

Overall, the literature on Georgia's weakness is marked by well trodden paths of scholarship from historians and economists, to transitoligists and foreign policy experts. However, none of the explanations alone addresses persistent weakness in Georgia, and no study has attempted to combine them. Granted, it was not the purpose of any of these studies to directly examine state weakness; it was rather an underlying theme among all of the discussions of Georgia's post-independence challenges. The transition literature has begun to explore the deficiencies in the newly independent state's reconstitution and developmental processes through the concept of networks. While not addressing Georgia *per se*, the more interesting explanations for persistent weakness are found in the studies on networks to follow.

1.3.2 Transition Literature on Networks

Network analysis has been used to interpret three main strands in the network literature. These include the institutional legacy of state socialism, organisational changes after 1989, and the dangers that could derail the process of economic recovery. One study of Central European states viewed the network as an alternative medium or 'deliberative association' of actors who conducted economic action between markets and bureaucratic regulation in the 1990s privatisation process (Stark and Bruszt 1998). However, it did not offer an example of how networks could influence the interacting processes of political and economic transition (Ganevt 2000). In Stark's more recent collaborative work on inter-enterprise formation, the authors touched on the interface between multinationals and locally embedded structures and concluded that foreign direct investment restructured, but did not eliminate, inter-enterprise ownership networks in Hungary (Stark and Vedres 2006). Another study detailed the active participation and undue power of 'particularistic networks' during the Bulgarian privatisation process (Bojicic-Dzelilovic and Bojkov 2005). These networks, composed of the political and economic elites, manipulated the 1990s privatisation process, negatively impacting on the efforts to transform the socialist economy to a market economy. Of most interest is the explanation of how the eclipse of the state by personal or party interests led to the public's growing discontent and mistrust of post-communist politicians. Consequently, societal groups created compensatory mechanisms for the endemic failures of the state.

Network analysis has also been used to discern the degree of influence sustained by the Soviet *nomenklatura* versus new political-economic structures in post-Soviet governing structures (Duffy Toft 2001a; Hughes, et al. 2002; Kirkow, et al. 1998). Hughes et al. (2002) studied Russian decision-making elites at the sub-national level, often overlooked in the transition literature. Their purpose was to determine whether local political structures converged to a western type, depending on the concentration of non-*nomenklatura* personnel in regional governing structures. The results showed that the regional elites in Russia were mixed and divided, and included a significant number of private sector actors. This contradicted an earlier study on networks in which the authors argued that there was little change in the *nomenklatura* from the Soviet to post-Soviet era (Khrystanovskaya and White 1996).

Another study factored in the role of sub-state activities in the western-assisted transition programmes. Wedel's comparative study of networks mapped the connections among consultants, cliques, reformers, and financiers and their defective application of foreign assistance in the early years of transition in Eastern Europe (Wedel 2003). Two network systems were compared – the 'partially appropriated state' of Poland and the 'clan state' of Russia.[3] The former was a case of substantial appropriation of the state and use of politics by private actors, while the latter was sweeping appropriation by a near wholesale intertwining of state resources and politics (Wedel 2003: 427). This study was particularly interesting for the intersection of state and societal groups in undermining the strengthening of the states.

A study on patron-client networks in post-communist Armenia explained how patrimonialism was used to rebuild the state following the war with Azerbaijan over Nagorno-Karabakh (Bremmer and Welt 1997). During the war, members of the Armenian National Movement (ANM) had acquired influence among substantial groups of industrialists, businessmen, and bureaucrats. By the mid-1990s, the ANM leaders gained the loyalty of these groups by granting two tiers of leadership oversight of a business or governmental agency. The first tier was reserved for the Armenian power ministries (e.g. Internal Affairs and Defence) and the second tier included the

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[3] Russian social scientists define 'clans' as informal groups of elites whose members promote their mutual political, financial and strategic interests. Rather than primarily family or kinship ties, the clan refers to long-standing associations and a desire to continue working together to enhance personal interests. In other words, the Russian clan could be substituted for the post-Soviet phenomenon of the new elite – a combination of the former Soviet *nomenklatura* and the new economic class.

prime minister and other ministries. While Armenian President Ter-Petrosian did not directly head a business network, he was involved in all matters concerning the legal, financial, and international decisions necessary for the business networks to succeed. These networks spanned out into the regions, resulting from the deliberate design of the legislative body. Another study of patronage networks concerned Uzbekistan, where the Soviet practice of using the formally structured administration system and legal regulations as a screen for informal power networks continued (Ilkhamov 2006). As with the study on Armenia, this research concluded that the exclusive central position of the government, combined with a new type of ideology to revive and enforce patriarchal norms and values, led to the loose application of the law in order to protect the single party of power in modern Uzbekistan.

Networks of a clan nature were featured in a study on Central Asia. Collins argued that the influence of indigenous clan-based networks usurped state power (Collins 2004). Clans in Central Asia served as an alternative to formal market institutions and official bureaucracies, and operated both horizontally, based on mutual levels of trust between members, and vertically, to include elite and non-elite members of society and state. Clans were formed as a result of ethnic, clientelist, and regional ties. Clan governance was defined as a separate functioning system that often interacted, in both manipulative and sometimes cooperative ways, with these other systems. The Central Asian state was often simply a shell in which competition took place among clans in their pursuit of resources (both material and political). The functional role of clans was particularly important in reducing the high transaction costs of making deals in an environment where impersonal institutions were weak or absent and stable expectations were hard to form. Thus, they acted as a second economy that interfaced with the official economy, compensating for the high costs of business by facilitating informal networks.

The non-governmental organisation, International Alert, conducted research in the South Caucasus, examining the nexus between corruption and the unresolved conflicts in an effort to identify opportunities for combining anti-corruption and peace building strategies (Mirimanova 2006). The study explored cross-border networks between people of comparable levels of authority from the recognised and unrecognised territories, including local authorities and law enforcement agencies.

Network connections were deemed corrupt because participants violated their mandate to guard and secure the economic interests of the state in the pursuit of personal profit. This study addressed society's 'reactive' participation in cross-border networks as a 'coping strategy', as well as those who 'proactively' participated for individual enrichment. Networks also included international governmental and non-governmental organisations and peacekeeping forces, which acted as both a source and beneficiary of illicit connections.

This brief survey of the transition literature suggests that the conventional approaches to the study of networks in the post-communist states appear to be focused primarily on political elites and economic development; networking is power driven and *nomenklatura* centred. Those studies that do broaden the scope of networks either examine the pattern of linkages between and state and societal spheres of influence at the sub-state level, or between the state and supra-state entities, such as trans-national or multinational actors. None of the studies attempts to examine a confluence of both. Absent are studies of networks among elites across borders, or among co-ethnic groups from two different states. Finally, networks are never treated as an actor in inter-state relations. While the transition literature on networks recognises the Soviet legacies of *nomenklatura*, patrimonialism, and the informality and non-transparency of network systems, it does not bring them together in a coherent way to examine the path of mutual dependency from the pre- to post-Soviet periods.

Nevertheless, this thesis is inspired by all of the studies of networks and it will endeavour to employ the concepts in a more comprehensive way. If the causes of Georgia's weakness are to be located, it will be necessary to take a somewhat broader perspective than is usual in post-Soviet transition literature. In particular, the whole notion of the weak state in the literature, even considering the references made to Georgia, lacks a refined understanding of the state and therefore does not capture the complexities that cause weakness. Building on the application of networks in the transition literature, this thesis will develop a network model of a post-Soviet state in Chapter 4. Then, in subsequent chapters, it will test the model in order to demonstrate the relationship between a network system and state weakness.

1.4 Theoretical Perspectives and Framework

A search for a conceptual framework within International Relations through which to examine the weak state's impact on inter-state relations soon reveals that scholars who concentrate on the grand theories of International Relations often ignore societal linkages across boundaries. While internationalisation is about states and describes the extension of their activities across state boundaries, globalisation is claimed to project us into a world beyond states and territoriality distinct from state-driven activities. Globalisation has received a lot of criticism from International Relations theorists. Realists believe that those who follow globalisation tend to underestimate the importance of state power and security. Pluralists argue that a focus on globalisation draws attention away from the more concrete understanding of international and trans-national actors. Structuralists believe that the process of globalisation is reordering the environment in which states operate, introducing a new era of state formation. Clark (1999) argues that all three theoretical schools unnecessarily disassociate changes in the international system from simultaneous domestic transformations in statehood. He suggests that it is precisely in the synergy between the global and domestic that dynamic change is to be located (Clark 1999).

Thus, when studying networks in a weak state, it is useful to move beyond the divisions within and between the international and globalisation literatures to a theoretical framework of trans-national relations (Risse-Kappen 1995). Except in limited cases, academics have treated them as residual to the states and populations that are affected by them, help to create them, or use them for their own purposes (Callaghy, et al. 2001: 11). Since the 1970s the typical application of trans-national relations has been to study non-governmental organisations or multi-national corporations. Hence, the focus has been on institutionalised structures that operate over a longer-term in formally recognised and somewhat regulated environments. In the mid-1990s, Risse-Kappen redefined trans-national relations as, 'regular interactions across national boundaries when at least one actor is a non-state agent or does not operate on behalf of the national government or an intergovernmental organization' (Risse-Kappen 1995). Since Risse-Kappen's work, ideas about trans-national relations have been substantially expanded in the globalisation literature. Patterns of enhanced worldwide connectedness, whether physical (transport or banking), normative (trade rules), or symbolic (common culture or language), have contributed to the growth of trans-national networks (Anheier and Katz 2005). Global flows of goods and information now 'enmesh' societies into trans-national networks (Held and McGrew 2000: 3).

However, the notions of 'deterritorialisation' and 'unboundedness' in the globalisation literature are not yet relevant to the trans-territorial network studied in this thesis. The networks traversing Georgia are, for the most part, restricted territorially and financially, simply due to the scale of the activity and types of transactions. Granted, opportunities have expanded for the former Soviet states, to include working with foreign companies and accessing international financing (Smith and Guarnizo 1998: 10-11). Most of these relations are simply the continuation of commerce between former Soviet republics when they existed within one state, particularly in the last twenty years of the Soviet Union. Moreover, while new business networks have emerged from increasing trans-national relations, to a great extent they have been the work of local businessmen, who have taken advantage of an ineffective legal system, non-transparent economies, and weak sovereignties (e.g. porous borders and the absence of enforced security). Thus, the notion of trans-national relations in this thesis will refer to the relations between global and local, state and non-state actors engaged in activities between the official and unofficial economies in trans-territorial networks.

Conceiving of trans-national relations of a weak state as networks allows for a greater understanding of how individuals or organisations are connected and relate to one another, and what structural patterns emerge from such interconnectedness. As already discussed, there are some studies of networks in the transition literature. The application of the concepts of networks is made across a spectrum of disciplines, which has grown over the past three decades in western social science. The application of networks analysis was first used by British anthropologists, and was later used by American sociologists in the 1970s.[4] By the 1980s, network analysis was being employed in comparative politics, public administration, organisation

[4] For a more detailed explanation of the development of network analysis in Western social science, see (Easter 1996: 557-559)

theory, and the sociology of stronger states (Degenne and Forsé 1999; Giddens 1984; Knoke 1996; Scott 2000; Wasserman and Faust 1994). International Relations began to conceptualise relations in networks when discussing the role of non-state actors, mostly in the form of non-governmental organisations or international financial institutions and their impact on either state sovereignty or world politics (Josselin and Wallace 2001). In the post-Cold War era, the globalisation literature advanced the notions of networks in the international system, focussing on trends in networking among various societal groups (Rosenau 1995), international organisations, corporate power structures, and regional-global networks (Beck 2000), and communications and technological links (Castells 1996). An underside to the literature addressed networks of organised criminals, the mafia, arms traffickers, and terrorists (Duffield 2001; Kaldor 1999; Pugh, et al. 2004).

Network analysis is not a theory but a set of related approaches, techniques, and tools for describing and analysing relationships among individuals, organisations, and other social entities (Anheier, et al. 2005: 207). Network analysis is a constellation of diverse methodological strategies, usually qualitatively applied, and used to depict organisational behavioural, societal connections, and, more recently, the globalisation of civil society (Anheier, et al. 2005; Emirbayer 1994). The most common way in which it is used in the political science literature is to break down institutions into positions or roles occupied by social actors and to map the relations or connections between these positions, explaining the distribution of power across networks (Knoke 1990: 7-10). Network analysts debate amongst themselves as to how various issues can be operationalised for the purposes of empirical research (i.e. social structure, distance, cohesion, or network centrality). What unites the various approaches of network analysis is the focus on structure or the relations between nodes, independent of the specific attributes of these nodes. It is most important to understand how individuals or organisations are connected and relate to one another, and what structural patterns emerge from such interconnectedness. It is this aspect of network analysis that will be applied in this thesis.

Thus, the theoretical perspective of trans-national relations, where the global and local intertwine, will be combined with the framework of network analysis to create a different analytical perspective for examining the weak state. In particular, a political network model of socio-economic relations will be developed to capture the complexity of trans-national processes. This should lead to a clearer understanding of trans-national relationships that exist beyond the traditional patterns of inter-governmental (state-to-state), non-state (civil society), or the interaction between state and non-state actors. Network analysis should also allow for a comparative analysis of the various group characteristics within networks and the dynamics of the network system. For example, it will be useful to study how networks comprised mostly of state officials operate differently from those that are more embedded in society. Finally, the relational evidence from specific case studies of energy commodity networks should ultimately produce a broader picture of a trans-territorial web of networks. Their combined force will provide a basis for deducing how trans-territorial networks impact on a weak state's relations with other states.

1.5 Methodological Approach

This thesis concentrates on a holistic single-country study, which is composed of eight cases of trans-territorial networks operating in Georgia's energy sector from 1993 to 2003. The purpose of the research design is to enhance empirical and theoretical work done previously on state weakness in International Relations. The eight energy sector studies are used as an explanatory aide to gauge causal inquiries as to why Georgia was persistently weak (Yin 1989). Yin refers to this as 'multiple-case, replication design' (Yin 1989: 55). The multiple-case design generates replication of the same methodology in several similar cases where outcomes are presumed to be consistent in order to demonstrate the theory that state weakness is a result of the actions among stakeholders within trans-territorial networks (Yin 1989: 52-3). This multiplicity of similar cases allows for observations of the same phenomenon, given variations across time and space (e.g. different regions within the state, multiple institutions, and different group compilations) (Van Evera 1997). Emphasis is placed on 'thick description' of the energy dynamics of the Georgian state in order to understand the system that permeates the state and its surroundings (Geertz 1973). This forms the basis for the assertion of general statements as to the characteristics of networks and the system in which they operate. The end product is a series of trans-territorial networks manipulating Georgia's energy sector which, taken together, offer a context for understanding how the networks impact on inter-state relations. This is achieved through multiple levels of analysis within the single-country study, including international, trans-regional, regional, and intra-state.

The heuristic use of the network model to discern the reasons for perpetual state weakness in Georgia provides a tool whereby new problems are located, possible theoretical solutions are suggested, and generalisable relations are formulated that were not previously apparent. It operates as a 'building-block' approach to the construction and development of the theory of trans-territorial networks weakening states in the post-Soviet space (George 1979). Van Evera refers to this theory building exercise as 'process tracing', whereby the puzzle is identified and the process of operation is traced backward to find the causal factors (Van Evera 1997: 62-64). Following the puzzle of how trans-territorial networks operate in the energy sector, and tracing backward from the result in each of the eight cases, allows for the identification of causal factors weakening the state. Applying this methodological approach, I can observe in multiple cases where trans-territorial networks have had an 'above normal' weakening influence. The literal replication of the operation of trans-territorial networks in each case provides a base from which to challenge the notion of state sovereignty, in particular its location in a weak state.

I selected the case of Georgia and its energy sector because it provided the most extreme situations and most observable cases of trans-territorial networks among the post-Soviet states. I chose the period from 1993-2003 to encompass three different periods of Shevardnadze's presidency, in which varying politico-economic developments did not appear to have an effect on energy security. My choice was supported by three factors. First of all, reviews of the quantitative indicators provided by international organisations showed that Georgia was one of the most persistently weak post-Soviet states, and yet it received the most amount of foreign assistance per capita. This allowed me to enter the debate as to why efforts by the international community had not strengthened the post-Soviet state, leading to explanations for the causes of state weakness. Second, while Georgia increasingly sought security guarantees from western security organisations as a result of the Russian government's increasing threats to its territorial integrity, the Georgian government sold strategic energy assets to Russian state-owned companies. This allowed me to enter the debate as to the inappropriateness of the neo-neo consensus on the rational state. Finally, Georgia's civil society was relatively freer than the other states that I visited, including Russia, Armenia, and Azerbaijan. This meant that more information was available on sensitive topics from the media, non-governmental organisations, and members of the opposition parties. Thus, I was able to triangulate information with several sources.

Thus, Georgia is a critical and limiting case, whereby it offers the most likely grounds upon which to confirm the theory (Van Evera 1997). Examining one country in depth over a period of time allows for a more detailed base from which to draw conclusions (George and Bennett 2005). A single country study should not be over-generalised, nor should weak states be categorised based on limited material. By detailing the particular historical, social, political, and economic dynamics of one weak state, the point of this thesis is to demonstrate the complexities of the state system, in terms of internal factors, trans-national actors, and international mechanisms that, taken together, perpetuate weakness. What can be applied more broadly is the appreciation of all of these factors, the understanding of state-societal networks, and the impact this type of system has on the state. What can also be applied is an understanding of how the trans-territorial networks that operate throughout the space occupied by weak states create an alternate force of inter-state relations. In the final analysis, I develop the network model and follow data collection procedures such that it can be repeated in other post-Soviet weak states and obtain similar results. Finally, it is designed so that it can be applied beyond the weak state to include regional area studies and international security issues.

The research design followed a multi-phased approach. First, there was an examination of secondary sources and the conduct of interviews with regional experts in London and Washington. Second, a preliminary three month field research trip was undertaken to obtain a practical and holistic understanding of the issues pertaining to Georgia's weakness. In addition to interacting with the professional and academic community as a resident in an established think-tank in Tbilisi, Georgia, trips were made to the separatist region Abkhazia, the autonomous region Adjara, and the Armenian-populated Javakheti, as well as to Armenia. I conducted all research alone except the Javakheti case, during which the interviews and observation were done with a Georgian expert on development aspects of the region. Operating as a team allowed us to view the case from different perspectives and share our observations.[5] The primary source material collected included works by Georgians in English and Russian languages and data collection from the government and international financial institutions. In addition, I conducted over eighty semi-structured interviews and made numerous observations while on trips to the regions. Appendix 2 offers a list of interviews on the thesis topic that were not cited, but that contributed to the overall evaluation of the cases.

In the second phase, I studied in Moscow for 5 months and interned at the Carnegie Endowment for International Peace, during which I was able to discuss my thesis with Russian experts on the Caucasus. When I returned to write up the field research, I realised that none of the weak state theories addressed the phenomena of trans-territorial networks, so I began to design the network model. I then undertook another more structured field study visit of three weeks to Georgia to conduct a series of interviews with experts in the energy sector, which included a field visit to the western Samegrelo region. Interviews were conducted in the capital and the region with parliamentarians, heads of businesses, current and former members of the government, trade organisations, donor organisations, and non-governmental organisations. This allowed me to refine the network model and to build evidence measuring the model in each case (Eisenhardt 1989). In between these trips, there were three additional opportunities to conduct research in Georgia. I worked as an election observer for two parliamentary elections, the first leading to the November 2003 Rose Revolution and the re-vote. Further, I was a student in a three-week conflict resolution course in Abkhazia, which was attended by representatives of all of the post-Soviet states and separatist regions.

There were two methodological challenges that had to be overcome: identifying members of the networks and their relations, and gaining trustworthy sources to confirm information. Network analysis assumes data collection on the complete

[5] My research colleague was Dr. Eka Metreveli, Director of the Center for Human Security at the Georgian Foundation for Strategic and International Studies. We subsequently co-wrote a conference paper on our research observations (Closson and Metreveli 2004).

network even though some analysts admit that connections may be arbitrary and that boundaries of networks can be hard to ascertain (Anheier, et al. 2005: 210). Because of the sensitive nature of the topic, I could not be so rigorous. One answer is to use the 'ego-centric' approach, that is, only focus on one node and the ties with other actors, using this as a representation of other networks (Anheier, et al. 2005). Much of the time, Georgian-produced reports in combination with an interview with the authors sufficed. Triangulation, or the process of garnering multiple perceptions or interpretations to clarify meanings, was used to create a pattern out of seemingly disparate information (Stake 2000: 437).

Persistence and patience was crucial in conducting research, as interviews often came up unexpectedly, and many times a second or third visit with the same person or organisation was necessary to glean the information required. Due to the sensitivity of the information, none of the interviews were recorded, and some of the useful information obtained during interviews was 'non-attributable'. In reality, conducting research on this type of topic meant that there were several times I did not ask for the status of information being provided and did not take notes immediately so as not to interrupt the information flow. Naturally, however, I abided by the requests of some of the interviewees that our conversation be off-the-record. The examples presented in this thesis are described as accurately as possible given the available material. However, it is recognised that the recollection of events and data may not be exact. Additionally, it was understood that there were several versions of events, several opinions as to why things happened, and no concrete statistical or financial data available. Thus, the purpose of the case studies was to draw inferences from the accumulation of stories about the implications of the operations of trans-territorial networks and not to reconstruct precisely the events.

1.6 Structure of the Thesis

The thesis proceeds in the following manner. Part I provides the background analysis by reviewing the existing literature on the weak state in theory and practice and places Georgia within this literature as it pertains to the post-Soviet experience (Chapter 2). Next, a politico-economic history of the energy dynamics during three distinct periods of the Shevardnadze presidency is provided as background for analysing the impact of the networks traversing Georgia (Chapter 3). With this theoretical, analytical, and historical backdrop, Part II of the thesis applies network analysis to describe the nature of Georgian networks defined in terms of their nascent Soviet origins and their post-Soviet manifestation, as well as the particular compilation and characteristics of a political network model of socio-economic relations (Chapter 4). Two sets of case studies of energy networks traversing Georgia follow. The first set of case studies is divided by function within the energy system: privatisation, production, transmission, transportation, and distribution (Chapter 5). The second set of case studies traces regional networks, including those encompassing Abkhazia-Samegrelo, South Ossetia-Shida Kartli, and Javakheti-Armenia. The thesis concludes with Part III, which begins by considering the implications of the weak state for inter-state relations (Chapter 7). Analysis focuses on the two previous case study chapters, as well as the impact of the networks on inter-state relations within the South Caucasus. One final example of the Baku-Tbilisi-Ceyhan oil pipeline is presented as a possible exception to the debilitating role of trans-territorial networks in Georgia's energy sector. The final chapter takes up the theoretical implications of the weak state in International Relations, in particular examining what trans-territorial networks tell us about the location of sovereignty in the state (Chapter 8). It also makes preliminary comments on the applicability of the political network model of socio-economic relations, both in terms of Georgia's post-Revolution energy sector, as well as to other post-Soviet weak states.

Chapter 2: The Weak State in International Relations

> …"governance" is simply a euphemism for what used to be known as "politics," the first requirement of which is to know where power resides (King 2004).

2.1 Introduction

The review of the literature in the preceding chapter suggested that some answers to the central conundrum of this thesis might be found in the developing study of the weak state. In particular, empirical case studies of states captured by networks appear to be exploring the types of questions that are salient to understanding why the Georgian state remained persistently weak. It is useful to continue to review the growing body of literature and western security documents on the weak state and to extrapolate from it what insights or propositions it can offer for explaining the puzzle at hand. The weak state has been the subject of research in several academic spheres, including post-Soviet transition literature, African studies literature, development studies, security studies, political science, and historical sociology. Despite, or perhaps because of, the numerous approaches to statehood in general, and the weak state in particular, there does not appear to be an agreed upon definition of the weak state. This chapter will begin with a discussion of the evolving notion of the state and locate the relevant departure point from which to challenge the traditional notions of statehood within the framework of contested sovereignty. It will then discuss the various theoretical approaches to the weak state in International Relations and relate it to trans-territorial networks as a challenge to the 'idea' of the state. It will conclude with a review of how the policy community has measured the weak state, revealing discrepancies in the quantifiable parameters, definitions, and categorisations.

2.2 The State in International Relations

Defining the state in International Relations and locating state sovereignty are perhaps the two most fundamental debates in the literature. Yet, the assumption of a state, its sovereignty, and the functioning of a specific kind of state sovereignty are often taken for granted in the literature regarding weak states. This not only places certain restrictions on the possible variations on stateness that can occur among weak states, but it also limits the debate about the causes of persistent weakness. Hence, this study will treat the 'state' and 'sovereignty' as problematic and will attempt to explore alternative conceptualisations of the weak state's sovereignty. Problems related to defining the state, locating its sovereignty, and post-modern articulations of *stateness* will each be addressed below.

2.2.1 Defining the State

One of the first issues regarding the definitional challenge of the weak state is the multi-disciplinary approach to the state, resulting in three distinct concepts (Willetts 2005: 427-8). First, in international law, priority is given to the juridical rather than the empirical attributes of a state. According to the 'Montevideo Convention on Rights and Duties of States', a state is an entity that is recognised to exist when a government is in control of a community of people within a defined territory. Second, in the study of international politics, each state is a country; a community of people who interact in the same political system and who share common values. Third, in philosophy and sociology, the state consists of the apparatus of government, in its broadest sense, covering the executive, legislature, administration, judiciary, armed forces, and police. In addition to the discrepancies among these definitions, none of these disciplines is sufficient on its own to analyse persistent state weakness. The legal and political definitions of the state do not account for the competing structures within and beyond a state, which vie for power in a weak state. That is, the 'government' as an apparatus composed of state institutions does not capture the real actors operating within the weak state.

The second issue in defining the weak state is getting beyond the state-centric approach of International Relations. For the most part, the realist and neo-realist schools have fairly consistently dominated the definition of the state and its place as a point of departure in the International Relations debates. For classical realists such as Machiavelli and Morgenthau, the state is the pre-eminent actor in world politics and state 'sovereignty' signifies the existence of a political body with juridical authority over its territory. The Weberian realist 'strong state' has served as the most frequently cited definition of the state and a base against which other states are compared. For Weber, the state is an institution with the capacity to implement and execute authority over a delimited territory and the population residing within the territory. It contains certain attributes, such as sovereignty, monopoly over the means of physical violence, rights to taxation, and setting and enforcing rules and regulations for citizens (Weber 1968). Neo-realists clarify the state's role as one of maximising its position in the anarchical international system, placing self-help and survival above all else (Waltz 1979). Neo-liberals have adopted much of the neo-realist position – both the state as a rational actor and the anarchy problematique (Ruggie 1998) – but also take into account the role of non-state and trans-national actors. Additionally, neo-liberals emphasise the state's willingness to cooperate with other states in the international system in order achieve common goals. Thus, while studying different facets of the international system (i.e. high versus low politics) and disagreeing on the level of inter-dependence required of states (i.e. absolute versus relative gains), neo-realists and neo-liberals share the same epistemology and agree on the actors, values, issues, and power arrangements in the international system. As a result, the 'inter-paradigm debate' (i.e. the neo-neo consensus) has served as the dominant mode of analysing the state in International Relations since the 1980s.

2.2.2 Problematic Sovereignty

The consensus in International Relations literature has unnecessarily limited the discourse on types of states, particularly those that appear less than rational, unitary, or that do not function for the purposes of survival. Krasner argued that 'neither of these schools [neo-realist and neo-liberal] is suitable for understanding some elements of sovereignty, especially the extent to which the domestic autonomy of states has been compromised' (Krasner 1999: 6). By the 1980s, there was general agreement that sovereignty, conventionally understood as equally distributed across all states, was a contested concept (Biersteker and Weber 1996; Buzan 1983: 68). Sovereignty was not to be accepted as a fact, but was rather a concept or claim about how political power was or should have been exercised (Hinsley 1986: 1). According to Hinsley, the relationship of sovereignty of states in relation to other states was a derivative of, or dependent on, their sovereignty in relation to their own people (Hinsley 1986).

The fact that sovereignty was both contestable and uninformative of political power arrangements seemed to be evident given that sovereign states could be both democratic and totalitarian, developed and undeveloped (Weber 1995). In the post-Cold War international debate, issues such as the proliferation of intra-state conflict, humanitarian disasters, and genocide called into question the existence of benign juridical sovereignty and the legitimacy of certain sovereigns. Globalists also challenged the nature of the sovereign state, arguing that the sanctity of the state is challenged by a global civil society (Kaldor 1999; Kaldor 2003) or a global economy (Strange 1996). Thus, there were increasing calls to widen the neo-neo consensus to account for the developments in the international system after the end of the Cold War.

The debate on problematic sovereignty originated from the general conception in the political science literature that the prime feature of sovereignty is juridical recognition by other states (i.e. international legal sovereignty), and the principles of exclusion of external actors from domestic authority configurations within a defined territory. This was encapsulated in the conception of the state conceived of in the 1648 Peace of Westphalia and the Concert of Vienna (Krasner 1999). The notion of domestic sovereignty was developed by Bodin and Hobbes, who wanted to establish the legitimacy of a single source of authority within a polity – a Leviathan for Hobbes. For Bodin, sovereignty was mainly legislative; the giving of laws to subjects or 'legislative sovereignty'. This was a political expression about the state's authority, not its capacity, to coerce (Bodin and McRae 1962). However, beginning with de-colonisation after the Second World War, some new states lacked internal legitimacy. That is, while the absence of an effective domestic authority did not necessarily challenge the international legal and Westphalian sovereignty of a state, it produced a situation in which some states served as an arena for activities not conducive to state-building (Krasner 2001: 7).

This was most thoroughly explored by Jackson (1990), who suggested that weakness persisted in African states because they were granted juridical sovereignty by the international community despite lacking sufficient empirical sovereignty (domestic control). African states, Jackson argued, were 'quasi-states' because they lacked the institutional features of sovereign states and were therefore deficient in responding to the will of their citizens. They were also deficient in the level of organised power to protect human rights or to provide socio-economic welfare. Paralleling Jackson's juridical/empirical sovereignty distinction was Walker's inside/outside sovereignty (Walker 1992). Sovereignty from the inside referred to the tensions between power and authority or between state and civil society. Sovereignty from the outside referred to the superiority of individual sovereign states as primary actors in the international system due to the absence of an overarching sovereign power/authority governing the system.

Thus, one of the most important challenges to the traditional notion of sovereignty was the idea that state sovereignty could be linked to the government's capacity to govern, a quality that varied among states regardless of their legal sovereign status. This created a situation in which stronger states were viewed to have more empirical sovereignty than weak states. This theoretical argument rendered the two paradigms of International Relations less relevant to the modern problem of weak states in the international system (Jackson 1990). Firstly, contradicting the tenets of realism (e.g. Machiavelli, Hobbes, Bodin), the weak state's deficient and defective apparatuses of power meant that there was little if any social contract between the ruler and people. Second, rationalism's (e.g. Grotius) absolute quality of sovereignty, mutual recognition, and reciprocity inadequately represented the interplay between weak states and the rule of law. Thus, the mainstream theories were irrelevant for analysing the states which possessed *de jure* sovereignty, but lacked *de facto* sovereignty, or the capacity to govern effectively.

Jackson's discussion of a lack of empirical sovereignty should not be construed to mean that a weak state necessarily lacks institutions or the capacity to govern. Rather, it is the lack of authority existing within the state to wield effective control over the state. The state consists of both an 'office of authority' and 'an apparatus of power' (Oakeshott 1977). The issue of authority and control are often misconstrued in discussions about the usage of domestic or empirical sovereignty. While control can be exercised with mere force, the very nature of authority would mean that force was not necessary; control would be a by-product of authority. Hence, while there still may be an authority at the helm of the state, the loss of control over territory or other responsibilities of the state would signify the weakening of domestic sovereignty (Krasner 1999: 10).

Moreover, the lack of empirical sovereignty should be understand not simply as the lack of control or power, but the lack of will to exert full authority. Westphalian sovereignty conveys the notion that domestic authority structures will preclude the intervention or infiltration by outside forces in the state's affairs (Krasner 1999: 20). However, in the weak state it is sometimes the case that connections with external actors are fostered by domestic structures, including those coercive forces which might eventually undermine control over aspects of the state. Thus, this thesis applies two, more micro-level notions of sovereignty employed in the literature – interdependence (ability of authorities to control trans-border movements) and domestic sovereignty (the level of effective control authorities have over a territory) (Krasner 2001: 2). Within these realms of sovereignty, the actions of various actors moving within and beyond the state, including those in charge of state institutions, cannot be assumed to be directed towards strengthening the state.

2.2.3 Post-Modern Stateness

Problematic sovereignty, and the emphasis on variations of domestic sovereignty across states, suggests that the state is always in the process of stateness. Stateness refers to the notion that the state is always incomplete and is in the process of being constituted (Burchill 2001: 197; Devetak 1995). The fundamental contribution of the post-modernist turn in International Relations theory has been the inclusion of alternative accounts of the state. Constructivists, for example, have been more sensitive to the problematic nature of sovereignty, arguing that structures and agents are constantly reconstituting each other, and neither can be taken for granted (Biersteker and Weber 1996). The post-positivist theories provide some space for utilising empirical analysis to go beyond the rational actor to examine forces that are impacting stateness. According to a post-modern theorist, the state is not a given, pre-ordained political structure (Ashley 1987; Ashley 1998). Instead, the state exists as a paradox, subverted by violence, issues of identity, and statecraft and should thus be studied not as a unitary actor, but instead as an arena of conflict, in which a variety of actors and forces impact on the authority over the state, affecting the level of control the government has within the territorial boundaries of the state.

This conceptualisation of stateness allows for a re-examination of several assumptions regarding the state. First of all, there is the assumption that the state is a coherent unit, acting with a common purpose. That is, the citizens of the state, including those in private and public capacities, are operating together towards the logical goal of strengthening the state. Another assumption is that people's loyalties to their states are greater than other loyalties, for example, to a resource that provides economic security such as co-ethnic populations across borders, diasporas, or foreign business partners (Willetts 2005: 428). Related to this is the assumption that internal order is solved by the government and that, therefore, citizens need not seek out other economic and physical sources of security. Finally, there is an assumption that domestic sovereignty resides either soundly or solidly in the authorities governing the state. Those states that do not follow these patterns are considered to be exceptions. These are the central conundrums of the post-modern weak state that must be dissected and analysed when considering how state weakness is perpetuated.

Some analysts have suggested that the challenges to the post-Soviet state are related to the post-Westphalian order more generally, in terms of either an expanding international society or a subsiding state. However, it is premature to discuss these trends as major contributing factors to developments in the post-Soviet space, since Westphalian sovereignty has yet to solidify. Thus, to go beyond Westphalian sovereignty would be to assume that the juridical sovereign state at some point had a degree of state control over the territory, was delivering goods to the public, and acted as a trusted and legitimate force over violence. Trans-national forces and their interactions with local forces are not creating some globalising entity beyond the state, nor are they challenging the state, as such. Instead, they are affecting the process of stateness to the point of offering an alternative source of authority within and beyond the state. This research attempts to reconceptualise the state as a space for the activities of a confluence of state and non-state and global and local actors traversing territories, both recognised and unrecognised by the international community. A more nuanced understanding of the intersection of global and local forces enhances the explanation of how state weakness can both be caused by, and can affect, the international system (Clark 1999). Transposing networks onto this 'glocal' medium should reconstitute the 'idea' of the state as an arena of conflicting groups and issues, providing a departure point from which to discuss the weak state. To place this debate within a theoretical framework, the following section addresses approaches to weak state theory.

2.3 The Weak State in Theory

Approaches to the weak state in International Relations literature have primarily followed two avenues. The first avenue has been the dominant rational choice model or the neo-institutional approach and the second avenue the ideational approach. The neo-institutional avenue followed three chronological approaches: institutional, post-colonial, and taxonomy. Neo-institutionalism was the development-inspired track, which focused on the institutions within the state and their ability to govern. This was, for the most part, a top-down approach to state-imposed institutional mechanisms to garner political influence for the mobilisation of societal groups and material resources for state action. The second was the conflict-inspired track, which focused on the regime as an abuser of the state. Mostly originating from post-colonial studies in the African context, this body of literature predominantly described the nature of the African weak state and its attributes. The third was the terrorism-inspired track, which attempted to provide a taxonomy of states, from collapsed to strong, in order to determine when a state is on the brink of failure. The ideational avenue to studying the weak state was the security-inspired track, which focused on the idea of the state as a legitimate actor in providing protection for the population. This 'idea' of a state was born of a bottom-up approach to societal support for the state's ability to provide for its citizens. Each of these bodies of weak state literature will be taken in turn, concluding with a discussion as to their appropriateness for this study.

2.3.1 Institutional Approach

By the 1980s, it was an accepted fact that most developing countries had weak domestic institutional capabilities (Krasner 1985). Thomas discussed institutional

capacity as represented by despotic power (coercion) and infrastructural power (provision of public goods and extraction of resources) (Thomas 1989).
Some theorists adopted a combined institutional/governance definition of a weak state, which addressed weakness inherent in both despotic and infrastructural power (see Brock 2005: 2; Clapham 1996; Jackson 1982). According to them, a weak state has ineffective institutional and administrative structures frequently controlled by state elites who do not primarily seek to provide public or collective goods. The state is unable to create a coherent national economy, but instead consists of incoherent amalgamations of agriculture, an informal petty urban sector, and some fragments of modern industry, mostly controlled by external investors. Exports consist of one or a few primary products and the economies are highly dependent on imports of manufactured and technology-intensive products. The state does not deliver goods of citizenship, such as legal, political, and social rights. Finally, state legitimacy fails to develop and people turn to ethnic communities for support. Thus, there were two main ideas in the institutional approach: the lack of physical administrative capabilities, including the capability to distribute resources, and the inability of the state to influence societal groups through state institutions.

Migdal (1988) claimed that there could be no understanding of state capabilities in the 'Third World' without first comprehending the social structure of which states [governments] are only one part. Like Thomas, Mann (1986: 113) called the power of the state to penetrate society and implement political decisions 'infrastructural power'. However, there are at least two challenges to this power: multiple actors within the state and the vertical and horizontal nature of relationships between state and society. The state is just one actor in the institutional equation and may not be the predominant one in some circumstances. In developing states, local power structures often view the centres more as a threat than a legitimate source of authority, direction, or service provider, and the rise of 'strongmen' in the periphery of a state and the segmentation of the political community into sub-units or 'publics' can threaten the state (Migdal 1988). Second, weak states tend to cultivate vertical, clientelistic ties and parochial relationships based on primordial affinities like ethnicity and kinship. The state is an arena for interactive relations between state and society and when certain elements, such as clans, are dominant, they put themselves between society and the state. Once established, this kind of social control can be difficult to transform (Migdal 2001).

There is a propensity for one individual, group, or community to eventually capture the state and use its authority to exclude others from participation and access to resources (Mann 1986). A government that has weak administrative and institutional structures often resorts to rules based on coercion instead of law, and there is no monopoly of the use of legitimate violence (Sørensen 2004: 173). Ergas termed this 'captured autonomy' to explain how elites control the state and exploit their control for personal or narrow (i.e. non-state) interests. The state is personalised to the extent that when the ruler loses authority, the state could collapse. This has also been called the 'patrimonial state' (Ergas 1987: 5) and Max Weber expected patrimonial tendencies to occur in states that were not yet fully monetised and lacked proper means of communication and transport (Weber 1968). While countries may have different genealogies of weakness, they seem to follow the same universal logic, that is, rent seeking in a densely knit network of violence, clientelism, world market integration, and coping mechanisms that are sufficient to uphold the weak state, but not effective enough to overcome weakness (Brock 2005: 27).

There is a related argument that, much as in the early stages of state development in Europe, post-modern weak states emerge through wars of conquest and domestic conquest of populations for taxation (Tilly 1985). Violence is therefore a critical element in the constitution of the state through the interaction of various informal parties, such as protection rackets or a mutual self-protection society. Barzel defined the state as: (1) a set of individuals who are subject to a single ultimate third party who use violence for enforcement; and, (2) a territory where these individuals reside, demarcated by the reach of the enforcer's power' (Barzel 2002). Tilly argued that the instruments and institutions of modern organised violence would ultimately be made to serve political interests, buttressing the state-building process, rather than undermining it. However, application of the Tilly/Barzel definition of the state means that weak states rarely succumb to the contradictions of their polities or societies and to the violence that can lead to a deterioration of the state (Krause 1996). Tilly also does not account for different historical phenomena that impact on states in different periods. Finally, as Derlugian argued, post-Soviet weak states neither fight real wars of conquest, nor do they go after the population as a revenue base (Derlugian 2005).

2.3.2 Post-Colonial Approach

The second approach to the weak state was developed by International Relations specialists on post-colonial Africa. This body of literature constitutes the richest of the regional area studies, which have undertaken empirical work on the weak state and informal networks. The literature deconstructs the state, challenges the realist and neo-neo consensus on the state, and differentiates between authority and control. It also addresses the informal political and economic system that has developed over time, challenging and sometimes usurping the state. There is very little assumed about the African state – including its sovereignty, authority, and control over security and rule of law. Insights from the study of post-colonial Africa have been comparatively applied to the case of the post-Soviet states in a recent work (Beissinger and Young 2002). The similarities, the authors argued, are located in the scope of pre-independence state power and the state's attempts at social engineering, the autocratic nature of that power, and the relatively recent timing of these experiences. In the post-independence period, there are analogous patterns of state breakdown related to autocratic state practices, particularly with regard to the role of networks. Thus, it is useful to review the approach to the post-colonial African state.

The study of persistent weakness in the post-colonialism literature was primarily focused on the predatory nature of regimes of African states. Weakness was attributed to the scramble for resources in order to sustain power over the state (Clapham 1996: 183) and the role of the informal political system of patronage networks, based on personal loyalty and coercion, in achieving this end (Bratton and Van de Walle 1997). The state intervened in the economic processes to the extent that it wished to redirect resources towards the elite (Clapham 1985: Chapter 5). This was characterised as 'Big Man' politics by Chabal and Daloz (1999), in which power is centralised in a leader who manages the administrative apparatus through clientelism and patronage. This results in a clientelistic system, which, 'lacks the capacity to create any sense of moral community amongst those who participate in them, let alone among those who are excluded' (Clapham 1996: 59). These patron-client linkages have their roots in colonial and post-colonial reality (Mamdani 1996). The legacy of Soviet era patrimonialism and its post-Soviet manifestation will be addressed in Chapter 4.

As in the former Soviet states, the networks in Africa are not just composed of non-state entities, dark criminal figures in the 'other world', but are very often formal state actors, who engage in informal or illicit economic activities (Reno 1998). This informal reciprocity often necessitates a tight hold over resources or the monopolisation of an industry in order to prevent competitive networks from arising and challenging the state's authority. Power is thus dispersed throughout the state by means of networks, which may or may not be visible. The African studies literature linked criminalisation and neo-patrimonialism, pointing out how fragments of state authority become instruments of predation among dispersed structural segments and individual actors (Young 1994). Rulers in West African countries, for example, have frequently dismantled state institutions, deliberately withholding public goods from their citizens in an attempt to force people to turn to clientelistic channels that were ultimately controlled by the head of the state. This 'shadow state' serves the private accumulation of power and resources of the ruler. The diminution of the 'official state' has been a necessary precondition of the shadow state's prosperity (Reno 1998; Reno 2000).

Scholars of post-colonial Africa do not discount the role of other actors, particularly societal groups, in forming an alternate force to the official state. Chabal and Daloz (1999) discussed the 'political instrumentalisation of discord', meaning that disorder created a vacuum through which an alternative yet effective system is established, the logic of which was quite different from that normally assumed by theorists. This notion of the invisible functioning of an alternative system to a transparent state was labelled the 'rhizome state' by Bayart (1993). Power, he wrote, could often be invisible to external actors, but nevertheless extended in an informal way, encompassing much of what may be considered as 'non-state' or 'extra-state' (Bayart 1993: 58-9). Some Africanists argued that the whole notion of Westphalian state sovereignty was troublesome in general and statehood could not be assumed as a future end-condition. Examining the process of state decay from below revealed the inability of many states and societies at the local level to meet the demands that state maintenance placed upon them (Clapham 2004 77). The fact that some factions claimed control of the capital was not, in fact, a substantial justification for the existence of a state (Herbst 2004: 303).

2.3.3 Taxonomy Approach

The third and most recent development in the weak state literature attempted to provide answers to two rising phenomena in the post-Cold War world – failed states as a result of intra-state conflict and international terrorism. International terrorist cells, which threaten international security, find haven in failing and collapsed states. Therefore, in order to combat terrorism, states must be strengthened. Experts concluded that to devise effective preventative measures, including improving the state-building capacities of stronger states, it was necessary first to define the indicators of potential state failure. Fukuyama produced a matrix of state strength (institutional capacity) and state scope (range of state functions), concluding that most developing countries have weak institutions, and compound this by taking on a wide range of functions that they cannot perform well (Fukuyama 2004). Rotberg conducted a five-year study, which resulted in the categorisation of 41 countries into four groups: weak, failing, failed, and collapsed (Rotberg 2003; Rotberg 2004b). Weak states were labelled a 'mixed bag' since they fulfil expectations in some areas and performed poorly in others (Rotberg 2004b: 10). This taxonomy approach followed the institutional approach, emphasising the 'tipping points' – economic, political, and numbers of deaths - at which states succumb to failure. Rotberg used quantitative indicators to qualify categories of states: the UNDP Human Development Index, Gross National Income per capita, illiteracy rate, mortality rate, and life expectancy. The categorisation placed security at the top of a state's list of primary functions, followed by the development of a participatory political system, social programmes, infrastructure, and banking and commerce (Rotberg 2004b: 3).

Despite the use of quantitative indicators, the definitions of each of the four categories – collapsed, failed, weak, and strong – provided more points of discussion than they did concrete parameters. An abridged discussion of the weak state included characteristics such as: harbouring inter-communal tensions on the verge of violence, high urban crime, lack of political goods provided by the state, declining infrastructure and services, falling economic indicators, high levels of corruption, and prevalent state predation (Rotberg 2004a). Weak states were one of two types: 'inherently weak' or 'temporarily or situationally weak'. The former were weak states due to their geographical, physical, or fundamental economic constraints placed upon them by the international system. The latter were labelled 'temporarily or situationally weak' due to internal issues such as greed, poor leadership, or internal antagonisms possibly also combined with external attacks. Of the Soviet states, Rotberg labelled Georgia and Moldova as 'inherently weak', while Belarus, Turkmenistan, Tajikistan, and Kyrgyzstan were labelled 'temporary or situationally weak' (Rotberg 2003: 4, 23 Table 1.1).

The western governments' efforts to identify weak states in order to prevent conflict and to improve development programmes resulted in more qualified lists. The UK Department for International Development (DFID) identified 46 countries as fragile states of concern (Department for International Development 2005). The UK Cabinet Office created a manual for performing risk assessment and strategic analysis of countries at risk of instability, but did not list the potential countries as such, although most data referred to African countries (Prime Minister's Strategy Unit 2005). The World Bank's 2002 Low Income Countries Under Stress (LICUS) Project arranged states along a continuum of policies, governance, and institutions, qualifying as LICUS in some categories and not in others (World Bank 2002). In fiscal year 2005, the World Bank identified 11 nations in the 'severe' state category and fifteen in the 'core' category. The only states from the post-Soviet space were Tajikistan and Uzbekistan, both labelled as 'core'. While adding an economic dimension to state weakness in terms of coupling financial assistance with reform measures, LICUS focused on the same underlying concepts of state weakness as previous studies.

The Fund for Peace, in cooperation with *Foreign Policy,* issued a 'Failed States Index' in 2005, in which they examined 60 states and identified 10 of these as 'at risk for failure' (The Fund For Peace 2005). The Fund identified governance, economy, and nationhood as areas of concern and employed twelve social, economic, political, and military indicators on a ten-point scale. The indicators included: demographic pressures, refugees and displaced persons, group grievance, human flight, uneven development, economic decline, delegitimisation of the state, public services, human rights, security apparatus, factionalised elites, and external intervention. It then ranked each nation on every indicator and added up the scores to determine the potential for failure. Of the 60 ranked states, 6 were post-Soviet states from most to least unstable: Uzbekistan (24), Ukraine (38), Belarus (43), Tajikistan (48), Azerbaijan (50), and Russia (59). It is interesting to note that Kyrgyzstan was not included, despite the turmoil caused by the post-Revolution battles among various groups in solidifying political power.

2.3.4 Ideational Approach

The fourth approach to state weakness looked beyond political-institutional capacities to question the 'idea' of the state in terms of its legitimacy, measured by the degree of state-societal cohesion (Buzan 1983; Buzan 1991). States must be 'constructed' in the minds of at least some of those who form them, including minimally those who run them. The construction of the state is legitimised through a 'social contract' in which the people grant the state the right to rule over them in return for stability and security (e.g. Hobbes, Locke, and Rousseau). According to this approach, state weakness consists of patterns of flawed legitimacy; the basic idea of the state constitutes an arena of conflict between the government and its citizens and among the citizens themselves. A breakdown in legitimacy is evident when the state frequently resorts to the use of domestic force, relations between state and society become personalised, and several political communities vie for power. The more a government loses support from the society, the more it relies on violence to control society (Holsti 1996: 116-119). This results in the regime losing its legitimacy, particularly the willingness of the citizens to accept the domain and scope of the regime as the appropriate entity for making legitimate decisions about their future (Linz and Stepan 1996: 16). In an attempt to find resources to remedy the situation, the regime presiding over the state relies on predatory and kleptocratic practices and either purposefully or, as a result of actions taken, inflames local tensions. Holsti labelled this the 'state-strength dilemma', explaining that society's reaction can be to endure, exit, voice their disapproval, or rebel. If the state-strength dilemma is not resolved over time, the state may fail (Holsti 1996).

Refining Buzan's notion of state-societal cohesion as an indicator of the level of legitimacy of the state, Pei (2003) proposed that it is not the degree of state-societal cohesion, but the degree and location of state predation that has been largely responsible for declining state capacity in transition countries, particularly as regards the lack of economic development. The predatory state is characterised by an incoherent and inefficient state administration with little capacity to promote economic and social development. Evans argued that the predatory state is controlled by a small political power elite, possibly an autocratic ruler who uses the state and its resources to promote his own narrow interests (Evans 1997). The more decentralised state predation is, the less likely it is that external assistance in enhancing state functions will be effective. That is, the more corrupt state agents are in using the state to carry out their own agendas in the pursuit of personal profit, the less likely the state is to prosper. Pei further differentiated between first- and second-generation theories of the predatory state (Pei 2003). First-generation theory does not distinguish between the principal and agents of the state. Instead, it considers state predation as universal, that is, all are monopolists of violence and public goods. Second-generation theory is more decentralised, emphasising predation by agents at various levels acting as 'independent monopolists'. Both first- and second-generation theories result in lost revenue for the state, which weakens it.

The debate about state-societal cohesion is also factored into the security debate, in particular 'societal security' (Buzan 1991). Following on the Hobbesian notion that absolute power is vested in the state to maintain order, Ikenberry argued that the state's most enduring role over time has been as the guardian of society's physical well being, and that there was little evidence that societal demands for security were diminishing (Ikenberry 2003: 353). Rotberg also defined the state as the entity that delivers certain things to society, physical security being at the top of the agenda (Rotberg 2003: 2). The governments of states were supposed to buffer or manipulate external forces and influences, champion the local or particular concerns of their citizens, and mediate between the constraints and challenges of the international arena and national interests.

However, in weak states, Buzan maintained that the state was a major source of both threat and security to its citizens (Buzan 1983; Buzan 1991). The principal distinguishing feature of weak states was their high level of concern with domestically generated threats to the security of the government. In other words, weak states either do not have, or fail to create, a domestic political and societal consensus of sufficient strength to eliminate the large-scale use of force as a major and continuing element in the domestic political life of the nation (Buzan 1983:99). Jackson explained that, 'Quasi-states possess arms but they usually point inward at subjects rather than outward at foreign powers which indicates that either no significant external threat exists or an internal threat is greater' (Jackson 1990). Signs of the government's focus on the internal threat to security include a high level of political violence, a conspicuous role for police in the everyday life of citizens, the presence of contending national identities, and the lack of a clear and observed hierarchy of political authority (Buzan 1983).

The 'societal security' approach was not without its critics, particularly with regard to the organising concept of identity. Shaw argued that Buzan did not consider the nation within a sociological framework, which viewed identity as a cultural-ideological-political construct. Thus, Buzan's restriction of identity to the 'human collectivities' constituting the nation-state was too limiting (Shaw 1993). McSweeney addressed this debate in a series of exchanges with Buzan and his Copenhagen School colleagues, arguing that the concept of the 'idea' of the state as being grounded in a collective and non-static identity misconstrued what was occurring within weak states (McSweeney 1996). Ultimately, Buzan, as well as others defining the weak state's security in terms of a 'societal issue', were arguing for a stronger state that controlled and subordinated sub-state groups and their values, including identity, to the state (Ayoob 1997; McSweeney 1996).

2.3.5 Limitations of the Four Approaches

All of these approaches offer useful insights into the problems of weak states. Nevertheless, there are five issues in particular that they fail to address. First, the theoretical literature on the weak state is unduly focussed on indicators of weakness; the Weberian instrumental approach serves as the foundation for all of the approaches. Thus, most of the literature tends to stress the *symptoms* of weakness, but not the underlying *causes*. For example, it is argued that violence is a signal of potential state failure (Rotberg 2003); however, violence does not begin to explain the *causes* of state weakness. It is rather a by-product of a multitude of factors, from grievances such as an imbalance in the economic distribution within the state, to power struggles among elites. Moreover, you can have a weak state without violence, and some strong states periodically experience violence (e.g. riots in Western Europe and America). Second, the ideational approach does not address the phenomenon of a weak state that *colludes* with society, or a society that does not consider legitimacy of the state a necessary attribute of survival. The argument that a loss in the state's legitimacy is the result of a breakdown in state-societal cohesion is an over simplification that misses the nuances of state-societal collusion in weak states. Often the 'legitimate state', that is, a government that operates effective, transparent, and law abiding institutions can serve as a barrier to commercial opportunities beneficial to state and societal actors. Within the networks described in this thesis, for example, it will become evident that while the state may be weak and lack 'legitimacy', state-societal cohesion is actually quite strong, directing activities to undermine the strengthening of the state for the purposes of creating an alternate force. Networks traversing state and societal sectors and organisations, both intra- and inter-state, defy the more traditional definitions of the state. This, as with the post-colonial African research, challenges definitions of state-societal relations.

Third, the fact that state weakness has been located in the development or international security debates can be construed as a discourse applied by western academics and practitioners in support of a pre-determined agenda to shape the international environment in the national interests of stronger states. Whether it is for the purposes of developing markets for trade, stabilising zones of conflict for the extraction of hydrocarbons, or neutralising a political opponent, the notion of the weak state is often rolled into a larger agenda. This agenda may or may not represent the interests of the citizens within these states. Basing an argument on the idea that state failure is a threat to global security is problematic because it concentrates on the impact of local forces on the international system, rather than looking at either the impact of global forces on the state, or, even more appropriately, the intersection of local and global forces, or the 'glocal' approach (Clark 1999). As Migdal points out, 'The role and effectiveness of the state domestically is highly interdependent with its place in the world of states' (Migdal 1988: 21).

Fourth, while the African studies literature made the most strides towards applying structural or historical approaches towards understanding state weakness, some of it is not directly applicable to post-Soviet states. There appears to be an understanding that the patronage system is rigidly organised and that the informal (shadow state) networks operate alongside government bureaucracies, rather than as an interwoven aspect of their operations (Reno 2000: 434-35). Further, the idea that competition is necessarily about 'capturing' the state, often resulting in a violent contest in which the state is partially destroyed, is not applicable in the post-Soviet space. The African literature assumes orchestrated conflict on the part of the state or society in order to exert control or domination over the order of things, which has not been the case in the majority of post-Soviet weak states.

Fifth, a comparison of the various reports providing taxonomies of states leads to the conclusion that the discrepancies in their categorisations make them difficult to reconcile for useful application. The reports differ in their demarcations between various degrees of stateness (weak, failing, failed, and collapsed) resulting in conflicting lists of countries and the categories to which they belong. The parameters for qualifying and quantifying weakness are still vague. If states are qualitatively ranked, it is primarily based on figures provided by international organisations, each of which has its own reasons for categorising states, from the neo-liberal Wilsonian promotion of democracy to identifying states on the brink of failure that might require intervention. The taxonomy approach underscores the utility of the institutional approach by measuring the degree of a state weakness in terms of effective institutions, governance, and security.

In sum, the predominance of the macro approaches (institutional and taxonomy) in both the academic literature and official reports leaves little space for taking into account more refined accounts of weakness. There are very few case studies considering domestic political configurations and their modern manifestations in the post-Soviet space. Finally, the international contexts in which weak states interact, including both the impact of neighbouring states, as well as trans-territorial forces that traverse regions, which may or may not originate within the region, are rarely considered. This results in a rather narrow conceptual and definitional lens through which to analyse persistent state weakness in the post-Soviet space.

2.4 The Weak State in Practice

A confluence of several historical developments made state weakness, and the potential for failure, come to the fore of the international security dialogue and, subsequently, receive an unprecedented level of attention from governments and international institutions. The first development was de-colonisation, particularly of Africa, and efforts to help the newly formed states develop. The next period came after the end of the Cold War and the dissolution of the Soviet Union and Yugoslavia. In the 'New World Order', first proclaimed by former President George Bush in 1991, the international community was to cooperate in responding to intra-state conflicts and humanitarian disasters plaguing weak states, both through increased technical and development assistance and through humanitarian intervention. In the early post-Cold War period, the phenomenon of state failure remained primarily within the African/Third World context, and the implications of state failure were contextualised within the immediate region. Finally, the rise of international terrorism, most dramatically displayed in the attacks of September 11, 2001 on America, propelled weak states to the front of the threats to international security. The weak state was now viewed in a global context as an arena for non-state actors, hostile to the fundamental interests of the international community, threatening the peace and stability usually enjoyed by developed countries. The developed world's approach to addressing the weak state will now be considered.

2.4.1 Development and Intervention

After the first wave of decolonisation in the 1950s and 60s, weak states were generally viewed as a symptom of underdevelopment, both in terms of governing capacity and modernisation (Lambach 2005: 5). It was thought that the development of public institutions would accompany economic growth, resulting in a stronger state. However, the debt crisis of African states in the 1980s, combined with a rise of demographic, environmental, health and social problems, brought the phenomenon of the weak state more clearly onto the security agenda of the international community.

The number of weak states in the international system increased once again in the 1990s as a result of the collapse of the Soviet Union and Yugoslavia. Similar issues to those of the post-colonial states arose, including the difficulties of political and economic transition, as well as ensuing conflicts. The addition of weak states to the international system challenged the international community to transform these states. This, in turn, placed the onus on the development community to define clearly state weakness. It was argued by specialists analysing the transformation of the former Warsaw Pact nations and Soviet states that the first decade of transition was not necessarily directed at strengthening the state, but on building alternative actors, such as non-governmental organisations and sub-regional entities, including the privatisation of state-owned industries and services (Ikenberry 2003). Critics claimed that the result was the creation of a feudalist type of system in which state actors formed a pyramid, with the point facing towards the capitals and the sub-regions acting in a predatory, clientelistic foundations for the pursuit of personal profit (Wedel 2001).

The struggle to assist the former Soviet states to transform was compounded by the fact that by the 1990s, many African states had not only failed to develop, but instead had descended into chaos and conflict. The rise in the frequency of intra-state wars and the humanitarian disasters that often accompanied these wars placed the weak state in the forefront of the international security dialogue, particularly within the United Nations (UN). The debate centred on whether or not the international community should intervene to help re-establish order and assist in the post-conflict reconstruction efforts, which conflated the notions of security and development. Whereas development was previously about promoting economic growth, it evolved to the task of changing whole societies (Stiglitz 1998). Duffield explained that development evolved from a post-war, post-colonialist obligation to a requirement for strengthening the security of western nations. Globalisation brought the conflicts to the doorsteps of the North; it was now in their self-interest to address problems through enhanced development programmes. Policy shifted towards interventionism not to restore the status quo, but to bring about better governance (Duffield 2001).

This shift in policy from development for development's sake, to enhancing governments' abilities to avoid conflict was reflected in the growing literature theorising intra-state conflict. One strand of theory concerned the globalisation of 'new wars' in the 1990s in the former Yugoslavia and the Caucasus. In these post-Cold War conflicts, the participants took advantage of a global system of trade and transactions to expand their ability to fight, both in terms of means (e.g. weapons, funds, and militants) and geographical space (Kaldor 1999). Another strand, influenced by the 'greed versus grievance' debate, concerned the causes of intra-state conflict in African weak states (Collier 2000; Duffield 2001; Malone and Berdal 2000; Pugh, et al. 2004). Prior to 1999, the reasons for civil war were linked to grievances of the parties. However, Collier, employing statistical analysis to examine civil wars from the mid-1960s, concluded that it was not grievance that started conflicts, but greed over commodities, particularly in Africa (Collier 2000). This eventually led to new actions taken by the UN in terms of preventative measures to preclude the escalation of intra-state conflicts, including targeting sanctions against trade in lucrative commodities (Ballentine and Sherman 2003). Since then the debate has shifted to a multi-causal argument for intra-state conflict, linking economic decline, dependency on primary commodities, and low per capacity income (Pugh, et al. 2004).

The devastation wrought by internal conflicts also became the focus of a heightened awareness by the international community of its perceived obligations under Chapter VI of the UN Charter. Secretary General Boutros Boutros-Ghali's *An Agenda for Peace* (1992) proposed a more active role for the UN in preventing state failure. The right to intervene in a state's sovereign affairs because of violations of humanity was a direct challenge to the notion of sovereignty, particularly the willingness of the international community to place human rights above the principle of non-interference in another state's internal affairs (International Development Research Centre 2001). However, attempts by the international community to intervene in intra-state conflicts in the early 1990s, including in Somalia, Haiti, northern Iraq, and Liberia met with great difficulties, both in terms of seeking international support for entering a sovereign nation and the actual military logistics of peace enforcement. As a result of lessons learnt from casualties and military withdrawal from Somalia and Haiti, there was a retreat on the part of the international community from getting involved in further intra-state conflicts, most notably displayed by inaction during the genocide in Rwanda in 1994. That said, the international community did respond to the Kosovo crisis in the late 1990s, albeit mostly in the form of air strikes rather than committing ground troops.

2.4.2 Globalisation and International Terrorism

The collapse of the Cold War bipolar power structure had a profound impact on how the international community reacted to weak states. Whereas during the Cold War, weak states in places such as Central America (e.g. El Salvador and Nicaragua) and South-western Africa (e.g. Angola and Congo) served as battlefields for ideological conflicts between the superpowers, these same states became a concern for global security after 1990. In the post-Cold War environment, there was a realisation that globalising forces both assisted and deterred state development. According to Doornbos, globalisation brought,

> economic liberalisation and privatisation, the pursuit of global market relations, the propagation of the rolling back of the state, the demanding role of the international financial institutions, and related features of global communications transformation that could weaken states (Doornbos 2002).

Further, the proliferation of non-state actors and their ability to operate across borders (e.g. ethno-nationalist movements, militias, international criminal organisations, and terrorists) could also threaten the viability of the state. Finally, the 'soft threats' emanating from weak states, such as AIDs, environmental hazards, humanitarian consequences of civil conflict, refugee flows, and migration were now increasingly a concern of the international community.

Numerous institutional studies were generated starting in the mid-1990s addressing the weak state's position in the globalisation trend and the threats these states could pose to international security. The first was the 1996 UN University research project on states and sovereignty, which included a section on failed states (United Nations University 1996). Purdue University, sponsored in part by the US Army War College, held three conferences between 1998 and 2001which discussed the nexus of failed states and international security, failed states and globalisation, and the causes of state failure (Purdue University International Programs 1998-2001). The Central

Intelligence Agency also sponsored two major studies in the 1990s initiated by Vice President Gore's *US Task Force on State Failure.* The attack on America by al-Qaida on September 11, 2001 in the US propelled the international community to view weak states as a threat to international security and led to a targeted effort, particularly among a coalition of strong states, to refocus their efforts to address the deficiencies of weak states. It was believed that the failure of states such as Afghanistan, Somalia, and the Sudan provided support for the strengthening of international terrorist cells, including their ability to attack western countries on a previously unmatched scale. Before 2001, these same states were deemed incapable of projecting power or influencing many aspects of inter-state relations beyond their immediate regions. However, by post-modern criteria, institutional weakness could affect global security and they were now understood to be 'states of international concern'.

The discourse on the causes of terrorism linked together a host of threats to the international community. The US Center for Global Government created a bi-partisan panel of thirty former government officials, senior business leaders, academics, and NGO representatives to issue a report. Regarding weak states, the commission wrote,

> These weak and failed states matter to American security, American values, and the prospects for global economic growth upon which the American economy depends. Spill over effects - from conflict, disease, and economic collapse - put neighbouring governments and peoples at risk. Illicit trans-national networks, particularly terrorist and criminal groups, target weak and failed states for their activities (Weinstein 2004: 1-2).

Both the US and the EU included the weak state in their security strategy documents. *The National Security Strategy* of the US stated,

> The events of September 11, 2001, taught us that weak states, like Afghanistan, can pose as great a danger to our national interests as strong states. Poverty does not make poor people into terrorists and murderers. Yet poverty, weak institutions, and corruption can make weak states vulnerable to terrorist networks and drug cartels within their borders (The White House 2002: 5).

The European Security Strategy listed failing states as one of the key threats affecting the security of the Western world, describing state failure as,

> Bad governance – corruption, abuse of power, weak institutions and lack of accountability – and civil conflict corrode States from within. In some cases, this has brought about the collapse of state institutions. Somalia, Liberia and Afghanistan under the Taliban are the best-known examples. Collapse of the state can be associated with obvious threats, such as organised crime, or terrorism. State failure is an alarming phenomenon that undermines global governance, and adds to regional instability (European Union 2003: 809).

Rectifying state weakness became part of the mission in the 'war on terror'. Fukuyama wrote that,

> Weak or failing states commit human rights abuses, provoke humanitarian disasters, drive massive waves of immigration, and attack their neighbours. Since September 11, it also has been clear that they shelter international terrorists who can do significant damage to the United States and other developed countries (Fukuyama 2004: 125).

Hence, improving state building became central to the future of 'world order' (Fukuyama 2004). The US and UK governments began to systematise their approaches to categorising states and identifying remedial programmes, captured in the USAID *Fragile States Strategy*, the US *Millennium Challenge Account*, the DFID *Millennium Development Goals*, and the UK Prime Minister's Strategy Unit for *Countries at Risk of Instability* (Department for International Development 2002; Prime Minister's Strategy Unit 2005; US Agency for International Development 2005; US Government 2002). For example, USAID's *Fragility Framework* analysed governance in fragile states in terms of their effectiveness and legitimacy in four sectors: security, political, economic, and social. The strategy's overall goal was to guide the US Government's efforts in reversing the decline of fragile states in order to achieve a situation in which states will be amenable to development efforts. Weak states were named the 'vector for destabilising forces', manifesting the 'dark side of globalisation', and posing 'a very difficult national security challenge.' (Goldstone 2005: v). A new State Department office was opened – Office of the Coordinator for Reconstruction and Stabilization – and at least ten congressional bills were passed addressing the urgent mission to rebuild weak states. All of this was carried out in the belief that strengthening a state's ability to reach development goals and obtain certain adequate and acceptable political and economic conditions was crucial to combating terrorism.

2.5 Conclusion

This chapter argued that recent theoretical works problematising the state, as well as empirical case studies of states captured by networks in the African studies literature, address the type of questions salient to the case of Georgia. However, the domination of the institutional approach, and the more recent trend to rely on taxonomies of states to provide indicators for potential state failure, do not address the question of why weakness persists in the post-Soviet space. None of the approaches agrees on a definition of the weak state and, apart from the post-colonial approach, all of them assume some element of will within the state to strengthen. In fact, state and society are viewed as either cohesive or non-cohesive, but not as a conspiratorial unit in their actions to undermine the state. The literature and policy reports appear to be framed by the stronger states' agenda in addressing international terrorism, which prescribes a combination of democratisation and development to overcome weakness. Efforts to account for varying dynamics among states, such as historical, political, economic, and regional conditions that may perpetuate weakness are minimal.

This thesis will attempt to understand the causes of persistent weakness not through the traditional methods, but rather by applying post-modern approaches to reconceptualising the state. In particular, the functioning of empirical sovereignty in a weak state will be scrutinised. The idea of the state as an arena of conflict suits the study of how state and society cooperate together in networks, constructing an alternate order. Most importantly, while accepting the juridical sovereignty of states and the viability of the definition of state borders, the parameters of a weak state will be expanded to include the actions of trans-territorial actors, both within a state and between states. This will then create a lens through which to analyse where sovereignty is located in a weak state and how the displacement of empirical sovereignty affects inter-state relations. It will become evident that it is problematic to define what is weak in a weak state in which members of state institutions, in conjunction with a multitude of sub-state and supra-state entities, undermine the strengthening of the state.

But first it is necessary to establish whether Georgia was considered a weak state. Therefore, in the following chapter, the developments in post-independent Georgia will be explored in two historically based contexts. The first will be a politico-economic history of post-independent Georgia. The second will be the transition of the energy sector from an integrated Soviet system to individually functioning entities increasingly reliant on external actors. This will provide a comprehensive background for understanding the development of the trans-territorial networks and their role in perpetuating state weakness that is developed in subsequent chapters.

Chapter 3: Georgia's Politico-Economic and Energy Transition

> Question for President Shevardnadze: The population cannot always understand why those responsible for the crisis [energy] are being detained and an investigation in their cases is being conducted today, in the year 2000, and not earlier when those crimes were committed, that is, in 1993, 1994 or in 1995.
>
> Answer from President Shevardnadze: At that time, the system of extortion was too strong for us to break it down with empty hands [...] the state was not strong enough. In fact, we did not have a state (Burke 2000).

3.1 Introduction

Newly independent Georgia quickly collapsed as a result of the civil war (December 1991-January 1992), the wars over South Ossetia (January 1991-July 1992) and Abkhazia (August 1992-September 1993), and intermittent conflicts between President Shevardnadze's regime and supporters of the first President Gamsakhurdia for control of the state (January 1992-November 1993). Georgia's independence was further eroded by the government's reliance on Russia for security (armed forces stationed on its territory) and economic viability (major trade partner and supplier of energy). After a period of relative economic recovery and political stability from 1995-1998 under President Shevardnadze, Georgia once again weakened and entered a period of permanent crisis, veering towards failure. This was exacerbated by the Russian financial crisis of August 1998 and negative repercussions for the Commonwealth of Independent States (CIS). After 1998, Georgia experienced persistent energy shortages, heightened conflict between the government and civil society, debilitating negligence by administrators, a reigniting of conflict in Abkhazia, and deterioration in relations with Russia.

In this chapter, the turbulent events following Georgia's independence will be explored through multi-contextual parallel accounts in order to appreciate the complexities of the struggles a new state faced in the post-Soviet space. The first account will be a politico-economic history of Georgia, from the early days of Shevardnadze's arrival in the midst of war to his ousting in the Rose Revolution of November 2003. The parallel account will be on the transition of the energy sector from an integrated Soviet system to one of informal networks, increasingly monopolised by President Shevardnadze's family and reliant on Russia as the major supplier and distributor. Three periods of Shevardnadze's reign as President will be traced: the warring years (1991-1994); the recovering years (1995-1998); and, the waning years (1999-2003). These three periods are mirrored by a discussion of the persistent energy crisis in three periods: destruction and dilapidation (1991-1994); deregulation and privatisation (1995-1998); and investment and disinvestment (1999-2003). This information will provide a context for analysing Georgia as a weak state.

3.2 Politico-Economic History of Independent Georgia

Three periods of Georgia's politico-economic history during Shevardnadze's reign as President will be traced, beginning with the warring years (1991-1994), followed by the recovering years (1995-1998), and concluding with the waning years (1999-2003).

3.2.1 The Warring Years: 1991-1994

Georgia declared independence from the Soviet Union in April 1991 based on a referendum in which the majority of people supported secession. The first president of independent Georgia, Zviad Gamsakhurdia – a fervent nationalist and an active anti-communist – was elected in May 1991 with 86 percent of the popular vote (Library of Congress 1994c). Jones called this turbulent period of Georgia's history 'nationalist authoritarianism' because of three factors: Georgia's conflicting relations with its minorities, the Soviet civil and political legacy, and the erratic and authoritarian style of Gamsakhurdia's government (Jones 1996b: 507). Three events led to the collapse of both Gamsakhurdia's regime and Georgia by 1992. First, in a show of defiance against South Ossetia's declared independence from Georgia, Gamsakhurdia sent Georgian forces (mainly police and paramilitary groups) into the regional administrative capital, Tskhinvali, arresting the newly elected chairman of the South Ossetian Parliament. On November 10, 1989, the South Ossetian Supreme Soviet had approved a decision to unite South Ossetia with the North Ossetian

Autonomous Soviet Socialist Republic. Then, on September 20, 1990 the South Ossetians declared independence from Georgia and demanded recognition from Moscow as an independent entity within the Soviet Union. In December 1990, South Ossetia held its own elections, which were declared illegal by Georgia. Under the leadership of President Gamsakhurdia, Tbilisi retracted administrative control from the South Ossetian authorities and in January 1991 fighting ensued. This act led to eighteen months of war, thousands dead, over 40,000 refugees (12,000 Georgians and 30,000 Ossetians) , and the loss of Tbilisi's control over the territory (Zurcher 2005: 107).

Second, Gamsakhurdia's increasingly dictatorial style gained him many enemies. He took control of the media, restructured the government without consultation, and appointed regional leaders more powerful than the elected councils (Wheatley 2005a: 54). As one Georgian political scientist recalled, 'he [Gamsakhurdia] was utterly intolerant of any and all opposition (whether radical or moderate), and commonly branded his critics traitors to the nation' (Nodia 1995: 110). In response to his authoritarian style of leadership, there developed a band of those who felt betrayed by his policies. These included a disparate and temporary alliance of disillusioned nationalists and democrats, and the former communist elite who had been replaced with Gamsakhurdia loyalists (Nodia 1995: 111).

Third, in contradiction to his fervent nationalism he took two seemingly 'pro-Soviet' actions that angered loyalists: he did not condemn the August 19, 1991 coup against Gorbachev and he acquiesced to demands of the Soviet military commander to disband the National Guard headed by Tengiz Kitovani (Suny 1994:327). Gamsakhurdia's fate was sealed when in the fall of 1991, Kitovani and the National Guard turned against him (Zurcher 2005: 105). At the end of 1991 during a two-week battle, Gamsakhurdia was overthrown by a coalition of forces consisting of democratic parties and organisations supported by large parts of the National Guard and the most powerful paramilitary *Mkhedrioni* (Cornell 2001b: 169). The National Guard was formed in 1990 and was supposed to become the core of the Georgian army. Due to the lack of state support, however, it was financed by black-market entrepreneurs. Its leader, Kitovani, while having no formal military training, was a loyal friend of Gamsakhurdia's and an effective fundraiser (Zurcher 2005: 105). The

Mkhedrioni was a 'loose union of criminal groups and juvenile gangs from Tbilisi' created in 1989 by Jaba Ioseliani, a former leader in the Soviet underworld. The *Mkhedrioni* funded its activities from criminal dealings, including extortion and racketeering (Zurcher 2005: 104).

Replacing President Gamsakhurdia's government, the triumphant Military Council, composed of paramilitaries and Soviet *apparatchiki,* requested that Eduard Shevardnadze return to Tbilisi in 1992 to help lead the country. Shevardnadze had already ruled Georgia for 20 years; he was first appointed Georgian Minister for the Maintenance of Public Order in 1965 and subsequently became Georgian Minister for Internal Affairs from 1968 to 1972. In this position, he gained a reputation as a fierce opponent of corruption in Georgia, launching the 'Struggle Against Negative Phenomena in Social Political Life in Georgia' (Library of Congress 1994d). When Vasili Mzhavanadze came to power in Georgia shortly after the deaths of Stalin and Beria, Georgia became burdened by abuse of public office and shadow economic activities. With the support of Moscow, Shevardnadze succeeded Mzhavanadze in September 1972 (Cornell 2001b). Some believed that Shevardnadze's subsequent dismissal and imprisonment of hundreds of officials allowed him to place loyal patrons around him (Library of Congress 1994c).

Shevardnadze was elected to the Central Committee of the Soviet Communist Party in 1976 and eventually became Foreign Minister in 1985, leaving Tbilisi for Moscow. After a seven-year absence and the disintegration of the Soviet Union, Shevardnadze returned to Tbilisi in March 1992 to serve as a member of the Military Council along with Tengiz Kitovani, Jaba Ioseliani, and Tengiz Sigua, each of them with veto power (Jones 1996b: 522). The Military Council was subsequently renamed the Presidium of the State Council. Ioseliani's *Mkhedrioni* was subordinated under the Ministry of Interior and one of its former leaders, Gemur Khachishvili, was appointed the Minister. The *Mkhedrioni* was given the task of fighting pro-Gamsakhurdia forces in western Georgia, but it turned into a looting campaign, further destabilising the country (Zurcher 2005: 106).[1]

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[1] In this chapter and throughout the rest of the thesis, several terms are used to denote unofficial organisations operating within the political and economic structures of the state. I will attempt to be specific, when possible, as to their names and/or origins. However, sometimes, a broad term will be

It was this ambiguity of leadership over the country and the consolidation of power in the hands of paramilitaries that ultimately contributed to the war in Abkhazia and the further degradation of Georgia's territorial integrity. Shevardnadze brought a resolution to the war with South Ossetia in the Dagomys agreement signed with Russian President Yeltsin in June 1992, establishing a tripartite (Georgian, Russian, and Ossetian) peacekeeping force. That same month, Abkhazia's leader, Vladislav Ardzinba, sent a draft treaty to the Georgian State Council proposing a federative or confederative constitutional arrangement, but the new leadership rejected it. In July the Abkhaz reinstated the 1925 constitution, which defined Abkhazia as independent, and Ardzinba declared that Abkhazia would seek membership in the CIS (Cornell 2001b). One month later, Defence Minister Kitovani took advantage of the agreement of the Presidium of the State Council calling for the restoration of Georgia's control of the railway from Tbilisi to Russia to launch an attack on Sukhumi[2], the administrative capital of Abkhazia (Wheatley 2005a: 72). Fighting ensued between the Georgian and Abkhaz sides and, by the end of 1993, there were over 280,000 internally displaced persons (mostly Georgians) and an estimated 10,000 civilians and combatants killed (Cornell 2001b).

In the midst of the Georgian-Abkhaz war, the State Council was replaced by a new Parliament in October 1992; 234 deputies were elected by mixed proportional and majority systems. Shevardnadze was elected Chairman of the Parliament by a direct ballot with 96 percent of the vote and was subsequently named 'Head of State'.[3] The duties of the new Head of State included acting as head of the executive power and as the Supreme Commander of the Armed Forces. The Head of State nominated the Prime Minister, ultimately elected by the Parliament, and appointed the ministers subject to confirmation by the Parliament. Shevardnadze retained the three original

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used for lack of more specific information, or because these are the terms employed by other authors. For example, paramilitaries, non-state/irregular armed groups, and private militias are all unofficial armed formations, some of whom have government sponsorship. Criminal organizations, criminal groups, and criminals are all unofficial groups conducting illegal business, but again often with state participation. This will be explained in more detail in Chapter 4.

[2] Throughout this thesis, I will use the Georgian spelling of towns in the separatist regions, for example, 'Sukhumi' rather than the Abkhaz spelling 'Sukhum'. I will also use the transliteration of proper names and titles as they appear in the majority of news sources and reports by international organisations.

[3] Elections were not held in nine districts comprising South Ossetia, Abkhazia, and neighbouring districts in Samegrelo region.

members of the Presidium of the State Council, appointing Sigua as Prime Minister, Kitovani as Defence Minister, and assigning Ioseliani to the Defence Council.

While the Russian armed forces were accused of assisting both the Ossetian and Abkhaz fighters with firepower and manpower during the wars against Georgians, it was ultimately the Russians who helped Shevardnadze restore order in Georgia and solidify his hold on power (Suny 1994:331). Gamskhahurdia returned to western Georgia in 1993 to lead a rebellion against Shevardnadze, occupying Poti, a strategic port on the Black Sea and moving into Samtredia near Kutaisi. President Shevardnadze received military support from Russia in return for joining the CIS. With Russia's help, the Georgian military forces and the *Mkhedrioni* were able to defeat Gamskhahurdia and his Zviadists in November 1993. In February 1994, Georgia signed a pact with Russia, allowing it to retain four military bases in Georgia until December 31, 1995 (Vaziani near Tbilisi, Akhalkalaki in Samkshte-Javakheti, Batumi in Adjara, and Gudauta in Abkhazia) in return for training and equipping the Georgian army (Center for International Peace January-February 1993). One of the conditions of the Russian-brokered ceasefire between the Abkhaz leadership and Shevardnadze signed in May 1994 was to permit Russian troops, under UN auspices, to serve as the CIS peacekeeping force between Georgia and Abkhazia along a natural ceasefire line skirting the Inguri river with a 12 kilometre buffer zone on each side (MacFarlane, et al. 1996). This left the Russian military with responsibility for four military bases and two peacekeeping forces (in Abkhazia and South Ossetia) on the territory of Georgia.

The centre also struggled to control the periphery. In addition to losing two territories, outlying regions were not allegiant to the centre, in particular the Zviadists in Samegrelo, some areas of Kvemo Kartli to the south of Tbilisi partially inhabited by the Azeris (Bolnisi and Dmanisi), and the majority Armenian-populated Javakheti (Ninotsminda and Akhalkalaki) (Center for International Peace July 1993). The situation stabilised to some extent due to the combination of a state of emergency, an end to the wars, and the arrests of politicians with links to criminal groups in areas outside of Tbilisi, such as in Mtskheta, Zestaponi, Bolnisi, and Dmanisi (including the mayor). In January 1994, there were just 920 criminal offences reported compared to an all-time high of 3,638 in December 1993 (Center for International Peace January

1994). Further, by early 1995 the Ministry of Internal Affairs gained some advantage in its monopoly over the use of force, particularly after *Mkhedrioni* groups were arrested and the government collected weapons (Wheatley 2005a: 87). Overall, however, Shevardnadze's early efforts at democratisation had little impact and were marred by intense factionalism.

During the war years, Georgia was in a state of financial crisis; no economic system had replaced the collapsed Soviet command system, much of the physical infrastructure was destroyed or abandoned, and Georgia remained isolated from world markets. The war with Abkhazia drove up the price of oil and food, prevented the harvesting of crops and collection of revenues, and created an artificial economic blockade on the import/export market as a result of the violence and destruction of the infrastructure (Jones 1996b). Georgia had a massive budget deficit and minimal state revenue, most of which went towards supporting military actions. Industrial output was at a virtual halt; real income, consumption, and capital investment were extremely low (Library of Congress 1994d). From 1990 to1994, real GDP fell 75.2 percent, that is, productivity levels were only a quarter of what they had been in 1989 (TACIS 1995: 7). Further, currency reserves disappeared, the Russian rouble was replaced with a coupon, and inflation ran at 50 to 70 percent (Gurgenidze, et al. 1994; Papava 2003). The scene on the streets was of looting, banditry, and robbery, with small businesses suffering disproportionately (Wheatley 2005a:55). Salaries went unpaid, leaving 89 percent of the population below the poverty line by 1993 (Center for International Peace January-February 1993). The government attempted to finance the budget and its balance of payments deficits through domestic and external funding, which only drove up arrears on international payments and overdrafts on correspondent accounts with other post-Soviet states (TACIS 1995).

In the place of a state economy, a lucrative shadow war economy grew, driven by networks of suppliers and consumers traversing the porous borders of the Caucasus. In preparation for war, irregular armed formations obtained considerable arsenals and linked up with criminal organisations trafficking illegal commodities. They also took control of many of the local administrations in and around the conflict zones. These groups used coercion-backed extraction and large-scale protection rackets, accompanied by violence and the disintegration of law and order (Demetriou 2002b: 25-29). There was a shortage of goods and official lines of transportation were blocked, which resulted in the practice of governments and individuals bartering and trading goods with neighbours (Papava 1995: 275). Most Georgians were only able to survive the collapse of the economy by relying on their traditional social support networks, through extended family and local community networks. Moreover, the absence of more widespread poverty and malnutrition lends weight to the argument that Georgians found informal sources of sustenance within the unofficial economy (TACIS 1995). Thus, the wars acted as employment mechanisms in the face of drastic budget cuts, while they also served to create new economic mechanisms that, in most circumstances, outperformed the contribution from the state.

By the end of the wars it was hard to discern between the private militias, police, the state armed forces, and state sponsored paramilitaries. All of the armed groups were likely to carry out political activities that undermined the sovereignty of the state (Fairbanks Jr 2002). For example, after the coup overthrowing Gamsakhurdia, members of the *Mkhedrioni* became a dominant force in the unofficial economy, retaining control of the petroleum and tobacco trade, and some of the members obtained key posts in the government, including Deputy Head of Parliament. The National Guard increasingly dominated the arms trade (Zurcher 2005: 105). This led to a confrontation between groups vying for influence over the political-economic direction of the country. *Mkhedrioni*, along with heads of state enterprises, were in opposition to Minister of Economy Gotsiridze – an advocate of 'shock therapy' reforms (e.g. price liberalisation, privatisation, and stabilising the currency) that was proving successful in Central Europe.[4] Recommendations from IFIs were not adhered to and ultimately the republic reached the 'brink of economic and social catastrophe' as the Cabinet of Ministers, stacked with conservatives, triumphed over reformers (Economist Intelligence Unit 1996: 5).
Prime Minister Sigua's government fell in August 1993 after his proposed budget was rejected twice by the parliament. This provided an opportunity for President Shevardnadze to further consolidate his power through astute political manoeuvring,

[4] Interview with David Losaberidze, Caucasian Institute for Peace, Democracy and Development (CIPDD), Tbilisi, Georgia, April 2005.

appointing a technocrat, Otar Patsatsia[5] (representative of the powerful western Georgia lobby), as Prime Minister and Vladimir Papava as Minister of Economy in July 1994 (Economist Intelligence Unit 1995: 21). President Shevardnadze's support for conservative factions over reformists, and his preference for personal allegiance in appointments, resulted in economic stalemate. During this period, Georgia was the least successful of the newly independent states in creating new forms of governance to replace the 'wiring of the old state' (Jones 1996b: 523-524).

3.2.2 The Recovering Years: 1995-1998

During the second period of Shevardnadze's post-independence reign, Georgia experienced consecutive years of growth as a result of constructive measures taken by the government. This progress gained praise from the international community, accompanied by grants, loans, and investment. A new Constitution was adopted in August 1995 in time for the first presidential election.[6] With the mandate of his victory, President Shevardnadze pushed through International Monetary Fund (IMF) and the World Bank (WB) recommendations for economic reforms and IMF funds were released in 1994 and June 1995 (International Monetary Fund 1995). Macroeconomic stabilisation policies, a wide-ranging programme for privatisation and structural reform, and the new currency 'Georgian lari' (GEL) were introduced in 1995, paving the way for an energetic though short-lived recovery. Georgia experienced double-digit GDP growth until 1998; GDP growth reached 11.2 percent in 1996 and 10.2 percent in 1997. The government established a legal framework for fiscal management, Parliament began adopting budgets in 1995, a banking system was established, external trade was liberalised, and foreign debts were restructured (Papava 2003: 10-11). As a result, Georgia managed to eliminate shortages of

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[5] Patsatsia was an influential member of the *nomenklatura,* formerly a Soviet factory director and post-independence politician first appointed by Gamsakhurdia to be the mayor of Zugdidi, the site of clashes between the Zviadists forces and state-sponsored militias.

[6] Article 2 of the 1995 Constitution stated that the internal territorial arrangement of Georgia was to be left undetermined until Georgia regained jurisdiction of the whole of the country. Thus, the internal territorial arrangement was left ambiguous until Georgia regained Abkhazia and South Ossetia. In the interim, it was left up to the citizens of Georgia to regulate matters of local governance. In reality, President Shevardnadze used this article to establish a system that ensured that people loyal to him gained leadership positions in several layers of regional administrations, including 9 regional governors, whose responsibilities were minimal, but rights extensive (Chiaberashvili and Tevzadze 2005: 8).

consumer goods, control hyperinflation, stabilise the exchange rate, and enlarge the private sector. A sign of confidence in Georgia was the 1997 recorded foreign investment of over US $203 million by 37 countries (TACIS 1997:7). The government attempted to promote productivity and the growth of businesses by cracking down on criminal groups, transforming much of the wartime shadow economy into the official sector, and providing social assistance for the poor, while facilitating social reforms (Papava 1995: 284).

However, President Shevardnadze's reform efforts met life threatening resistance. The first attempted assassination of Shevardnadze occurred in August 1995 and was attributed to a faction of *Mkhedrioni* elements within the security services (Wheatley 2005a). Shevardnadze used the opportunity to move against the *Mkhedrioni*, arresting its head, Ioseliani, and the former Prime Minister and head of the National Guard, Kitovani. The head of the Georgian security services, Igor Giorgadze, was charged with conspiring to assassinate the President, and he consequently fled to Moscow. To counterbalance the destructive effect of the paramilitaries, Shevardnadze co-opted powerful entities and persons. Relying on old networks from the communist political and security structures, as well as heads of state-owned enterprises, he revitalised the party patronage system, distributing power to 'informal centres' of economic power. However, compared with other post-Soviet states, most particularly Azerbaijan under Aliyev, Belarus under Lukashenko, and the more authoritarian Central Asian states, power was less centralised in Georgia. In Georgia, power was 'feudalised' sectorally and geographically (Wheatley 2005a: 109-110). This allowed outside figures, both within the political circles of the president, as well as those governing areas outside of the capital, to develop their own fiefdoms.

Two political figures emerged during this time who, while not directly confronting the presidency, increasingly sought to present themselves as separate sources of power. The first was the head of the Autonomous Republic of Adjara, Aslan Abashidze, who consolidated his power, creating a de facto state with a Supreme Council and Presidium, a government with twelve ministries and eleven government departments, a tax inspectorate, and a Supreme Court (Wheatley 2005a: 115). Because the 1995 Georgian Constitution did not specify how powers and assets were to be divided between the centre and Adjara, Abashidze was able to use this in his favour. He oversaw a separate and non-transparent economic system. His command of the lucrative port of Batumi and its rail link with Baku, plus customs fees received from the Sarpi border crossing with Turkey, sustained his power. The other emerging figure of this time was Zurab Zhvania, a leading member of the younger, pro-Western generation, who had begun his political career as one of the prime figures in the Green movement during *perestroika*. By 1994, Shevardnadze had appointed him Secretary General of his political party Citizens' Union of Georgia (CUG) and Zhvania recruited Saakashvili and others back from the US and Europe to join the party. Securing a majority in the 1995 parliamentary elections, Zhvania was named Chairman of the Parliament. While being viewed as Shevardnadze's protégé, he was much more outspoken on the issues of abuse of public office, shadow economic activities, and interference by Russia in Georgia's internal matters, in particular Russia's increasingly overt support for the separatist regimes in Abkhazia and South Ossetia (Economist Intelligence Unit 1999: 9-10).

Increasingly, the Georgian government was under pressure from foreign governments and societal groups to combat undue privilege granted to government employees. In 1996, Shevardnadze ordered the Prosecutor's Office to investigate whether directives and regulations issued by the Cabinet of Ministers from 1992-1995 had been legal. Over 3,000 regulations were deemed to have been illegally drawn up and signed by top cabinet members during this period, some of which had Shevardnadze's signature (Anjaparidze 2001). In the end, however, the campaign was abandoned. Shevardnadze then pronounced 1997 the 'year for combating corruption' and parliament established an Anti-corruption Commission chaired by Gia Baramidze. The commission's work led to the resignation of the Minister of Finance, Davit Iakobidze, in September 1997 and of the Minister of Fuel and Energy, Davit Zubitashvili, in April 1998. However, Zubitashvili was cleared by the Prosecutor's office and was appointed as the Deputy Minister of Economics, Trade and Industry. While the entire government resigned in July 1998, most of the ministers were returned to their original positions or moved around (Anjaparidze 2001). Over the next several years, significant accusations were made against government officials.[7]

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[7] These accusations included the embezzlement of US$ 14 million from the state budget by the Minister of Post and Communications, Pridon Injia, the misappropriation of a Japanese government grant by the Minister of Agriculture, Bakur Gulua, the misuse of US$ 5.2 million of credit earmarked

In total, between January 2000 and May 2001, the Prosecutor's Office investigated 1,400 cases of abuse of power, embezzlement of property and money, bribe taking, violations of customs regulations, and tax evasion. However, only 128 cases made it to court and there were no indictments (Anjaparidze 2001).

One aspect of the economic revitalisation plan was the privatisation of former state enterprises. The Law on Privatisation of State Enterprises was adopted in August 1991 to outline general principles, and the Committee on Privatisation was established in 1992 (Government of Georgia 1991). Under Shevardnadze, privatisation began cautiously in August 1992 when the State Council adopted the State Programme on the Privatisation of State Enterprises. The law copied Russia's approach to privatisation by allowing for several methods, including popular privatisation, consisting of a combination of vouchers distributed to the public and auctions of state enterprises. However, the country's political crises delayed meaningful measures; by 1993 few Georgian industries had been privatised, although large numbers of small enterprises were scheduled for privatisation in 1993 and 1994 (Library of Congress 1994b). Beginning in 1995, there was a privatisation effort encouraged by the IMF and WB mainly in the trade and retail sectors. It was not until June 1996, however, that small-scale privatisation of nearly 10,000 firms was nearly complete and over 1,800 large and medium-sized enterprises (employing more than 50 persons) were turned into joint-stock companies. As with the rest of the former Soviet states, the privatisation process of state property was subject to abuse (Library of Congress 1994b). Many of the privatisations were done through employee buyouts and/or tenders that were either never announced or had only one applicant. This process allowed Shevardnadze's inner circle, including former communist party loyalists and his family members, to cement their holdings over state assets.

In the first half of 1998, foreign assistance and increased trade led to a boom in services, development of the telecommunications sector, and road and pipeline construction. Despite this, structural, institutional, and legislative reforms lagged behind and this factor, together with the collapse of the Russian rouble in 1998,

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for soldiers' food and clothing by the Defence Ministry, and the embezzlement of millions of dollars from the pension fund under the Social Security and Labour Minister, Tengiz Gazdeliani.

eventually harmed Georgia's sustained growth. By the second half of 1998, a series of escalating crises marked the end of the recovering years and the start of a decline of the state. A fall in Russia's export demand, following its financial crisis, hurt Georgia's economy and GDP fell to 1995 levels of 2.9 percent growth. The effect of the Russian crisis on Georgia proved that Georgia was not resilient enough to withstand external or internal threats. For all of the reforms, Georgia had only restored one-third of its economic capacity compared to that during the Soviet Union (The Strategic Research Institute 2004: 288). Due to inefficient reform efforts and a government mired in corruption, the IMF suspended lending operations to the country for the first time and the lari collapsed (International Monetary Fund 2000).

The economic malaise was matched by an increase in violence. In February 1998, Shevardnadze survived the second of two assassination attempts in three years. Supporters of deceased former Georgian President Zviad Gamsakhurdia attacked Shevardnadze's motorcade. After the government arrested eleven people, some of the remaining assailants kidnapped four United Nations observers from their compound in Zugdidi, western Georgia. They held the captives ransom in return for the release of their fellow conspirators. The hostages escaped or were released following a dialogue between the Shevardnadze government and former members of Gamsakhurdia's faction (US Department of State 1999). According to a former assistant to President Shevardnadze, his personality changed and his mental abilities weakened as a result of the second attempt on his life, which led to the death of two of his bodyguards. He became weaker, more authoritarian, lost public support, and his family gained more power over state and private assets, particularly in the energy sector. Further, he began to rely more on an inner circle of counsellors, who briefed him according to their personal interests, and increasingly insulated the president from the realities of the affairs of the state.[8]

Two months later the worst outbreak of fighting in Abkhazia since 1983 occurred between Abkhaz separatists and ethnic Georgian militiamen, resulting in some 30,000 ethnic Georgians fleeing the Gali region (The Associated Press 1998). Violence in Abkhazia also accounted for several incidents that involved foreign personnel. In

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[8] Interview conducted off-the-record with Georgian government official, Tbilisi, Georgia, April 2005

July four UN military observers were taken hostage and in September three UN military observers and their Abkhaz driver were wounded in Sukhumi during an ambush (US Department of State 1999). In response, Shevardnadze attempted once again to shift political personalities around in order to create some stability in the country. In August of that year, he reshuffled the government and appointed Vazha Lortkipanidze as the head. The first local government elections were held in independent Georgia in November 1998. Notwithstanding these moves, Georgia once again descended into a state of crisis.

3.2.3 The Waning Years: 1999-2003

Despite all of the achievements following the war period, political and economic stability in Georgia continued to be fragile. Following the parliamentary elections of 1999, the political elites were focused on an intense power struggle, which yielded no clear winners. Shevardnadze allowed this process to run its course, but as a result of that power struggle, Georgia again became very weak and disorganised by the fall of 2001 (Tsereteli 2002). While Shevardnadze's political discourse, particularly when engaging with foreign western interlocutors, was one of democratic liberalism and the market economy, practice was something quite different.[9] The waning years frustrated the public and officials alike. Tensions between all parties ran high, including between the centre and peripheral regions, Georgia and neighbouring states (particularly Russia), the presidential administration and society, and the government and foreign donors.

By this period, it was evident that the prevalence of the shadow economy jeopardised macro-economic stability, impeding real sector growth (International Monetary Fund 2003a). Informal institutions, a large illegal sector of the economy, a high level of administrative corruption, a weak tax administration, and an inefficient privatisation process all provided obstacles to adequate economic growth (Chkhartishvili 2002). The shadow economy was estimated to be between 25 and 40 percent of GDP (International Monetary Fund 2000; TACIS 2000). According to the Georgian State Department of Statistics, the Georgian shadow economy from 2000 to 2003 was

[9] Interview conducted off-the-record with Georgian government official, Tbilisi, Georgia, April 2005.

between 32 and 34 percent (TACIS 2003). However, Georgian pundits unofficially estimated that as much as 80 percent of all consumption was obtained through contraband by 2000 (Lynch 2003: 111). By the late 1990s, Georgia's shadow economy was estimated to be the largest of all of the states of the former Soviet Union (Schneider and Ernste 2002). The IFIs became increasingly frustrated with the lack of reform in Georgia and, in early 2001, the IMF suspended funds due to insufficient tax and revenue collection. Years of unrealistic and therefore unmet state budget targets left pensions and salaries unpaid for months at a time. After 1998, GDP growth slowed to less than 2 percent in 2000, though it recovered to 4.1 percent in 2002 (TACIS 2003).

Georgia never established functioning and transparent government institutions operating under the law. Shifting alliances in the political system, particularly just before an election, were more important than institutions, political parties, and the rule of law. Shevardnadze was in his element when applying 'tactics for balancing political forces, recruiting people with tainted reputations, and manipulating people through bureaucratic mechanisms' (Nizharadze 2005: 110-11). A debilitating level of corruption acted as its own source of stability, like an insurance policy or a 'defence against uncertainty'(Nizharadze 2005:111). Although the President's party, CUG, won a majority in the 1999 parliamentary elections and Shevardnadze was re-elected in 2000, both elections were mired in controversy with accusations of vote rigging (OSCE/ODIHR Election Observation Mission 2000). This election marked the shattering of the 'Shevardnadze Myth', at home and abroad, due to egregious acts of falsifying the vote carried out by the President's loyal clients, particularly in the provinces. Shevardnadze's appeasement of the various factions, in particularly the presidential family, significantly undermined his authority.

The older generation retained control of the executive, but the new generation progressively penetrated the Parliament and the business community. In Parliament, Zurab Zhvania, Mikheil Saakashvili, and Nino Burjanadze formed an informal alliance to reform the political system. Mikheil Saakashvili was named by Shevardnadze to be the Minister of Justice in 2000 but, to the President's chagrin, he used his post to publicly accuse senior members of the government of general abuse of their posts and financial graft. According to a local opinion poll in 2001, Saakashvili was considered to be the most trustworthy politician in Georgia (Economist Intelligence Unit 2001: 11). After 2000, the ruling CUG party splintered into reformist and conservative factions. In an open letter to Shevardnadze in August 2001, the reformers, led by Zhvania and Saakashvili, accused the president of involvement in corruption and demanded that he fire dishonest ministers and purge his corrupt entourage. A battle ensued between the 'reformers' and the entrenched *nomenklatura* and other business elites who stood to lose from proposed anti-corruption measures. (Nizharadze 2005:111). Meanwhile, Shevardnadze's unpopularity with the Georgians was increasing; his approval rating in 2001 had fallen below 10 percent (Freedom House 2003). The President lost his ability to balance the two sides and it is said that at this point, he fought reform efforts and became a magnet for the 'darker forces' that operated in a shadow economy of corruption, as he needed their support and financial assets to hold on to power.[10]

The climax of the conflict between these factions came when the Minister of State Security, Vakhtang Kutateladze, a member of the conservative faction, ordered a controversial raid on an independent TV news company, Rustavi-2, which had been highly critical of the government (Papuashvili 2002). This resulted in mass street protests in late October 2001 of more than 10,000 people, some demanding the resignation of Shevardnadze and the Minister of Interior, Kakha Targamadze. When it became clear that Shevardnadze had condoned the actions of the security ministries and was not going to support the reformists, Zhvania announced that the President had 'lost touch with reality' (Papuashvili 2002). Though Shevardnadze admitted that the action taken by the state police was wrong, he openly defended the Minister of Interior, threatening that if Targamadze and the Prosecutor General, Gia Meparishivili, were forced to resign, then he would follow. After parliamentary chairman Zurab Zhvania's resignation and the dismissal of the entire government, the demonstrations outside the Parliament stopped (Petersson 2001). Shevardnadze stepped down as chairman of the CUG but did not get rid of his loyalists, Kakha Targamadze, and Economics Minister, Vano Chkhartishvili. Meanwhile, Saakashvili and Zhvania created their own political parties – United National Movement and United Democrats respectively (Anjaparidze 2002). Some labelled this the 'October

[10] Interview conducted off-the-record with Georgian government official, Tbilisi, Georgia, April 2005.

Revolution' and considered the events to be the beginning of the end of Shevardnadze's legitimacy (Chiaberashvili 2001).

By this point, Russian-Georgian relations had deteriorated to the point of being on the verge of direct military confrontation. Russia imposed a unilateral visa regime, cut the gas supply to Georgia, urged Georgia to leave GUAM (a nascent security alliance between Georgia, Ukraine, Azerbaijan, and Moldova) and join the Moscow-led Eurasian Economic Union. The Russian government also refused to finalise arrangements for its military withdrawal from its bases in Georgia despite an agreement reached in the 1999 Istanbul Treaty (non-binding) brokered by the OSCE (Baran 2001; Kandelaki 2000). While the Russian army had vacated the Vaziani and Gadauta bases, they maintained two bases in strategic Georgian areas populated by minorities, Alkhakalaki in Javakheti and Batumi in Adjara.[11] Tensions peaked in October 2001 when ethnic Chechen fighters residing in Georgia launched an assault on breakaway Abkhazian forces in the Kodori Gorge. Some alleged that the Georgian Ministries of Internal Affairs and State Security had arranged to ferry the Chechen fighters from the Pankisi Gorge in north-eastern Georgia to the Abkhaz-Russian border. In the following six months, Russia violated Georgian airspace twice, bombing three villages and killing civilians. The international community was not immune to this violence – in October a UN Observer Mission in Georgia (UNOMIG) had been struck by a missile over the Kodori Gorge, which killed nine (Human Rights Watch 2002). Then in early 2002, there were reports that Arab militants, driven out of Afghanistan by US-backed forces, could also be operating in Pankisi. Partly to quell the violence, the US government announced a US$ 64 million train and equip programme for the Georgian armed forces in May 2002. Georgia conducted counter-insurgency operations in Pankisi throughout 2002, due in part to US pressure to capture supposed al-Qaida members seeking refuge in the gorge, as well as to put a stop to repeated bombardments by Russia of its territory (Peuch 2002).

[11] While the Vaziani base was closed on time (July 1, 2001), withdrawal from the Gudauta base in Abkhazia was not fully completed within the agreed upon time frame. While the Russian Ministry of Foreign Affairs (MFA) announced the de facto dismantling of Gudauta on 9 November 2001, the Georgian MFA still claimed the non-fulfilment of the agreements by the Russian side.

By 2002, internal security had begun to collapse, abuse of public office impeded government performance, and the presidentially mandated Anti-corruption Commission had failed to undertake any substantial measures. Criminal behaviour thrived within branches of the government, most especially the security forces, including those serving in the interior ministry, armed forces, border guard, and customs. The government became mired in scandals related to foreign assistance and the IMF suspended its lending operations to the country. In the June 2002 local elections, the CUG suffered a major defeat. Partly as a result of increased military cooperation between the US and Georgian militaries, both separatist regions, Abkhazia and South Ossetia, requested 'associate status' with Russia. Georgia's internal security deteriorated, with a renewed spate of kidnappings, attacks on human rights groups, and a mutiny by a National Guard battalion that reminded many of the pre-1995 chaos. Within this context, Shevardnadze made four moves that ultimately led to the unravelling of his allegiant webs of clients and his ousting in the November 2003 Rose Revolution.

First of all, he allowed for a free press and the proliferation of non-governmental organisations, which relentlessly pursued government officials for abusing the privileges of their office. Second, his recruitment and promotion of young reformers created a cadre of those in power who had never belonged to the power structures of the *nomenklatura*. Third, the prolonged disruption of reliable state goods and services eventually led the majority of Georgian citizens to deem the regime incapable of leading the state. Relations with Russia had deteriorated and the separatist regions were gaining in strength in their prolonged *de facto* independent status. Finally, in the lead up to the November 2003 parliamentary elections, western governments warned Shevardnadze to ensure that the results of the elections reflect the choice of the people. When the results were deemed by the OSCE and other organisations to have been falsified, western governments denounced the handling of the elections. The many non-governmental organisations, members of the media, and the political opposition who were anxious to see his era come to a close interpreted this as proof that Shevardnadze had lost the support of western governments.

3.3 Transition of the Energy Sector in Independent Georgia

Given the politico-economic history above, three parallel periods of persistent energy crises during Shevardnadze's presidency will now be traced. This section will begin with the years of destruction and dilapidation (1991-1994), followed by deregulation and privatisation (1995-1998), and concludes with a period of investment and disinvestment (1999-2003).

3.3.1 Destruction and Dilapidation: 1991-1994

The first period was marked by efforts to fulfil the immediate demands for energy amid the turmoil of the dissolution of the integrated and centralised Soviet energy system, as well as to survive the destruction of the energy infrastructure during the wars. Since the 1980s, the Georgian energy industry had suffered from neglected maintenance, a fall in production, and increasing reliance on other Soviet republics (Black Sea Regional Energy Centre 1996). Towards the end of the 1980s, Georgia's industrial sector was reliant on its only primary energy source, hydropower, or bartering for 15 percent of its electricity through the Trans-Caucasian Interconnected Power System, and importing virtually all of its oil and gas (Black Sea Regional Energy Centre 1996). By 1990 Georgia imported over 95 percent of its petroleum products from Russia and Azerbaijan, all of its natural gas from Turkmenistan, and 25 percent of its electricity from Russia and Azerbaijan (International Monetary Fund 1996). Georgia suffered an unusually harsh winter in 1991/1992, which led to an increase in fuel demand and a curtailment of domestic hydroelectric production. Thus, by 1992 Georgia was vulnerable to its neighbours for energy supplies in all three sectors – oil, gas, and electricity.

Sources of energy and rates of consumption over this time changed with the politico-economic situation within Georgia as well as the region (Black Sea Regional Energy Centre 1996). Between 1990 and 1996, total energy consumption in Georgia fell by almost 70 percent, corresponding to the GDP decrease of over 83 percent. Meanwhile, the use of natural gas was limited to two of Georgia's enterprises – *Rustavi* metallurgical factory and *Gardabani* power station. As a result, the domestic use of hydro energy doubled and wood use rose nine times (Black Sea Regional Energy Centre 1996). The wars further exacerbated the situation by blocking key energy transit corridors, as well as destroying transmission lines and internal production capabilities. Supplies of fuel were further limited due, in part, to the war between neighbouring Armenia and Azerbaijan. The situation worsened with the destruction in October 1992 of a stretch of the gas pipeline running through North Ossetia (southern Russia) to Georgia (Economist Intelligence Unit 1993: 24). Georgia's gas transmission system was designed during the Soviet period and for far higher transport volumes than it handled after independence. Georgia had trunk gas pipelines with Russia, Azerbaijan, and Armenia allowing for increased gas transport. However, lack of investment and instability prevented this from happening. Gas leakage due to corrosion and theft, low pressure, and periodic attacks were central problems in the operation of Georgia's gas transmission network. Likewise, Georgia could import electricity from Russia, Azerbaijan and, via low voltage lines, from Turkey and Armenia. However, system losses of electricity remained endemic at almost 30 percent, due to overload, decaying infrastructure, and sabotage (Krishnaswamy and Stuggins 2003).

The situation was further exacerbated by the absence of government regulation, inefficient management, and neglect. From 1992 to 1994 the government simply could not manage to provide a regular service, nor could it handle the financial aspects of the collection of tariffs for services provided (Library of Congress 1994a). A series of ill designed policies, including the government's setting of low prices, insufficient investment, and false financing schemes, perpetuated the crisis (Papava 1995:275-276). Under the Soviet system, Georgia was accustomed to very low energy prices and was therefore confronted with trade shocks in the 1990s. The increase of energy import prices to world market levels in 1993 and acute shortages of foreign exchange to pay for the imports led Georgia to a sharp accumulation of external arrears to exporting countries and dramatic cuts in domestic consumption and imports of energy (International Monetary Fund 1996: 9). External arrears on energy payments became common, particularly for electricity and gas. Georgian authorities frequently breached contractual arrangements, particularly over transit obligations for gas and electricity. Inter-state issues related to non-payment became a recurrent source of tension between Georgia and its neighbours, and failure to settle disputes often led to disruption in trade flows.

Thus, the combined factors of shortage of supply, an insufficiently monitored financial and legal system, economic blockades, and porous borders offered lucrative opportunities for supply through alternative channels. Various forms of barter and other non-cash payment arrangements flourished between Georgia and exporting countries, often in a non-transparent way through third party intermediaries. The two most prevalent channels were using war-time links to transit petroleum products and creating third-party companies for the purposes of accruing state debt for undelivered or diverted gas and electricity from neighbouring states. Case studies of these alternative channels of business will be explored in Chapters 5 and 6. Hence, as a result of the disintegration of the Soviet Union, combined with the dilapidation of the infrastructure, and speeded up by the wars and the inefficient management of the energy sector, Georgia's collapsed economy was matched by its collapsed energy system.

3.3.2 Deregulation and Privatisation: 1995-1998

In the post-war period, there was great improvement in Georgia's energy sector. This was a period of the dismantlement of the former Soviet giant state-owned companies into smaller state-owned or joint-stock companies. It was also a period of the privatisation of parts of the energy sector, from small hydropower plants to larger electricity distribution centres. Despite these positive developments, however, the absence or vagueness of legislation, abuse of the privatisation of state assets, and deregulation of the electricity sector prevented sustainable reform. For example, the absence of oil and gas legislation resulted in the practice of companies negotiating with Georgian officials on a case-by-case basis with few guarantees for their investments (Kotetishvili 2005). Meanwhile, the entrenchment of the *de facto* separatist regions with unrecognised and unprotected borders resulted in a multi-party transit system protected by officials and armed forces across the region. Finally, as a result of deregulation, electricity distribution companies in Georgia's regions became a source for major graft, as local politicians were able to gain control of the distribution mechanism of electricity and divert unmetered electricity to 'private' sources for sale across the region under their jurisdiction.

Beginning in 1995, the Georgian government implemented several economic transition programmes. A privatisation programme of state energy firms, guided by the IFIs, was initiated. However, it proved difficult as no local or foreign business was willing to invest in Georgia and provide the capital for infrastructure improvements (Economist Intelligence Unit 1997: 10). Efforts made to privatise the state gas company *Tbilgaz,* for example, ran into several problems, including a 1998 tender, which was rescinded due to a question of earlier liabilities. The government also attempted to liberalise prices for petrol and gas, and to collect tariffs from customers. A policy was implemented to allow energy companies, as well as big industrial enterprises and municipalities, to enter into direct agreements for the import of supplies (Papava 1995: 278-79). However, attempts to eliminate electricity subsidies provoked strong public and legislative criticism in July 1995 when the state power company, *Sakenergo*, raised rates and then, citing large arrears, shut off supplies to consumers in areas of eastern Georgia. Parliamentarians began calling for criminal proceedings against *Sakenergo's* management (Economist Intelligence Unit 1996: 12). As a result, a presidential decree of July 1996 split the *Sakenergo* monopoly into *Sakenergo-generatsia*, a holding company with the function of generating power, a state-owned enterprise called *Sakenergo-gadatsema* with transmission functions, and *Sakenergo-dispetcherizatsia,* responsible for distribution functions. Distribution was at first delegated to the municipalities under the locally elected leaders, but was later transformed into state owned joint-stock companies (Krishnaswamy and Stuggins 2003).

Additional reforms were made to governmental management systems that were supposed to coordinate policymaking and improve the efficiency of the energy sector. In June 1996 the Ministry of Fuel and Energy was established with the task of designing and coordinating reform policies, as well as promoting foreign investment in the energy sector, while refraining from direct intervention in energy production and distribution. Following the adoption of new energy laws on electricity and gas (Government of Georgia 1997, 1999), Georgia and international experts together developed a national energy policy concept urging the government to generate greater production capacity, enhance efficiency of use of energy resources, balance imports and exports, and liberalise the fuel and energy complex (Didebulidze 2001). The 1997 electricity law separated the policy, regulatory, and ownership functions of the government, disengaged government from business operations, and established an independent electricity regulatory commission (GNERC) with authority to approve energy tariffs and issue, enforce, and revoke licenses. GNERC also oversaw the Georgian Wholesale Electricity Market (GWEM), which was responsible for organising trade in electricity between generating entities, as well as between distributors and major consumers. It was meant to serve as an enforcement agency of financial transactions, ensuring payment of tariffs and dispatch from seller to buyer. However, technical losses remained high and collections low (International Monetary Fund 1998: 30). And, ultimately, the new agencies and the unbundling of large state enterprises offered additional opportunities for managers to divert state assets for private benefit.

As energy sector privatisation efforts had not resulted in the desired foreign investment, much of the assistance came in the form of grants and concessional loans. The WB, EBRD, EU, Germany's KfW Bankengruppe, and USAID all encouraged the Georgian government to carry out energy sector reform. Grants were provided to support cost recovery from unpaid tariffs, increase energy efficiency, improve energy policy, and support the future privatisation of energy companies. During this time, grants and technical assistance to Georgia's energy sector also came from UNESCO, International Group E7, and individual governments including Greece, France, Switzerland, Japan, China, and Iran, among others. By 1999, US$ 110 million worth of investments had been provided to Georgia's energy sector (Black Sea Regional Energy Centre 1996). Because substantial privatisation still did not occur, the donor community turned to management contracts, particularly in the electricity sector, to prepare state assets for future sale.

The potential development of Georgia's sea ports for the resource-rich landlocked states of Central Asia to export hydrocarbons was once again raised. The Baku-Batumi pipeline had been constructed at the beginning of the twentieth century, and for many years served as the principle means of transporting oil from Azerbaijan to Europe. In 1995, the Azerbaijan International Oil Company (AIOC) selected the Baku-Supsa (Georgia) route to serve as one of two routes for transportation of 'early oil' from Azerbaijan (Karagiannis 2002: 74). On March 8, 1996, Shevardnadze and

Azerbaijani President Heydar Aliyev signed a 30-year agreement to pump a portion of the AIOC's 'early oil' via Georgia to its Black Sea port of Supsa. The Georgian International Oil Company (GIOC), a counterpart to AIOC established in 1996, made substantial improvements to the existing 515-mile pipeline along this route and built the US$ 565 million Supsa terminal on the Black Sea, partly funded by EBRD and the WB's International Financial Corporation (IFC). It oversaw the construction of the Baku-Supsa oil pipeline and facilitated other oil pipeline projects (International Monetary Fund 2000: 71). No oil was planned for Georgian domestic use, but it was anticipated that economic activity from transit tariffs and construction works, and the possible flow of foreign exchange would boost the economy (International Monetary Fund 1998: 7).

3.3.3 Investment and Disinvestment: 1999-2003

Beginning in 1999, Georgia received the largest foreign investments in its energy infrastructure, including hydrocarbon transport, oil and gas industries, and electricity distribution. However, the end result of this investment was not, for the most part, positive. On the one hand, there were signs of external confidence in Georgia's potential role as a regional transport corridor from the resource rich Caspian Sea basin to Europe, as well as a lucrative market for investment. On the other hand, Georgian society continued to suffer severe energy shortages, resulting in mass protests on the streets of several cities starting in 2000. In the winter of 1998-99, Tbilisi had only 4-6 hours of electricity per day while the rest of the country received an average 3-4 hours (International Monetary Fund 2000: 67). Rather than becoming a source of development in Georgia, the energy sector became a destabilising factor. Power cuts harmed those running small businesses; the added cost of generating one's own electricity supply remained a major cost burden to many enterprises (International Monetary Fund 1998: 9). There was a striking paradox in the contrast between a relatively positive macro-investment climate and the micro-level struggles of the Georgian citizens. By 2003, however, the two converged as clientelistic practices ensured that 'outsiders' failed at running Georgia's energy companies.

After 1998, because of non-payment by citizens for electricity coupled with the heavy debt of the Georgian government to neighbouring countries, Georgia no longer received annual subsidies from international lenders (up to US$ 20 million), nor did it have access to long-term credits to the energy sector provided by international organisations (more than US$ 176 million) (Didebulidze 2001). Despite these conditions, this was a period of the largest foreign investment in Georgia's electricity sector. In addition to the over US$ 500 million spent by international donors, delineated in Table 1 below, a private western firm entered the market. In April 2000, the American company *AES* acquired *Telasi* (the capital's electricity distribution company), two out of ten blocks of the *Gardabani* thermal power generation plant near Tbilisi, and the *Khrami*-1 and -2 hydropower plants (after the World Bank spent US$100 million on repairs). Eight small distribution companies in the Kakheti region were also privatised (International Monetary Fund 2001: 86).

As had occurred in the electricity sector, the natural gas law of 1999 separated the gas industry into transmission and distribution enterprises (Government of Georgia 1997, 1999). Transmission remained state-owned, under *Saktransgasmretsvi.* Distribution was organised around 29 gas distribution companies, six of which were bought by the Russian company *Itera* (through its subsidiary *Sakgaz*) (International Monetary Fund 2003b: 11). The natural gas sector had similar problems to that of the electricity sector; massive debts and aging infrastructure meant that supply was reduced six-fold and minimal privatisation took place. A 2001 US government study estimated the levels of losses from the energy sector for one year at US$ 600 million from foregone taxes (US$ 300 million), electricity losses (US$ 200 million), and natural gas losses (US$ 100 million) (United States Agency for International Development 2001).

At the same time, however, Georgia's transit potential increased exponentially. By 1999, Georgia had two operational terminals on the Black Sea coast, one in Supsa and one in Batumi. In 2000, under the management of the Turkish firm *Channel Energy,* Georgia's largest port, Poti, was greatly enhanced for use as an oil storage and transit facility, partly financed by a US$ 12 million loan from EBRD and US$ 8 million from the Black Sea Development Bank (Menas 2006). A mixture of pipelines and rail traversed Georgia to Batumi and Poti ports, moving oil from Azerbaijan and Kazakhstan. This was administered by the GIOC, responsible for east-west transit of oil and gas, and was expected to earn Georgia about US$ 6.3 million in transit revenue in 2000 (Economist Intelligence Unit 2001: 18). At the end of 1999, the presidents of Azerbaijan, Georgia, Turkey, and Turkmenistan signed a package of agreements to establish the Baku-Tbilisi-Ceyhan pipeline (BTC) and a parallel gas pipeline Baku-Tbilisi-Ezerum (BTE) with projected completion dates of 2005 and 2006 respectively. Combined, they were estimated to generate over US$ 2-3 billion in investment, with US$ 200 million spent locally and an additional US$ 80 million in social and economic investment in the country. British Petroleum, the lead company of 17 consortium partners, became the biggest source of foreign investment in Georgia (Digings 2005).

This period also saw investment in Georgia's hydrocarbon extractive industry. Between 1995 and 2000, foreign investment in the oil sector was about US$ 125 million (International Monetary Fund 2001: 92). In 1999 Parliament adopted the Law on Oil and Gas, which created the Oil and Gas Resources Regulation Agency (Government of Georgia 1999), As a result, the state company *Gruzneft* was reorganised into a joint-stock company, 'National Oil Company of Georgia – *Gruzneft'*, enabling it to carry out large-scale research and survey operations jointly with foreign companies. By 2000, Georgia was producing around 1 million barrels of oil a year from 10 minor joint ventures between *Gruzneft*, known locally as *Saknaftobi,* and various small companies from the US, UK, Switzerland, and Germany. Oil and gas exploration and production in Georgia was minimal compared to the Central Asian nations, but nonetheless significant for a resource dependent state. From 1995 to 2000, three joint ventures were operating in Georgia: the Georgian-British company *Ninotsminda*, the Georgian-Swiss company *Ioris Veli*, and the Georgian-American company *Frontera Eastern Georgia.* As of 2000, there were nine companies in total prospecting for oil and gas in Georgia and estimated future investments for the period from 2001 to 2005 were US $452 million (Kavkasia-Press 2000b). Additionally, there were 16 companies that had applied for oil refining licenses and of these, the Georgia-America Oil Refinery (GAOR) in Sartichala, was the biggest (Sarke Information Agency 2003c).

Table 1 - Foreign Assistance in Georgia's Electricity Sector, 1994-2004

Organisation	**Purpose**	**Donation/ Duration**
World Bank	Electricity Rehabilitation, including procurement of natural gas for *Tbilresi*	52.3 million USD 1997-2000
World Bank	Credit for structural reforms	25 million USD 1999-2002
World Bank		56 million USD 2001-2006
UN Development Programme (UNDP)	Solar energy systems	55,000 USD 1996-1998
UNDP	Develop small size hydroelectric power stations and reduce gas emissions.	25,000 USD 1999
UNDP	Enhance local energy supply	12.5 million USD 2002
European Union (EU)	Rehabilitate *Inguri* Hydroelectric Power Station (HES)	10 million Euro 1997-1998
EU	Energy structural reforms	1 million USD 2000-2002
EU	Reorganise *Sakenergo* management system	399,000 Euros 1993-1994
EU	Elaboration of energy sector development strategy	500,000 Euros 1994-1995
EU	Support to Ministry of Fuel and Energy	1.3 million Euro 1997-1999
EU	Establishment of centre for energy efficiency	2 million Euro 1998-2000
EBRD	*Gardabani* rehabilitation	18.1 million USD 1994-1997
EBRD	Rehabilitate *Inguri* Hydroelectric Power Station	38.7 million USD 1998-2002
EBRD	*AES Telasi* energy distribution network (metering)	30 million USD 1999 to 2004
International Financial Corporation	*AES Telasi* – reform company, rehabilitate physical assets, install meters, etc.	30 million USD 1999 to present
China	Rehabilitate *KhadoriHES*	n/a
Germany	Emergency Programmes (Sectors 1-5): electricity system reform	132.5 million DM 1995-2004
Germany	Training and qualification in Germany for employees	3.5 million DM 1997-2002
Germany	Small loans for energy (reusable) development	5.1 million Euros
Germany	*VartsikhHES's* 4th cascade	63.5 million DM
Japan	Rehabilitate *LajanurhesiHES* and *Khrami*-2 power stations	40-45 million USD 1998-2005
Turkey	Electricity Supply	60 million USD 1992-1996

Source: (Centre for Economic Corruption Monitoring November 9, 2004)

However, two problems plagued the petroleum industry in Georgia: smuggling and illegal refining. First, the fuel import and distribution business in 1998-2001 was in the hands of two competing monopolies. Nugzar Shevardnadze, the President's nephew, monopolised petroleum imports and Guram Akhvlediani, a member of the Shevardnadze family by marriage, had a monopoly on oil production. Second, imports were mostly transported through the grey market and therefore did not bring in revenue for the state. If you compare Georgian annual petrol and diesel consumption figures compiled by the three organisations in Table 2, it appears that a discrepancy in the figures provided by customs officials could be the result of the practice of purposefully under-calculating trade. Georgia also suffered from the lack of a management information system, corrupt import/export/transit regimes, and an inefficient tax administration. According to a US government sponsored report, only 10 to15 percent of legally imported gasoline in 1999, or 48,000 tonnes out of 331,000 tonnes were registered as official retail sales in Georgia (Shenoy 2002a). The business interests of the Shevardnadze family and their allies were eventually responsible for the demise of the GAOR oil refinery.

Table 2 - Comparing Georgia's Imports of Petroleum Products

Source	**Petrol**	**Diesel**
World Bank	600,000	432,000
Parliament's Budgetary Office	600,000	400,000
Georgia Department of Customs	132,000	60,000

Source: (Metreveli 2003)

Georgia's instability and dependency on Russia made it vulnerable to disruptions in supply of gas and electricity from Russia, as well as vulnerable to internal attacks on its energy infrastructure. Russia would often cut off supply at critical moments in Georgian domestic political developments, such as during elections, bilateral negotiations with Russia, or Russian military activity on Georgian territory. This was most often done because of Georgia's alleged non-payment for supply (Cornell

2001a: 10). During 2002 and 2003, accidents, bad weather, a lack of maintenance, and sabotage on the Russian side of the border were also cited as reasons for a disruption in services (Gularidze 2003). These incidents were not just confined to Russian-supplied energy. Within a period of a month in 2003 there were 3 major acts of sabotage against Georgian energy facilities. First, on January 10 in the Gori district, a Baku-Batumi cargo train transporting oil went up in flames as two tank wagons were set on fire. A week later, also in the Gori district, plotters tried to drill a hole in the Georgian section of the Baku-Supsa oil pipeline to pump oil, but failed. Finally, a third incident took place at the end of the month when a 30-wagon train with Azerbaijani oil on route to the Black sea port of Supsa crossed a railway bridge across the Hevisckali river in the Samtredia district of Georgia and exploded, throwing it into the river. According to the president of GIOC, Giorgi Chanturia, all these actions were directed at sabotaging Georgia's role as a future hydrocarbon transit corridor (Ismailova 2003).

As Russia was increasingly viewed by Georgians as both an unreliable provider, as well as a potential obstructer to its participation in east-west projects, Shevardnadze's reign ended with two secret energy deals with Russia. In summer 2003, he revealed that most of the gas and the electricity sectors would be controlled by Russian state owned companies. The controversial exit of the American electricity company and its turnover of management of Georgia's largest electricity distribution company to a Russian state-owned company was a low-point for President Shevardnadze. The secrecy of the deals and the agreement to sell strategic assets to Russian companies led to a surge in Georgian antipathy towards Russia, as well as adding to popular mistrust of the Shevardnadze government. It also made clear to the majority of Georgians, at a critical point in Georgia's independent history, the need for a new system of governance. Increasingly, what Georgian society and interested members of the international community realised by the early 2000s was that, despite millions of dollars of foreign investment, changes to laws, the creation of governmental bodies, agreements with neighbouring states, and the expertise of numerous foreign technical advisors from Europe, America, and Asia, the energy system had not improved enough to provide the basic foundation for development. Georgia was a country that could not be trusted, should not be invested in, and may not prove to be a stable transit corridor.

3.4 Conclusion

The lethal combination of economic malaise, a perpetual energy crisis, diversion of foreign assistance, and increasing reliance on Russian companies for energy supply not only left President Shevardnadze very unpopular with Georgian citizens, but also compromised the survival of the state. Beginning in 1999, the aforementioned anti-corruption faction, spurred by the Minister of Justice, Mikheil Saakashvili, began to denounce the 'energy bosses' publicly and call them in for questioning by the Anti-corruption Commission. Pressure from western donor organisations, a better functioning Parliament, and the gradual exposure of the Shevardnadze family's monopolisation of the energy sector in the media all led to greater public awareness about the high levels of abuse and neglect in the energy sector. Further, the international consortium that was investing billions in pipelines traversing Georgia now felt it urgent to ensure that Georgia would provide a stable and secure transit corridor. Saakashvili used the media to publicly address the nation and accuse energy bosses of specific illegal acts. The Minister of Fuel and Energy, Temur Giorgadze, was accused of diverting public funds. The Director General of *Sakenergo,* Emzar Chachikhiani, resigned (Sarke Information Agency 1999b). In 2000, a special commission of the General Prosecutor's office was established to look into violations in the energy sector since 1995. Thereafter, several more officials resigned, including the First Deputy Minister of Fuel and Energy, Malkhaz Kipshidze, and JSC *Sakenergo* Director General, Zurab Menabde (Sarke Information Agency 2000e).

Throughout all three periods of Shevardnadze's reign as President, through the years of war, recovery, and waning, Georgia was unable to develop a dependable energy sector. Ridding state institutions of individuals had little influence on the ability of the energy sector to function adequately. This indicated that there was a broader system of actors across multiple organisations that continued to collude in business arrangements to the detriment of securing reliable energy resources. This system operated aside from the state, but with the state's protection. In order to understand how a state could remain so persistently weak for a decade despite unprecedented levels of foreign assistance, it is important to re-examine the relevant political agencies within the state, the system in which they operate, and how the state serves their objectives. As Chapter 2 demonstrated, the typical approaches to state weakness do not allow for such a broad and encompassing reconceptualisation of the state. Thus, this thesis will next turn to creating a political network model of socio-economic relations for this purpose.

Chapter 4: Network Model for a Post-Soviet State

> Everyone knows well who backs whom, but everything is on the level of whispering and rumours. Nobody wants to say or write about it in public (Tengiz Makharadze, Prosecutor General of Tbilisi in Anjaparidze 2001).

4.1 Introduction

As discussed in Chapter 3, Georgia's early years of independence were mired in economic collapse, three wars, a dilapidated infrastructure, and the absence of a reliable supply of energy to the population. State institutions were established beginning in the mid-1990s, but by the end of the decade they were still not providing basic services, such as electricity. Further, Georgia's security was compromised by the absence of control over its territory, not just in the two separatist regions Abkhazia and South Ossetia, but also in one autonomous region Adjara. The Georgian government also exercised varying degrees of control outside of the metropolitan area. Thus, while an internationally recognised Georgia existed, it is clear that the state existed for something other than the normative functions attributed to a juridical sovereign state. That is, there was something in the post-Soviet state that thrived on state weakness. As Chapter 2 pointed out, neither the neo-institutional nor the ideational explanations of state weakness addresses the systematic and pervasive weakening of the state in the post-Soviet space. In fact, most of the literature on the weak state assumes: (a) an empirically sovereign state; (b) an enforceable rule of law that distinguishes between the formal and informal economies; and, (c) a clear division between those who manipulate the state for personal gain and those who are manipulated. However, post-Soviet Georgia displayed none of these conditions. Thus, it becomes necessary to re-examine the state to understand the particular dynamics at play in the post-Soviet period.

Building on the use of networks in the transition literature discussed in Chapter 1, this chapter will be dedicated to reconceptualising the post-Soviet state through the construction of a political network model of socio-economic relations. The development of the network model comes as a result of field research conducted in

Georgia from 2003 to 2005, during which time it became evident that beneath the veneer of the state was another ordering of actors, a second if not substitute economy, and an unwritten and yet understood set of rules that served the interests of those in power and sustained the livelihoods of those who were not. A variety of Soviet structural and ideational factors were transformed in the turmoil of early independence, replaced by new foreign actors and an influx of resources. Whereas before, the system functioned as a single isolated unit, the new states experienced a profusion of local and global, state and non-state, and public and private actors. Their combined actions created regimes, understood in this thesis as *trans-territorial* networks, which traversed the state in pursuit of resources and markets. The trans-territorial networks took the lead in conducting inter-state relations, including in Georgia's relations with its neighbours and international actors.

This chapter is divided into two sections. Constructing a political network model of socio-economic relations requires, first, an analysis of the Soviet structural and ideational factors that served to support the proliferation of networks (e.g. favours (*blat*), patrimonialism, and the informal economy) and their post-Soviet manifestations. With this background, the second section develops a network model of the post-Soviet state by identifying the actors (stakeholders) within the networks, the characteristics of these networks, and the dynamics of the network system. This will provide a framework, which will be used in subsequent chapters to analyse Georgia's energy sector in the Shevardnadze era and its implications for Georgia's inter-state relations.

4.2 Factors in Network Transition

Networks were a prominent feature of the Soviet Union, where they existed both hierarchically within Communist Party structures, as well as more horizontally among society. Networks were necessary for leveraging oneself into better social and economic conditions within Communist Party structures, as well as for compensating society for an increasingly unresponsive and overstretched state. Resource constraints and unrealistic production targets made it necessary for networks based on personal ties, patronage, and the unofficial exchange of services to compensate for the state. The official communist ideology was reduced to ritual observance; the notion of public interest, collectivism, and duty to one another and to the state were virtually meaningless by the 1970s. Informal institutions were responsible for carrying out the state's primary economic and social security functions (Lande 1977). Three factors accounted for the proliferation of networks. The first was *blat,* or the generation of socio-economic advantage through a process of establishing personal networks of exchange. The second was patrimonialism, serving as the principle managerial instrument within Soviet governmental structures to ensure the Communist Party's hold over the state. The third was the second economy, or the compensation of the command economy through informal exchanges of material items. These three legacies will be elaborated on in the following section.

4.2.1 Soviet Era Networks

During the Soviet period, socially constructed ladders of opportunity developed, thriving on the interaction of personal networks (Vorozheikina 1994: 110). These societal patterns of interchange were captured by the Russian term *blat*, which meant 'the use of networks as an exchange of favours at the public expense, serving the needs of personal consumption' (Kurkchiyan 2000; Ledeneva 1998). *Blat* was the reverse side of an overly controlling centre, a reaction of ordinary people to the structural constraints of the command economy. During the Soviet period, *blat* was a non-monetary exchange in which bartering took place based on personal relationships. These exchanges were not derived from personal material resources, however, but were made at the expense of state property, usually from someone formally entitled to this resource (Ledeneva 1998: 34-35). Exchanges could include arranging jobs, acquiring desired commodities, accessing better health services, and being permitted to take trips abroad.

Personal networks were composed of a set of nodes (e.g. kin, neighbours, friends and colleagues) connected through ties (e.g. intimate/non-intimate, routine/non-routine, active/non-active) (Ledeneva 1998: 104). *Blat* exchange was often mediated and covered by the rhetoric of friendship or acquaintance. It fostered individual initiative in forming social networks for the purpose of material advantage; something the official system forbade. In Georgian traditional society, personal relationships took precedence over formal structures. Society was divided into families, networks of friends, ethnic, or religious groups. They operated on the idea that one could not trust the state, but could rely on one's own group for support (Fairbanks Jr 1996). *Blat* was never recognised by the state as an attribute of the Soviet system and remained unmentioned in official discourse. However, its origins can, in fact, be traced to the post-Stalin Soviet system, which relied almost entirely on informal connections and informal practices, partly due to insecurity in power structures and economic scarcity (Ledeneva 1998). Thus, one of the consistent themes in the reliance on personal networks was the society's lack of trust in the state.

The mirror image of *blat* in the Communist Party was patrimonial networks, commanded by the Soviet *nomenklatura.*[1] Patrimonialism was a socio-political system of mutual exchange in an asymmetric relationship between a patron and client (Losaberidze and Kikabidze 2002: 4). According to Scott, the patrimonial relationship occurred when 'an individual of higher socioeconomic status (patron) used influence and resources to provide protection and benefits, or both, for a person of a lower status (client) who reciprocated by offering general support and assistance, including personal services, to the patron' (Scott 1977: 124). Willington defined patron-client relations as 'informal mechanisms that became individualised, reciprocal, political relations that often culminated in networks, which served to link individuals' interests and help them preserve or expand their positions' (Willerton 1992: 6). Therefore, patron-client networks were designed to act as guarantors of loyalty within the ranks of the Communist Party of the Soviet Union (CPSU) and instil discipline within the system of economic management and planning (Zurcher 2005).

Stalin made patrimonialism of the traditional Caucasian type a central organising institution of the Soviet system at the national level (Fairbanks Jr 1996: 373). After Stalin, the Soviet state continued to secure its power over the republics by

[1] For the purposes of this thesis, *nomenklatura* will refer to a small, elite subset of the general population of Party members in the Soviet Union who held various key administrative positions in the following: (1) Politburo of the Central Committee of the Communist Party (CPSU) responsible for foreign, defense, and economic policy; (2) Central Committee Secretariat headed by the General Secretary responsible for supervising all ministries, state committees and public organizations, drafting proposals for consideration of the Politburo, and recruiting personnel; (3) Komsomol acting as a youth recruitment mechanism for the Party; (4) Directors of state companies and the industrial complex; and, (5) senior leadership of KGB.

incorporating local patronage networks (Easter 1996). By the time Brezhnev became General Secretary of the CPSU, patron-client relations were a widespread phenomenon and had successfully undermined the formal institutions (Clark and Wildavsky 1990). Derluguian explained that the Brezhnev period rendered the state structures brittle as a result of the corrupt practices such as paternalistic patterns of governance (Derlugian 2005). Moreover, an entrenched and effective system of patron-client relations among the Soviet *nomenklatura* served as the management structure of the bureaucracy overseeing the Soviet industrial complex (Vorozheikina 1994:105). The state controlled Soviet redistributional economy provided ample leverage for the patronage networks to thrive (Zurcher 2005). Thus, throughout the Soviet Union, patronage networks infiltrated every level of governing structures in all republics, from the central to the regional organisations and had a debilitating effect on strengthening state institutions (Willerton 1992: 429).

Over time, patrimonial networks resembled webs, with multiple networks intersecting, such that people were simultaneously in positions of patron and client (Scott 1977: 127). In analysing Scott's work, Stefes notes that the networks extended both horizontally and vertically, connecting individuals of equal socio-economic status on a horizontal level. This complexity of ties, particularly among equals, provided a mutual support and protection system, fostering the coordination of activities among equals (Stefes 2005). His analysis moves beyond the traditional vertical structure of patrimonialism that follows a hierarchical pyramid structure (Feldbrugge 1984) to a complex reordering of socio-political relations within the Soviet state. It is this more complex understanding of patron-client networks that will be applied in this thesis.

The medium through which networks operated was the second economy, which acted as a self-protective response by ordinary people to the failures of the planned economy. The second economy functioned as a vast network of informal dealings. It was necessary to fulfil the obligations of the official economy in order to obtain benefits from the second economy, because the latter was inextricably connected to the former. That is, the informal economy was embedded in society and dependent on the structure and institutions of the formal economy (Feldbrugge 1984; Ledeneva 2000). The official economy became a competition for limited resources from the second economy between networks spanning almost the entirety of society (Kurkchiyan 2000: 85). 'In effect, the Soviet Union developed a significant redistribution mechanism with crude free market characteristics, operating in parallel with the official economy' (Kurkchiyan 2000: 86). Often to successfully engage in the legal sector of the Soviet economy, it was necessary to employ illegal mechanisms to obtain adequate resources for production and distribution. This included such practices as diverting state property, circumventing administrative authorities, private trading, private enterprise, and bribery (Feldbrugge 1984: 530). By the time the Soviet Union collapsed, the second economy was the dominant force in providing goods and services. Thus, it was artificial to differentiate between the formal and the informal and the licit from the illicit in the Soviet economy; they were one and the same system.

People in the Caucasus were particularly skilled at using networks to achieve material gain well beyond the regulated levels of social welfare set by the Communist Party (Grossman 1977). The degree to which networks were institutionalised, and the extent to which individuals were linked through trust-based honour commitments, was higher than in the other republics (Mars and Altman 1983: 559). Georgian kinship ties intensified the cooperative and effective nature of the second economy, providing an alternative source of income to the command economy for much of the population. Family determined the types of networks one was able to enter, the extent to which that network could facilitate the gaining of honour, and the subsequent ability to expand the network to 'peer group membership' or those who gained the trust of the family, referred to in Georgian as *samakhatsi* (Mars and Altman 1983: 549-550). Members of the networks were primarily responsive to the claims of reciprocity within the network relationships and decisions were taken on the basis of honouring commitments (Mars and Altman 1983: 555). In Georgia, a Communist Party First Secretary's appointee was referred to as *chemi katsia*, or, 'he is my man'. All positions ultimately belonged to the Party First Secretary through his appointments and owed their power and financial advantage to him. Eduard

Shevardnadze proved to be the master of balancing the network system in order to ensure maximum accumulation of compensation for his men.[2]

Thus, *blat,* patrimonialism, and the second economy were all inextricably linked, contributing to a system of networks that undermined the political and economic basis of the Soviet Union. The common feature shared by the three factors was their role in compensating for the deficiencies of the state and the resultant lack of regard for official political and economic institutions. Patron-client relations created a system of integrated authority structures in which state assets were distributed in return for loyalty. *Blat* allowed citizens to engage in a system of favours to compensate for a deficient state. Both *blat* and patrimonialism operated within the medium of the second economy, using assets in the formal economy to gain leverage in the second economy. Eventually, multiple networks were interwoven in a web-like fashion of favours and honour to one's extended family. These practices did not disappear with the dissolution of the Soviet Union and the end of the communist system, but were transformed both as a result of convention and necessity. Post-Soviet networks followed path-dependent patterns. Tracing the evolution of the networks after the dissolution of the Soviet Union will offer insights into the nature of the post-Soviet political and economic systems.

4.2.2 Post-Soviet Era Networks

The bond of trust, so important in the network system, was strengthened in post-Soviet society due to collapse of the communist system. In the absence of civil society or a multi-party system, the old ties were transferred to the new system virtually unbroken (Losaberidze and Kikabidze 2002: 16). The phenomenon of *blat* did not disappear completely, but initially lost its purpose, which was to serve the needs of personal consumption. Post-Soviet reforms establishing a market economy and privatising state property undermined *blat.* Private property changed the economy of favours, and socialist guarantees ceased to operate (Ledeneva 1998). However, where social change lagged substantially behind political modernisation,

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[2] Interview with Alex Rondeli, Director, Georgia Foundation for Strategic and International Studies (GFSIS), Tbilisi, Georgia, April 2005.

networks of dependency were the most resilient. In the midst of the political and economic turmoil that beset much of the post-Soviet space, old systems of social relations, such as the informal groups and networks that functioned for *blat* during the Soviet period, became crucial instruments in the exchange of favours. For example, people used networks to make contacts in search of employment and business opportunities, as well as bribes to secure favours from the state. In the Caucasus, the notion of exchange or favour in the war-torn states took on a more significant meaning of duty. As Suny explained, 'So powerful [were] the obligations to one's relatives and friends that the shame incurred by non-fulfilment [was], for most of Caucasians, much more serious than the penalties imposed by law' (Suny 1996: 381).

Patronage groups located in administrative and economic sectors of the newly independent states tried to preserve their position in the emerging pluralist arena of the post-Soviet state. The democrats in Russia and nationalist movements in the South Caucasus attempted to dislodge the former Soviet *nomenklatura,* but were dislodged themselves by the mid-1990s. Kirkow explained that there was a 'revitalisation of power exerted by former *nomenklatura* members and an activisation of previous social networks' (Kirkow 1995). Relations among the *nomenklatura*, particularly former members of the *Komsomol*, allowed individuals to obtain control over resources through informal networks, either as a result of their newly assigned political positions or former connections (Glinkina 2003: 1). Eventually, a new elite composed of the former *nomenklatura* networks and new economic actors secured control of state assets in both their public (official) and private capacities (Vorozheikina 1994: 113). Over the next decade, in the place of weakened or non-existent governmental structures, patron-client networks strengthened and once again became instruments of rule. Nonetheless, they were not as united as they had been during the Soviet period; patronage networks became fragmented by personal rivalries and political differences (Jones 2000).

Several terms have been developed to describe the post-Soviet patrimonial regimes. Aprasidze labelled the post-Soviet state a *bureaucratic-patrimonial* state, in which political power is informal and political rule is based on personal contacts and loyalty (Aprasidze 2004). Hale used the term *patronal presidentialism* to describe power structures based on widespread patron-client relations at the intersection of the state and the economy (Hale 2005: 10). Both terms describe a system in which the president directs resources and wealth outside of official channels in an effort not only to meet policy goals, but more importantly, to preserve power by rewarding allies and punishing disloyalty. Key elites in the state are reliant upon the leadership for wealth and resources, while the patron (President), in return, demands their political support. In a patronal system, business leaders are prone to use their resources to support the president for fear that he might use his powers to disrupt their businesses. Hence, patron-client relations manifest themselves in highly personalised politics, the monopolisation of key commodities, and the allegiance of the security services to individuals. In fact, strong and entrenched networks in the post-Soviet states have been so ubiquitous that their activities have impeded the institutional development required for the creation of democracies and, by extension, effective market economies (Losaberidze and Kikabidze 2002: 4). The extension of the patronage system from the pre- to the post-Soviet period has turned the state into a shell for personal interests, the most important commodity of which has been power through protection and the ability to impose the patron's will over the clients.[3]

As discussed in Chapter 3, when Eduard Shevardnadze returned to Georgia in 1992, he oversaw the creation of formal state institutions – a constitution, structures of state power, and laws governing these institutions. However, in the latter years of his presidency, 'he saw the rise of a neo-patrimonialist state, in which notions of public accountability, constitutional review and normative rules and standards of government played little role' (Broers 2005). Thus, it was the personification of power through Shevardnadze's personal networks and their vested interests that ruled the state and not the institutions (Jones 1996a). Shevardnadze's thirty years at the helm of Georgia through various Moscow and Tbilisi based positions meant that he had had a direct hand in creating generations of networks. He had always dealt with the evolving network system through an orchestrated game of balancing the various factions vying for privilege. The networks that he first encountered in Tbilisi in the 1970s when he was named Communist Party First Secretary of Georgia had been formed in the 1950s by mostly young men, graduates of universities and institutes, who were named to top levels of management of state-run enterprises. This was a relatively new elite given

[3] Interview with Alex Rondeli, GFSIS, Tbilisi, Georgia, June 2003.

the purges of the 1920s and 1930s, in which the former Georgian bourgeoisie were either killed or exiled. On his return to Tbilisi in 1992, he named many of these same 1970s *nomenklatura* to leadership positions within the newly established government.[4] There was also a new elite composed of the nationalists who had fought against the Soviet leadership in the 1980s (initially supportive of the first Georgian President Gamsakhurdia), the new democrats, professional criminals who had turned into paramilitary leaders during the war and subsequently into shadow businessmen, and those who had benefited from the privatisation schemes of the early 1990s.[5] His power rested in carefully balancing various interest groups, while ensuring that they all remained loyal to him.

Shevardnadze's patron-client networks permeated the whole of society, and they tended to follow one of two general patterns. The first was that of the classical patron-client relations defining elite politico-economic circles, controlling state offices in the pursuit of material gain. The second pattern was born of necessity and operated among society, which used the networks as a means to prevent extreme marginalisation. To say that this was a voluntary system would be misleading. Perhaps a member of society could opt not to participate in the networks, but this would be almost life threatening in Georgia, particularly during the period of state collapse and subsequent slow climb out of the destruction wrought first by wars, and then by economic collapse after the 1998 rouble crash. Furthermore, the inclusiveness of the patron-client system meant that many people were implicated, providing sufficient compromising material, or *kompromat,* to ensure the loyalty within the state machinery (Wheatley 2005a: 104). *Kompromat* had been a tool employed by the Communist Party during the Soviet period to discredit adversaries and, perhaps more importantly, to keep the ruling inner circle under the tight control of the leader. In the post-communist period, anti-corruption programmes, encouraged by the international community, became mechanisms through which to obtain

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[4] Interview with Nini Zureishvili, investigative journalist for '60 Minutes' new programme, Rustavi television station, London, UK, August 2004.

[5] The Zviadists were more or less excluded after Gamsakhurdia's ouster. However, the National Democratic Party led by Giorgi Chanturia and later, Irina Sarishvili, continued to play a role. Giorgi Chanturia, like Gamsakhurdia, was a nationalist ex-dissident but was Gamsakhurdia's rival.

kompromat on opposition (Wheatley 2005a).[6] Thus, the patron, Shevardnadze, ruled through a series of personal networks and economic incentives, enforced by the threat of revealing compromising material.

The second economy in the communist system was transformed into the post-communist shadow economy. In the economy of collapse that followed independence, 'the system was paralysed, the state became incapable of providing any regulations, and daily life degraded to such an extent that people began to question their own basic norms and values' (Kurkchiyan 2000: 89). Uncertainty extended from jobs and wages, to provision of goods, and to rules of conduct in the economy. The economic survival of each individual and his or her immediate family became the basis of the economy. As a result, the second economy took several new directions, serving first as a survival mechanism and then developing into a more formalised system by the mid-1990s. First, an 'informal' economy of traders and sellers appeared, operating clandestinely across newly designated state boundaries. Second, a 'hidden' or 'underground' economy of businessmen developed, evading state fees and regulations. Third, a 'parallel' or 'black' economy of unrecorded activity became the norm (Kurkchiyan 2000: 83-89). Nevertheless, while often outside the formal or state-regulated system, the 'other' economies operated through complex relations of collusion, complicity, and competition with this system (Duffield 2001: 145). It was in the shadows, between the official and unofficial economies, that the patron-client networks functioned according to unwritten, yet understood rules.

Even after economic recovery began in 1995, most of the efforts by the Georgian government and heads of the businesses (frequently the same persons) were focussed on immediate economic gain rather than on long-term business development, or the creation of a strong legal base to attract investment. The majority of those in charge of enterprises did not change their working methods from the Soviet period. These methods included distorting financial information, producing inferior products and selling leftover material, misappropriating public property for sale in the shadow economy, and bribe taking (Papava and Khaduri 1997). Most business transactions

[6] President Shevardnadze appointed the son of an old friend, Mirian Gogiashvili, as the head of the 2001 presidentially-mandated Anti-corruption Co-ordinating Council. He engaged in finding *kompromat* to discredit opponents of the President.

were dominated by a closed circle of friends and family with political connections, particularly outside the metropolitan area.[7] The combination of new business opportunities and a state that was unable to enforce regulations provided seemingly unchallenged opportunities for those with previous connections. In Georgia, this resulted in three types of business networks: import/smuggling, niche markets competitive on the international market (e.g. scrap metal), and regionally based networks for the creation of locally generated financing (United Nations Development Programme 2000). Many of the businesses relied on goods and labour rather than money, and the law provided minimal protection to informal contracts. Commercial banks were virtually nonexistent and rarely used or understood outside the metropolitan area, where there was unequal access to scarce resources (Humphrey 2002: 13). The result was that enterprises and individuals turned to barter, forming an unregulated and largely unreported economy. The state's administrative and regulatory control over the informal economy throughout the country was negligible (Kurkchiyan 2000: 94).

The robustness of the shadow economy was due to several circumstances that coalesced to challenge the strengthening of an official economy. The first factor was the practice of presidential appointed ministers selling public offices at the state and local levels, including the positions of politicians, policemen, judges, and tax and customs officials.[8] The buying and selling of public offices strengthened the networks because the seller was indebted to the system and was therefore expected to participate in shadow activities.[9] The second factor reinforcing the shadow economy was the lack of state resources. A combination of the meagre salaries paid to state officials and the small departmental budgets were compensated for through a well organised and functioning system of extracting payments from official and unofficial sources. The third factor was a set of complex tax codes and high tariffs, which

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[7] One indication of the extent of the second economy is to compare recorded income to consumption. By one estimate, from 1998 to 1999, wages and salaries accounted for one-third of total family income; two-thirds consisted mainly of 'concealed' income. In 1999, the level of consumption in monetary terms by the wealthiest 10 percent of the population was US$ 38 million; in the case of the poor this indicator was US$1.1 million. In 1998-1999, consumption of the wealthiest rose by US$4.5 million, while consumption of the poor fell by US$0.3 million. (Sulaberize 2004: 80).
[8] For example, centrally-appointed district administrators were known to have paid up to US$50,000 for their positions (Wheatley 2005: 105).
[9] Interview with John Wright, Political Advisor, European Centre for Minority Issues, Tbilisi, Georgia, April 2005.

forced entrepreneurs to seek a *krisha* (literally 'roof' in Russian) by a state official in return for not paying the official tax (Kharabadze and Bokeria 2004). The fourth factor was the influx of trans-national actors and funds from trans-national activity. At first, the source was mainly businessmen (most often politicians with business interests) or 'suitcase traders' (citizens bartering wares) taking advantage of non-transparent economies, porous borders, and the absence of enforced security.[10] With the introduction of foreign grants and investment, trans-national business arrangements increased exponentially. Further, networks of trans-border trade became multi-levelled systems of producers, traders, fixers, carriers, and suppliers linking previously isolated regions (Duffield 2001: 147-150). Finally, the shadow economy was increasingly infiltrated by criminal elements, driving the activity further into the shadows. The second part of this chapter will seek to develop a network model which captures such a post-Soviet state.

4.3 Network Model for a Post-Soviet State: The Georgian Case

The network model described in this section will consist of three parts: stakeholders, network characteristics, and dynamics of the network system. The functioning of Georgia's energy sector during the Shevardnadze period will be discussed to illustrate the model.

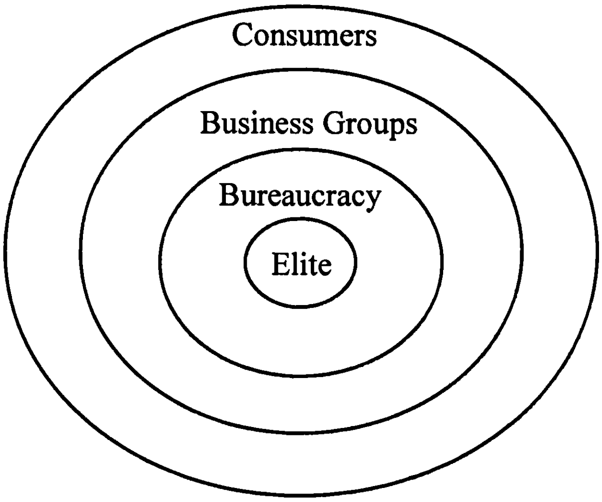
4.3.1 Stakeholders

Beginning at the macro-level of analysis, the networks in Georgia can most broadly be conceptualised as four concentric circles (see Figure 1 below). Each circle is bigger than the previous one, representing the increasing size of the groups. The four groups, going from smallest to largest are labelled *elite, bureaucracy, business groups,* and *consumers.* The four circles fit inside one another, symbolising the fact

[10] In the republics where there were armed conflicts (e.g. Armenia, Azerbaijan, Georgia, Moldova, Northern Caucasus, Tajikistan), armed forces, including militia, security services, paramilitaries, and 'partisans' turned their wartime provisions of supplies into a full-time business operation at the end of the conflict. Former enemies developed ties across so-called borders and established a profitable smuggling system, operating above the law and below the official system of taxes and customs duties. Post-conflict 'blockades' on trade, combined with the non-recognition of de facto borders separating recognized states from separatist regions, served to increase the profits by pushing the market underground.

that the stakeholders in each circle relate to, cooperate with, and can overlap in membership with the other circles, while also retaining their own identity within a circle. The four groups of stakeholders will be enumerated in turn below.

Figure 1 - Network Stakeholders



Elite

The smallest, most powerful, and most exclusive group is the *elite*. The *elite* is most appropriately understood as the fusion of high-level politics and business, comprised primarily of political actors at the top of governmental structures in the executive and legislative branches who use their posts to pursue business interests. It also includes a few select private entrepreneurs, most often related to, by blood or marriage, the head of the state and/or government. The *elite* is the most insular and non-transparent group in the networks and has the most to lose from the failure of an operation. Members of the *elite* have a stake in converting a lucrative commodity, or demand for a commodity, into profit. Access to, and protection by, the state is crucial for the success of business ventures. Thus, the *elite* most often acts as both the major investor and guarantor of a network's operation, providing the links to capital and protection from having to adhere to legal requirements. The other three groups of stakeholders are beholden to the *elite*.

President Shevardnadze used his position as the head of the state administration to manoeuvre, arrange, and deploy political support throughout the central and regional bodies of governance. He determined who would join the elite, forming a shadow apparatus of the most powerful persons, such as the head of State Security and the Interior Minister, to implement his policies (Chiaberashvili and Tevzadze 2005: 9). Directors of the main banks within the state – both private and public – participated in the *elite* networks. The *elite* included some elected Members of Parliament, who often owned lucrative businesses and could use their positions in parliament to obtain immunity from the law. Other members were 'temporary', joining the *elite* if they gained political advantage or when individuals became invaluable to the *elite* for operations that enhanced personal incomes. There were the new members of the *elite* who gained significant wealth in Russia in the 1990s and returned to Georgia to invest in certain sectors, in particular, the media. These included the owner of 'Imedi' television company, Badri Patarkatsishvili, who also had holdings in an oil terminal, and Bidzina Ivanishvili, owner of 'Channel 9'. They, together with local new Georgian businessmen formed the Taxpayers' Union, whose members increasingly gained prominence among the *elite*.[11] Finally, the *elite* included high-level political and business interlocutors in neighbouring states. For Georgia, this was most often *elite* from Russia, the Caucasus, Central Asia, and Turkey, but also from Europe and the United States.

In Georgia, the Shevardnadze family was at the nucleus of the *elite* (see Figure 2 below). Aside from the President, family members included the President's daughter's father-in-law, Guram Akhvlediani (whose daughter Nino was married to Shevardnadze's son Paata), his nephews Nugzar and Ceasar Shevardnadze (sons of his deceased brother), and Gia Jokhtaberidze, married to his daughter Manana Shevardnadze (Targamadze 2000). During Shevardnadze's presidency, Guram Akhvlediani was the *de facto* head of Poti Port on the Black Sea, managing the petrol import business from Europe, as well as overseeing numerous small oil refineries within Georgia. He served as the Chairman of the Georgian Chamber of Commerce and Industry for much of the Shevardnadze era and represented Russia's LUKoil.

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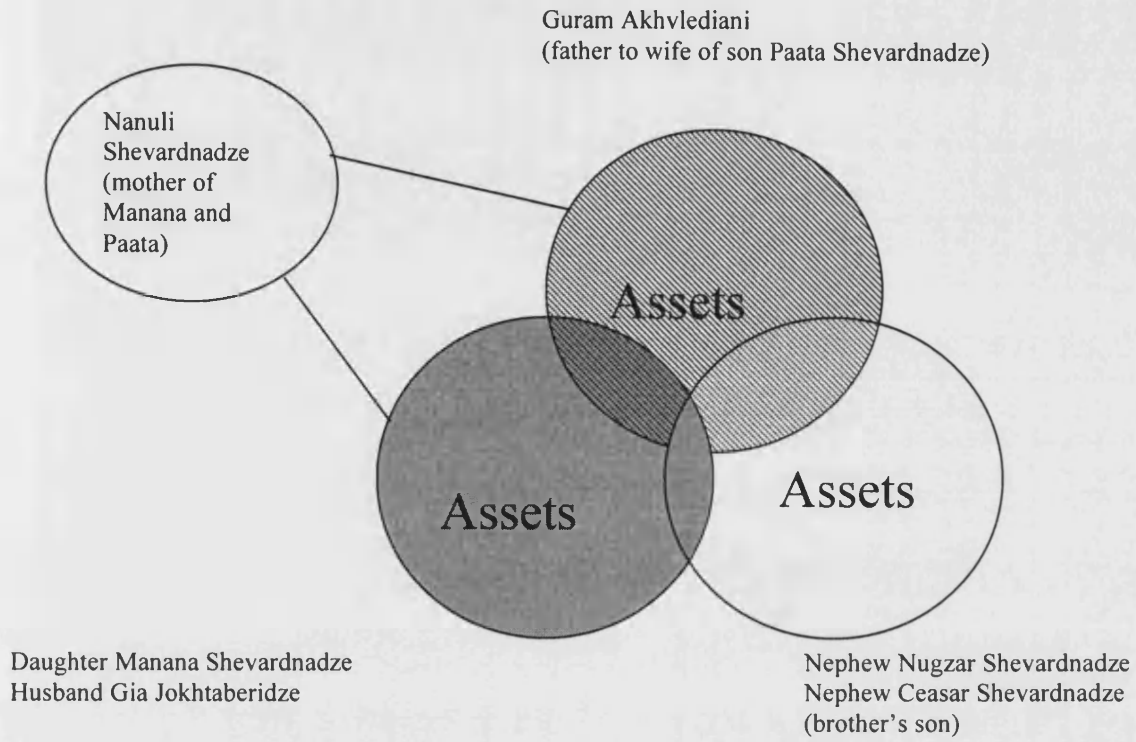
[11] Members included such figures as Davit Gamkrelidze, founder of *Aldagi* insurance company and leader of the New Rights Party in Parliament, and former State Minister, Niko Lekishvili, the head of the Taxpayers' Union (Wheatley 2005a).

Nugzar Shevardnadze, and to a lesser extent his brother Ceasar, were viewed until the late 1990s as the primary figures in the petrol business, working mostly with Russia and Azerbaijan to import and distribute products for sale. Nugzar also held majority assets in two energy companies - *Iveria* and *Neogeneratisa.* Nugzar's elite associates included the close friend of Paata Shevardnadze, Kakha Targamadze – the Minister of Internal Affairs from 1995-2001.[12] Gia Jokhtaberidze oversaw operations at Supsa Terminal on the Black Sea coast (the end-point of an oil pipeline from Baku), as well as the *Magti Group* (i.e. telecommunications, electro energy stations, and chemicals operations), which gave him a stake in the Rustavi nitrogen and Zestafoni non-ferrous metallurgy plants. The Shevardnadze family had particularly close relations with the Chairman of the Railway Department, Akaki Ckhaidze, and the Chairman of the Road Fund, Boris Salaridze (Chiaberashvili and Tevzadze 2005: 5).

All members of the Shevardnadze family had links to numerous other businesses, from airports to tobacco, spirits, and publishing. By the late 1990s, allegations of illegal business practices pursued by Nugzar Shevardnadze were beginning to undermine the President's position as a champion of anti-corruption efforts. Interpol had begun to question Nugzar's activities and increasingly the press covered the illegal activities of the Shevardnadze family. Furthermore, family members found themselves in competition with one another in the energy market and, towards the end of Shevardnadze's reign, this competition led to poor relations between Guram Akhvlediani and Nugzar Shevardnadze. They aired their differences in the public arena, in particular the media, each accusing the other of corruption, which ultimately exposed the family business arrangements to the public and broke the silence on their activities in the energy sector.

[12] Kakha Targamadze worked for Eduard Shevardnadze in the Ministry of the Interior in Tbilisi during the Soviet period.

Figure 2 - Shevardnadze Family Network



There were three avenues to *elite* appointments made by President Shevardnadze: family, *nomenklatura*, and his political party Citizen's Union of Georgia (CUG). Shevardnazde not only kept energy assets in the hands of his family and trusted members of the *nomenklatura*, but he also followed the practice of appointing several members of one family to *elite* positions. For example, Merab Adeishvili's brother, the Minister of Transport, Connections and Communications, Gia Adeishvili, became the Deputy Minister of Fuel and Energy. The brother (Shalva Chkhartishvili) of the former Minister of Economics, Manufacturing and Trade, Ivane Chkhartishvili, became the Deputy Head of Inspection for Large Tax Payers (literal translation). The second avenue was through former Soviet era *nomenklatura*. For example, by 1994, Georgia's banking sector was dominated by a group of men who had been members of a 1980s *Komsomol* cell at the economics faculty of Tbilisi State University. Shevardnadze appointed five members of this cell to head five state banks, which controlled 80 percent of national bank holdings (Tugushi and Chapidze 2001 in

Chiaberashvili and Tevzadze 2005).[13] The third avenue to *elite* appointments was the President's party CUG – which represented a post-Soviet continuum of the CPSU in Georgia. The CUG offered a path for interested persons to pledge their loyalty to the President through membership, which could potentially result in an appointment in the administration (Chiaberashvili and Tevzadze 2005: 12). Many of its leadership positions were given to younger leaders, such as Zurab Zhvania, whose job it was to build contacts and strike deals with western governments and potential investors.

By 1995, Shevardnadze had consolidated enough power to be in charge of the state and he became deft at forming coalitions when he needed them, using conflicts between his rivals, and only striking against his enemies when absolutely necessary (Nodia 2002). As previously discussed, his style of management was to balance forces, making sure that no one group became too powerful (Targamadze 2000). However, by the late 1990s, there were five increasingly competitive centres of power in Georgia composed of members of the *elite.* These were Shevardnadze and the State Chancellery, the Ministry of Internal Affairs under Kakha Targamadze, Abashidze and his government in Adjara, the 'reformers' mostly serving in the Georgian parliament (younger members of the CUG), backed up by the support of non-governmental organisations, and a group of businessmen from the Taxpayer's Union (Wheatley 2005a: 110). In addition to the reasons mentioned previously in Chapter 3, Shevardnadze's loss of control over all of these groups contributed to his demise in the November 2003 Rose Revolution.

Members of the *elite* were the most effective interlocutors with foreign governments and businesses. By the mid-1990s, the Soviet *nomenklatura* had regained control of the political and economic sectors across the former Soviet Union. As a result, they were able to re-unite and cooperate across borders. In the Caucasus, ties were reformed among the former colleagues from the CPSU, particularly between

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[13] Shevardnadze appointed the heads of the five state banks in 1994, including his second cousin, Zaza Sioridze, to head Eximbank, Ivane Chkartishvili to head 'Savings Bank', his sister's son, Vladimir Pateishvili, at 'Bank of Georgia', Andro Devdariani at 'Agro Industrial Bank, and Tamaz Maglakelidze, who had previously worked for the President of the National Bank to head 'Industry Bank'. These five banks held 80 percent of the national bank holdings. Later, three banks combined to form the United Bank of Georgia, holding 60 percent of the assets and Mamuka Kharradze headed the most powerful bank 'TBC' and 'Bojormi' Mineral Water Company (Chiaberashvili and Tevzadze 2005: 5).

Presidents Shevardnadze and Heydar Aliyev of Azerbaijan. In Georgia's energy sector, ties with the Soviet *nomenklatura* of Russia, Kazakhstan, and Turkmenistan were also valuable. The heads of the autonomous and separatist areas of Georgia – Ardzhimba of Abkhazia, Kokoity of South Ossetia, and Abashidze in Adjara – also cooperated with one another and with other former Soviet era colleagues. Moreover, as with the Shevardnadze's family assets, the heads of the autonomous and separatist areas allowed their relatives to gain considerable power and wealth, either through public or private avenues.[14]

Bureaucracy

The second group of stakeholders is the *bureaucracy* composed of appointed and elected officials serving in central and regional state offices. The higher echelons of the *bureaucracy* are, to a great extent, composed of people who were part of the Soviet *nomenklatura.* In the networks, their function is to be at the disposal of the *elite* and to guarantee that the business interests of the *elite* are secure and profitable. Part of this involves ensuring that the clients within the patronage networks are loyal to the patron. There is no distinction at this level between party politics and business interests. As members of the *elite* networks, the *bureaucracy* is assured some portion of the profits from their participation. Further, as certain members of the *bureaucracy* gain in stature, particularly in the regions outside of the metropolitan area, they establish their own business operations, with the protection of the *elite.* Members of the *bureaucracy* range from those who regularly interact with the *elite*, such as the political appointees overseeing governmental agencies, to lower level bureaucrats who are expected to participate in networks. The stakeholders who most often engage with the *elite* are heads of the power ministries (e.g. Ministry of the Interior, Ministry of State Security, National Guard, and the Ministry of Defence), the heads of state energy companies, the heads of transportation agencies, and the heads of state regulatory bodies and property management.

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[14] The Abashidze elite grouping comprised practically his entire family. His son was the mayor of Batumi; his nephew, Giorgi Tsintskaladze, was Chairman of the Council of Ministers; his cousin, Antaz Mikava, was the second Deputy Chairman of the Council of Ministers; his brother-in-law, Ilia Tsulukidze, was Minister of Security; his son-in-law, Temur Komakhidze, was Minister of Culture; another son-in-law, Nodar Tamazishvili, was Minister of Communications; another cousin, Guram Gogitidze, was Head of Tax Service; and, half of the members of the local parliaments (40 persons) were his close relatives (Chiaberashvili and Tevzadze, 2005).

In Georgia, the destruction and degradation of the energy sector wrought by the war years and economic decline meant that most of the major assets remained in state hands, unattractive to potential local and foreign investors. Thus, a group of former 'Red Directors' (CPSU members and heads of the Soviet state-owned firms) and the managers of the State Trade Organisations (STO) maintained their hold over the energy sector either through posts in the *bureaucracy* or through the creation of companies, often registered in the name of a member of their own families or a business associate. The state companies included: *Saknaftobi Saknavtobproductebi* (Georgian Oil Products), *Sakgaz* (Georgian Gas), *Saknakhshiri* (Georgian Coal), and *Sakenergo* (Georgian Energy). There were also state joint-stock companies overseeing the management of the pipelines: *Saknaftobi* (Georgian Oil) State Joint-Stock Company, Georgian Gas International Corporation (GIC) State Joint-Stock Company, and Georgian International Oil Corporation (GIOC). The state electricity sector was managed by *Sakenergo-Generatsia* (Georgian Generation), *Sakenergo-Gadatsema* (Georgian Transmission), and *Sakenergo 2000* (Georgia Energy). Some of these agencies will feature in the case studies in Chapter 5.

In order to facilitate energy distribution at the regional level, as well as to manage critical transport corridors across Georgia, a selection of stakeholders in the *bureaucracy,* allegiant to the *elite,* operated as regional networks. Article 2 of the 1995 Constitution stated that the internal territorial arrangement of Georgia was to be left undetermined until the state regained jurisdiction over the whole of the country. Thus, the internal territorial arrangement was left ambiguous until Georgia regained Abkhazia and South Ossetia. President Shevardnadze used this article to establish a system, under the directorship of the Service of Regional Management of the Office of the President, that ensured that his men gained leadership positions within several layers of regional administrations (Chiaberashvili and Tevzadze 2005: 8). Power arrangements in the regions were confusing by design, which contributed to the competition among networks, preventing any single network from gaining too much authority.

There were three levels of regional politicians, two of which were appointed by the president. Those appointed included the 12 macro-regional leaders of the *mkhare* called *gubernatori* (governors)[15] and the micro-regional leaders of the *raioni* and cities called *gambgebeli.* The micro-regional level also had an elected council called the *sakrebulo* (see Figure 3 below). Shevardnadze appointed the *gambgebeli* (mayors) of Tbilisi and Poti, and Kutaisi and Rustavi until the law was changed in 2001. After that, a pseudo-democratic system was established that assured that his men would still win. Regional governors ran for Council of a village or *sakrabulo.* When they won, their names were submitted by the Council of representatives of the *sakrabulo* to a regional council. Then, the regional council approved the head of the regional executive authority, or *gambgebeli.* Between the *gubanatori* and *gambgebeli,* there was no strict division of power and no clear designation of one single posting with the executive authority, which resulted in the two positions holding equal levels of power and legitimacy (National Association of Local Authorities of Georgia 2006). Officially, the *gubanatori* had authority to distribute resources, less autonomy over trade and business, and no authority regarding security.[16] However, as the case studies will show in Chapter 6, the positions of *gubanatori* and *gambgebeli* had the potential to create shadow systems beyond the control of any other branch (Chiaberashvili and Tevzadze 2005: 8).

[15] Only 9 were in fact appointed, as South Ossetia, Abkhazia, and Ajaria remained *de facto* separate entities.
[16] Interview with Iraqli Botcheridze, Service of Regional Management, Office of the President, Tbilisi, Georgia, July 2003.

Figure 3 - Regional Governing Structures in Georgia[17]

Tbilisi -----------Central Government --------------------- Autonomous Republics

| |

Macro-regions (*mkhare*, administered by governors, *gubernatori*) (Abkhazia, South Ossetia, Adjara)

|

Regions (*raioni and cities*)

| |

Executive (*gambgebeli*, appointed by President) (in cities = mayor) Elected council (*sakrebulo*)

|

City Districts

|

Communities (*temi*)

|

Small Settlement (*daba*)

|

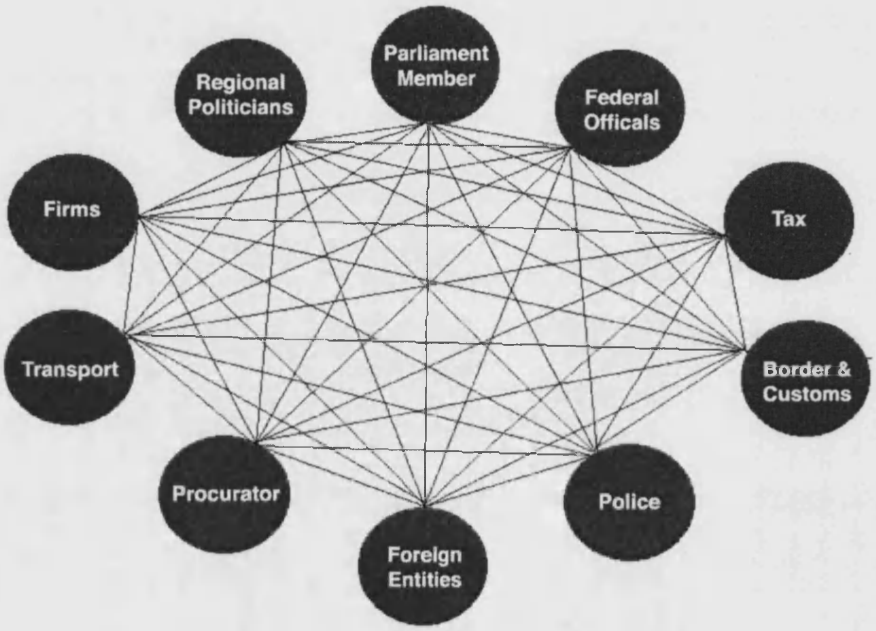
Village (*sopeli*)

Shevardnadze also consolidated power and established *de jure* control over the regions by giving regional figures access to governing structures that could be converted into profit from the shadow economy (Metreveli 2004b). The regional authorities were then able to strengthen their informal networks through the monopolisation of local businesses. This inclined stakeholders to protect their business interests by superseding, or simply not enforcing, the law. Regional leaders created networks with members of the state bodies in local jurisdictions. These included local representatives from the Tax Administration, Prosecutor's Office, Traffic Police, Border Guard, and Customs Department (see Figure 4 below). Working together, these stakeholders formed powerful networks generating revenue

[17] This figure was taken from a Civitas report, shown to me by Giorgi Meskhidze, Tbilisi, April 2005.

from inter-state business, particularly in regions of Georgia which bordered other states, or those regions situated along lucrative transit corridors. This eventually called into question the ability of the government to act as the sole source of power in inter-state negotiations. Chapter 6, which looks at regional case studies involving inter-state relations between autonomous or separatist regions of Georgia and regions in neighbouring states, offers a more detailed examination of the problem.

Figure 4 - Regional Trans-territorial Network Stakeholders



Business groups

The third group of stakeholders are non-state actors who operate as private entrepreneurs and form *business groups.* These stakeholders usually work in concert with the *bureaucracy* and require sponsorship by the *elite. Business groups* tend to be members from one of the following entities: paramilitaries, peacekeeping forces, criminal groups, organised crime, and partisans. They are not part of the legitimate business community, but rather use their recognised or unrecognised positions in the states and the separatist regions to transit across porous borders in the pursuit of profitable opportunities, or to launder money gained from illegal activity. *Business groups* often operate where the state is inefficient, such as in providing a commodity, service, or market. They can also operate with supposed enemies across borders, forming transit corridors that are secured by both state and separatist armed forces working in tandem.

It is becoming increasingly difficult to distinguish between *business groups* and organised crime, or between members of *business groups* and other stakeholders, in particular the *bureaucracy*. This is due, in part, to the fact that organised crime is often rooted in family and kinship and relies on patron-client networks, which is also the foundational organising principle of weak states (Williams 2004). For example, it is alleged that organised crime has infiltrated the governments of the post-Soviet states, acting as an intermediary to enable illegal operations through extortion of the *bureaucracy*. According to the former Russian Prosecutor General Ustinov, 80 percent of criminal organisations in the CIS gain protection through connections with law enforcement agencies (Library of Congress 2002). Organised crime is also able to influence politics depending on the extent of their ties with the *elite,* including the selection of Members of Parliament and local leaders, campaign financing, and drafting legislation (Shelley 1999). According to a leading British academic on organised crime, distinctions between organised crime, professional criminals with well established links to government officials, corrupt officials engaging in private enterprise, and business people prepared to bend or break the law are not always clear.[18] This creates interesting opportunities, because it challenges existing definitions, which attempt to create boundaries between a variety of illicit stakeholders.

Makarenko distinguishes between three groups implicated in trans-national crime in the South Caucasus (Makarenko 2003). First of all, there are the small, localised gangs or trans-national actors operating in networks. These are low-level players who primarily target businesses or individuals through robbery, racketeering, or kidnapping. Often these types of crimes are isolated to a specific territory. Second are the organised crime networks, which are extremely developed criminal groups who engage in smuggling narcotics, weapons, and humans. They are usually based at

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[18] Interview with Mark Galeotti, Director Organized Russian & Eurasian Crime Research Unit Keel University, UK, Spring 2005.

ports or in territories beyond the control of state security services, such as the separatist regions. Criminal organisations that are controlled by individuals in senior positions in the government, military, security services, or law enforcement also fit into this group. And yet a third group are militants, who engage in trans-national crime in the region. These include indigenous groups who form paramilitaries and engage in illegal activity, such as Georgia's *White Legion* and *Forest Brothers.* External groups, such as Chechen insurgents, also operate in the South Caucasus. In Georgia, organised crime groups have tended to be disorganised, lack an operational ideology or central command authority, and have operated locally rather than globally (Galeotti 2001). Further, there are conflicting reports as to the level of criminality, extent of their penetration of state offices, and the impact that they have had on the state.

On the one hand, it is reported that by the mid-1990s, much of Georgia's major criminal elite had moved to Europe, establishing networks across the continent, engaging in more lucrative sectors (Kupatadze 2006) or that they had been jailed by Shevardnadze, such as the head of the paramilitary group *Mkhedrioni*, Jaba Ioseliani. On the other hand, one expert alleged that there was a high level of collusion between Georgian criminal leaders and some members of the Georgian *elite* in the Shevardnadze era, including members of the *thieves-in-law.*[19] Those that remained, such as Shakro Kalashov, Dato Tashkenteli, Taril Oniani, Gia Kvaratskhelia, and Babua Khasan, gained the respect of many in the government and had access to President Shevardnadze.[20] Members of Parliament are known to have interceded with law enforcement on behalf of leading criminals who had been arrested (Williams 2004). In particular, those operations which required the cooperation of law enforcement, customs agents, and border security were alleged to involve connections to *thieves-in-law* for the purposes of protection. A 2004 study estimated that 30 percent of revenues in Georgia's banking system, 40 percent of income from hotels and restaurants, 60 percent of the gambling business, 15 percent of the energy sector, and 40 percent in the construction industry was in the hands of criminal groups,

[19] *Vory-v-zakone* or *thieves-in-law* refers to a Soviet phenomenon begun in the gulags of the 1920s, in which gangs followed a strict and secret 'honour' code and served as arbiters between rival groups. Eventually, the *vory-v-zakone* garnered more respect and authority than the police. In Georgia, they maintained a prominent position in enforcing unwritten laws within society.

[20] Interview conducted off-the-record with Georgian government official, February 2007.

although these groups were not specifically identified (Mamiashvili 2006). Given all of these variables, in the case studies in Chapters 5 and 6, every effort will be made to specifically identify the *business groups* participating in networks.

Consumers

The fourth group of stakeholders within the networks are the *consumers*. This is by far the largest group (roughly estimated to be 70 percent of the population) and includes the most disenfranchised members of society due to their un- or under-employment, and lack of access to state goods and services. Their income is supported by the informal economy, remittances from family members working outside of the state, and international assistance. The term *consumers* should be understood to encompass passive recipients as well as active merchants and traders. Members of this group also vary in their socio-economic status, according to age, access to members of the other three groups, and region in which they live (urban versus rural). *Consumers* are most likely to participate in the largest of networks as the end-run consumer of a product or service supplied by the *bureaucracy* and *business groups,* under the cover of the *elite. Consumer* participation in networks is particularly active in rural or isolated areas, where civil society is least developed, minority groups are inadequately represented in the political system, and the provision of state services, such as gas and electricity, is the most derelict. Other areas where *consumers* are particularly active include regions encompassing large markets contiguous to two or more states, or along the trading corridors adjacent to the separatist regions.

In Georgia, these areas have tended to be outside of the former industrial centres, such as Tbilisi, Rustavi, and Kutaisi. *Consumer* networks have been the most highly concentrated and effective in the minority populated areas of Maneurli (Azerbaijanis) and Javakheti (Armenians). These regions border ethnic kin and/or trading partners in neighbouring states — Azerbaijan and Armenia. *Consumers* in these regions participate in networks for various reasons, some as a result of coercive measures and some due to necessity for survival. Georgian sociologists explained that *Consumer* participation in patron-client networks occurs most often in the regions where,

> there is a persistent and self-reproducing, strictly hierarchicalized [sic] vertical of power to which the population easily submits and which, taking advantage of the people's passivity[...] reproduces itself quite successfully. Very often we can observe examples of what is essentially a kind of medieval clientelism, especially when it comes to any attempt to distribute skimpy entrepreneurial resources, and moreover relations that are essentially feudal in nature between the patrons in the structures of ruling authority and their clients (Zurabishvili and Zurabishvili 2004: 96).

Consumers also create their own networks for survival in the absence of the state. These networks are mostly composed of informal groups organised along ethnic, regional, and family ties, through which members promote their mutual financial interests based on a contract of trust. Stuvoy labelled this phenomenon an 'insurgent social order', or an alternative arrangement born out of society in its quest to secure economic benefits given the extralegal status of citizens residing in an extremely weak state (Stuvoy 2002). 'Extralegal' referred to the disenfranchisement of citizens from the official economy and the subsequent poverty that leads people to create an alternative system for survival (de Soto 1989). This was particularly true in Georgia, where societal disorientation after the collapse of the state pushed individuals to search for security in family and friendship networks based on ethnic and confessional identities. A large proportion of the population relied so substantively on informal activities as a source of supplementary income that by 2000 the combined monetary and non-monetary income of the average Georgian surpassed minimal subsistence levels (United Nations Development Programme 2000). Georgians thus achieved a remarkable ability to detach from the formal structures of governance in their pursuit of income and access to social services.

Nevertheless, the gains made by *consumers* from participating in the trans-territorial networks are only temporary. They gain an immediate supply of energy, avoidance of paying higher tariffs for electricity, short-term employment opportunities in smuggling networks, and are part of a larger system of patrimonial networks that offered other opportunities, such as protection, in exchange for their allegiance. Williams called the progress *consumers* are able to make by participating in the informal market a 'safety valve and safety net' (Williams 2004). However, as the marginalised majority, *consumers* perhaps lose the most in the long-term. As no substantial investments are made in the infrastructure of the state, no solutions are sought for the long-term development of the economy, and no sustainable employment opportunities become available, their gains are only temporary and highly unpredictable. Finally, the criminalisation of *consumers'* participation in networks dominated by *business groups* is detrimental to the longer-term socialisation of citizens and their respect for state governing structures.

4.3.2 Network Characteristics

The networks are *semi-permanent,* set up for one operation or a fixed period of time and then disbanded. This makes them *unique,* their configurations and rules dependent on the mission. Every network's operation is *sponsored,* usually by someone in the *elite.* The practice of a patron selecting clients, or the patron's agreement to provide a *krisha* for a group of stakeholders in a network, results in highly *personalised* structures. The networks are also *non-transparent,* governed by a set of unwritten and yet binding rules. The stakeholders in the networks are *multi-sectoral,* covering a variety of state and non-state offices, as well as crossing physical (state) and financial boundaries. Finally, the networks operate according to a certain *logic* — for profit accumulation or welfare maximalisation. Each of these network characteristics will be expanded below.

First, the networks are *semi-permanent*, set up for one operation or a fixed period of time and then often disbanded. The reasons for disbanding a network include completion of a mission, competition, disruption in supply, change in support from a patron, or external pressure from an international organisation or foreign government. A network's power is most forcefully checked by another rival group, and those networks that have a greater degree of cohesion, in terms of shared goals among the participants, tend to thrive.

Second, each network is *unique,* made up of different actors and ordering principles, depending on the mission and the environment in which it operates (Wedel 2003: 430-32). For example, *business groups* smuggling across territories of varied control require the support of persons working in several official and unofficial capacities. Their networks, therefore, tend to be more fluid constructs, with a lesser degree of cohesion. *Elite* networks, on the other hand, rely on a small group of centrally located persons, regulated by a strict code of conduct to ensure loyalty among stakeholders for the protection of their financial interests.

Third, the networks are *sponsored.* Most networks require the protection of someone from the *elite* or *bureaucracy* in order to operate within Georgia and beyond. This sponsorship takes on a supervisory role; that is, a central 'clique', including the sponsors, most often takes the main decisions within a network. Therefore, the primary unit of analysis in a network is likely to be a group of people rather than an individual, and decision making is likely to be made by committee (Wedel 2003: 431). Relationships between the clique and other stakeholders often involve domination, the result of a scarcity of alternative resources (Knoke 1990: 13-14). The domination can also be the result of the indebtedness of the resource-poor client to the patron due to the inability to fully reciprocate favours resulting in unequal power distributions over time (Blau 1964: 113-8).

Fourth, the networks are *personalised.* Exchange is of a personal and informal nature (based on social contacts) and knowledge and initiative are decentralised and widely distributed (Ansell 2000: 311). Preference for positions in networks is given to members of those 'in trust' over better-qualified outsiders. Membership is often exclusive to a particular network. For example, membership in a *consumer* network, particularly those operating in rural areas, tends to be founded on familial and social ties, sometimes ethnic or kinship based. *Business groups,* on the other hand, tend to create networks from less familiar contacts across borders.

Fifth, the networks are *non-transparent*. Depending on the size of the network, some of the participants may not be known to one another. This does not compromise the mission of the network, as it is most often governed by a set of unwritten rules, one of which is a code of secrecy. Patron-client relations also tend to ensure loyalty of the stakeholders to protect the mission as 'payment' for membership (Knoke 1990: 13). Ultimately, participation in networks restricts the stakeholder's activities; membership is part of a social contract based on commitments to the group (Ledeneva 2004). The principle of reciprocity not only serves to enhance ties among stakeholders, but also isolates potential opponents.

Sixth, the networks are *multi-sectoral*. Networks crisscross organisations and boundaries in search of wealth, or as compensation for the absence of functioning state services (Ansell 2000). Effective networks require assistance from multiple sectors of the state, including political, economic, judicial, and security (Wedel 2003: 430-32). One actor can participate in several different networks simultaneously, resulting in the interconnectedness of networks. For example, *elite* stakeholders tend to invest in multiple networks.

Seventh, networks operate according to a certain *logic*. Their purpose is to gain access to resources in order to increase levels of consumption, either for the accumulation of personal wealth or, at the opposite end of the economic spectrum, to compensate for the absence of the state (Ansell 2000: 311). Networks pool risk among members and protect their businesses against threats and abuses of law enforcement bodies, as well as to gain influence and power within governmental structures in order to enhance their share of the market captured by their network. Thus, networks both take advantage of, and compensate for, the absence of the state. As they gain power, they also gain credibility among the population and grow to eventually usurp state functions.

4.3.3 Network System Dynamics

The relationships within the networks neither resemble a hierarchical nor a horizontal pattern, but are more likely to form web-like *heterarchical* structures. Networks traverse both defined and undefined territorial and financial zones, and are referred to as *trans-territorial.* The system is neither directly sponsored as an official state function, nor is it part of an unofficial or shadow economy, but instead comprises the *grey market*. Finally, all actions are *conditioned* by current socio-political and economic factors. The networks eventually create an *alternate force*, which challenges governmental institutions as the primary inter-state actor.

First, due to the multi-sectoral character of the networks, the network system neither functions hierarchically, in a strict patron-client configuration, nor horizontally, but is instead *heterarchical* (Ansell 2000, applying Hedlund 1994). That is, the networks tend to operate in a web-like formation with a sponsor somewhere towards the middle of the web and various nodes connected to stakeholders fanning out in multiple directions as demonstrated above in Figure 4. However, there remain relationships of inequality within this web, where some members are more in command and others more dependent on patrons for goods and services. This notion of a *heterarchical* structure is also useful when examining extended spheres of networks, which include multi-national stakeholders. The stakeholders in heterarchical webs can be global and/or local in terms of their relation to the state.

Second, while the network system is not bound by the state, it does not operate freely within a de-territorialised world. It is best to conceptualise the space in which the operations of networks take place as a *trans-territorial* sphere. Given the economic and energy deficiencies of a weak state, activities are rarely only intra-state. Neither are activities simply inter-state, as the networks take advantage of the porous borders and un-enforced legal regimes. The notion of a *trans-territorial* sphere also applies to the financial aspects of operations, both in terms of the flows of funds and the registration of a company in a protected economic zone, or in the name of a non-transparent third party, such as a family member or business associate.

Third, the system operates neither strictly in the official market nor in the shadow economy, but instead comprises the *grey market*. In a weak state, arrangements are realised on an informal level based on the control of the *grey market*, defined as that between officially sanctioned transactions and unofficial transactions. Using terms such as 'shadow' or 'black' to convey this sector of economic transaction runs counter to the reality that these activities are co-terminus with the official economy and transparent to all (Ledeneva 2000). In fact, the *grey market* is the nexus of interaction between the bureaucracy and the market, public and private, legal and illegal, and central and peripheral activity (Wedel 2003: 432). In other words, the *grey market* is embedded in society and dependent on the formal structure and institutions of the bureaucracy to operate much like the second economy was in the Soviet era. Hence, the *grey market*, while not directed by the government, has the consent of the state.

Fourth, the network system is *conditional.* The response to an action is often dependent on what came before. This is the result of the fact that a network's influence and control over resources is contingent upon the environment in which it operates, and it therefore has to remain flexible in determining a future direction (Wedel 2003: 430-32). While activities can appear to be chaotic, this notion does not capture a system which, while not functioning on organisational management principles, nevertheless does produce results according to some understood plan known to the clique and participants alike.

Fifth, it is necessary to reconceptualise the state, not as a functioning, transitioning, altruistic block of parts moving towards the goal of serving society, but as a shell occupied by individuals who use the system for wealth, both for themselves and their fellow stakeholders in networks. The state lacks legitimacy precisely because there is no will among the stakeholders to create normative state structures as understood by political scientists. Determination among a compilation of state and non-state actors to collude in networks undermines the strengthening of the state. This eventually creates an *alternate force,* which replaces the state as a primary actor in inter-state relations.

Table 3 - Summary of Network Model

Stakeholders	**Network Characteristics**	**Network System Dynamics**
Elite	Semi-permanent	Heterarchical
Bureaucracy	Unique	Trans-territorial
Business groups	Sponsored	Grey market
Consumers	Personalised	Conditional
	Non-transparent	Alternate Force
	Multi-sectoral	
	Logical	

4.4 Conclusion

A summary of the stakeholders, network characteristics, and the network system dynamics is depicted in Table 3 above. Georgians viewed the internationally recognised 'state' as a medium through which to pursue operations that would gain them economic advantage in a resource starved market. Incentives for their participation in the networks varied, ranging from substantial profit to survival. The general lack of will among state and societal actors to construct a legitimate state provided an opening for a host of actors to participate in the networks. These networks, in turn, became more important for economic transactions within and across the state than the institutions to which the members of the networks belonged. While their participation in networks was born out of necessity, their activities, nevertheless, contributed to the perpetuation of state weakness.

The use of networks in compensating for a weak state had its origins in the Soviet Union. The politico-economic transition from the command economy was more of an evolution of pre-existing structures than it was about evolving towards more capitalistic means of exchange. By the late 1990s, many of the old means of exchange among societal groups were being reconstituted and strengthened, benefiting from an influx of new material and financial resources. Informal groups and networks that functioned for *blat* during the Soviet period became crucial instruments in the exchange of favours among societal groups in the new states. In the place of weakened or non-existent governmental structures, patron-client networks strengthened and once again become instruments of rule, permeating every level of public-sector management and the new private enterprises. The overlapping politico-economic networks meant that, despite programmes of privatisation, it was often difficult to distinguish between politics and business in the transitioning economy. Finally, the second economy was now flourishing as the grey market, operating with the support of, and in many cases performing better than, the official economy.

The next two chapters will apply this network model to case studies during the time of Shevardnadze's leadership of independent Georgia (1993-2003). Chapter 5 examines the energy sector from the perspective of five functional areas, while Chapter 6 examines energy networks in three regions of Georgia. In each of these case studies, the specific stakeholders or their positions will be identified, followed by a discussion of the network characteristics of that particular operation, and concluding with an analysis of the network system.

Chapter 5: Functional Trans-territorial Networks

> It would take too long to explain why there was very little electricity and no heat in Tbilisi in the winter months...The reasons were so intertwined with Georgian networks of 'patronage', black hole, patchwork, and jerry-rig that it was impossible to separate sabotage (a strange and sudden fire at *Gardabani*, the country's only thermal power station) from corruption (the bungling and greedy idiots at Sakenergo, the state energy concern) from non-payment (less than 30 percent of the population in Tbilisi paid their electricity bills; Georgia owed Russia millions in electricity back debts) from theft (part of the copper transmission line between Armenia and Georgia was nicked one winter), from black clan economics (someone had the kerosene trade sewn up; it was in someone's interest to make sure there was no cheap clean alternative), from incompetence (the next winter the pride of *Gardabani*'s brand new gleaming Unit 10, repaired with sackfuls of Germany money, broke down because the engineer on duty didn't know what to do when a red light on the computerized panel started to blink unexpectedly), from infrastructure deterioration (once the whole of eastern Georgia went black as the 500 kW line from the Inguri hydro plant collapsed under the weight of what one commentator described as 'pre-election' abuse), from the oft-repeated worn excuse: 'The Soviet Union collapsed; there was a civil war' (Steavenson 2002: 15).

5.1 Introduction

The last chapter provided a model through which to examine the weak state as a medium for trans-territorial networks. I shall now use the model to examine five examples of networks traversing Georgia involved in functional aspects of the energy sector. All of the examples in this chapter include stakeholders from the *elite* and *bureaucracy,* using their official capacities in the government to further private financial gain. As we have seen, this was not a new phenomenon, but was grounded in practices honed during the Soviet era in the parallel economy. Working in the Soviet energy sector was one of the most lucrative means for the *nomenklatura* to generate extra currency from the second economy. During the latter half of the Soviet period, as the number of production plants increased, so too did supply and distribution routes, breaking down the tightly controlled vertical networks that were the trademarks of the command economy. With the proliferation of production plants, the management structures overseeing the supply of energy resources to these plants also grew across the republics, forming a heterarchical pattern of networks. Moreover, the electricity and petroleum products supplied to these plants became more difficult to detect and a substantial percentage was redirected and resold.[1] The dissolution of the Soviet Union did not bring about the end of this lucrative system; rather the directors of power plants, state-owned oil and gas distributors, and regional power stations created alliances across state boundaries to continue operating in the grey market.

Not only did the trans-territorial networks continue to operate in the energy sector after the break-up of the Soviet Union, but the financial resources at their disposal grew, including sources of public and private capital, as well as new means of operating in the grey economy. Opportunities to gain unprecedented amounts of private financing, foreign grants and investment, as well as the ability to move funds across borders with relative ease, enhanced the incentives of working in trans-territorial networks. New states entered Georgia's energy market, including Canada, China, Germany, Greece, Ireland, Japan, the Netherlands, Norway, Spain, Sweden, Turkey, the United States, and the United Kingdom. Those operating Georgian state assets in the energy sector also benefited from loans, grants, and technical assistance provided by international organisations, including the UN, EBRD, WB, IMF, and the EU. According to the Georgian Centre for Economic Corruption Monitoring, between 1994 and 2004, Georgia received almost US$ 500 million in foreign assistance to help it generate electricity (Ulushadze 2005). This money, combined with new sources of private funding, provided stakeholders with the means to manipulate public projects for private gain through such schemes as creating joint-stock companies,[2] registering companies off-shore, employing false accounting practices to account for undelivered or diverted supplies, bankrupting state firms 'insured' by private entities, misappropriating foreign grants, and artificially shifting

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[1] Interview with Peter Mamradze, former Chief of Staff to President Shevardnadze and first Head of the Government Chancellery under Saakashvili, Tbilisi, Georgia, April 2005.

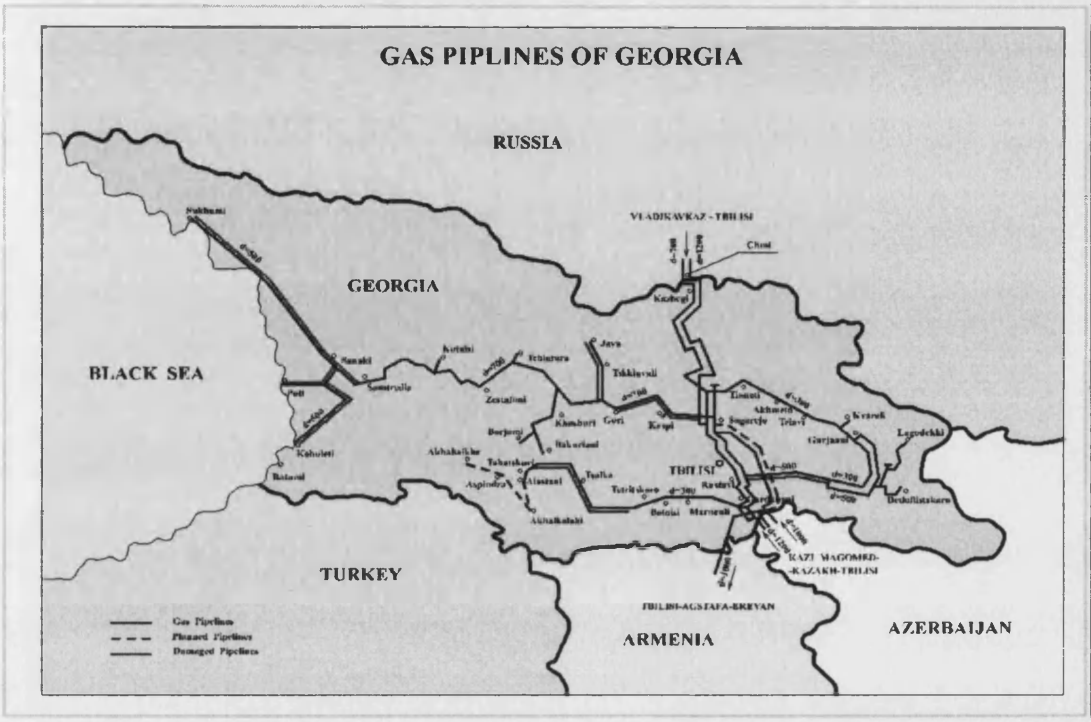
[2] A joint-stock company is a company (usually unincorporated) which has the capital of its members pooled in a common fund; transferable shares represent ownership interest; shareholders are legally liable for all debts of the company.

demand across markets through acts of sabotage and theft. These efforts were undertaken with the sponsorship of a member of the government, but carried out by a personalised and semi-permanent network of energy sector employees, select members of the *elite* and *bureaucracy*, and private entities such as banks and companies.

This chapter provides examples of trans-territorial networks operating in five functional areas of the energy sector: natural gas imports, electricity distribution, production of petrol, transportation of petrol, and electricity transmission. All five areas involve state owned companies located in Tbilisi or international companies investing in Georgia. All of these networks were created on a temporary basis among *elites* who operated across a multi-sectoral spectrum of petroleum, gas, and electricity sectors. Two of these cases follow a pattern that begins with an inter-party agreement and ends with Georgia faltering on its payments and transferring strategic assets to third countries, notably Russia. Another two cases involve the manipulation of competition in the petroleum business to secure a hold on the production and smuggling markets. The final example deals with the manipulation of foreign loans to create private companies. The deals contradict the rhetoric of a government that claimed to wish to strengthen its energy security and political and economic independence from Russia. The impact of these trans-territorial networks will be more thoroughly analysed in Chapters 7 and 8 in terms of both the empirical and the theoretical implications.

5.2 The Privatisation of a Gas System

Map 1 - Gas Pipelines of Georgia



Source: (Government of Georgia 2005)

During the Soviet period, 70 percent of Georgia's population had access to natural gas. The gas supply to Georgia was highly diversified, arriving from Azerbaijan, Iran (via Azerbaijan), and Russia. Georgia's main gas pipeline was constructed in the mid-1980s as a transit branch for Turkmen and other Russian and Central Asian gas shipments to Georgia, with a branch to Armenia (see Map 1 above). Beginning in 1992, Russia had a virtual monopoly on supplying natural gas from Central Asian sources (Turkmenistan and Kazakhstan) to Georgia due to its ownership of the main pipeline connecting Central Asia and the Caucasus. Georgia remained energy deficient, as its domestic production of natural gas never exceeded 10 percent of consumption. Georgia concluded a gas supply contract with Turkmenistan and transit agreements with Russia, covering the costs of supply with goods and services due to a lack of funds. However, during the war years in Georgia (1992-1995) there were many disruptions to road, rail, and pipeline supply routes, hampering Georgia's ability to deliver goods and services as payment. As a result, by 1995 Georgia's debt to Turkmenistan for gas totalled US$ 454 million, but was restructured at US$ 393 million and the IMF suggested that Georgia suspend the gas contract. Georgia's subsequent gas debt to alternative suppliers included US$ 27 million to Kazakhstan and US$ 12.5 million to Iran. The heavy debt Georgia owed its neighbours drove Kazakhstan and Uzbekistan to refuse to allow Turkmen gas destined for Georgia to transit their territories without receiving a share of higher transit fees. Thus the price Georgia paid for gas rose to levels far higher than in the rest of the former Soviet states (Jervalidze 2006).

Several reasons have been offered to explain the accumulation of such high debt. Some blamed a faulty metering system on the Russian-Georgian border. Until 1995, there was no meter on the Georgian side of the Russian border where the Turkmenistan-Daghestan-Georgian gas pipeline crossed. When the Georgian government constructed a meter on its side of the border, there were discrepancies between recorded gas imports. The Russian suppliers maintained that the agreements on gas supply with Turkmenistan and later *Itera* would be solely based on data provided by its meter (Jervalidze 2005). There were other structural issues that made it virtually impossible to verify the volume of gas supplied to Georgia, including sabotage of the pipelines, explosions in energy plants, and decaying pipes and equipment. There were also early indications of *elite* members operating in trans-territorial networks registering gas imports, which could not possibly have been delivered. For example, the Iranian supply to Georgia allegedly came via a pipeline built in Soviet times; however, the Azerbaijani sections were deemed unusable by Iran for the transit of gas. Nevertheless, the Georgian authorities claimed that the gas was supplied and blamed losses on misappropriation by local people. The pipeline crossed a tri-state area called Red Bridge, where there was a thriving smuggling ring between Armenians, Azerbaijanis, and Georgians. This incident became a flash point for potential ethnic conflict in a particularly heated period of history (directly after the 1994 cease-fire in the Nagorno-Karabakh War) (Jervalidze 2005).[3]

The result of all of this internal and external debt from gas procurement was the increasing reliance of the Georgian government on Russia. In 1994, the Presidents of

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[3] Interview with Liana Jervalidze, author of the study and independent energy analyst, Tbilisi, Georgia, April 2005.

Georgia and Russia concluded a new intergovernmental agreement stipulating that *Transgaz* in Georgia, with all of its assets (gas pipeline grid, transit sections to other countries, and service centres), was to be transferred to the Russian state-owned company *Gazprom* until 1999 (Jervalidze 2006: 14). Concurrent with this, *Itera*, an offshore Russian gas trader and producer, acquired exclusive rights to trade gas among the former Soviet states. Between 1995 and 2002 Georgian enterprises incurred a heavy debt to Russia's *Itera*. A 1995 Georgian presidential decree allowed individual companies to conclude contracts directly with the Russian gas company *Itera*. A multitude of actors arose as intermediaries in the gas supply business, some of whom entered into deals with the management of enterprises in Georgia targeted for privatisation. The intention of the scheme was to use the intermediary company to incur debt for gas supply, transfer the debt to creditors backed by the Georgian government, creating a situation in which a debt-for-equity swap could be arranged.

One such case involved the Georgian state-owned *Azoti* chemical fertilizer plant in Rustavi. In December 2000, 90 percent of the shares in *Azoti* were sold to *Itera* for US$ 500,000 in exchange for the rescheduling of gas debt owed to Russia by *Azoti* at US$ 100 million. *Itera* also secured monopoly control over supply to *Azoti* (Kavkasia-Press 2002). Beginning in 2001, *Itera* operated the *Azoti* plant's rehabilitation programme and obtained the right to export 90 percent of the plant's production of chemical fertilizers (Sarke Information Agency 2002). Allegations were made by a Georgian investigative news programme, '60 Minutes', on *Rustavi* television station that *Azoti* had signed a gas supply agreement with a company, *Magti Energy and Chemicals,* belonging to President Shevardnadze's son-in-law, Gia Jokhtaberidze (Rustavi-2 TV 2002). Jokhtaberidze's company, *Magti,* operated as the middle company for energy transfers from *Itera* to *Azoti.* When the press revealed the arrangement between *Itera-Magti-Azoti*, President Shevardnadze cancelled the *Magti* contract with *Azoti.*[4] Givi Targamazde, then a member of the government's Anti-corruption Commission, reported that *Magti* had accumulated debt from the business deal and transferred this debt to *Azoti.* The case was studied by the Prosecutor's

[4] Interview with Givi Targamadze, Chairman of the Parliamentary Committee on Defense and Security Issues, Tbilisi, Georgia, April 2005.

office, the police, the courts, and the Audit Chamber, but no one was charged (Rustavi-2 TV 2002).

These transfers of shares culminated in the July 2003 sale of Georgian strategic assets to Russia. Georgians, through their unusually free investigative press, discovered that President Shevardnadze had, on July 1, secretly signed a 25-year agreement on strategic cooperation with Alexei Miller, the chairman of *Gazprom.* Chapter 2 of the agreement provided for gas supply, rehabilitation, expansion, joint management, and operation of the Georgian pipeline network and its potential use by transit partners (Jervalidze 2006). As a result, *Gazprom* would be allowed to participate in future privatisation tenders for the Georgian gas pipeline system and to continue to use Georgia for transit to Armenia. The gas deal, while not changing drastically previous patterns of generation and distribution, did extend and deepen it.
There was immediate protest from various factions within Georgia, as well as western governments. What bothered the Georgians was the series of denials leading up to the agreement and the long-term contractual arrangement with a Russian company at a particularly contentious time in Georgia-Russia relations. Factions within the Georgian government, particularly Parliament, opposition figures, and some members of the President's cabinet, were surprised by the agreement with Russia. One year before, Georgia's then head of the National Security Council, Tedo Japaridze, had assured those concerned that Georgia would puts its efforts into diversifying sources away from Russia. He proclaimed,

> Georgia is still a weak state and without diversified energy supplies we also cannot have strong foreign and security policies. And that is also what I mean by the price. We experienced gas and electricity cut-offs from Russia. It would have been easier to reach contracts with Russia, but we were willing to pay the price of our independence and security of long term supply and decided to wait for the Azeri gas. Which, by the way, does not exclude cooperation with Russia in multiple energy projects (Baran 2002).

Leading up to the July agreement, key energy officials had denied both in public and private that a deal with Russia was pending. The Chairman of the Parliamentary Committee for Economics, Demur Giorkhelidze, said,

> I have talked with David Mirtskhulava [Energy Minister] several times and he personally assured me that no agreement with the Russian company would be signed [...] Of course there is no doubt that the entrance of the Russian company in the Georgian energy system will have an extremely negative impact on our strategic interests and security (Sephashvili 2003).

After the agreement, the governments of the United States and Turkey expressed great concern about the implications for the east-west gas pipeline from Baku, Azerbaijan to Ezerum, Turkey, named the South Caucasus pipeline (SCP). They questioned whether Russia could obtain the legal rights to the gas transited through the Georgian section of this pipeline. Following *Gazprom's* visit to Georgia in May to discuss the potential deal, the American President's Senior Advisor for Caspian Energy Issues, Stephen Mann, visited Tbilisi to urge the government to consider carefully the deal offered by the Russians out of concern that it could hinder the strategic importance of the SCP, scheduled to begin operations in 2007 (Sephashvili 2003). There were precedents in the region for this concern; in the proceeding two years, the governments of Ukraine, Moldova, and Armenia had accumulated alarming debts to *Gazprom* and *Itera*. As part of the debt repayment, Moscow requested that these governments hand over vital energy assets to the Russian companies.

To those who followed developments in Georgia's gas sector, however, the purchase by *Gazprom* of Georgia's strategic assets was not a surprise. A leading Georgian energy analyst wrote several papers about *Gazprom's* slow and steady efforts to acquire major assets in Georgia. In one study, she traced how the process of the re-nationalisation of Russia's gas companies, including *Itera,* coincided with the gradual transfer of Georgian state assets to *Gazprom* (Jervalidze 2006: 17029). A semi-permanent tri-state grouping of *elite* stakeholders, who had worked together in the Soviet era, were now placed to make money in the grey market. The network was established when Shevardnadze's former Minister of Economy, Temur Basilia, allegedly collaborated with a Turkmen businessman, Yuri Otchertsov (former Second Deputy Secretary of the Communist Party of Turkmenistan during the Soviet Union and Deputy Prime Minister of independent Turkmenistan from 1993 to 1996), and a Russian businessman, Yuri Skidonov (who formerly worked in the banking sector in Turkmenistan), in the establishment of *Itera* for regional gas business. *Gazprom* held a 20 percent stake in *Itera* and the two companies traditionally coordinated their activities.

Itera gradually created regional networks of *elite* stakeholders and purchased parts of Georgia's gas distribution system. In 1997, *Interpac* – a Georgian-British offshore company - purchased 6 main regional gas distribution companies in Georgia: *Kutasigaz*, *Caspigaz*, *Gorigaz*, *Tetritskarogaz*, *Bolnisigaz* and *Rustavigaz* for US$ 545,000. However, according to the Chairman of the Chamber of Control, Sulkhan Molashvili, the actual price of the package exceeded US$ 2 million. Further, the Chamber of Control reported that the purchase was conducted illegally, since 54.5 percent of the stocks in *Bolnisigaz* were sold by the Ministry of State Property Management 20 months before *Bolnisigaz* was established as a joint-stock company. The Ministry of State Property Management had already sold *Kaspigaz* and *Kutaisigaz* to *Itera* in 1996 for 67,000 GEL, despite the fact that the annual profit of *Kaspigaz* was 93,400 GEL. The Chamber of Control concluded that, 'The conduct of privatisation in this way can not be in the interests of the country' (Georgia Chamber of Control 2001).

Itera secured its hold on the Georgian gas sector in 1998 through a series of transfers of shares among the *elite* stakeholders. An international company, *Intergas Ltd,* was established in Cyprus in February 1998 with the help of Georgian businessman, Robert Bezuashvili (Jervalidze 2006: 19). In 1998, Bezuashvili's holding in *Intergas Ltd* was sold to *Interpac,* the Georgian-British off-shore company. In August 1998, *Intergas* became the Georgian national gas company *Sakgaz,* divided as follows: 50 percent *Interpac*; 40 percent *Itera* (Russian-Turkmen group); and, 10 percent *Itera Georgia* (reportedly owned by ranking members of Georgia's secret services) (Jervalidze 2006: 20). The 'Black Sea Energy Survey' produced by the International Energy Agency in 2000 provided a slightly different list of the holding interests of *Sakgaz.* The report suggests that Russians and Georgians established a joint venture with *Itera* in 1998 composed of 45 percent *Gazprom* holdings, 45 percent Georgian Minister of Fuel and Energy, and 10 percent *Itera* (International Energy Agency 2000). No matter what the exact division, in October 1998 Robert Bezhuashvili sold

40 percent of his shares in *Sakgaz* to *Itera* and 10 percent to *Itera Georgia.*[5] The end result was that *Itera* became both the monopoly supplier to, and the major shareholder in, Georgia's largest gas distribution company *Tbilgaz* (Gochitashvili and Gotsiridze 2002).

Ultimately, the accumulation of gas debt resulted in the transfer of almost all of Georgia's import and distribution system to Russia's state-owned *Gazprom.* As of 2000, Georgia owed *Itera* US$ 70 million; US$ 14.2 million of which was owed by the state-owned *Sakgaz* and the remainder by private companies. Beginning in April 2001, on *Itera's* initiative, Georgia's *Sakgaz* joined the gas supply system, and together they raised the price of gas imported from Russia. In addition, all shares owned by local *Sakgaz* holders became the property of *Itera* (Gochitashvili and Gotsiridze 2002). In 2002, *Itera* claimed that the Georgian government owed it US$ 91 million for gas previously supplied (Jervalidze 2006: 23). *Itera* wanted a debt-for-equity swap, including 51 percent ownership each of Georgia's gas pipelines from Russia, *Azoti* chemical plant, and the *Gardabani* gas generating units. In the end, *Itera* gained controlling interest in *Tbilgaz* (gas distribution company for the capital), distribution companies to Georgian towns along the pipeline route (Kazbegi and Dusheti regions), and the *Azoti* plant.

However, the Georgian government annulled the decision and announced it was looking for a new gas supplier. There was another company interested in investing in Georgia's gas sector – *Tahal* – a member of Israel's largest holding groups, *Kardan Ltd.* In concert with *Tahal's* interest in Georgia starting in 2001, *Itera* had pressured *Tbilgaz* to pay off its debts, using the tactic of cutting-off gas supply to most of Tbilisi for months (Kalandadze 2002). Tenders for the sale of *Tbilgaz* had already faced numerous challenges; *Sakgaz* won the first tender in 1998 but the offer was rescinded because the question of the company's previous liabilities was never resolved. A second effort to sell it in 2001 with the help of the US government failed because no company was willing to accept the conditions of sale. Finally, in 2003, it was

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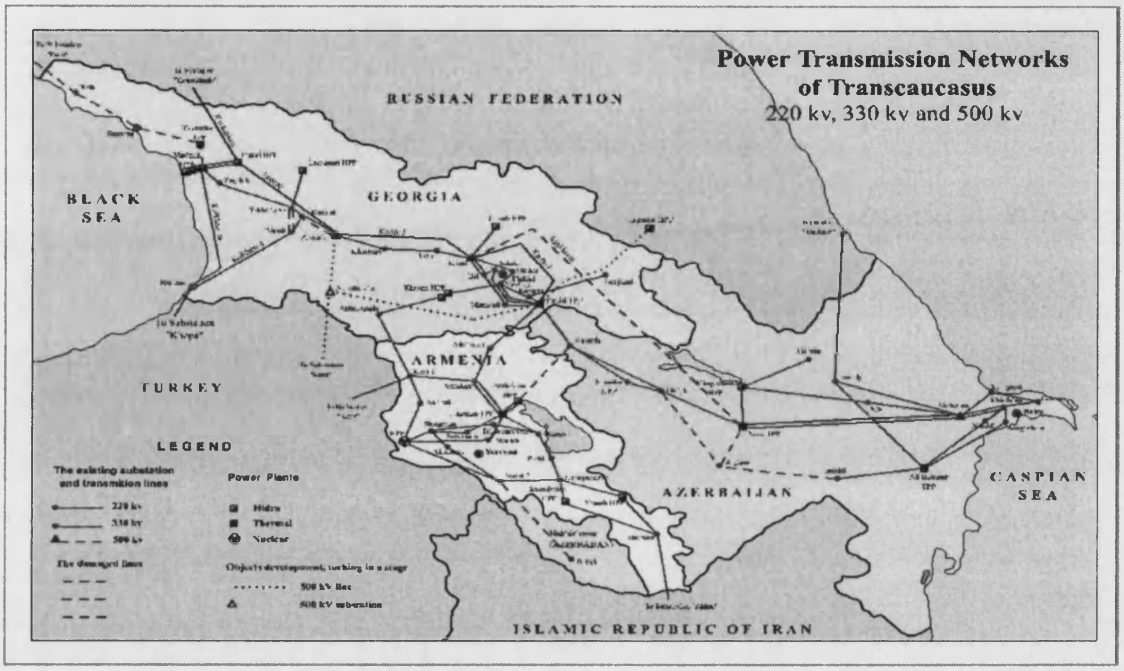
[5] Interview with Liana Jervalidze, independent energy analyst, Tbilisi, Georgia, April 2005. She explained that she had access to the Chamber of Control's report and over 80 original documents regarding this transfer of company shares.

awarded to Russia's state-owned *Gazprom* and, as of October 1, 2003, *Gazprom's* export arm, *Gazexport,* became the main supplier to Georgia.

5.3 The Privatisation of an Electricity Company

Map 2 - Power Transmission Networks of South Caucasus



Source: (Government of Georgia 2003)

One month after most of Georgia's gas distribution sector was sold to *Gazprom* in 2003, the Georgian parliament was told by the executive branch that *Unified Energy Systems Nordic*, a subsidiary of the Russian Joint-Stock Company *Unified Energy Systems of Russia (RAO-UES*) under the directorship of Anatoly Chubais, had already bought a 75 percent controlling interest in the Tbilisi electricity generator *Telasi* for US$ 26 million (Bit-Suleiman 2003). The biggest foreign investor – *American Enterprise Services Corporation* (*AES*) –had pulled out of Georgia, after almost 5 years of negative returns and a deficit expenditure of US$ 190 million. *AES* paid US$ 34 million to leave the country and an additional US$ 60 million to cover EBRD and IFC debt. In addition to *Telasi, RAO-UES* purchased the 9th block of the *Gardabani* power station (the only one in working condition) from *AES*, as well as the right to manage the hydroelectric power stations, *Khrami*-1 and *Khrami*-2, on a 25-year lease. Through its 50 percent shares in the *Sakrusenergo* (a Georgian-Russian joint venture), *RAO-UES* also acquired ownership of half of all the high voltage power lines in Georgia. Thus, given that Georgia's primary transmission line, *Kavkasioni* (see Map 2 above, upper left corner), originated in Russia, and that most of its customers were now served by *RAO-UES,* by 2003 Russia dominated Georgia's electricity market.

RAO-UES's takeover of Tbilisi's electricity distribution from the American *AES* company was done with the consent of the Shevardnadze regime, in what was viewed by Georgian analysts as a move by the government to balance its increasing politico-military cooperation with America, European countries, and NATO against business opportunities for Russian companies. President Shevardnadze had prepared the ground for the transfer of the American company to Russia by openly criticising *AES* five months prior to the company's departure, expressing his dissatisfaction with the unreliability of electricity transmission (Prime-News News Agency 2003a). When the sale was announced, the President justified it by saying,

> I cannot say that a crowd of companies are showing a desire to take over the electricity distribution system. For the time being, we can speak of only the Russian company as a contender. There are no other companies in perspective because the legacy left by *AES-Telasi* is very poor. This includes the 10^{th} power generating unit which exploded and needs to be repaired, which is the company's duty (Georgian Radio 2003a).

The story of *AES* shows how a series of actions by various intersecting heterarchical trans-territorial networks, whether orchestrated or not, ultimately undermined the ability of the company to operate successfully in Georgia. The following series of events do not tell the whole story; plenty of criticism was levelled at *AES* for how it conducted business in Georgia. This criticism was directed at a perceived lack of experience in operating in a country such as Georgia, including poor management style, too much focus on raising tariffs, and providing too much investment too soon.[6] The purpose of this aspect of the study is to demonstrate the role trans-territorial networks had in hampering the company's ability to succeed in Georgia.

At the time of the *Telasi* acquisition in December 1998, *AES* Corporation was the largest independent power company in the world, operating in 14 countries and its

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[6] Interview conducted off-the-record with former employee of *AES Telasi*, Tbilisi, Georgia, April 2005.

purchase of the Georgian company was part of a major expansion to 31 new countries (Henisz and Zelner 2006: 3). *AES* offered US$ 25.5 million for 75 percent of the *Telasi* Georgian electricity supply company. The remaining 25 percent belonged to the state and to employees of the company. Additionally, *AES* offered US$ 10.35 million for partial debt repayment to the government, with a commitment to invest US$ 22.6 million in the first year and US$ 84 million over ten years (Henisz and Zelner 2006). *AES* controlled 20 percent of Georgia's generation capacity and 60 percent of its distribution capacity. Subsequently, *AES* invested US$ 275 million, including over US$ 200 million towards upgrading the Tbilisi electricity grid and installing meters in households in the capital. In October 1999, *AES* purchased units 9 and 10 of the *Gardabani* power station for US$ 16.5 million plus a commitment to pay US$ 2 million in back wages and invest US$ 100 million. *AES TransEnergy* was established with the Georgian Ministry of Fuel and Energy to gain the rights to export electricity from *Gardabani* to Turkey.[7] Finally, *AES* gained a 25-year lease over the management of the hydroelectric power stations, *Khrami*-1 and *Khrami*-2. In the first year of operation, the company incurred operating losses of US$ 40 million per year, and after 16 months the company was losing US$ 120,000 per day and only managed to collect payment from 10 percent of its customer base. The then leading member of the ruling CUG party, Mikheil Saakashvili, appeared on Georgian television accusing the Minister of obstructing the ability of *AES* to operate effectively (Sarke Information Agency 1999a). Partly as a result of *AES's* difficult first year, the Minister of Fuel and Energy, Temur Giorgadze, was forced to resign in November 1999.

Semi-permanent arrangements of stakeholders in trans-territorial networks mounted at least six challenges that ultimately undermined *AES's* operations in Georgia. First, prior to the company's entry into the Georgian market, the government had accrued massive debts for electricity from neighbouring countries, some of which refused to supply *AES* until debts were paid. As of February 2002, the Government of Georgia was in debt to its neighbours for electricity supplied since 1998 to non-*AES* customers. It owed US$ 4 million to Russia, US$ 4.5 million to Armenia, US$ 6

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[7] The primary reason behind the establishment of *AES Transenergy* appears to have been an effort by *AES* to prevent a situation in which its newly purchased plant *Gardabani* was accused of not providing electricity previously owed by the Government of Georgia to Turkey.

million to Azerbaijan, and 1.5bn kilowatt hours of electricity to Turkey (Prime-News News Agency 2002). This impacted on *AES's* negotiations with these states for the necessary import of electricity. Second, the authority's protection of big business from paying for electricity put *AES's* accounts in arrears. Georgia's *Azoti* chemical plant, for example, used US$6 million worth of power in 2001, but did not pay *AES* for this supply. According to Michael Scholey, General Director for *AES* in Tbilisi, if *Azoti* had paid its bills, the funds would have been sufficient for power generation for all of Tbilisi for one month (Devlin 2003). This lack of government initiative in assisting *AES* to rectify this problem was due, in part, to the fact that the government billed companies for value-added taxes based on the quantity of electricity distributed, as opposed to the quantity actually paid for by recipient companies (Black Sea Press 1999). Third, the Government's continued practice of paying low salaries to employees at the National Dispatch Centre led to corrupt practices, such as the taking of bribes from customers to redirect supply to them despite non-payment at a loss to the company (Devlin 2003).

Fourth, by 2001, *AES* faced a trial in Georgia's constitutional court and was under scrutiny by a parliamentary commission for raising rates. Eventually, the Parliament, Tbilisi City Council, and the executive branch joined forces in opposition to *AES's* policy of raising rates and punishing non-payment with disruptions to supply. In early 2003 the Georgian Constitutional Court, on appeal, reversed a decision to raise electricity prices, and enforced price cuts, further undermining *AES's* financial position. At the same time, the Georgian Ministry of Finance seized *AES's* bank accounts and arrested the company's financial manager, Giorgi Gvichiani, for failure to pay taxes amounting to US$ 1.2 million. Following this, *AES* halted the import of electricity from Armenia, claiming it no longer had sufficient funds (Civil Georgia 2003). Fifth, *AES* became the victim of heightened political conflict between Russia and Georgia. In 2001, Russia cut gas and electricity supplies to Georgia as part of a dispute regarding allegations that Georgia was allowing Chechen guerrillas to operate out of its Pankisi gorge. Russia's irregular supply of gas and electricity resulted in unpredictable levels of electricity transmission in Tbilisi, undermining *AES's* ability to enforce the collection of payments. When the company could find an alternative supplier, it was often at a higher price.

Sixth, the aforementioned *AES TransEnergy* became embroiled in a trans-territorial network of Russians, Georgians, and Turkish stakeholders from the *elite* and *bureaucracy.* Georgia owed Turkey for oil imports. *Sakenergo*, the Georgian government's electricity regulatory body, headed by Emzar Chachkhiani, and the Georgian-British off-shore registered firm, *Anglo Oil*, headed by Levan Pirveli (also a Member of Parliament), signed an agreement. The third party was the head of the state-owned Turkish Electricity Generation and Transmission Corporation, who was convicted for making illegal profits from this deal.[8] Under the agreement, *Anglo Oil* was to give *Sakenergo* cash to buy fuel oil to generate electricity, which would then be transmitted to Turkey. A loan from Raiffeisen bank to the Georgian government guaranteed by the Minister of Fuel and Energy, Teimuraz Giorgadze, for US$ 46 million in 1998-1999 was provided to *Anglo-Oil.* This loan was to be spent on equipment for the *Gardabani* thermal power plant to export electricity to Turkey under the management of *Sakenergo* (Central Asia & Caucasus Business Report 2001). Experts investigating IFI loans to Georgia report that officials at *AES TransEnergy* and the Georgian government bought electricity from Russia for US$ .23 and resold it to Turkey for US$ .345 per kilowatt (Kochladze and Georgia 2000).

A Georgian newspaper reported that the scheme was much more complicated. Georgia sold electricity to Turkey at US$ .35 per kilowatt and Turkey paid *Anglo Oil* US$ .7 per kilowatt, generating the first illegal profit. Then, if Georgia was delayed in providing electricity to Turkey, it was liable to pay a 10 percent fine, rendered through 'in kind' electricity. In reality, Georgia's system was not technically able to provide the agreed volume of electricity to Turkey from *Gardabani.* Meanwhile, despite laws to the contrary, *Anglo Oil* took over temporary management of the Tbilisi-Rize (Turkey) power line that supplies electricity from Russia to Turkey (7 Dghe 1999). Several months later *Anglo Oil* suspended operations of the Tbilisi-Rize power line, making *Sakenergo* liable for a fine worth US$ 4 million to Turkey, as well as being liable to Russia for suspending its use of the power line. In order for the troika of stakeholders to make such illegal profits, *Sakenergo* banned *AES* from importing electricity for the first three months of their initial contract in relation to *Anglo Oil's* operations, hampering the American company's ability to deliver

[8] Interview with Levan Ramishvili, Director, Liberty Institute, April 2005, Tbilisi, Georgia.

electricity to its Georgian customers (7 Dghe 1999). For four years, Levon Pirveli managed this operation and allegedly made US$ 43 million profit.[9]

The *AES* story is particularly interesting as there are multiples layers of intersecting trans-territorial networks of *elite, bureaucracy,* and *consumers*, undermining the effectiveness of the company's operations. As one business case study concluded, 'Scholey [Director of *AES* in Tbilisi] had not rooted out the corruption networks within his firm nor the influence of the 'energy mafia' that linked Georgian industrial interests, Georgian politicians, and the Russians.' (Henisz and Zelner 2006: 2). At the top of the network were the directors of the state-owned companies who formed trans-territorial networks with fellow *elites* in Russia, Turkey, and Armenia to undermine the supply of gas and electricity to *AES* for generation and distribution. A second level of networks consisted of members of the *bureaucracy* – state officials and directors of the largest state plants and heavy electricity *consumers* – who avoided paying for the supplied electricity. Stakeholders included the Ministry of Defence, Shevardnadze's security forces, and the Tbilisi airport, among others (Henisz and Zelner 2006: 13).

The *bureaucracy,* in particular the electricity regulating agencies, the Justice Ministry and parliamentarians, also worked to ensure that *AES* could not legally raise prices in order to compensate for the funding shortfalls experienced from non-paying customers and cuts in supply from neighbouring states. When the Constitutional Court annulled the rate increase set by the Georgian National Energy Regulatory Commission (GNERC), *AES* refused to lower rates and threatened to sue the government for breaking the conditions of the contract (Rustavi-2 TV 2003b). A third level of networks consisted of employees working for *AES* (*business groups)* and its customers (*consumers*) who cooperated to increase the profits of the employees and reduce the amount customers paid by tampering with the meters, under-reporting usage, or selling equipment belonging to *AES* and declaring it stolen (Henisz and Zelner 2006: 13). An unidentifiable network was responsible for 15 attacks against the offices and personnel of the company, including a threatening letter to the then-

[9] Interview with Givi Targamadze, Parliamentary Chairman of the Defense and Security Committee, Tbilisi, Georgia, April 2005.

Director, Igancio Iribarren. Further, Niko Lominadze, the Chief Financial Officer and highest-ranking Georgian in Tbilisi's distribution company *AES*, was found dead in his apartment. He had been tied up and killed by a gunshot to his head in August 2002 (Devlin 2003). Despite assurances from the Georgian Interior Minister, Koba Narchemashvili, none of these cases were ever solved during Shevardnadze's presidency (Prime-News 2002).[10]

After the departure of *AES*, pressure from parliamentarians and Georgian non-governmental organisations resulted in the resignation of Energy Minister Mirtskhulava. However, President Shevardnadze quickly named him the head of GNERC. In his new position, three western energy companies operated under his supervision: Georgian United Distribution Energy Company run by American *PA Consulting*, Energy Wholesale Market run by Spanish *Imiard*, and the Georgian United State Electricity System run by Irish *ESBI*. It became Mirtskhulava's responsibility to balance these three companies and prevent *UES* from monopolising the energy sector.

5.4 Production of Petroleum Products

Two problems plagued the petroleum industry in Georgia: smuggling and illegal refining. They were intricately linked because the refineries operated with smuggled or stolen crude or low quality petroleum. Both aspects of the industry were monopolised by two figures in the Shevardnadze family, who cooperated with members of the *bureaucracy* and *business groups* to undermine the success of a professional refinery established by the *Georgian American Oil Refinery (GAOR)*. The illegal smuggling of petroleum was controlled by Nugzar Shevardnadze, in concert with key *elite* members of the government, particularly those who managed and provided security for transport corridors. Oil processing in Georgia was carried out by about 24 registered and 17 unregistered 'teakettle' refineries producing about 100 tonnes per day. To put this in perspective, it is uncommon to find an oil company that would build a refinery that produces less than 3 million tonnes per year, while all

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[10] In August 2006, the former *Tbilgaz* General Director, Georgi Gvichiani, was sentenced to life in prison in connection with the murder of Lominadze. The motive is thought to be an effort to cover-up financial mismanagement within *AES*, uncovered by Lominadze (Civil Georgia 2006)

of Georgia's refineries together produced 365,000 tonnes per year (Shenoy 2002a: 17). The owners of these unregistered oil refineries were never identified in any report, but were rumoured to be the father of the wife of the President's son, Guram Akhvlediani, and regionally-based politicians (Shenoy 2002a: 17).

The regulation of the refining industry and the transparency of the petroleum business was seen to be of central importance to strengthening the Georgian economy (Petroleum Advisory Group 2003). A State Council of Petrol Products was established to regulate the market and an estimated minimum 30 percent of Georgia's budget revenue should have come from taxation of the petroleum sector (Shenoy 2002b). During Shevardnadze's presidency, there were no reliable statistics on petroleum consumption in Georgia, nor was there credible information about the exact number of refineries, their annual capacity, ownership, what products were processed, how the products were marketed, the export of products from these refineries, or taxes paid to the government. From the mid-1990s, registered petroleum imports into Georgia steadily decreased, resulting in a reduction in tax collection, disruption of the legal market of petroleum products, and an increase in the volume of traffic and trade in the second economy. According to a study carried out under the auspices of the American Chamber of Commerce in Georgia (AmCham), only 10-15 percent of legally imported petroleum in 1999 was registered as official retail sales in Georgia, resulting in a critically low tax threshold (Petroleum Advisory Group 2003: 6).

In the midst of this, *GAOR* began negotiations with the Georgian government in the late 1990s to establish a refinery in Georgia. The key investors in *GAOR* were a Canadian company *CanArgo* (51 percent), the Georgian state oil joint-stock company *Saknavtobi* (30 percent) and an American company *Makoil* (19 percent).[11] Initially, President Shevardnadze was a supporter of the *GAOR* oil refinery. In an interview, he explained,

> I consider it expedient to turn our attention to *GAOR* and help run it at its full capacity [...] the number of makeshift facilities has increased substantially. These facilities actually produce poison, using crude

[11] Interview with Dr. David Robson, Managing Director and Chief Executive Office *CanArgo*, London, UK, February 2007.

> naphtha. About 20 makeshift facilities of this kind are operating in Georgia at present. Yet, given proper support from the state and technology that it has in its possession, the *GAOR* refinery is capable of producing quality products, which would not have a harmful effect on the environment. Consequently, the budget will receive substantial amount of money from this refinery and all the benefits that we will grant to this company will be repaid (Georgian Radio 2003b).

A mini plant was imported from America and constructed in Georgia. Four products were produced: petroleum, diesel, naphtha and fuel oil (or mazud – used by *Tbilgaz* to generate electricity). It was a joint operation in which *CanArgo* extracted oil from its Ninotsminda oil field in Kakheti, and sent it first by a 17 kilometre pipeline, and later by truck due to theft, to the *GAOR* refinery. Petrol was then distributed to *CanArgo* owned petrol stations.[12] *CarnArgo* held a 100 percent stake in the Ninotsminda oil field, investing US$ 50 million since 1996, accounting for more than half of Georgia's oil exploration (Oil and Gas Investor.Com 2005). At its height, *GAOR* could produce up to 10,000 tonnes of oil monthly (4,555 tonnes of petrol, 2,800 tonnes of diesel, and 2,500 tonnes of fuel oil annually) and it was estimated that even at 20 to 25 percent working capacity, it could cover the local Georgian market demand for diesel fuel and kerosene at a cost 10 percent cheaper than imported products (Sarke Information Agency 2003b). *GAOR* had even begun exporting to Armenia (Kavkasia-Press 2000a).

GAOR was so efficient that it became the target of trans-territorial networks of *elite* and *bureaucracy* stakeholders, who sought to undermine the operation. Pushing *GAOR* out of the Georgian market was one of the known cases in which Guram Akhvlediani (producer) and Nugzar Shevardnadze (importer) joined ranks to ensure that *GAOR's* business in Georgia failed to the point of forcing it out of the country (Sarke Information Agency 2000a). First, the Georgian government imposed a 60 percent excise tax on *GAOR's* products, which made the company less competitive than importers. *GAOR* approached the government through multiple channels, including writing letters to Parliament requesting a reduction in the excise tax, but the tax remained in force.[13] Then in 2000, the Georgian Parliamentary Committee on

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[12] Interview with Tea Shatirishvili, VIP Manager of CanArgo and former employee of *GAOR*, Tbilisi, Georgia, April 2005.
[13] Interview with Tea Shatirishvili.

Environmental Protection banned the use of tetra-ethyl lead, which was a primary ingredient in *GAOR's* production of high-octane petrol.[14] The committee also banned the import of its substitute, pyrolysed tar, from Azerbaijan. The Committee determined that this substance was a major health hazard, despite the fact that the Minister of Environmental Protection, Nino Chkhobadze, had issued a permit to import the tar expressly for use by *GAOR* (Sarke Information Agency 2000b).

In response, President Shevardnadze threatened to sign a decree that would enable the refinery to operate despite parliamentary objection. The President introduced a new standard on September 15, 2000 that reduced the acceptable level of benzene in petroleum to 3 percent from the previous Soviet standard of 5 percent, with a phased approach for requiring companies to meet the new standard (Sarke Information Agency 2000c). According to the Georgian newspaper *7 Dge*, the Chairman of the Parliamentary Committee on Environmental Protection, Kakha Chitaia, who accused the Minister of Environmental Protection Chkobadze of illegally issuing a licence to *GAOR* to import pyrolysed tar from Azerbaijan, was a good friend of Nugzar Shevardnadze (Sarke Information Agency 2000d). It is interesting to note that after *GAOR* left Georgia, the same Ministry issued environmental clearance to 24 refineries, despite a lack of information about their operations, including an assessment of their operations on the environment (Shenoy 2002a).

The President and members of his Cabinet defended *GAOR* until its owners made the decision to sell. Following the suspension of *GAOR's* operations in 2000, President Shevardnadze told oil producers, 'If *GAOR* is not put back into operation in two weeks' time, I will have to take measures stipulated in the Criminal Code against those who are hampering the creation of wealth in Georgia' (Kavkasia-Press 2000a). The Georgian Minister of Fuel and Energy, Davit Mirtskhulava, told a Georgian newspaper that, given the positive conclusion of an expert panel, the refinery would resume importing 1,000 tonnes of pyrolysed tar from Azerbaijan (Kavkasia-Press 2000a). The *GAOR* manager, Givi Asatiani, defended the refinery by arguing that the company would contribute 24 million GEL to the 2002 budget and that this figure would double and even treble over the next several years. Instead of generating

[14] Interview with Dr. David Robson.

income for Georgia, however, the impasse regarding licenses meant a loss of 9.6 million GEL for the *GAOR* owners over several months (Kavkasia-Press 2000a). Meanwhile, the company was exploring the construction of a larger refinery that could be fitted with a catalytic reformer that was economically viable, allowing it to continue operations and meet the environmental regulations (CanArgo 2001). However, none of this transpired and the refinery and entire operation was forced to close in 2001 and *GAOR* sold its remaining shares to *Saknavtobi.*[15]

Following the sale, the State Minister, Giorgi Arsenishvili, pronounced at a session of the Investment Council on April 7, 2001 that 'nobody is able to say' why the oil refinery was shut down (Sarke Information Agency 2001). He thought that it was the indolence of Georgian officials that ultimately strangled oil extraction and refining in the country. 'There is little oil and gas in Georgia so far, but this is one more source of the budget revenues', said Arsenishvili. President Shevardnadze, chairing this same session, called the people hindering the development of the oil industry in the country 'enemies of the nation' (Sarke Information Agency 2001). Reporting on the *GAOR* refinery, the *Mtavari Gazeti* wrote that this 'sphere became the victim of clan-relations opposition and parochial interests of the state structures' (Sarke Information Agency 2003a). Former Minister of Fuel and Energy, David Zurapashvili, believed that the government destroyed *GAOR* because the stakeholders involved in smuggling did not want internal competition.[16] A leading Georgian newspaper, *Akhali Taoba* (*New Generation*), wrote that *GAOR* was a, 'weakness of President's kin people' and the 'object of battle between President's [father]-in-law (who has an interest in the enterprise) and nephew (whose business is petrol import) (Sarke Information Agency 2000b). Despite the President's display of support for the operation of the *GAOR* refinery, and his professed angst over its closure, no one was prosecuted and no new foreign refinery was built during Shevardnadze's time.

[15] *CanArgo* also sold its 20 service stations in Tbilisi and 25 stations in Poti, Kutaisi, Khashuri, Zestaponi and Telavi. *CanArgo* had contracts to supply the Ministries of Finance, Economics, Security, and Embassies (United States, United Kingdom, and Turkey).
[16] Zurapashvili was the Minister in 1996 and he helped establish the legal framework for the import of the refining plant.

5.5 Transport of Oil from Azerbaijan to Armenia through Georgia

One question that was never fully answered by the American Chamber of Commerce's Petroleum Advisory Group (mentioned in 5.4) was the origin of the crude oil refined in Georgia. Officially, Azerbaijan, Turkmenistan, Kazakhstan, and Russia were not exporting crude oil to Georgia and other states because they had a strategy to protect the financial advantage of operating refineries on their own territories for export. However, there were reports of crude oil being transited from these countries to Georgia, as well as smuggled crude oil available from Chechnya. There were also reports of numerous incidents (1500 as of April 2005) of the siphoning of crude oil from the Baku-Supsa pipeline. Another question unanswered by the Petroleum Advisory Group was, given that the teakettle refineries did not have the ability to produce petroleum that could meet the Georgian standards of 1977 (5 percent benzene), how did they fulfil the requirements established by the Ministry of Environment, so stringently placed on *GAOR*. Finally, they queried how the teakettle refineries in Georgia could be economically viable if they had to buy crude oil from outside the country paying international prices and taxes. The answer to all three questions must have been that the owners of the refineries were either processing smuggled crude oil or buying crude oil at international prices and avoiding taxes. Moreover, their products could not have been environmentally sound due to the lack of available material for clean processing (Shenoy 2002a). Finally, the trade in crude and the operation of the teakettle refineries must have been a professional operation of *elites* operating across borders with the support of numerous actors from the *bureaucracy* and *business groups* at the border crossing points. Otherwise, how else could Georgians have avoided detection of unrecorded imports and managed unregulated refining operations for such a long period of time?

The biggest volumes of smuggled crude to Georgia came by railway. This trans-territorial network is believed to have been supported by the highest levels, guarded by the close personal relationship between Presidents Shevardnadze and Heydar Aliyev of Azerbaijan.[17] Business between the two states was conducted at the

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[17] In Shevardnadze's autobiography released in Georgian in May 2006, he dedicated an entire chapter to his friendship with Heydar Aliyev.

presidential level and all that was needed was 'the word' of one or the other to secure a business arrangement. The close ties between the presidents filtered down to include the energy magnates of both states and the presidents' families. Nugzar Shevardnadze and the younger son of President Aliyev, who was the Director of the State Oil Company of Azerbaijan (SOCAR), Ilham Aliyev, were business partners. Relations between Aliyev and Abashidze of Adjara were also conducted at a 'presidential' level, and former President Aliyev's brother had direct connections with Batumi Port.[18] Georgia was the only export route for Azerbaijan to international railways and the Black Sea, which made Azerbaijan reliant on Georgia for reaching lucrative export markets. Azerbaijan transported hydrocarbons from Baku through Georgia to Black Sea ports, including Supsa (via a refurbished Soviet era pipeline) and by rail to Batumi in Adjara for transport to Europe by ship. This transport corridor was hailed as the revitalisation of the 'Silk Road' and extended east to Kazakhstan and Turkmenistan.

Some of the crude smuggled from Azerbaijan to Georgia eventually made its way to Armenia. By the mid-1990s, a trans-territorial network of *elites,* assisted by members of the *bureaucracy* and *business groups,* smuggled crude oil and petrol across the Azerbaijan border into Georgia. The primary Georgian stakeholders in the network were the Georgian Minister of Interior, the Minister of Transport, the Head of the Railways, and members of the Shevardnadze family, in particular Nugzar Shevardnadze. They were supported by the Governor of Marneuli in eastern Georgia and numerous members of the security services patrolling the border and railway line. It has also been mentioned that Armenian groups living in Georgia near the Armenian border worked with Gia Jokhtaberidze in supplying Azerbaijani petroleum to Armenia.[19] According to the Georgian investigative programme, '60 Minutes', on Rustavi television, an offshore company, *Argomaroil,* was set up by Alexander Tavadze, the son-in-law of the Head of the Railways, Akaki Chkaidze. This company was used primarily for laundering money gained from the transit business (Rustavi-2 TV 2003a).

[18] Interview with Gadjiev Gadjan, Ambassador of Azerbaijan to Georgia, Tbilisi, Georgia, April 2005.
[19] Jonathan Wheatley's interview notes with Armen Amirkhanyan, Representative of the Akhalkalaki office of the European Centre for Minority Issues, Ninotsminda, Georgia, March 2004.

Crude oil was transported via railway from Baku into Georgia, refined in the eastern part of Georgia and sold to customers, including Georgian petrol stations.[20] According to a security officer for a major western oil firm in Georgia, this was not the job of amateurs, but part of a business venture, which included the transport of crude oil from the taps to the 'teakettle' refineries previously mentioned, mostly located in the eastern *Gardabani* district of Georgia near the Azerbaijan border. These teakettle refineries were built towards the end of the Soviet Union, conveniently located next to the railroad and were extraordinarily large in number compared to the relatively small volume of crude oil extracted in Georgia.[21] A comparison of the data published by the Azerbaijani and Georgian Departments of Statistics in 2001 reveals a difference in the value of the petroleum products exported from Azerbaijan to Georgia of US$ 30 million more than what Georgia officially received (Petroleum Advisory Group 2003: 8). One theory is that at a certain point in the late 1990s most of the imported crude to Georgia arrived by railcars from Baku on their way to Batumi or, later, Poti port. The stakeholders in a trans-territorial network would declare the transit as export, therefore avoiding almost double import taxes and duties. Then, somewhere along the railway route inside of Georgia, approximately 13 rail cars per day were diverted and the contents were sold within Georgia or resold to Armenia.[22]

The Armenian demand for petrol was particularly acute during and after the war with Azerbaijan because of the Turkish/Azeri embargo. The challenge came in getting petrol into Armenia given the trade embargos. During the war, the Armenian Ministry of Interior under Vano Siradeghian controlled the trade and imposed a tax on every litre of imported fuel, which theoretically went to finance the war. After the war, it is alleged that there was a group of Armenian, Georgian, and Azerbaijani veterans of the war in Afghanistan, all of whom were involved in the national chapters of the Union of Afghan Veterans, who bought Azeri crude oil for shipment and sale in Georgia, and then altered documents and smuggled it into Armenia for sale at inflated prices. In the mid-1990s, the Government of Azerbaijan broke up the ring and there were rumours that high-ranking Azeri officials were profiting from the

[20] Interview conducted off-the-record with energy company employee, Tbilisi, Georgia, April 2005.
[21] Interview conducted off-the-record with energy company employee, Tbilisi, Georgia, April 2005.
[22] Interview conducted off-the-record with energy expert, Tbilisi, Georgia, August 2003.

trade, but no evidence came out at the trial.[23] However, the diversion of petroleum from Azerbaijan through Georgia to other parties continued. An Azerbaijani newspaper reported in 2001, 'it is known that fuel is being passed on to Armenia from our country [Azerbaijan]. Nor is it a secret that the fuel is being transported to Armenia via Georgia and Iran' (Yeni Musavat 2001).

The continuation of fuel diversion through Georgia did not become a major diplomatic issue until eight Azerbaijani tankers belonging to the Azerbaijan Transport Ministry containing fuel products were delayed by Georgian law-enforcement agencies for almost two months on the Azerbaijan-Georgia border in early 2005. Accusations flew between the governments as to the ultimate destination of this petrol, with Azerbaijan accusing Georgia of plans to redirect it to Armenia and Georgia claiming that the petrol was registered under false documents. According to an Azerbaijani newspaper, top Georgian officials passed on the information regarding the Azerbaijani involvement in the smuggling operation and President Aliyev of Azerbaijan ordered a meeting with the Minister of Transport (Azadliq 2000). A leading Azerbaijani opposition leader gave two reasons why the Azerbaijani authorities would want to stop the railroad tankers full of petrol on the border and accuse Georgians of redirecting the supply to Armenia. First, he believed it could have been Azerbaijani businessmen who wanted to punish the post-Rose Revolution Georgian businessmen and prove that without collaboration from elements within Azerbaijan, the Georgians could not conduct business as usual. Or, it may have been due to Moscow's interference, implying that perhaps Russian authorities were attempting to expose corruption in the region, despite rhetoric from the new Georgian President to the contrary[24]

Combining the case study above regarding illegal petroleum refining with this one on the re-export of Azeri crude to Armenia reveals a supply chain involving many stakeholders across several states. Figure 5 below was drawn up by the US Agency for International Development (USAID) after consultation with the Saakashvili administration in order to deconstruct the trans-territorial networks. The purpose of

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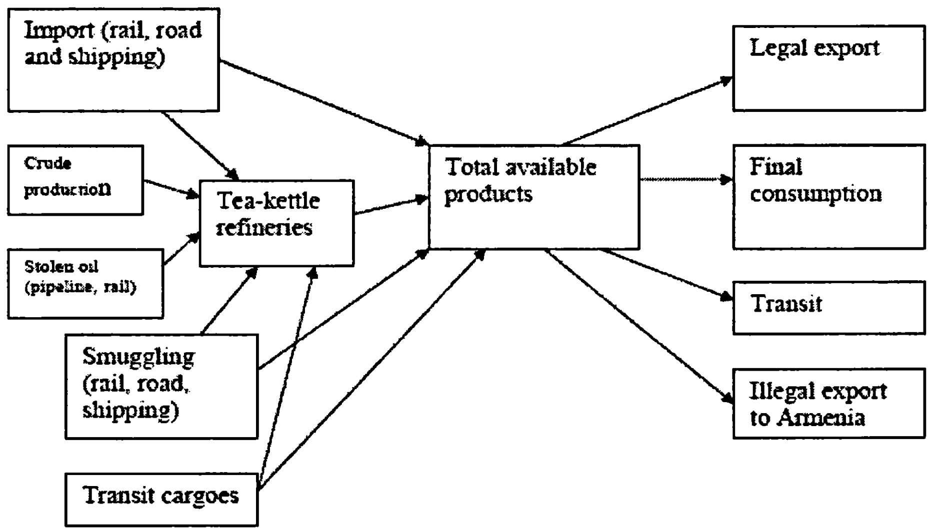
[23] Interview with Robinder Bhatty, formerly of Cambridge Energy Resource Associates. Email correspondence, London, UK, June 2004.
[24] Interview with Isa Gambar, Chairman of the Musavat Party of Azerbaijan, London, UK, May 2005.

the USAID study was to identify ways to break these networks by enforcing regulations in order to realise the missing revenues (Downey 2004b). This figure suggests that the crude oil came by import, was stolen from the pipeline or from rail cars, or was smuggled into Georgia. It was then produced in tea-kettle refineries, many of which were not registered. Products were then consumed locally or exported legally and illegally, namely to Armenia. Chapter 6 of this thesis will analyse further cases of petroleum smuggling which, while involving far smaller volumes, are perhaps even more critical to the weakening of Georgia. This is because the networks unite the separatists in Abkhazia and South Ossetia together with Georgian and foreign forces, who are allegedly meant to be safeguarding the *de facto* territorial delineations, as well as the citizens that live in and around the disputed zones. However, by cooperating together in smuggling networks, all sides are undermining the security of both the territory and the citizens.

Figure 5 - Petroleum Chain



Source: (Downey 2004a)

5.6 Generation and Distribution of Electricity

Problems in the electricity sector persisted throughout the Shevardnadze era, particularly in the regions of Georgia. Issues plaguing the system included theft of electricity, shortages of electricity in the autumn and winter seasons, low execution of dispatching centres, faulty power transformers and cables, low levels of payment, unfinished re-metering of homes, inefficient utilisation of power plants, ineffective legislative and regulatory mechanisms, and a tainted regulatory commission (JSC Telasi Representative 2005). As mentioned in Chapter 3, a 2005 parliamentary commission headed by Gia Natsvlishvili investigated the power generation sector over the previous decade and concluded that a great amount of foreign assistance was either 'embezzled or used for wrong purposes' (Sarke Information Agency 1998). Natsvlishvili said that the Commission had investigated only part of the documents available due to lack of time and the huge amount of materials to be studied. He focused on the years when David Mirtskhulava had been Minister of Fuel and Energy, during which US$ 65 million in loans were supposedly spent on the power sector.

One example of how loans were diverted is the international community's support for the most powerful hydropower station in Georgia, *InguriHES*, straddling the Georgian and Abkhazian territories. It was originally commissioned in 1975 to support the energy requirements of the Soviet Union. After Georgia's independence, *InguriHES* lost half of its energy production capacity. It is capable of producing much more energy (1300 megawatts), but after years of neglect and misuse, the plant produced just 40 percent of its potential output (Rimple 2006). *InguriHES* was touted as a success story by the conflict resolution community, which viewed the joint Abkhaz/Georgian operation as the only functioning cooperative effort between the two sides. While the reservoir was located in areas under the Georgian government's control, the Abkhaz authorities controlled the power station, generators, and main transformer station. Electricity was distributed in part to the Abkhazian system (40 percent) and in part to Georgia (60 percent). The staff was composed of both Abkhaz and Georgians, who first began working together on the rehabilitation of the plant with the assistance of an EBRD US$ 62 million loan and an additional 5 million Euro from the EU.

The actual operation of the plant, however, turned into a profit making industry for a trans-territorial network. Electricity was provided to Abkhazia free of tariffs and was more than the region required. It is alleged that the Georgian authorities and residents of Abkhazia created a trans-territorial network composed of stakeholders from the *elite* and *bureaucracy* to sell the surplus electricity to Russia. In July 2003, the Chairman of a special parliamentary commission looking into the energy crisis, Irakli Chubinishvili, accused the former head of the joint Russian-Georgian electricity company *Sakrusenergo*, Shota Maisuradze, of being involved in the energy triangle involving businessmen from Abkhazia, Georgia, and Russia. A Russian company named *Winnfield* reportedly charged Georgia three times the original production price of electricity produced at *InguriHES* for the electricity Georgia received through the *Kavkasioni* line from Russia (Prime-News News Agency 2003b).[25] It has been noted by a former employee of *InguriHES* that it is technically impossible to reroute the same electricity produced at the hydropower station through Abkhazia to Russia and back again to Georgia.[26] However, the perception held by Georgians of a cyclical routing of electricity was the result of their knowledge of the trans-territorial network of electricity generation and distribution that benefited the Abkhaz and the Russians, to the detriment of Georgia.[27] That is, the Georgian state was producing electricity, Abkhazia was receiving electricity free of charge and making a profit from its resale to Russia, while the majority of Georgians were at the mercy of Russian supplied electricity at a higher price, through an unreliable transit system.

The stakeholders included not only the appointed ministers, but also members of their families, particularly the sons. For example, the previously mentioned parliamentary investigative commission established that Giorgi Mirtskhulava, the son of the former Fuel and Energy Minister, David Mirtskhulava, and Giorgi Chachkhiani, the son of the former head of *Sakenergo*, were linked to the misappropriation of the funds allocated for the restoration of *InguriHES* under a US$ 38.6 million EBRD loan. Giorgi Natsvlishvili made public information pertaining to 8.4 million GEL (approximately US$ 4.2 million) purportedly misappropriated by the pair. These funds were redirected to a limited liability company (LLC) founded by four persons – the sons of Mirtskhulava and Chachkhiani, Irakli Sulaberidze (the *InguriHES* rehabilitation project coordinator) and Grigol Macharadze. According to the commission, about US$1 million was diverted from the EBRD loan, US $4.8 million

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[25] This company has also been referred to as 'Winnfield International Limited', registered in the Virgin Islands and there was speculation that Georgian and Russian politicians established the company.
[26] Interview with Mikheil Babukhadia, former Chairman of the Supervisory Board of *InguriHES* and former commercial manager for *AES Telasi*, London, UK, June 2006.
[27] Interview with Mikheil Babukhadia.

from *Telasi*, and US$ 2.2 million came from *InguriHES* itself. Further, the parliamentary commission determined that the LLC was established illegally in 1999 with only 2,000 GEL (approximately US$ 700) (Prime-News 2004). Misha Antadze, Head of International Relations Department at the Georgian Ministry of Energy, surmised that had the grants been spent properly, there would have been enough locally produced electricity to meet domestic demand and to export. Due to the fraud, however, Georgia had only exploited about 12 percent of its potential hydroelectric power (Saginadze 2006).

5.7 Conclusion

These cases cover only the most infamous trans-territorial networks that existed during the Shevardnadze era, many of which are slowly being revealed by the investigations and prosecutions carried out by President Saakashvili's government. Table 4 below displays, as an example, the stakeholders, network characteristics and the system dynamics of the trans-territorial networks that undermined the success of *AES Telasi*. All of the cases set out in this chapter demonstrate how the entire system of mostly state run energy enterprises existed for the enrichment of the *elite,* key ministers and their family members in Georgia and their partners in Russia, Turkey, Azerbaijan, Armenia, Kazakhstan, and Turkmenistan. However, they could not operate without the assistance of the *bureaucracy* and *business groups.* In order to succeed, the *elite* needed to secure foreign funds directed towards government agencies. The *elite* also required assistance from Parliament to pass laws, the courts to make decisions in their favour, operational crews to help divert supplies to third parties, and security for transit routes. Those people who were purportedly running the state, and who were charged with strengthening energy security through various plans, programmes, and financial assistance, were simultaneously acting to enrich themselves and weaken the state. This runs counter to the view propagated by the literature discussed in Chapter 2, that weak states necessarily have weak institutions, or that the population is in conflict with the government. In fact, the judicial, legislative, and executive branches worked quite effectively in carrying out measures to undermine the success of two foreign investors. Further, society colluded with members of the government in extracting free rents from the system.

As a result, within less than a decade, Georgia had gone from independently managing its gas and electricity infrastructure, to going heavily into debt to numerous neighbouring states for gas and electricity, and ceding control of most of its supply and distribution system to the Russian government. The diversion of foreign assistance by the Georgian *bureaucracy* meant that it could not exploit its potentially most abundant source of electricity – hydropower. Georgia's relationships with neighbouring states were based on the knowledge that a great section of the energy sector was relegated to the grey market, and that many of Georgia's business relationships were non-transparent and semi-permanent. What is perhaps most surprising is that the Georgian government, facing political and military pressure from Russia, nevertheless created trans-territorial networks with private and state entities in Russia, undermining not only its own fiscal health, but also ceding strategic assets in the energy sector to Russian state-owned interests. Despite the pro-western position espoused by the Georgian government, policies adopted by various branches of the government ensured that two major western investors in its energy sector would fail. As demonstrated in the case of *Gazprom*, this was less a purposeful policy decision than it was the result of years of schemes through which the Georgian government made itself vulnerable to a debt-for-equity swap.

Thus, rather than viewing regional energy relations as driven by inter-state arrangements, it is more useful to conceptualise the state as a transit route for non-transparent trans-territorial networks. Eventually, as discussed in Chapter 4, the networks create overlapping heterarchical webs, generating an alternate order that is responsible for events in the regional energy system. This will be made clearer in the next chapter, which will apply the network model to demonstrate that these trans-territorial networks also existed in the outer regions of Georgia, with supposed adversaries in Abkhazia, South Ossetia, and Javakheti.

Table 4 - Trans-territorial Networks Undermining AES Telasi

Stakeholders	Network Characteristics	Network System Dynamics
Elite – Managers and shareholders of state and private companies: *Gazprom Interpac, Itera, Sakenergo, Tbilgaz, Magti Energy, Anglo-Oil.*	**Semi-permanent** - Each network lasted until legal measures were threatened against them or until *AES* sold its assets to *RAO-UES.*	**Alternate Force** – Despite Georgia's pro-western rhetoric, the networks propelled business towards Russia.
Bureaucracy – Heads of state firms and government ministries that did not pay tariffs. Members of Ministry of Justice and Parliament.	**Unique** – The configurations of stakeholders depended upon a particular mission and were not set.	**Heterarchical** –There were several intersecting networks, including varied arrangements of networks, all sponsored by the *elite.*
Business groups – Employees of *AES* who diverted funds and equipment.	**Sponsored** – The networks were either directed by, or had the consent of, the *elite.*	**Trans-territorial** – Networks included Armenians, Georgians, Russians, Turkmen, and Turks.
Consumers – Customers who did not pay or tampered with equipment.	**Personalised** - Membership was based on: (1) *nomenklatura ties;* (2) position in the government.	**Grey market** – Joint-stock companies, electricity diversion, misappropriation all done with official cooperation.
	Non-transparent - The names and affiliations of the stakeholders were unknown, until either the *AES* exposed them deliberately or they committed grievous acts.	**Conditional** – Actions based on the strength of personal relations, manipulation of the law, and willingness of the Georgian political *elite* to go against the American company.
	Multi-sectoral - The gas and electricity sector were intertwined.	
	Logical - The Russians wanted to gain control of Georgian assets. The Georgians wanted to enhance profits and placate Russia given contentious political issues.	

Chapter 6: Regional Trans-Territorial Networks

> I have to tell you that in line with its commitments to fight corruption, the Ministry of State Security has sealed and inspected a large number of petrol stations where glaring and outrageous instances of corruption have been uncovered. An operation, which covered hundreds of filling stations, has revealed that representatives of the local administration and law-enforcement agencies or even representatives of the central executive authorities and legislative bodies are behind virtually all of these facilities. This is corruption, genuine corruption (President Shevardnadze giving an interview to Georgian Radio 2003b).

6.1 Introduction

The previous chapter applied the network model developed in Chapter 4 to functional aspects of the energy sector during the Shevardnadze era. It was evident that trans-territorial networks comprised mostly of *elite* and *bureaucratic* stakeholders were responsible for undermining the strengthening of the energy sector. The deficiency in energy supply during the Shevardnadze era served as both a source of paralysis, as well as an enabler. On the one hand, the various schemes employed stifled development and eroded security. On the other hand, the lack of energy supply led to an entrepreneurial society, enriching some and pushing the marginalised majority to find alternative sources of supply. This chapter will add another dimension to the networks, demonstrating how states and separatist regions can be connected along transit corridors composed of stakeholders from the *bureaucracy, business groups,* and *consumers* with the sponsorship of someone from the *elite.* With the centre weak in will and ability to adequately govern the territories of the state, the regions of Georgia provided fertile ground for those wishing to pursue business interests in the energy sector. *Business groups* and local *bureaucracy* were able to take advantage of societal disorientation among the *consumers* due to the collapse of the Soviet system of state support. *Consumers* sought security in family and friendship networks based on ethnic and confessional identities. Thus, networks were particularly strong in rural or outlying areas of Georgia, where the state provisioning of goods and services was minimal, and societal bonds were strong.

Applying the network model, this chapter will examine trans-territorial networks operating in Georgia's energy sector traversing three regions: Abkhazia-Samegrelo, South Ossetia-Shida Kartli, and Javakheti-Armenia (see Map 3 below). By 1995, as a result of violent conflict, Georgia had lost control of 15 percent of its territory (Abkhazia and South Ossetia). Through negligence, the central government had also lost influence in Javakheti, leaving residents to rely on neighbouring states for goods and services. The case studies feature one primary business sector in all three regions: the smuggling of petroleum. In the case of Javakheti, the manipulation of electricity generation and transmission facilities is also discussed. Each region addressed in this chapter has its own particular ethnographic composition, geographical setting, internal and external influences, historical circumstances, and degree of connection and disconnection to the centre. What they have in common is the great extent to which these regions acted as thoroughfares for trans-territorial networks, linking them with neighbouring states in the pursuit of energy resources. In each of the studies below, it will become apparent that what were described by Georgian government officials as 'no-go zones', dominated by 'dangerous forces' as a result of 'frozen conflicts', were areas in which an alternative system controlled by multiple stakeholders operated in heterarchical structures along lucrative transit corridors.

Map 3 - Regions of Georgia

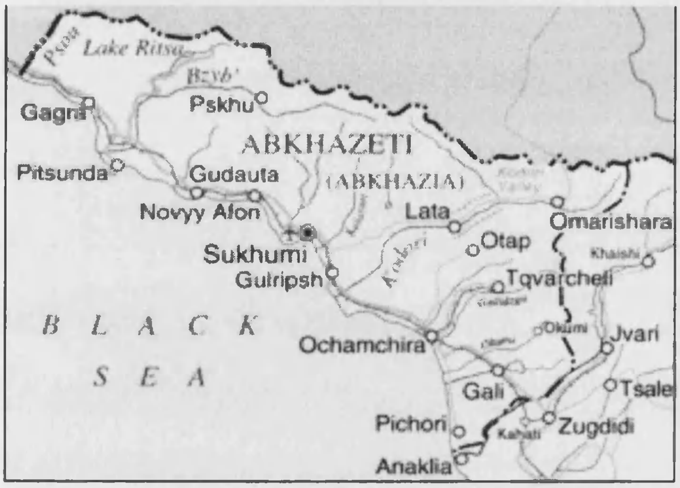
Source: (GlobalSecurity.Org 2006)

6.2 Abkhazia-Samegrelo

Abkhazia is located in the northwest corner of Georgia. Russia borders it to the north and the Black Sea to the west. Under the terms of the Soviet Constitution, Abkhazia was an Autonomous Republic within Georgia with Sukhumi as the administrative capital. The region to the east of Abkhazia is called Samegrelo-Upper Svaneti and its administrative capital is Zugdidi as (see Map 4 below). The region of Abkhazia is a *de facto* state; while it is not internationally recognised as a state, in many ways it functions like the rest of the post-Soviet states (Pegg 1998). In fact, the model developed of the post-Soviet state in Chapter 4 could be applied to both the *de facto* states of Abkhazia and South Ossetia. The conflict with Georgians in 1992-1993 had a significant impact on the formation of the *de facto* state Abkhazia in terms of the demographic shift in population. The 1989 Soviet census counted 17.8 percent Abkhaz (93,267) compared to 45.7 percent Georgians (239,872) (Bronshteyn 1994). While the numbers are politically charged and disputed by the Georgian government, a 2003 census carried out by the Abkhaz counted 45,953 Georgians and 94,606 Abkhaz, with Russians, Armenians, and Greeks totalling 68,476

(United Nations Association of Georgia 2003). Regardless of the exact figures, the trend is that the Georgians lost their majority status and the Abkhaz took over political and economic control of most of the territory.

Map 4 - Abkhazia-Samegrelo Region



Source: (United Nations Cartographic Section 2005)

It is necessary to consider the different motivations behind the activities of *de facto* states such as Abkhazia. Since 1993, residents of Abkhazia had lived under the constant threat that a resurgence of the violence could end in the loss of control over the territory and an exodus. The socio-economic conditions in Abkhazia were more extreme than in the internationally recognised post-Soviet states because of the destruction wrought by the war, the 1996 CIS-imposed blockade on normal economic activity across the *de facto* borders, and the limitations placed on international assistance. In general, the combination of political determination to survive and deep economic weakness in the *de facto* state produced a subsistence syndrome among the citizens (Lynch 2002: 842). This was characterised by the dependence of the *elite, bureaucracy, business groups* and *consumers* on the grey economy, often under the protection of private security forces. The propensity to create networks was strong, but the networks tended to be semi-permanent and conditioned on fluctuating political and economic factors. Ultimately, trans-territorial networks were a means for the survival of the *de facto* state.

Reliable economic data for *de facto* states is difficult to obtain and there are only five studies that include data on Abkhazia's budget. These include a United Nations Development Programme Needs Assessment Mission report of 1998 (United Nations Development Programme 1998), a report by the Georgian Parliamentary Budget Office in 2001 (Gotsiridze 2001), a chapter in a 2004 book by International Alert on the war economies of the Caucasus (Chkhartishvili, et al. 2004), a 2004 study on smuggling in Abkhazia and South Ossetia by the Transnational Crime and Corruption Centre (Kukhianidze, et al. 2004), and a report by the International Crisis Group on the way forward in the Abkhaz-Georgian conflict (International Crisis Group 2006). Abkhazia's GDP in 2001 was estimated to be about US$ 70-80 million or US$ 350 dollars per capita per annum, on a par with the lowest tier of states in the international community. The state budget was US$ 7.2 million in 2001; too small to sustain the residents of Abkhazia (Gotsiridze 2001: 23). In 2005, state revenues were reportedly US$ 27 million (US$ 9.3 million from customs collected on the Russian border) and the state budget was US$ 34 million (International Crisis Group 2006). Abkhazia's energy situation was also dire; petrol had to be imported, there was no access to natural gas, and electricity supply was irregular due to the state of disrepair of *InguriHES* (see Chapter 5). Abkhaz officials listed the most substantial sources of income as customs on the Russian border, railroad tax from Sochi (Russia) to Sukhumi (Abkhazia), wood exports to Turkey, Russian tourism, and selling foodstuffs in Russia.[1] In general, the Akhbaz government was reliant on financial assistance from Russia, remittances from Abkhaz working in Russia, and trade in the grey market.

By 2001, the Abkhaz territory was split into zones of influence controlled by different business interests. Groups formed to move commodities in and out of Abkhazia and their alignment changed over time. The western Abkhazia group had control over the oil, food, and tobacco shipments and cooperated with the Russians in transporting goods over the Psou River by motor and railway. The Gagra group (mainly the Armenian Diaspora)

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[1] Interviews with Giorgi Artoba, *de facto* Deputy Minister of Foreign Affairs and Konstantin Tuzhba, Minister of Finance, Abkhazia, Georgia, July 2003.

was involved in illegal drug production. The Gadauta group (Abkhazians) controlled the export of products to Georgia mostly through the Gali region. The Chechens controlled the eastern part of the self-declared republic, the Sukhumi railway station and main transportation routes, and the cargo movement on the northern half of the Georgia-Abkhazia border. The Abkhaz authorities reportedly struggled to control these groups, which were sponsored by individuals in positions of power. In addition, they allowed the illegal activities to continue in exchange for the groups gathering operative information on the Georgians living and operating in eastern Abkhazia (Grunin, 2003).

The Ardzinba family, like the Shevardnadze family, was at the centre of the *elite* in Abkhazia for much of the first decade of its *de facto* independence and the family controlled much of the grey market activity. The president of Abkhazia from 1994-2005, Vladislav Ardzinba had been a member of the Soviet parliament of the Autonomous Republic of Abkhazia prior to the disintegration of the Soviet Union. Like President Shevardnadze's family, Ardzinba's family was deeply involved in the economy and had a monopoly over most industries.[2] His daughter, Madina Ardzinba, was involved in the tourism industry. His daughter's husband, Alkhas Argun, was in charge of the mobile telephone sector and his nephew, Levan Ardzinba, had a lucrative petroleum smuggling business. Another relative, Zurab Ardzinba, was in charge of Sukhumi port and Zurab's brother, Aka, had a major role in petroleum smuggling. Zurab imported the petroleum from Russia by ship and it was moved by Aka's trucks to the Samegrelo region of Georgia. Levan Ardzinba was the primary interlocutor with Georgian authorities in the petroleum business, but he was assassinated in September 2004 (Kukhianidze, et al. 2004: 30). The President's relative, Pavel Ardzinba, controlled timber manufacturing and export. Pavel, together with Genadi Gagulia and Ruslan Ardzinba, another relative of the President, were thought to be the *krisha* of much of the economic sector in Abkhazia for the decade of Ardzinba's presidency.

[2] Interview with Liana Kvarchilia, Programme Coordinator for the Centre for Humanitarian Programmes, Abkhazia, Georgia, July 2005.

In 1996 the CIS imposed an embargo on Abkhazia, and this was a major factor leading to the primacy of the grey market in the region. The embargo permitted direct import only of food products, medical supplies, petrol, and household items. A licence from the Georgian government was required for everything else. It also prohibited participating governments from establishing contact with representatives of Abkhazia and forbade financial and military support to Abkhazia (Chkhartishvili, et al. 2004: 134). To circumvent these restrictions and to compensate for the poor state of the economy, the Abkhaz resorted to trade along undetected or illegally sanctioned passageways, including the *de facto* borders with Georgia over the Inguri River and with Russia over the Psou River, as well as its seaports. Keeping trade in the grey economy eliminated the need for a licence and the payment of taxes and customs fees. Bribes also facilitated a cheaper and more efficient transaction than that established by low-waged state officials (Gotsiridze 2001). One expert estimated that activity in the grey economy between the Abkhaz and Georgians accounted for half of the Abkhaz economy.[3] The Georgian Mission to the United Nations suggested that by 2002 there was actually little real evidence of an economic blockade of Abkhazia. The reality was that Russian and Turkish companies were investing in Abkhazia. Moreover, most goods were allowed into Abkhazia without documents from Tbilisi, because Georgian stakeholders were operating lucrative trade corridors across the *de facto* Georgian/Abkhaz border, demarcated by the Inguri River.[4]

The 1994 Moscow Agreement on Cease Fire and Separation of Forces established the CIS Peacekeeping Force (CISPKF) of 1,650 Russian soldiers, responsible for cooperating with the Abkhaz and Georgians on the respective sides of a security zone divided by the Inguri River running from the Black Sea north about 70 kilometres to upper Gali region (Georgian and Abkhaz Authorities 1994). United Nations Security Council Resolution 937 of July 27, 1994 authorised the UN Observer Mission in Georgia (UNOMIG) to verify the implementation of the 1994 Moscow Agreement, observe the operations of the

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[3] Interview with Paata Zakareishvili, Independent Political Analyst, Tbilisi, Georgia, June 2003.
[4] Interview with Gorcha Lordkipanidze, Deputy Head of Mission, Georgian Mission to the United Nations, New York, USA, April 2003.

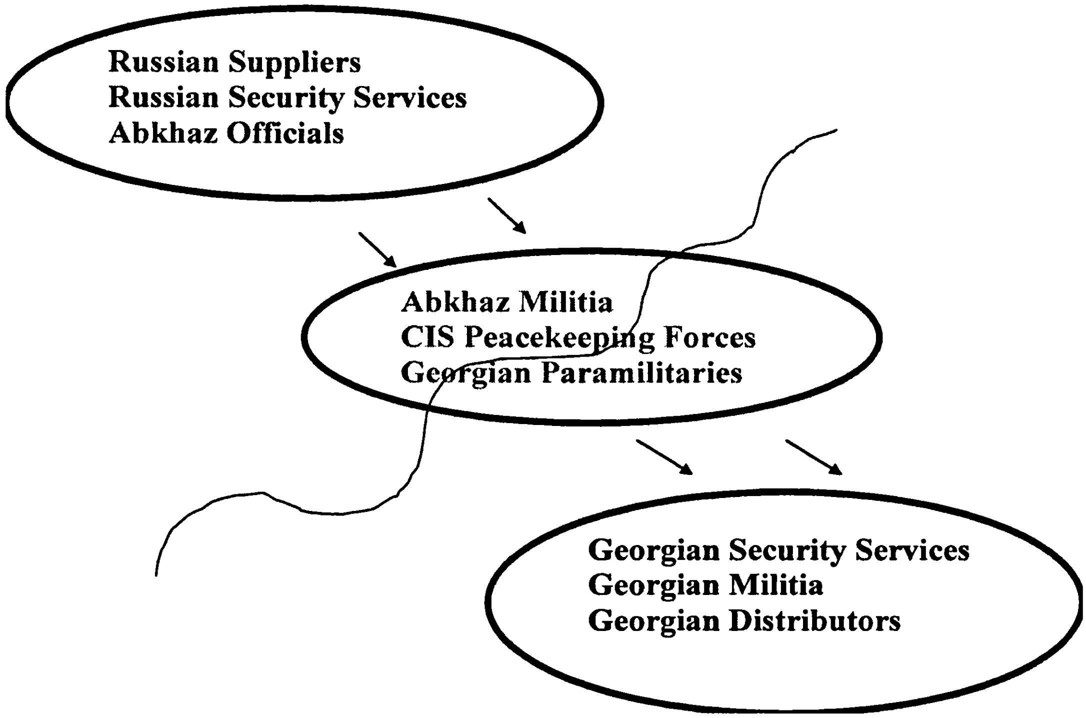
CIS peacekeeping force, and verify that troops and banned weapons did not enter the security and restricted weapons zone (United Nations Security Council 1994). The UN was also tasked with patrolling Kodori Valley, an area to the north of Gali not included in the security zone that sometimes became the site of low intensity conflict between Georgian and Abkhaz forces.

However, the CIS peacekeepers and the UN observers could neither prevent, nor even collect enough information to report objectively on the smuggling operations. The Inguri River was 70 kilometres long and could be crossed in numerous places when the water level was low, particularly in the dark of night. The Georgian-Abkhaz networks were complex, including members from all four groups of stakeholders on either side of the Inguri River (see Figure 6). The stakeholders included government authorities, armed forces, law enforcement authorities, peacekeeping forces, private militias (paramilitaries), criminals, and local residents as go-betweens (Kukhianidze, et al. 2004: 6). This last group were most often composed of internally displaced persons (IDPs), who had been living in Abkhazia at the time of the war and had returned to the eastern Gali region (approximately 35, 000) or who now lived in the neighbouring Georgian region of Samegrelo and its administrative capital Zugdidi (approximately 40,000) (UNHCR 2002).

A 2001 UNOMIG report described the security situation on the *de facto* border as follows, 'While partisan activities continue to be of concern, the main threat [...] is the high level of criminality in the area of conflict and the inability of local law enforcement agencies to deal with the problem effectively.' It went on to explain that the Abkhaz law enforcement authorities did not control the lower Gali security zone and the Georgian authorities did not control the upper Kodori valley (United Nations Security Council 2001b: 3). Georgian security services in the region only earned US $7 per month and supplemented this by working with the Abkhaz authorities (Korsaia, et al. 2002). Disputes occurred among various Georgian groups regarding control over the contraband trade. The Ministry of State Security of Georgia routinely accused Georgian militias and vice versa of being involved in smuggling (Civil Georgia 2002). Thus, the Ceasefire-

Line (CFL) actually became a competitive market for various Abkhaz and Georgian forces vying for the spoils of trans-border trade.

Figure 6 - Inguri River Smuggling Trans-territorial Network



The trans-territorial petroleum networks originated in Russia, continued through Abkhazia to the Gali region and were joined by Georgians in Zugdidi districts and onto Tbilisi (Ministry of Internal Affairs of Georgia 2003). Petroleum entered Abkhazia over the River Psou, crossing at the Russian border, or by ship to the Abkhaz ports of Sukhumi, Ochamchire, Gagra, and Gudauta. It originated from Russia, Romania, Turkey, and Bulgaria. Smuggling was made easier after 1999, when Russian President Putin signed a decree in September 1999 cancelling all previous documents concerning the restriction of the border crossing at the Psou River. This rescinded both in principle and practice the CIS economic blockade (Diasamidze 2003). According to the Georgian State Department of the Secret Services, petrol was also shipped from Sochi to Sukhumi in railway tankers belonging to the Russian peacekeeping forces. It is reported that Abkhazia imported more than 8,000 tonnes of petroleum products from Russia monthly and an additional 1,000 tonnes from Turkey (Chkhartishvili, et al. 2004: 137). Approximately 2,000 to 2,500 tonnes per month or 5 to 6 percent of Georgia's overall contraband fuel transited Abkhazia (Kukhianidze, et al. 2004: 38).[5] Petrol arrived in the Samegrelo region in 20 ton tanks, approximately 2 to 3 times per week and was distributed to local stations (Kukhianidze, et al. 2004: 15).[6] It should be noted, however, that smuggling of petroleum through the separatist regions provided only about 18 percent of Georgia's total annual consumption – approximately 5 percent through Abkhazia and 13 percent through South Ossetia (Kukhianidze, et al. 2004: 7). However, it was the collusion of stakeholders, the seemingly counterintuitive relationships that developed among supposed enemies, and the violence that accompanied this business that made these routes particularly relevant for this study.

The formation of the trans-territorial networks began in the early 1990s. In the lead up to the war between Georgians and the separatist forces in Abkhazia and South Ossetia, motley gangs of approximately 50 to several thousand people created irregular armed formations as private militias (groups forming the armed wings of political organisations) and paramilitary groups (armed units loosely affiliated to but possessing considerably autonomy from state structures) (Demetriou 2002a). Zurcher argues that these armed formations, unrestrained by the weak state, became 'entrepreneurs of violence' and triggered the violence in Abkhazia in order to control their business assets (Zurcher 2005). During the war, these armed formations and criminal groups - which were sometimes linked - took control of local administrations within Georgia and the separatist regions. As a result, economic transactions were dominated by 'coercion-backed extraction and large-scale protection rackets, accompanied by violence and the disintegration of law and order' (Demetriou 2002a: 29). In the aftermath of the conflict, the economic situation fostered an environment in which it was hard to discern the difference between the armed forces, police and private armies, paramilitaries, and militias (bandits or gang formations). Those forces involved in counter-insurgency

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[5] Information from Kukhianidze's interview with an officer of the Ministry of State Security of the Government of Abkhazia in Exile, Tbilisi, Georgia, 2003.
[6] Information from Kukhianidze's interview with Ministry of State Security of the Government of Abkhazia in Exile, Tbilisi, Georgia, 2003.

operations and illegal commercial activities overlapped to some degree (Fairbanks Jr 2002).

By 1995 two of the three main Georgian armed groups operating in Abkhazia — *Forest Brothers* led by David Shengelia (formerly of *Mkhedrioni)* and *White Legion* headed by Zurab Samushia — had slowed down their counter-insurgency operations and were more involved in commercial activities as *business groups* (Billingsley 2001). They had established links to Abkhaz authorities, security services, and law enforcement agencies to transit goods across the Inguri River. The *Forest Brothers* were by far the most active group in smuggling, while the *White Legion* was more notorious for instilling fear in the Abkhaz community (Kukhianidze, et al. 2004: 23). In Kodori Gorge, there were three paramilitary groups — *Monadire, Svaneti*, and *Khevsureti* — operating under the control of the Georgian government. The group *Monadire* or 'Hunter', led by Emzar Kvitsiani, included a 200-man battalion and operated criminal rackets in the area (Socor 2006c). President Shevardnadze appointed Kvitsiani as his representative in the Kodori Gorge.[7] *Zviadists* still allegiant to the deposed first president of Georgia, Zviad Gamsakhurdia, allegedly operated in the Tsalenjikha district of Georgia neighbouring Gali. There were also other Georgian armed groups, such as the *Patriots' Union* that operated out of Zugdidi, as well as armed paramilitary groups in the regions of Samegrelo. Finally, there were splinter groups as well as 'copy' groups, who called themselves guerrillas but were in fact private security groups protecting politicians' business interests.

Given the non-transparent, semi-permanent, and highly personalised nature of the networks, it is unclear who acted as the main sponsor or how the financial gains were divided among the stakeholders. On the Georgian side, petroleum smuggling was allegedly organised and controlled by the *bureaucracy*, in particular local departments of the Georgian Ministry of State Security with the participation of other law enforcement

[7] Interview with David Darchiashvili, CIPDD, Tbilisi,Georgia, July 2003. He also explained that *Monadire* cooperated with an infamous 'thief-in-law', Tariel Oniani from the neighbouring Georgian region of Svaneti. Oniani contributed to the release of UN officials kidnapped in the Kodori gorge in 2001 and subsequently left for Spain. After the police failed to arrest Oniani in Spain in the summer of 2005, an international warrant was issued against him. He is reported to be in Russia.

agencies and Georgian guerrillas. In discussions during 2003 to 2005, Georgian experts suggested that some Georgian groups were paid by the Abkhaz Ministry of Interior and State Security to cooperate with them in transiting goods, while others suggested that they worked for themselves, and still others suggested that the various groups were proxies for the Georgian armed forces in their efforts to destabilise Abkhazia. Abkhazia's Deputy Minister of Foreign Affairs admitted that trade between the Abkhaz and Georgians was substantial and linked the Georgian parties, including the *White Legion* and *Forest Brothers*, to Georgian government 'security services', which he labelled 'terrorists.' Further, he thought that many of the local Georgian groups did not have direct support from Tbilisi, but instead operated locally for business purposes, controlling the markets based on their level of influence in a particular village.[8]

The *elite* providing sponsorship for such activities are variously named. One influential stakeholder in the trans-territorial networks was the Abkhaz Government-in-Exile, composed of Georgians who had fled Sukhumi during the war and were headquartered in Tbilisi. From 1994 to 2004, they were led by Tamaz Nadareishvili, a member of Shevardnadze's *elite,* who was a member of the National Security Council.[9] According to Nadareishvili, he would only engage in economic relations with the Abkhazians when the region was once again under the jurisdiction of Georgia. In an interview, he said that he sympathised with the Georgian 'partisan' activities in Abkhazia, but he denied that these groups were engaged in trade across the Inguri river. He explained that the Russian peacekeepers and Abkhaz law enforcement agencies conspired to rob and kill Georgian residents of the Gali region and that the 'partisans' were there to ensure their safety.[10] However, those who were knowledgeable about the activities of the Special Forces of the Ministry of State Security of the Abkhaz Government-in-Exile, located in Zugdidi, believed that this organisation sponsored the trans-Inguri trade. In particular, the forces

[8] Interview with Giorgi Artoba, *de facto* Deputy Minister of Foreign Affairs, Abkhazia, Georgia, July 2003.
[9] With the support of the Georgian state, the Abkhaz Government-in-Exile formed a state-like administration and bureaucracy numbering 5,000 people, including a military directorate, tax authority and a police force, as well as several designated seats in Parliament. They also had security forces stationed in the Samegrelo region.
[10] Interview with Tamaz Nadareishvili, President, Abkhaz Government-in-Exile, Tbilisi, Georgia, July 2003.

provided political and financial support for the activities of some of the groups in the trans-territorial networks. Other stakeholders named as providing support for the trans-Inguri trade were the Georgian Tax Department and politicians in Samegrelo led by the powerful governor, Bondo Jikia. Finally, several Members of Parliament representing districts in Samegrelo who owned the petrol stations in the region had a stake in selling contraband products.[11]

The best explanation of these networks is provided in an in-depth study on smuggling through Abkhazia and South Ossetia:

> Smuggling is impossible if there are no criminal networks that link different crime groups with corrupt law enforcement officers and government officials [...] these groups collaborate with each other regardless of their ethnic origins and political orientation. They have different, sometimes paradoxical partnerships with other crime groups, law enforcement bodies, and governmental structures (or individual government officials) [...] Importantly, all links of this intricate network must be in place, for if smugglers lose even one link, the entire smuggling process stops [...] All main actors (law enforcement bodies, crime groups, and Russian peacekeepers) especially in the Gali and Zugdidi regions and in the Ergneti [South Ossetia] market, along with their links to other groups or individuals, compose a successful smuggling network that operates with near impunity and increasingly expands its influence by involving more and more poor people in the contraband trade (Kukhianidze, et al. 2004: 21).

The mixing of forces, duties, allegiances, politics, business, and crime resulted in a violent combination. Violence in the form of assassinations and kidnappings occurred when the sides did not agree on the division of spoils (Khubutia 2003). This violence was at its worst in the Gali region of Abkhazia and neighbouring Samegrelo in Georgia, where various Abkhaz and Georgian security forces, official and unofficial, were stationed for the protection of the citizens living there (mostly Georgia), but, in fact, used their positions to destabilise the other side, as well as to protect their part in trans-territorial smuggling networks. Georgians and Abkhaz forces maintained a low intensity conflict throughout 2001, including incidences of shooting, killing, abducting, mine

[11] Interview conducted off-the-record with Member of Parliament for Zugdidi, Tbilisi, April 2003.

blasting, ambushing, and robbery. There were major outbreaks of violence in 1998 and 2001 that threatened to trigger a resumption of hostilities. In May 1998, there was a sharp rise in activity by Georgian paramilitary units in western Abkhazia. This led to clashes with the Abkhaz militia and an unsuccessful attempt by Georgia to seize the Gali region, which resulted in some 30,000 mostly Georgian residents being displaced (United Nations Secretary General 1998). Again in April 2001, a conflict over smuggling between the *Forest Brothers* and Abkhazian separatists resulted in violence. Allegedly, the Abkhaz captured a vehicle loaded with contraband arms and ammunition belonging to the Georgian partisans. In their attempt to seize the goods, the Abkhazians reportedly killed two Georgians and captured three hostages. The Georgians, in turn, captured five hostages and took them to the Zugdidi area. Through UN mediation, the conflicting parties reached an agreement and hostages were exchanged (United Nations Security Council 2001a).

The Georgian authorities attempted to curb petroleum smuggling from Abkhazia. Georgian Presidential Decree No. 434 of July 12, 1999 required a Special Freight-Customs Declaration (SFCD) to import products into Georgia (Kukhianidze, et al. 2004: 55). The transportation, storage, and sale of imported and locally produced petroleum products required a SFCD. Subsequent regulations established by the Georgian Customs Department permitted the import of petroleum from Russia into Georgia only at the Kazbegi checkpoint on the Military Highway. In 2000, the Ministry of Tax Revenues of Georgia added Gori customs to Kazbegi. The Government of Georgia even created an armed unit under the Ministry of Tax Revenues to deter smuggling into Georgia (Kukhianidze, et al. 2004: 55).

However, by the early 2000s, the territory encompassing Zugdidi (the administrative centre of Samegrelo) and Gali had become a lawless zone. The competing interests of Abkhazian separatists and Russian peacekeepers versus armed groups and Georgian law enforcement bodies in controlling and profiting from contraband kept the region unstable. In the first two months of 2003, there were 13 major crimes and three high-profile murders in the Samegrelo area. According to the Chief of the Samegrelo Office of the

Ministry of Security, Gogi Nachkebia, 'In most of our investigations of these incidents we've come to the conclusion that both Georgian and Abkhaz smugglers are involved' (Khubutia 2003). Georgia's non-recognition of the territorial boundaries of Abkhazia was used by the Georgian government as the primary reason for the absence of prosecutions against known criminal forces, including law enforcement agents. Compared to the volume of illicit traffic, there were relatively few criminal proceedings. In the Samegrelo region just across from Abkhazia, for example, the number of cases of reported customs violations was 0 in 2000, 0 in 2001, 2 in 2002, and 12 in 2003 (Ministry of Internal Affairs of Georgia 2003: 8). Thus, despite decrees and rhetoric, the cycle of collusion and conflict between the Abkhaz and Georgians continued.

6.3 South Ossetia-Shida Kartli

South Ossetia is located on the southern foothills of the Caucasus mountain range in northern Georgia, seperated by the mountains from its northern neighbour North Ossetia just across the Russian border (see Map 5 below). Under the terms of the Soviet Constitution, the South Ossetian Autonomous Republic was part of Georgia and consisted of the four districts of Tskhinvali (the administrative capital), Akhalgori, Java, and Znauri. South of this region is the Georgian area known as Shida Kartli with Gori as its administrative centre. Like Abkhazia, the region of South Ossetia functions as a *de facto* state. In 1992 the Ossetians, with the help of volunteers from the other autonomous republics of the North Caucasus, claimed control of most of South Ossetia and, after a short war against Georgia, a ceasefire agreement was signed in June followed by population exchanges. During the war, 60,000 ethnic Ossetians were displaced, 40,000 of them fleeing to North Ossetia. The population is estimated to have dropped from the pre-war 100,000 to 70,000 with approximately 17,000 Ossets staying in North Ossetia.[12]

[12] North Ossetia is the most economically viable economy in the northern Caucasus, with factories producing metals, electronics, chemicals, alcohol, and processed foods.

Map 5 - Map of South Ossetia

Source: (International Crisis Group 2004c)

After the cease fire, Tbilisi maintained control of part of Akhalgori and several isolated ethnic Georgian villages comprising less than one-third of South Ossetia's total population (Office for the Coordination of Humanitarian Affairs-Georgia 2003: 1). Under the auspices of the Organisation for Security and Cooperation in Europe (OSCE), a Joint Control Commission (JCC) of Russians, Georgians, and Ossetians was created to monitor the conflict zone. In October 1994, a quadripartite agreement was signed, which divided Ossetian participation in the JCC into North and South, and elaborated on the steps towards a peaceful resolution of the conflict. After the war, relations between the Ossets and Georgians were better than between Abkhaz and Georgians due to several factors. These included the lower scale of conflict and casualties during the war, the co-existence of the two groups in villages, and greater economic cooperation. Some economic cooperation was restored between Tbilisi and Tskhinvali in the public and private sectors and some Georgian refugees returned to their homes (Darchiashvili and Tevzadze 2003).

The first *de facto* leader of South Ossetia was Ludwig Chibirov, who had chaired the Supreme Soviet in South Ossetia since 1992. During his administration, law and order collapsed and the region degenerated into heavily armed banditry. The absence of central control over the region, the loss of the South Ossetian government's authority, and the region's contiguity to the Russian Federation allowed for organised criminal activity, specifically smuggling (Hansen 1998; MacFarlane, et al. 1996). In 2001, Eduard Kokoity replaced Chibirov. Kokoity had worked as a businessman in Moscow since 1992 and, prior to that, had been the First Secretary of the Tskhinvali branch of the *Komsomol*. President Kokoity's 2001 electoral victory was due in great part to support from Albert Tedeyev, whom he named as his National Security Advisor. His brother, Jambulat Tedeyev, had financed Kokoity's presidential campaign. Tedeyev is related to Chibirov on his mother's side of the family and had previously supported Chibirov until he tried to diminish the power of Tedeyev's group. Kokoity proved to be more successful in this effort, issuing a decree in July 2003 sacking Tedeyev, as well as the Minister of Defence, Minister of Security, and Minister of Justice. He disbanded the intelligence and the security departments within the Defence Ministry, ordered the paramilitaries to disarm, and took over responsibility for customs. All of those sacked had held powerful positions in South Ossetia since 1992 and had been part of the Tedeyev group (Liklikadze 2005).

South Ossetia was a poorer region than Abkhazia, with far fewer natural resources, only one major crossing connecting it to North Ossetia, and two trading partners — Russia and Georgia. Estimates put South Ossetia's GDP at US$ 15 million or US$ 250 per capita per annum (US$ 100 less than Abkhazia) (Dzhikaev and Parastaev 2004: 194-195). Residents existed on subsistence agriculture, remittances from family working in Russia, and small-scale trade. Customs duties at the Roki Tunnel pass on the border with North Ossetia provided most of South Ossetia's state revenues. The Roki Tunnel is on the TransCam transportation corridor, which runs north from Vladikavkaz (Russia) through the tunnel and south to Tskhinvali on the way to the rest of Georgia. An estimated 62 percent of all South Ossetia's budgetary income came from the TransCam transportation corridor and more than one-third of the entire population was dependent on salaries from the government (Dzhikaev and Parastaev 2004: 194-195). From 1999 onwards, the South Ossetian government compensated for minimal revenues by borrowing from Russia. South Ossetia bought natural gas from the Georgian pipeline and was tied into Georgia's electricity grid. However, as with the rest of Georgia, South Ossetia suffered from the irregular gas and electricity supply, and gradually the authorities integrated into North Ossetia's electricity system, as well as relying on burning wood for heat (Caucasus Foundation 2006). Demand for petroleum became the means for a lucrative trans-territorial network along the TransCam.

After the declaration of the ceasefire in 1992, trade developed spontaneously on neutral territory between Tskhinvali and the Georgian-controlled villages in Gori. Between 1993 and 1997, profits from the petroleum trade averaged between 250-300 percent (Dzhikaev and Parastaev 2004: 199). The success of this trade was based initially on the large number of mixed marriages between the Georgians and Ossets, which helped to cultivate post-war entrepreneurial relationships based on friendship and family ties (Dzhikaev and Parastaev 2004: 199). By 1999, this trade, which took place mostly among *consumers* out of the necessity to survive, had developed into a more structured and profitable business for members of the *bureaucracy* and *business groups*. The ability to transit freely along the TransCam transportation corridor was enhanced by the refusal of Georgian authorities to establish border guard and customs service checkpoints on the border with Russia (Kukhianidze, et al. 2004). Further, Georgian legislation did not require that the goods transiting South Ossetia should be registered with customs officials, as the goods were not 'officially' imported (Kukhianidze, et al. 2004: 19). The result was a managed, secure, duty free corridor for the transit of goods between Russia and Georgia that had its main hub in an area outside the village of Ergneti in South Ossetia.

The flow of goods across the Russian border through South Ossetia to Georgia was considered illegal as a result of Russian customs officials extracting bribes, plus the restrictions imposed by the Government of Georgia on the types of commerce that were considered legal. However, it was possible to pre-pay bribes and arrange for unfettered transit along TransCam. Russian military vehicles used TransCam to move personnel and goods through Ossetia to their military bases in Georgia without undergoing inspection by Georgian security services.[13] As one expert reported,

> the crossing between South Ossetia and Georgia is open with only the most superficial semblance of control by the authorities on either side under the watch of the (mainly Russian and North Ossetian) peacekeepers. It is an open secret that the profits are shared with politicians on all sides, and with the peacekeepers (Vaux 2003).

The most lucrative of the trans-territorial networks were those composed of Russians, Georgians, and South Ossetians operating between Tskhinvali, South Ossetia, and the Georgian regions of Shida Kartli and Kvemo Kartli. The network chain included stakeholders from the *elite, bureaucracy, business groups,* and *consumers.* The stakeholders' professions ranged from former members of paramilitaries who had fought in the war, to law enforcement bodies, governing structures, armed forces, private entrepreneurs, and a broad social base of the population (e.g. IDPs, refugees, and people living in the conflict zone). The petrol chain usually included stakeholders from the *bureaucracy,* such as customs, border guards, police, state security, and the tax administration.[14] On the Georgian side, an *elite* grouping of Nugzar Shevardnadze, the Georgian Minister of Interior and the Ministry of Transport, controlled the heaviest trade of petroleum. In 2004, President Saakashvili's Minister of Interior named his

[13] Interview conducted off-the-record with Georgian familiar with Ergneti market, April 2005, Tbilisi.
[14] Interview with Vano Nakaidze, Director, Group of States Against Corruption (GRECO), American Chamber of Commerce, Tbilisi, Georgia, August 2003.

predecessor, Koba Narchemashvili, and former Shida Kartli Governor, Davit Koblianidze, as the two main Georgian government officials who had sponsored the operation of TransCam trade during the last years of the Shevardnadze era (Freese 2005b: 110). Another source mentioned three senior Members of Parliament and the Deputy Governor of Shida Kartli as being in control of the market (Areshidze 2002).

Political and economic power in South Ossetia remained in the hands of a few stakeholders who operated in the grey economy, particularly those who controlled the trade and transport in and out of the Ergneti market (Dzhikaev and Parastaev 2004: 184). Lokha Chibirov, the son of the former President of South Ossetia, controlled the Ossetian part of the Ergneti market. Liangi Chavchavadze, a former official of the Ministry of Internal Affairs, controlled the Georgian part of the market (Kukhianidze, et al. 2004: 19). Georgian law enforcement officials provided security for the transit corridor into Georgia. A company was created for safe freight delivery of goods – 'Express Service Ltd' - controlled by the nephew of Chavchavadze. As in Abkhazia, there were also criminal groups that operated in the region, the most infamous of which was *Robota,* composed of 40 members residing in the Georgian-Ossetian conflict zone. This group's *krisha* was named by Georgia's State Minister, Avtandil Jorbenadze, to be a collection of officials in the Georgian State Chancellery (Freese 2005b: 110). There were also remnants of paramilitary groups that had fought for Georgia during the war, but were now engaged in trade on the TransCam. These included the *White Eagles, White George, White Falcons, Black Panthers,* the *Kutaisi National Guard,* and the *Merab Kostava Society* (Helsinki Watch 1992: 20-21). On the South Ossetian side were former members of the Republican Guard, established in November 1991, consisting of 2,400 men at the time of the conflict (Helsinki Watch 1992: 20).

According to the Georgian Ministry of Finance, illegal fuel products entering Georgia's market amounted to approximately 5,000 tonnes per month. Of this, fuel products transiting through Ergneti amounted to 7.7 percent of monthly consumption and 13 percent of all illegal fuel traffic into Georgia (Kukhianidze, et al. 2004: 41-42). At its peak, the average monthly transport of petroleum flowing through South Ossetia was estimated to be between 2,800 to 3,400 tonnes per month, worth roughly US$ 840,000 to US$ 1.26 million. The average monthly transport of diesel transiting South Ossetia ranged from 4,000 to 6,000 tonnes, worth between US$ 950,000 and US $1.45 million profit. The amount of natural gas in condensed form for shipment in tankers transiting South Ossetia averaged between 420 and 800 tonnes monthly, worth up to US$ 140,000 (Dzhikaev and Parastaev 2004: 201). One estimate of total combined petrol, kerosene, diesel, and oil products smuggled through Ergneti was as high as 1.4 million tonnes annually. According to Georgian tax authorities, up to 150 vehicles moved from the Ergneti market in the direction of Tbilisi daily, carrying half a million US dollars worth of smuggled goods (Gotsiridze 2001). An expert estimated that two runs of taxi drivers with 1,000 litres of petrol departed daily from Ergneti market towards Tbilisi.[15] One observer noted that along the Georgian road leading into Ergneti over 100 oil tankers stood alongside a 1 kilometre stretch.[16] Large fuel deliveries were known to be made at night and could be unloaded into underground pipelines that ran a kilometre to a Georgian petrol station (Areshidze 2002).

The paths of petroleum smuggling were semi-permanent, remaining dynamic over time. This was due, in part, to the stakeholders' efforts to deter detection. The stakeholders created artificial shortages in supply from one direction in order to gradually shift to another transit corridor, resulting in a rush on demand and increased profits.[17] In 1998, changes in Georgia's tax system made the price of officially traded petroleum from Russia into Georgia increasingly more expensive, particularly as world prices rose after 1999. The law enforcement agencies tracked, to some extent, the inflow of petroleum into Georgia. If, for example, the average spot price for illegally imported petrol was US$ .15 per litre, the price of legally imported petrol was twice that, providing a 50 percent profit for the stakeholders. Thus, favourable economic conditions for smuggling petroleum into Georgia from Abkhazia and South Ossetia resulted in an increase in

[15] Interview with Vano Nakaidze, August 2003.
[16] Interview with Lord William Wallace, Professor (Emeritus) London School of Economics and Member of the House of Lords, London, UK, 2004.
[17] Interview with Vano Nakaidze, August 2003.

volume of smuggling from 1998 to 2000. However, by 2001 petroleum smuggling had shifted to Red Bridge on the Azerbaijan-Georgia border.

Starting in 1999, there was an effort by the Georgian government to impose customs tariffs on freight originating from Tskhinvali into the neighbouring region of Shida Kartli. However, collusion between Georgian law enforcement bodies, customs officials, and politicians was so endemic that the mechanism failed to operate effectively (National Security Council of Georgia 2001: 18). In 2002, the level of criminality in South Ossetia was on the rise and the European Union proposed establishing joint customs and taxation regimes with the proceeds from TransCam going to the population. In exchange for agreement to this regime from the South Ossetian authorities, the EU would initiate a 2.5 million Euro rehabilitation of the roads. However, the South Ossetian authorities did not agree to the plan, expressing concern that the programme would impede the sovereignty of the territory (Office for the Coordination of Humanitarian Affairs-Georgia 2003: 2). By 2003 the illegal trade was crucial to South Ossetia's existence; the market provided most of South Ossetia's employment, financial transactions, GDP, and state revenue. On the other hand, lost revenue to Georgia from smuggling through South Ossetia was estimated to be around US $10-12 million per month, or nearly half of Georgia's budget (Areshidze 2002). At the same time, there was an increase in the level of violence between factions vying for control of trans-territorial smuggling and a breakdown in the credibility of the JCC because of its inability to deal with it. Thus, Georgia had more to lose from its continued participation in the TransCam smuggling corridor, and yet the Georgian stakeholders did not curb their activity until directed to by President Saakashvili in 2004.

6.4 Javakheti-Armenia

Javakheti is situated in the Samtskhe-Javakheti region southwest of Tbilisi, bordering Turkey and Armenia to the south (see Map 3 above).[18] Javakheti lies at the crux of two

[18] A part of the material on Samskhte-Javakheti was originally included in a conference paper I co-wrote with Eka Metreveli, 'Energy Networks Across a Weak State: the Case of Samskhte-Javakehti', Central

emerging, competing trade routes: the east-west corridor connecting Central Asia to Europe and the north-south corridor from Moscow through Yerevan to Tehran. The Samtskhe-Javakheti region is composed of six districts: Borjomi, Adigeni, Akhaltsikhe, Aspindza, Akhalkalaki, and Ninotsminda. The administrative headquarters are in Akhaltsikhe. The political administration of the majority Armenian populated Javakheti province encompasses the districts of Akhalkalaki and Ninotsminda. According to the electoral register, 95.3 percent of the inhabitants of Ninotsminda and 93.6 percent of those who live in Alkhakalaki are Armenians (Antonenko 2001a). There is one border crossing from the Javakheti region to Armenia (Bavra) and one with Turkey (Vale). Unlike Abkhazia and South Ossetia, this region did not have a special administrative status during the Soviet Union. However, as with Abkhazia, there was a Russian military base in Javakheti.

During the Shevardnadze era, Javakheti was economically, politically, and linguistically isolated from the rest of Georgia and this posed numerous challenges for centre-periphery relations. The isolation of Javakheti was due to at least four factors: the Cold War legacy of serving as a 'secured territory' sharing a 78 kilometre border with NATO (Turkey), poor transportation routes, lack of central government integration programmes for ethnic minorities, and calls for autonomy by local political groups. Despite the lifting of the restricted access to the territory at the end of the Cold War, the isolation and limited civilian infrastructure continued to define the region. While several important transportation and railway routes connected the region with Tbilisi to the north, Yerevan to the south, and Batumi on Georgia's Black sea coast, most routes were inefficient. The local population accused the central government in Tbilisi of deliberately isolating the majority ethnic Armenians in Javakheti. The province's isolation was also due to its ethnic composition, which was determined mostly by politically motivated forced migration of various ethnic and religious groups over the past two centuries. By 1990 the Samtskhe-Javakheti region was composed of Orthodox Christians, Roman Catholics,

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Eurasian Studies Society, Bloomington, IN, USA, October 14, 2004. We collected much of the material during joint field research to Javakheti in July 2003.

Apostolic Armenians of both Georgian and Armenian ethnicity, Dukhobors,[19] and Muslims (Meskhetian Turks). Such an ethnic and confessional mix represented a major political challenge to the region's integration into the rest of Georgia. This was further aggravated by poor grasp of the Georgian language among the Javakheti Armenian population, related to the state's failure to provide adequate resources for language study. The isolation of this region allowed local stakeholders to strengthen their political and economic hold on the area to the detriment of strengthening Georgia.

In the early 1990s, Javakheti was under the control of the *Javakhk*, a group founded by Samvel Petrosyan in 1987-88 during *perestroika,* dedicated to the preservation of Armenian culture and the development of the region. During Gamsakhurdia's presidency, the *Javakh* refused to accept Tbilisi's appointed regional governors for Javakheti. To fill the political vacuum, a 24-person council was created, which ruled Javakheti until Tbilisi appointed candidates acceptable to the local people (Darchiashvili 2002). President Shevardnadze managed to establish *de facto* control over the region in 1994 by combining Samskhte with Javakheti and granting the local Armenian power brokers positions in the district administration and parliamentary seats (Landru 2002). Though stability was maintained and the public confrontations between the Armenian and Georgian representatives over the question of regional autonomy lessened (December 1996 and August 1998), factors such as geography, demographic/religious composition, historical legacies, the Akhalkalaki Russian military base, arms availability, and economic assistance from neighbouring Armenia provided bargaining tools in the centre-periphery power dynamics.

For example, when the central government in Tbilisi attempted to extend more control over the province in the early 1990s, 1998 and 2001, local political organisations such as *Javakhk* and *Virk*[20] were among the main organisers of anti-government social protests. And, when the Georgian Ministry of Defence tried to enter the region for military

[19] Ethnic Russians who rejected both the authority of a Orthodox Church and the state and were forcefully relocated to the region by Tsarist Russia in the 1830s.
[20] Political movement established by David Rstakyan to promote Javakheti autonomy within Georgia.

exercises in 1998, armed groups blocked them.[21] Despite the role of Armenian nationalist groups in Javakheti, the political dynamics between Georgia and Armenia over the Javakheti issue, albeit strained at times, was carefully managed by Yerevan. As a result of the war fought between Armenia and Azerbaijan over Nagorno-Karabakh, there was an embargo officially imposed by Azerbaijan and Turkey against transporting any goods to and through Armenia. Thus, Armenia was dependent on Georgia as its only major transit corridor to Europe, as well as its primary source of hydrocarbon supply.

As with most of Georgia, economic conditions in Samskhte-Javakheti were unpromising for much of the Shevardnadze era. Difficulties caused by unpaid pensions and wages by the government were aggravated by problems of power supply, which only worsened the psychological impact of the economic situation. Transfers from the central budget constituted less than 50 percent of the Akhaltsikhe regional budget and the shortfall had to be supplemented by other means. All formerly state-run enterprises (e.g. cheese, tin cans, and knitted goods production) were closed and the people of Javakheti survived on employment provided by the Russian military base plus remittances from Russia, supplemented by subsistence farming and low-level trade with Turkey and Armenia. An estimated 1,200 Russian personnel of the 62nd Division occupying the 5,000-hectare military base in Akhalkalaki employed approximately 2,000 Armenian residents.[22] When shared with family members, this sustained about 6 to 8 thousand residents or 10 percent of the Akhalkalaki population (Caucasus Institute for Peace 2002). The base also recruited and trained the local population for military service, paying substantial salaries of US$ 100 per month (Wheatley 2005b). In addition, the military hospital was the primary provider of medical care for the local population. The Russians ensured that the region stayed economically tied to it rather than to Georgia by paying the locals in Russian roubles (Gotsiridze 2003: 17). Moreover, as a result of the 1998 Russian requirement that all servicemen at its bases hold Russian citizenship, the local Armenian

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[21] Interview with Temur Mosiashvili, Governor of Samtskhe-Javakheti February 2002-August 2003, Akhaltsikhe, Georgia, July 2003.
[22] Interview with Temur Mosiashvili, July 2003.

population serving as soldiers at the Russian base acquired Russian citizenship in addition to their Georgian citizenship.

The Armenian residents of Javakheti also believed that the Russian military provided a security guarantor in case of Turkish aggression. Armenians of Javakheti viewed with suspicion any official cooperation with Turkey, partly due to their historical memories of the 1915 massacre of Armenians under the Ottoman Empire. Their suspicion was reinforced by a 1999 agreement between the Council of Europe and Georgia on the relocation of Meskhetian Turks back to the Akhaltsikhe region. In 1944, Stalin had forcibly removed 100,000 Meskhetian Turks (along with approximately 20,000 ethnic Kurds and Muslim Armenians known as Khemshils) to Central Asia. President Shevardnadze agreed to a 12-year framework to repatriate the Meskhetian Turks as a condition of entry into the Council of Europe. However, a required law on repatriation was never passed by the Shevardnadze government and only about one hundred Meskhetian Turks returned during this time (Pentikainen and Trier 2004). For the Armenians in Javakheti, the need for protection was exacerbated further by Turkey's military aid to Georgia. The Turkish government had provided US$ 1.27 million towards reconstructing a military airfield in the Azeri populated region of Georgia, Marneuli, as well as providing 2 helicopters as part of a joint US-Turkey military assistance package in 2001 (Ordenidze 2001). Additionally, diplomatic discussions were underway regarding a proposal for a 287 kilometre railway connection between Tbilisi and Kars, Turkey via the Akhalkalaki region. All of these factors were used by the leadership of *Javakh* and *Virk* to foment the idea that Armenians were under threat and that they needed the Russians to protect them.

The lack of diversification in the economy meant that whoever controlled the border posts, transit corridors, and trade in petrol had political power in the region. As a result, political power at the local level was concentrated in the hands of a few powerful economic groups (Wheatley 2005b: 9). The power structures in Javakheti depended largely on the relationship between *bureaucratic* stakeholders in the provinces and the *elite* in Tbilisi, formed on the basis of mutual business interests. The local *bureaucracy* and their trans-territorial networks, which included *business groups*, dominated smuggling through Samskhte-Javakheti. There were three key groups, each centred on a family, which controlled all major energy businesses in the province, including the sale and transit of petroleum products, the smuggling of timber and building materials, and the distribution of electric power. They were the Raisyan group, the Mkoyan group, and the Arzumanyan group. The Raisyan group was the oldest, dating back to the Soviet period, and was based in Akhalkalaki. Melik Raisyan was elected to the Georgian Parliament three times, while his brother, Grigori, was the Prosecutor General of Akhalkalaki for over 10 years under an exceptional legal provision.[23]

The Mkoyan group, based in Ninotsminda, was perhaps the most powerful group, uniting with two other groups — the Shakhbekian and Ambartsumian families — to form a politico-economic power base. Enzel Mkoyan served as a Member of Parliament for Ninotsminda. He was from Alkhakalaki and cooperated with the Head of the Russian military group in the Caucasus, Zolotov, who was also the former head of the Russian military base in Alkhakalaki. Mkoyan's group ran several businesses, including the export of building material to Armenia and exporting stone to Russia. Later, the group switched to the more lucrative fuel import/export business.[24] The Mkoyan family's supplier of fuel products was *Iveria Plus*, owned by Nugzar Shevardnadze (Glinkina 2003: 14). Enzel Mkoyan's brother is thought to have been involved in the trans-territorial network exporting Azerbaijani oil to Armenia, as discussed in Chapter 5.[25] The third and most moderate group was the Arzumanyan group. It was led by Rafik Arzumanyan, who served as the *gamgebeli* (head of the regional executive authority appointed by the President) of Ninotsminda district from 1993. The Arzumanyan group was considered to be exclusively a 'family clan' and had the reputation for ensuring a

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[23] According to the law adopted by the Georgian Parliament on 21 November 1997, a Prosecutor General cannot serve more than two terms of five years each. Amendment 14, Article 7 of the same law adopted on June 12, 1998 provided for exceptional circumstances under which a Prosecutor General could serve for a third term. After this exception was applied to the case of Raisian, it was made obsolete on May 12, 1999. Interview with former Prosecutor General of the Samskhte-Javakheti region, Tbilisi, April 2004.
[24] Interview with Temur Mosiashvili, July 2003.
[25] Jonathan Wheatley's interview notes with Armen Amirkhanyan, Representative of the Akhalkalaki office of the European Centre for Minority Issues, Ninotsminda, Georgia, March 2004.

stable environment.[26] Rafik Arzumanyan operated only in Ninotsminda, where he maintained significant influence and allegedly controlled the Armenian-Georgian border.[27]

The Raisyan and Mkoyan groups competed for a monopoly over the sale and transit of fuel products. In their struggle for influence they leveraged the support of the authorities in the central government. Shevardnadze played one group against the other in order to prevent a group becoming too influential and powerful. As a result, the once dominant Raisyan clan was neutralised by the shift in Shevardnadze's support to the less influential families.[28] Wheatley best explained this power play by the centre to balance the region in a study on the Javakheti region. He wrote,

> Many local observers believe these so-called clans to be artificial structures created by the government in Tbilisi to 'divide and rule' Javakheti. By dividing the political elite, they argue, the central government ensures that no united voice is heard from Javakheti. The 'clan' leaders, they point out, were often on friendly terms during the late communist period and only later became rivals, as a result of conflicting business interests. Indeed it is clear that divisions within the local political and economic elite do not reflect any deep-seated sociological divisions within the population of Javakheti, and that the failure of the political elites to find a common language reflects their inability to establish a meaningful dialogue with the population as a whole. What we see is a fractious local elite beset by personal rivalry and shifting alliances, easily manipulated by the centre and lacking the will and/or resources to respond to the needs of ordinary people (notwithstanding those sporadic acts of charity that members of this elite undoubtedly care for the benefit of the most vulnerable members of the population) (Wheatley 2005b: 17-18).

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[26] Jonathan Wheatley's interview notes with Arnold Stepanyan, Chairman of the public movement 'Multinational Georgia', Tbilisi, Georgia, September 2003.
[27] Interview with members of the Georgian customs department at the border crossing with Armenia in Ninotsminda, Georgia, July 2003.
[28] The Raisyan group was close to Zurab Zhvania. After Zhvania resigned as Chairman of Parliament and formed the opposition United Democrats in June 2002, Raisyan became a member of that parliamentary faction. Mkoyan remained loyal to Shevardnadze and his group therefore prospered. Earlier, the Mkoyan group had also benefited from the support of the President's authorised representative to Javakheti, Gia Baramidze, who held this position from 1994 to early 2002. Mkoyan was elected MP for Ninotsminda in 1999.

In order for a network to move a commodity through Javakheti, it required the assistance of many agencies, all receiving a percentage of the profit, including the Ministries of Economy, Industry and Trade, Finance, the Tax Inspectorate, the Transport and Communications, Fuel and Energy, the Border Guards, the Department of Customs, the Police, the Russian military, and local politicians. The police chiefs were powerful, in particular Mkhitar Abajyan, who was appointed in 2000 to head the Akhalkalaki region. Previously he had been the head of the Tax Inspectorate in Javakheti (Wheatley 2005b: 16). For example, the police chief of Alkhakalaki got a 20 percent share from the local business and then transferred a share to the centre.[29] Additionally, to secure these operations, the Armenian families often acquired their own private armed formations as a security guarantor in anticipation of violence. There were periodic violent acts against influential families, including bomb attacks targeting members of the centrally appointed local administration. For example, just before the November 2003 parliamentary elections, there was a bomb attack on the building housing the governor of Samtskhe-Javakheti in Akhaltsikhe. Gela Kvaratskhelia, an ally of Shevardnadze, had replaced the former Governor Mosiashvili and the bomb was allegedly a protest against this appointment.[30]

The region was a cross roads for the transit of petrol from Azerbaijan westwards to Georgia's Black Sea ports, from Russia south to Armenia by truck, and from Georgia's seaports to Armenia by road. The other possible way of getting petrol into the region was in Russian armed forces' tankers travelling from Russia through Tskhinvali, South Ossetia and on to the military base in Javakheti.[31] In some cases, operating in Javakheti would require support from the Armenian groups in Armenia and the Armenian government, namely the Ministry of Defence in the case of fuel smuggling. Of the fuel that reached Javakheti, only a small amount was for local use; the rest was smuggled to

[29] Interview with Gia Kopadze, Chairman of the New Rights Party. He was the Gamgiabeli of Akaltsikhe from 1991 to 1995, Samskhte-Javakheti, Georgia, July 2003.
[30] Interview with Eka Metraveli, Fellow, Georgian Foundation for Strategic and International Studies, Tbilisi, Georgia, November 2003.
[31] Interview with Mark Grigoryan, Journalist, BBC, London, UK, May 2004.

Armenia and some was trucked to Turkey up until the late 1990s.[32] Georgian companies operated between various European and Russian suppliers and Armenian buyers, charging Yerevan higher than market prices.[33] For example, by the early 2000s, there were 14 petrol stations in a town of 11,000 people in Akhalkalaki. Three belonged to Enzel Mkoyan (Chevron), three to the Raisyan group, and the remaining to family members of the *gamgebeli*. The petrol was bought in Russia on the official market (papers were provided and taxes were paid to Georgian authorities) for 'import'. However, rather than being delivered to the stations within Javakheti, it was exported to Armenia without paying the required taxes on the border for resale at a higher price.[34] The trans-territorial networks had to remain flexible, as various legal restrictions required a change in direction of the petroleum business through Javakheti.

It is clear from a series of presidential decrees passed in the 2000s, that petroleum smuggling routes became a political tool of control by the centre. Before 2000, when a visa regime between Georgia and Russia was introduced, Russian military vehicles were free from customs duties and were rarely stopped by the police. After the introduction of the visa regime, land transportation between Georgia and Russia became more complicated and the route for supplies to and from Akhalkalaki was switched to Batumi Port in Adjara (Antonenko 2001: 33). In 1999 and 2000 Shevardnadze's government attempted to stop illegal trade from Georgia through Javakheti to Armenia. All trade flows were redirected to transit Sadakhlo to the east of the Samskhte-Javakheti region. Melik Raisyan explained that his father had been responsible for transiting Azeri petroleum to Armenia; however, after the new regime through Sadakhlo, he lost his control over the business.[35] The Mkoyan group was allegedly able to gain a monopoly over the grey market supply of petroleum after this.[36] The Shevardnadze government was also reluctant to open the Kartsakhi customs checkpoint on the Georgian-Turkish

[32] In 1997, 80,000 tonnes were trucked to Turkey through the region, worth GEL 700 each. Five percent was given to local businesses and 3 percent to the state budget for transit. By 1998 the business had ended and Tskinvali became a major source of petroleum products. Interview with Gia Kopadze, July 2003.
[33] Interview with Giorgi Glonti, Research Director, TRACCC, Tbilisi, Georgia, October 2003.
[34] Interview with Mark Grigoryan, Journalist, BBC, London, UK, May 2006.
[35] Jonathan Wheatley interview with Melik Raisyan, Member of Parliament for Akhalkalaki, Akhalkalaki, Georgia, March 2004.
[36] Interview with Zura Chingilashvili, Channel 9 producer in Akhaltsikhe, Georgia, July 2003.

border at Vale in Samskhte-Javakheti. This was believed to be the result of a bargain struck between Shevardnadze and Abashidze of Adjara, whereby Adjara would get 95 percent of the traffic in return for sharing the profit from the customs checkpoint at Sarpi, Turkey.[37]

This chapter has concentrated on regionally based trans-territorial networks engaged in the smuggling and sale of petroleum. However, similar networks operated in other fields, for example, electricity generation. Electricity generating facilities served as a lucrative business venture for trans-territorial networks. They also strengthened the position of Armenia in Javakheti. Akhalkalaki received electricity from Yerevan in the winter months via the Ashotsk-Ninotsminda-Alkhakalaki line, bypassing the main Georgian grid. The construction of this line was agreed between the Presidents of Georgia and Armenia on September 29, 1999 (Kublashvili 2003: 17). However, disagreement by a panel of Georgian electricity experts regarding the necessity of this line for technical and financial reasons delayed Georgian construction of its section of the line. Meanwhile, the Armenians began constructing the line and completed its extension to Ninotsminda, Javakheti, despite the fact that the agreement did not mention specific electricity sub-stations Ashotsk or Ninotsminda. Further, *Armenergo* (Armenia's state run electricity company) took full control of the output of the Ninotsminda station to Georgian citizens in Javakheti, with payments transferred to Armenia. Armenia began supplying electricity in January 2001, but deliveries to Akhalkalaki were soon halted temporarily over disagreements regarding payment and local theft of supply (Matveeva 2003). *Gamgebeli* Mkoyan of Ninotsminda became a major stakeholder in the operation of the transmission line and wielded power through providing electricity to residents. [38]

A combination of stakeholders found ways to compensate for the central government's inability to provide reliable sources of electricity to the region. In particular, stakeholders in the local *bureaucracy* developed sources of generation and established private

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[37] Interview with Eka Metraveli, June 2003.
[38] Information sent to me in an email from Eka Metraveli, Fellow, GFSIS, Tbilisi, Georgia, September 2004.

electricity supply businesses. One example of grey market electricity supply in the region were mini hydropower stations owned by the Akhalkalaki governor and his associates who sold the citizens electricity generated at their facilities at higher rates. Another example is the family of the former *gamgebeli* of Alkhalkalaki, Sergo Darbinyan, who supplied power to the region from a commercial power plant (Wheatley 2005b: 11). One expert who frequently travelled to the region was made aware of the rehabilitation of local power stations by *business groups,* under the sponsorship of Members of Parliament from the region. In several villages, the *consumers* even built temporary hydropower stations by placing turbines in small rivers to generate electricity.[39] Thus, while calls for autonomy may have decreased over the decade of Shevardnadze's presidency, and the power arrangement between the centre and periphery solidified in the form of patron-client networks, the region as a whole, and the majority of the residents therein, operated increasingly independent of the centre due to the social and economic realities of living in a weak state.

6.5 Conclusion

Each of the three regions discussed in this chapter were part a larger heterarchical formation of trans-territorial networks operating in the grey market, conditional on a sequence of factors during certain periods of time. As an example, Table 5 below displays the stakeholders, network characteristics, and the system dynamics of the Abkhaz petroleum smuggling trans-territorial networks. Everyone, from the most powerful to the marginalised majority, participated in networks and was affected by this system. The trans-territorial networks permeated both horizontal and vertical structures of power. It is useful to conceptualise the networks not as mechanisms for state-to-state activity, but rather a compilation of stakeholders traversing multiple undefined and variously regulated regions along a corridor temporarily structured around the smuggling of a commodity. Declared enemies, including officials and undeclared paramilitaries, use their positions to cooperate in business opportunities in the grey market. As the regions

[39] Interview with Giorgi Meskhidze, President, Civitas non-governmental organization, Tbilisi, Georgia, April 2005.

through which these networks traverse remain weak, the population living along the corridors have little choice, and are sometimes forced to participate in the networks. None of this is, of course, officially sanctioned, documented, or discussed. And yet, it is the main source of income, interaction, and communication among numerous groups across territories.

Measures were taken towards the end of the Shevardnadze era to legalise the petroleum trade. The government departments which gained responsibility for countering smuggling in Georgia included the Ministry of Finance, the Ministry of Internal Affairs, and the State Department of the Border Guard. Additionally, parliamentary committees and the National Security Council had legislative and oversight responsibilities. However, as of 2003 there were no major cases under investigation and no prosecutions of those operating in the trans-territorial networks. From 2001 to 2002 there were 82 cases of 'light smuggling' and the majority of those sentenced came from socially vulnerable groups (Kukhianidze, et al. 2004: 67). Thus, despite the anti-corruption rhetoric and legislation, the damage smuggling did to the financial viability of Georgia, and the power it provided to separatist groups, Georgians continued to operate in trans-territorial networks in the grey economy throughout the Shevardnadze era. More specific empirical implications will be discussed in the next chapter.

Table 5 - Abkhaz Petroleum Smuggling Trans-territorial Network

Stakeholders	**Network Characteristics**	**Network System Dynamics**
Elite – Shevardnadze and Ardzinba families; IDP Head Nadareishvili, Samegrelo MPs and Governor; Georgian Ministers of State Security and Interior.	**Semi-permanent** - Networks were disrupted by a break in the supply chain or when there was a need to avoid detection. Networks were disbanded when competition turned violent.	**Alternate Force** – Protection granted to networks by both Abkhaz and Georgian officials shifted an aspect of their conflict to a non-transparent arrangement.
Bureaucracy – Gali political representatives; Samegrelo Procurator, Tax Administration, and district politicians.	**Unique** – The configurations of stakeholders depended upon a particular mission and were not set.	**Heterarchical** –There were several intersecting networks, some stakeholders more allegiant to the *elite*.
Business groups - Georgian and Abkhaz armed forces, security agencies, customs and border patrol; paramilitary groups; CISPKF; suppliers from Russia, Turkey, Romania, and Bulgaria.	**Sponsored** – The networks were alleged to have *elite* sponsorship on both sides.	**Trans-territorial** – Networks traversed Russia, unrecognised Abkhazia, and Georgia. Some networks began in Turkey and Europe.
Consumers – IDPs and broader population living in Gali and Samegrelo.	**Personalised** - Membership was based on: (1) ethnic, kin and confessional basis; (2) war-time contact; and, (3) relationship to *elite*.	**Grey market** – Trade occurred with the unofficial consent of governments, but was forbidden.
	Non-transparent - The names and affiliations of the stakeholders and their operations was kept out of the public domain, for the most part.	**Conditional** – The ebb and flow of trade was conditional on the political climate, regional petroleum market, and violence prone competition among stakeholders.
	Multi-sectoral - The stakeholders smuggling multiple products.	
	Logical - The Abkhaz needed to compensate for the CIS embargo. The Georgians wanted to enhance profits and maintain a presence in Abkhazia. The Russians were mostly interested in business.	

Chapter 7: The Inter-State Relations of a Weak State

> What we have to come to terms with is a type of state that artfully manipulates its rule-setting capabilities not for the sake of shaping reality, but with the clear purpose of creating insecurity as an ideal condition for satisfying the resource hunger of its agents and for choosing the precious few that may do business without [sic] tiresome competition (Christophe 2004).

7.1 Introduction

The operations of trans-territorial networks described in Chapters 5 and 6 covered both the functional areas of the energy sector, as well as smuggling operations traversing Georgia's regions. The examples of the way in which the heterarchical webs of stakeholders worked demonstrated the extent to which the networks usurped the state. As discussed in Chapter 2, the assumptions made in the International Relations literature about the functions and operation of the state are not valid in the case of a weak state. In relation to Georgia, the assumptions that the state is a coherent unit acting with a common purpose, that people's loyalties to the state are greater than their loyalty to resource-driven networks, and that domestic sovereignty resides within the authorities governing the state are not appropriate. In the case studies presented here, the incentives to create a system that served the interests of the stakeholders operating within trans-territorial networks were greater than the incentives to strengthen the state. State actors used their positions to cooperate with non-state actors in such a way as to compromise the financial and physical viability of the state. While the state was weak and lacked legitimacy among the broad population, however, it was clear that state-societal cohesion was quite strong within the networks. In the end, the stakeholders created an alternate force that was more influential than the government, and this system became the medium for inter-state relations.

The understanding of the weak state as a shell for strong trans-territorial networks provides a different analytical lens through which to understand persistent state weakness. At the empirical level, the focus is on the reordering of relations within the networks among a combination of state and non-state, and local and global actors (Krasner 2001). Thus, it is within the framework of trans-territorial networks that the implications of a weak state's relations with other states are found. This chapter will consider the effect that the trans-territorial networks had on Georgia's inter-state relations. It will first discuss the impact of the networks operating in functional areas which were covered in Chapter 5, before examining the effects of the networks in the regions of Georgia which were covered in Chapter 6. The third section looks at the effect of trans-territorial networks on the inter-state relations within the South Caucasus region. In conclusion, one case in which the trans-territorial networks were considerably neutralised so as to allow multiple states' energy sectors to benefit from a large-scale regional project will be discussed.

7.2 Implications of Functional Trans-territorial Networks

Trans-territorial networks dominated the functional areas of Georgia's energy sector, including natural gas imports, electricity distribution, production of petrol, transportation of petrol, and electricity transmission. The primary conclusion reached from the cases presented in Chapter 5 is that non-transparent arrangements among the regional *elite* to extract rents from the energy sector in the grey market took precedence over the legitimate development of Georgia's energy sector. Networks were set up on a temporary basis among *elites,* often former associates or *nomenklatura* from the Soviet Union, who operated within multiple aspects of the oil, gas, and electricity sectors. The stakeholders manipulated state owned companies located in Georgia, or manipulated the operations of international companies investing in Georgia to enhance their personal earnings. Profits that could have been spent on strengthening the financial and technical aspects of the energy sector were instead spent keeping clients loyal. The stakeholders co-opted members of the *bureaucracy* in the legislative and judicial branches in order to purposefully weaken state institutions. The actions of these networks had three debilitating effects on Georgia's inter-state relations. First, they created a non-competitive and inefficient energy sector, which curtailed the expansion of the domestic economy. Second, the viability of western companies and donors operating in Georgia was undermined. Third, Georgia ultimately sacrificed its energy supply by transferring most of its strategic oil and gas assets to Russian state-owned companies during a tumultuous time in the two state's diplomatic relations. Each of these effects will be examined in turn.

First, the alternate order disallowed competition from domestic and foreign entities, which led to a non-competitive and inefficient energy sector. The case study in Chapter 5.4 demonstrated how members of the Shevardnadze family came together to ensure that the only modern oil refinery – *GAOR* – was unsuccessful. Their actions deterred competitors from entering the Georgian petroleum market, including importing petroleum products and refining crude for domestic consumption and export. They also withheld taxes, tariffs, and customs revenue from the central budget. A report prepared in 2002 for USAID indicated that the Government of Georgia could realise as much as US$ 250 million per year from the petroleum sector – petroleum and diesel alone would account for US$ 180 million of this potential revenue. In actual fact, in 2002, Georgia only collected US$ 46 million or 5 times less than the potential revenue (Shenoy 2002b). Smuggling put legal businesses in a non-competitive position, giving smuggled goods a major price advantage over locally produced goods (Tsereteli 2002). By the early 2000s smuggling had become the prime factor in Georgia's economic crisis due to lost revenues, estimated to be up to 50 percent of Georgia's GDP (Vaux 2003). Most of the profits stayed within a circle of customs and law enforcement officials, strengthening the stakeholders in Georgia's regions (Dzhikaev and Parastaev 2004: 206). The monopolisation of industry and the handling of transactions in the grey market also deterred Georgia from becoming self-sufficient. *GAOR* was working with the IFC to expand its operations in Georgia. Had it been successful, Georgia could have become self-sufficient in petroleum supply, as well as creating a larger revenue base. This left Georgia perpetually dependent on the grey market to secure short-term supply agreements. As a result, the state lost funds that could have been spent on upgrading its electricity generation, transmission, and dispatching units (Kublashvili 2003).

The second effect on Georgia's inter-state relations was that the alternate order challenged Georgia's credibility with western donors, who had granted and loaned hundreds of millions of dollars to transform Georgia's energy sector. This was exemplified by the under utilised *Inguri* hydropower plant, from which international grants were diverted, leaving the state dependent on Russian supplied electricity at much higher rates. As a result of the misappropriation of over US$ 500 million in international grants and bank credits directed at strengthening Georgia's energy sector, by 2003 Georgia became known as a 'no go' state for international investors and institutions (Jervalidze 2006: 30). In 2001 and 2002, the IMF withheld funds due to uncollected tax revenues and the misappropriation of foreign assistance. In 2003, the US government did not object to the sale of Tbilisi's electricity generation and distribution system by the American company *AES* to the Russian state-owned company *UES*. Moreover, there were no successful private joint ventures between Georgian companies and western entities investing in Georgia's energy system during the Shevardnadze era. The President of the American Chamber of Commerce in Tbilisi blamed this on the 'poor reputation of Georgia', which suffered a lack of fiscal incentives, declining security, harassment by 'collectors', and the unpredictability of the overall business climate.[1] By 2003, donor funds to Georgia's energy sector were dwindling, both from officials and private entities.

The third effect was that the joint ventures that did succeed were conducted in the grey market and were also detrimental to the state. Various schemes were used to bankrupt Georgian state assets in the gas and electricity sectors. Up until the mid-1990s, stakeholders in Georgia's gas market included officials and businessmen from Russia, Turkmenistan, Kazakhstan, Azerbaijan, and Iran. However, starting in the late 1990s, powerful Georgian-Russian networks took control of Georgia's gas and electricity sectors. In the gas import sector the stakeholders included *Itera, Sakgaz, Tbilgaz, Azoti*, and *Gardabani*. In the electricity sector, *Sakenergo, RosGruzEnergo*, and *Winnfield* were joint Georgian-Russian ventures. In the electricity re-export business to Turkey and Azerbaijan, *Anglo Oil, RosGruzEnergo,* and *Winnfield* were involved. While most actors in these networks operated for immediate financial rewards, there was a point at which factions within the Russian government began to use the debt Georgia owed to state-owned companies, and the assets these companies held in Georgia's energy sector, to gain control of Georgia's strategic assets.

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[1] Interview with Vadi Asli, President of the American Chamber of Commerce, Tbilisi, Georgia, April 2005.

There were several concerns expressed about the implications of Russian ownership of Georgia's strategic assets. These included questions about the effect it could have on Georgia's geo-strategic positioning along a lucrative hydrocarbon corridor, as well as on President Shevardnadze's proclamations of Georgia's intentions to seek future membership in such organisations as the EU and NATO. Georgia's increasing reliance on Russia for gas and electricity supply appeared to run counter to its stated objectives of enhancing its own energy security and related political independence. The year before the sale of Georgia's major energy assets to Russia, President Shevardnadze had said that, 'The Georgian energy system cannot depend on one single country or one gas pipeline' (Interfax 2002). Russia could raise prices and use supply as a political lever, and Georgia would have little ability to object. While the Russian government never explicitly linked energy cut-offs to geo-strategic issues, the gas cut-offs and sabotage to the gas pipeline and electricity line from Russia to Georgia were often curiously timed to respond to Georgian policy. During the time when Moscow intermittently cut-off gas to Georgia in winter 2001, the two states were negotiating the withdrawal of Russian armed forces from Georgia, and Moscow was protesting against Georgia's alleged support for Chechen rebels.

Russia's politicisation of gas supply to Georgia was vocalised several years later. Before Russia announced a price hike in gas in January 2005, Georgia and Ukraine had publicly announced their intentions to withdraw from the CIS. A Russian government source told the RIA-Novosti news agency, 'In the wake of statements made by the leaders of Georgia and Ukraine about the possibility of their withdrawal from the CIS, the government of Russia is considering cancelling a number of benefits, which these states enjoy within the CIS' (United Press International 2006). One of these benefits was subsidised gas supply. Russian sources of gas and electricity remained vulnerable to sabotage. For example, in January 2006, two blasts hit the Mozdok-Tbilisi gas pipeline and the reserve pipeline on the Russian territory of North Ossetia. This, coupled with Russian demands for a doubling of the price of gas to Georgia and Ukraine, left Georgia without gas for several of the coldest months of the year. Meanwhile, Georgia's import of electricity from Russia on the *Kavkasioni* line through the Kodori gorge in Abkhazia remained prone to sabotage and general poor maintenance, leading to frequent problems with supply (Chkhartishvili, et al. 2004: 129).

After 2003, Georgia's efforts to diversify its supply of gas and electricity was made more difficult by Russia's monopoly of potential sources of supply, either directly, or indirectly though transit rights. This included supplies from Kazakhstan, Turkmenistan, and Iran for gas, and Azerbaijan and Armenia for electricity. Many of the proposed hydrocarbon transit routes from the Caspian Sea to Europe placed Georgia at the centre, allowing it to potentially gain from transit revenue and alternative supply. A Trans-Caspian gas pipeline from Turkmenistan and Kazakhstan via the South Caucasus to European markets was proposed. Other possibilities included connecting the gas pipeline from Baku to Turkey via Georgia with the Nabucco project (Turkey-Bulgaria-Romania-Hungary-Austria), or constructing a Georgia-Ukraine-EU (GUEU) gas pipeline under the Black Sea. Georgia also planned to extend the Iranian-Armenian gas pipeline into Georgia and onto Ukraine. However, Russia was able to use various methods to delay, and perhaps ultimately block, these plans. Russia opposed the Trans-Caspian pipeline proposal, citing the non-resolution of the legal status of the Caspian Sea as an obstacle to the construction of such a pipeline (Socor 2006b). The plans to build a Trans-Caspian pipeline were probably negated by a deal between *Gazprom* and Turkmenistan, locking in gas prices at US$100 per cubic metre. Tbilisi also tried negotiating possible gas imports from Kazakhstan, but this plan was blocked by Moscow when Russia refused to give Georgia permission to use its pipeline (Corso 2005). Russia warned against the idea of GUEU, citing potential complications for its Blue Stream pipeline to Turkey under the Black Sea (Ukrainian Journal 2006). Finally, pressure from Russia on Armenia resulted in restricting volumes of imported Iranian gas to Armenia, as well as limiting the diameter of the Iran-Armenian gas pipeline so that its capacity was insufficient for transit of Iranian gas further north to Georgia or Ukraine (Khachatrian 2006).

7.3 Implications of Regional Trans-territorial Networks

Map 6 - Petroleum Smuggling Networks

Source: (Adaptation of Kukhianidze, et al. 2004)

The trans-territorial networks operating through Abkhazia, South Ossetia, and Javakheti linked multiple state and non-state stakeholders from the *bureaucracy, business groups*, and *consumers* with the sponsorship of someone from the *elite*. When all of the petroleum smuggling routes mentioned in this thesis are captured on a single map of Georgia (see Map 6 above), the weak state's role as a corridor for trans-territorial networks becomes clearer. The primary conclusion reached from the case studies presented in Chapters 5 and 6 is that the trans-territorial networks hampered the central government's control over peripheral activity and consequently weakened the state's role as the primary actor in inter-state relations. Hence, the ability of the state to control regional energy trade and, ultimately, the activities of political and security structures in the regions, was compromised by the actions of the trans-territorial networks. The weakened central control over the periphery of the state had three implications for the state. First, it strengthened local fiefdoms within Georgia that were able to act independently of the centre and develop relations with neighbouring regions, including the separatist zones and co-ethnic groups across state borders. Second, smuggling routes created by trans-territorial networks were controlled by criminal groups and could serve as corridors for other illicit goods. The criminalisation of the transit routes was accompanied by a rise in violence among competing groups, which could be mistaken for ethnic conflict or irredentism. Third, it is hypothesised that the trans-territorial networks were so profitable that they served to discourage *elites* from resolving the separatist conflicts.

The central government distributed local political positions and, in return, those who were appointed shared the financial benefits gained from trans-territorial networks with central stakeholders in the *bureaucracy* and *elite.* This arrangement became the power bargain between the centre and periphery (Metreveli 2004). Everything traversing a certain region became the *de facto* property of the local politicians and profits from these assets were divided among regional *bureaucrats* and *business groups* to ensure their allegiance to the regional authority.[2] Towards the late 1990s, three factors shifted the power dynamic gradually from the centre to the periphery. The first factor was the growing influence that local families obtained in regional governing structures as a result of deals made with the centre. The second factor was growing cooperation between regional stakeholders and actors in neighbouring states. The third factor was the heightened criminality of trans-territorial networks and accompanying violence displayed among competing groups. However, the extent to which these phenomena threatened central control is debatable, given the participation of the Shevardnadze family or the president's loyal clients in the trans-territorial networks. As King argued, weakness was not a coincidence, but a well orchestrated plan. He argued, 'Throughout these conflict zones, the weak state is not a condition that has somehow simply happened. Continued weakness, whether in the separatist regions or in central governments, is in the interests of those in power' (King 2001).

The Georgian government's inability to provide a reliable supply of petroleum, gas, and electricity led to *de facto* abdication of responsibility for providing energy to localised networks in the regions of Georgia. These networks were composed of *bureaucracy, business groups,* and *consumers.* Beginning in the mid-1990s, the *gubanatori* and *gamgebeli* took over local generators, transmitters, and distribution networks in the energy sector, enhancing their power as both service provider and

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[2] Interview with David Darchiashvili, Member Executive Board, CIPDD, Tbilisi, Georgia, July 2003.

revenue generator.[3] For example, the heads of regional state owned electricity distribution companies would sign contracts with the Georgia electricity wholesale market, and then establish several private companies with politicians for the distribution of electricity. They would claim that *consumers* did not pay for public electricity and split the profit.[4] A Member of Parliament from Zugdidi in western Georgian recalled how the regional Head of Taxation inspected alleged violations within the electricity sector in his district.[5] The inspection uncovered the fact that only 200,000 of the official 800,000 lines actually functioned under the assigned authorities. Instead, there were 600,000 lines serving as contraband under the control of *business groups*, to which some officials in the regional government belonged. At any one location in Georgia, it was not uncommon to have two to three different sources of electricity; one official, one diverted from a government-owned facility (such as the train station, hospital, or bread factory), and a third from a 'private' source.[6] The same trans-territorial networks would control the transportation systems throughout a region. The transport of petrol provided a source of income to regional authorities; for every one ton of petrol travelling through Georgia to other destinations, it is estimated that stakeholders in each of the transiting regions kept US$ 150 in 'taxes' (Kukhianidze 2003: 93).

These centre-periphery power arrangements were particularly evident in the autonomous and separatist regions of Georgia, and their adjacent regions. In the case of the Armenians of Javakheti, who received electricity from Armenia, this contributed to irredentist sentiments, which already existed among the community. The local Armenian population perceived shortages, high prices, and generally poor economic conditions as a deliberate policy of the central government to force them out of the area. Further, as they became more reliant on Armenia for electricity and the Russian military base for cheaper fuel, their allegiances shifted from Tbilisi.[7] During Shevardnadze's presidency, the Armenians in Javakheti were reluctant to use

[3] Interview with John Wright, ECMI, Tbilisi, Georgia, April 2005.
[4] Interview with Levan Ramishvili, Liberty Institute, Tbilisi, Georgia, April 2005.
[5] Interview conducted off-the-record with Member of Parliament from Zugdidi, Tbilisi, Georgia, April 2005.
[6] Obtained through interviews during field research trip to Zugdidi, Georgia, April 2005.
[7] These observations were gleaned during conversations with people in Javakheti during a research trip to the region, July 2003.

the Georgian language, even in official correspondence, they preferred to use Russian roubles, and they avoided serving in the Georgian army. Further, the reliance of the Armenian population on the Russian base in Javakheti for their livelihoods created a situation in which an unofficial security alliance was created between the Armenians and the military forces serving at the Russian military base.[8] Georgians were prone to blame Armenian nationalism and the *Dashnaktsutyun* party, allied with President Kocharyan since 2000, for inciting separatist sentiments among the population in the region. The Armenian Ministry of Foreign Affairs explained that Armenian government support for the population residing in Javakheti, including the supply of electricity and goods, far from intending to incite separatism, was part of an effort to quell calls for autonomy, which would be a problem for both Georgia and Armenia.[9] In fact, it was the inability of the central government in Tbilisi to provide economic and physical security that incited the separatist sentiments.

The rise of regional fiefdoms in Georgia was detrimental to the strengthening of the Georgian state. Abashidze, Ardzinba, and Kokoity, the leaders of the Autonomous Republic of Adjara, of Abkhazia, and of South Ossetia respectively, were able to strengthen their hold over the regions due, in part, to revenues from the energy sector. In 1989 Adjara joined South Ossetia and Abkhazia in demanding autonomy, but President Gamsakhurdia blocked this effort and Abashidze came to power in 1991 as the Chairman of the Supreme Council of the Autonomous Republic of Adjara. He focused on economic self-determination and enhancing relations with Russia and Turkey (Cornell 2001b: 177). While avoiding the bloodshed that plagued Ossetia and Abkhazia, Abashidze gave unyielding support to the Russian armed forces stationed in Batumi, and also prevented Georgian border troops from patrolling the border with Turkey. In the late 1990s, Abashidze also began to increase his profile by engaging with Georgia's separatist regions, visiting Abkhazia in 1998 and even suggesting an alliance with Javakheti (Jamestown Foundation 1998).

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[8] Interview with Ghia Nodia, Chairman of the Board, CIPDD, Tbilisi, Georgia, November 2003.
[9] Interview with Arsot Voskanyan, Government of Armenia Ministry of Foreign Affairs, Policy Planning Staff, Yerevan, Armenia, July 2003.

State structures in Adjara were dominated by a few clans related to Abashidze and his wife, and he governed a tightly-controlled regime, particularly concerning investments (Wheatley 2005a: 115). His assets included the lucrative port of Batumi linked by rail to Baku, plus the Sarpi border crossing with Turkey. There were confrontations between Shevardnadze and Abashidze regarding the latter's unwillingness to pay taxes, tariffs, and customs fees to the central budget. A Member of Parliament from Adjara, Hamlet Chipiashvili, explained that for every US$ 12 million Adjara sent to Tbilisi, they only got back US$ 1 million, which was not enough to pay for the army and police. As a result, Adjara stopped sending funds in 2000.[10] The Finance Minister of Adjara, David Gogoshvili, clarified that as of 2003, he had twice initiated paying back the money owed to Tbilisi, but his attempts were rejected.[11] It was believed that the non-payment to the central budget was the result of a deal struck between the two politicians, in which Abashidze agreed to back Shevardnadze in the 2000 presidential election with the support of his political machine 'Revival' in exchange for financial independence.[12] Others suggested that part of this deal was that Shevardnadze guaranteed that the 'Revival' party would always meet the 5 percent threshold for inclusion in Parliament.[13]

The trans-territorial networks traversing regions of Georgia were predisposed to criminal activities and violence, creating an unstable environment and increasing the power of criminal organisations over official bodies and citizens. As South Ossetian researchers wrote, 'Economic systems – in an extremely truncated manner – have been created in [the separatist regions] that provide for the survival of most of their residents, while simultaneously creating the conditions for enriching criminal organisations' (Dzhikaev and Parastaev 2004: 184). The merger of state and criminal entities, both within Georgia as well as across separatist borders, had multiple effects on Georgia and its neighbours. Key positions in law enforcement agencies were for sale; the price of a position could eventually be recovered from engaging in

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[10] Interview with Hamlet Chapiashvili, Member of Parliament from Adjara and Deputy Head of Foreign Affairs Committee, Revival Party, Tbilisi, Georgia, July 2003.
[11] Interview with the Dato Gogiashvili, Minister of Finance of Adjara, Batumi, Georgia, July 2003.
[12] Interview with David Darchiashvili, Tbilisi, Georgia, July 2003.
[13] Interview conducted by Jonathon Wheatley with Tamaz Diasamidze, Batumi Republican Party, Tbilisi, Georgia, June 2004.

smuggling and extraction of rents along smuggling corridors.[14] There was also a general proliferation of 'criminal' societal practices within these regions, including the role of *consumer* networks in smuggling petrol, tapping gas pipes, and stealing electricity. In a survey conducted by the Centre of Economic Corruption Monitoring in Georgia, 58 percent of respondents did not consider stealing electricity to be a crime when the state is negligent (24 Hours Newspaper 2004). What was perhaps most dangerous, however, was that the same transit corridors established for petroleum products could be used for other commodities, from drugs to weapons and components of weapons of mass destruction (Cornell 2002b). By the early 2000s, Georgia was at the crossroads of the Afghanistan-Europe heroin traffic, as well the Russia-Middle East arms smuggling (Cornell 2003).

Some analysts believed that the existence of trans-territorial networks discouraged the resolution of the secessionist conflicts. King, for example, explained that because of the 'beneficial economics of stalemate', both sides were willing to negotiate, knowing that very little, if anything, would be implemented due their interests in maintaining the stalled status of the conflict (King 2001). Vaux suggested that the financial benefits from operating within trans-territorial networks traversing separatist zones and unrecognised borders were so substantial as to encourage the political elite to maintain the 'frozen' status of the conflicts for much of the Shevardnadze era (Vaux 2003). A recent study conducted by the NGO, International Alert, corroborated Vaux's argument with interviews conducted in the field. The report suggests that the *elite* in Georgia and the non-recognised entities were comfortably benefiting from the situation and that they had no effective settlement plan to offer the citizens of these entities (Mirimanova 2006: 16). In the study, a Georgian government official explained,

> [...] let's say simply that the conflict in South Ossetia in the end revolved around the problem of Ergneti and the main representative of the previous government [under President Shevardnadze] in the figure of the governors of Kvemo Kartli[15] and Gori [the administrative capital of Shida Kartli],

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[14] Interview with John Wright, Political Advisor, European Centre for Minority Issues, Tbilisi, Georgia, April 2005.

[15] Levan Mamaladze of Kvemo Kartli was the longest serving and most powerful governor in Georgia. His children were baptized by the late Zurab Zhvania and he was intimate with most of the *elite* during

> [who] had a partial share in the Ergneti market and directly profited from the conflict (Mirimanova 2006: 18).

Some experts, such as Jonathan Cohen, took issue with the 'vested interests' argument, citing numerous reasons for the non-resolution of conflict, such as historical grievances.[16] It is difficult to make a direct correlation between the trans-territorial networks and the 'stalled' status of the conflicts in the South Caucasus. Given the examples provided in this thesis, however, financial incentives do appear to have been a major factor in delaying a settlement. Firstly, the levels of violence among competing groups in the grey market depleted confidence between the sides. And, secondly, the power of the *elite* rested in the financial benefits gained from their sponsorship of the trans-territorial networks.

In juxtaposition to the idea that trans-territorial networks harmed conflict resolution, they were also a medium for cooperation among stakeholders. Cooperation was a particular feature of the Ergneti market, as described in Chapter 6, in which Russians, Ossetians, and Georgians worked together for almost a decade. However, this cooperation was halted in June 2004, when President Saakashvili began a concerted effort to break the trans-territorial networks operating through South Ossetia by closing the Ergneti market. Traffic through the Roki tunnel on the Russian border side of the border with North Ossetia was initially halted. All imports of petrol and petrol products were to be directed first to Tbilisi for official accounting purposes and then distributed out to the regions. As a result, the only official checkpoint on the border between Georgia and Russia, at Kazbeki, reported a five-fold increase in revenues from imports, jumping from 900,000 GEL in August 2004 to 4.6 million GEL in January 2005 (Sepashvili 2005). However, in early 2005 the new governor of Shida Kartli, Mikheil Kareli, was accused of knowing about the 'Tkviavi group', which was allegedly still running contraband from Russia to Georgia through South Ossetia, using towns in Gori as transfer points (Biganishvili 2005). President Saakashvili sacked over 20 top police officials in Shida Kartli for participating in trans-territorial networks (Freese 2005a). Compounding the loss of the market was

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the Shevardnadze era. His control over the Kvemo Kartli region and the financial benefits garnered from a substantial share in the trade through Ergneti market likely bolstered his power.

[16] Interview with Jonathan Cohen, Co-Director of the Caucasus Programme, Conciliation Resources, London, UK, April 2003.

the Georgian government's decision in May 2004 to order the Interior troops to make incursions into South Ossetia allegedly to stop illegal trade. The real goal was to repeat the successful ousting of the *de facto* leadership, as they had accomplished in Adjara. However, this time the Ossetians with the help of Russian arms and ammunition, defended their separatist status and, after six weeks of low level conflict, the Georgian troops retreated (International Crisis Group 2004b).

Ultimately, the losers in Saakashvili's closure of Ergneti market were the *consumers*, who were almost totally marginalised from participating in the cross-border trade. The closure brought about the loss of the major source of income for poor Ossets and Georgians, the loss of a source for relatively low priced goods, and the destruction of a regular meeting place between the two populations (Areshidze 2004). The Ossetians became more convinced that the new leadership in Tbilisi was not acting in their interests and the anti-contraband campaign turned into a sustained low-level armed conflict, reigniting tensions among the now isolated and divided communities. Whereas previously the resolution of the conflict with South Ossetia appeared to be easier than that of Abkhazia, the participants in the South Ossetian conflict became just as intransigent as the Abkhaz. The cooperation among various groups in the Ergneti market could have provided a means through which the conflicting sides learnt to coexist, thus making resolution more possible. For example, the Georgian government could have chosen to regulate the market, rather than close it down completely, thereby demonstrating to the residents of South Ossetia how a more fair and transparent system of business could benefit all sides. Thus, it appeared that while vested interests may have prevented a resolution to the conflicts for much of the Shevardnadze era, Saakashvili's approach of restricting trans-border trade actually escalated the confrontation and resulted in a deeper level of mistrust.

The participation of Georgian armed forces, security services, politicians, and state-sponsored guerrilla groups in the trans-territorial networks with Abkhaz groups undermined the credibility of the Georgian state. The competition for control of the smuggling networks damaged efforts by the Georgian government to convince the Abkhaz that living together was in their interests. This fostered the perception among residents of Abkhazia that Georgia lacked transparent and accountable governance and civil society institutions, as well as a fully-fledged private sector and market economy.[17] Vaux explained that if Georgia wanted to establish its credentials as a functioning nation-state, it was going to have to reduce the power held by criminal groups (Vaux 2003). The confidence residents of Abkhazia had in the Georgian state was further eroded by violence in the Gali region of Abkhazia (Wennmann 2004). The same forces that were meant to be protecting Georgian citizens in Gali were actually perpetuating violent clashes with the Abkhaz, making their lives extremely difficult. A group of Georgian researchers argued that,

> The limitation of democratic freedoms, especially at the grassroots level, has led to the formation of political clans who dispose of public property in their own interests and keep citizens in extreme poverty. They use militant ideologies and corrupt, coercive and criminal structures to keep citizens terrorized (for example, through a permanent irrational fear of war) or implant feelings of revenge in their minds [...] Any democratic change is a serious threat to the power of the ruling groups (Kukhianidze, et al. 2004).

This lack of faith in Georgia as a responsible interlocutor also led to greater cooperation between the separatist regions and Russia, as well as among the separatist regions themselves. Russia actively enhanced the livelihoods of the citizens of these regions through multiple channels of assistance (Popescu 2006). Militarily, the support came in the form of military forces, bases, and the training and equipping of secessionist forces. Economic support included subsidies, paying pensions, special trade regimes, investment in the infrastructure and companies, banking, energy subsidies, and providing passports for easier transit to Russia for work. Politically, Russia increasingly convened meetings of the heads of the separatist regions in Moscow and was viewed by Georgians to be representing the separatist agenda in multi-national consultations, such as the Joint Consultative Committee on South Ossetia and at the United Nations on Abkhazia. The separatist regimes recognised one another's right to independence, signed trade agreements, and promised to support one another in military conflict with Georgia. Further, Russia delegated its former civilian and military leaders to serve in key posts in the unrecognised governments. For example, the defence ministers of both Abkhazia (Sultan Sosnaliev) and South Ossetia (Anatoli Barankevich) were appointed by Russia. The

[17] Perception gleaned from discussions with a cross-section of residents of Abkhazia in July 2003 and July 2005.

former Abkhaz Prime Minister in 2004/5, Nodar Khashba, previously worked in the Russian Ministry of Emergencies, and Prime Minister Morozov of South Ossetia was sent from Russia (Popescu 2006; Socor 2006a). These policies ultimately strengthened the position of the secessionist regimes and enabled them to survive economic sanctions and isolation, as well as to become more forceful in their calls for international recognition as states.

For the Georgians, the trans-territorial networks probably provided a cover for incursions into Abkhazia to collect intelligence information. They also lent credibility to the argument that the separatist authorities were unable to maintain control over their territory (although at the same time they also made it clear that the Georgian authorities were equally unable to maintain control over Georgia). What is unclear, however, is why, if its aim was to resolve the conflicts, the Georgian government maintained support for the trans-territorial networks. There is a possibility that if Georgia had stopped participating in these networks, particularly the more lucrative ones transiting illicit material, that violent activity would have decreased, deflating the power of the paramilitaries seemingly acting as independent criminal operatives. Eventually, this could have fostered a better environment for negotiations, and given greater credibility to the Georgian side in negotiations over the more difficult points of negotiation, such as whether the residents of Abkhazia would allow Tbilisi to once again be responsible for their territorial security.

7.4 Regional Relations

Georgia's location along a hydrocarbon rich corridor, combined with its status as an energy deficient state, should have encouraged the government to integrate its energy system with the neighbouring states Armenia, Azerbaijan, Russia, and Turkey. As one expert explained,

> Cheap and accessible energy could become a driving force behind the development of the entire economy, helping it to attract investments and extricate the countries from the clutches of economic collapse. Creation of an integrated energy market and, ultimately, some kind of South Caucasian economic formation may be the only way to disavow the pessimistic forecasts about the region's future (Khachatrian 2001).

In addition, regional integration could have enhanced Georgia's economic efficiency and sustainable growth, and created a platform for cooperation among the neighbours in other sectors. By the second half of the 1990s there was increased interest among the regional states to reconnect the South Caucasus into an integrated energy system, or, at the very least, to enhance energy cooperation. By 1998, the region had experienced several years of stable economic growth. Plans were underway to diversify the upstream sources for exporting Caspian hydrocarbons to Europe, and electric energy flows were being incorporated into these plans (Strategic Research Centre 2004: 313).

Azerbaijan was already exporting crude to Europe by rail through Georgia, and the government had plans to expand its oil refining industry. According to 1998 data, Azerbaijan exported US$ 145 million-worth of petroleum products to the CIS states, and approximately twice as much to other countries. At the same time, Georgia and Armenia imported petroleum products amounting to US$ 422 million. Thus, a vast potential market existed for Azerbaijani energy resources (Khachatrian 2001). By 2001, progress was also underway to create a multi-state regionally integrated electricity enterprise, *Pontoil,* including Russia (*RAO UES* with 40 percent), and 20 percent each for Armenia (*Armenergo*), Azerbaijan (*Azerenerzhi*), and Georgia (*Sakenergo*). The goal was to ensure stable electricity supply in the region and eventually to export electricity. However, *Pontoil* was hindered by bureaucratic inefficiency in the individual states, and the political and economic blockade between Armenia and Azerbaijan (Khachatrian 2001).

Because of its geo-strategic position, Georgia was the recipient of numerous grants under the European Union-sponsored TRACECA (Transport Corridor Europe-Caucasus-Asia) or 'Silk Road' project that sought to upgrade and integrate rail and road transportation networks from China to Europe in an effort to promote trade ties (Edmunds and O'Brien 2003). In the Caucasus, TRACECA provided the only properly functioning multi-state east-west transport corridor, diversifying the transit routes from the previously Russian dominated north-south routes (Edmunds and O'Brien 2003). Many bilateral and multilateral transportation agreements between countries in the region, often supported by the US or by other western states, corresponded with the spirit of the TRACECA and enhanced the transport of petroleum products across the region. Notable among them were the 1996 agreement between Georgia, Ukraine, and Azerbaijan on the construction of a transport corridor, and the agreement between the EU, France, Georgia, and Armenia on the reconstruction of a highway linking Georgia's Black Sea port, Poti, to Yerevan. Moreover, beginning in 2000, the group of countries comprising the Black Sea Economic Cooperation (BSEC) organisation sought to form a regional electricity market and network of oil pipelines, although many of the regional objectives remained in the planning stages.[18]

This is due to the fact that long-term and beneficial regional cooperation in this sector would have required the implementation of practical measures, such as harmonisation of national trade, customs and border legislation, and strengthening pipeline protection capabilities. However, these measures were never implemented (Salukvadze 2001). Instead, cooperation among Georgia and its immediate neighbours in the South Caucasus remained dominated by non-transparent trans-territorial networks across borders, which limited the use of Georgia's strategic location fully for shipments from the Caucasus and Central Asia to Europe. The Soviet legacies addressed in Chapter 4 which affected all the post-Soviet states, such as the shadow economy and patrimonialism, acted as negative re-enforcers and worked towards strengthening informal networks. All three states were dominated by non-transparent trans-territorial networks, particularly in the energy sector. When this group of weak states attempted to cooperate, the *nomenklatura* monopolised business arrangements and co-opted the *bureaucracy*, to the detriment of the development of an effective and integrated system. An IMF study on the Caucasus reported that 'the obstacles to regional energy reform are severe. They stem primarily from strong vested interests, such as owners of transit pipelines and energy resources as well as governments that receive a share of the monopoly rents' (Dodsworth, et al. 2002). The level of corruption and criminality was thought to be so high as to prevent the realisation of most energy integration projects (Strategic Research Centre 2004: 314). The extraction of legal and illegal payments often led to delays and increased the cost

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[18] The BSEC members are: Albania, Armenia, Azerbaijan, Bulgaria, Georgia, Greece, Moldavia, Romania, Russia, Serbia-Montenegro, Turkey, and Ukraine.

of doing business, and thus discouraged investment in creating a more transparent and integrated system (Ollivier, et al. 2003).

Increasingly, the idea of regionalism became unpopular within the South Caucasus, and it was only kept alive in the policies and programmes of Trans-Atlantic organisations and western governments. A leading Georgian analyst on the South Caucasus agreed with Buzan's description of the region as linked through enmity or hostility rather than amity (Buzan and Wæver 2003).[19] Rather than work together, the three South Caucasus states sought to strengthen their energy security through alliances with regional and non-regional powers. Tom de Waal argued that the vested politico-economic interests of the three South Caucasus states kept them divided, obstructing the development of a 'common Caucasian market'. Each state focussed first internally on their own issues and then secondly on external relations. For Georgia, the focus was primarily on enhancing relations with America and Europe (de Waal 2005).

All three states became increasingly dependent on Russia for the supply of gas and electricity. As a result, Russia was able to re-assert itself as the dominant player in the states' energy infrastructures. Armenia became dependent on Russia, while also increasing cooperation with Iran as a source of gas. By 2006, Russian state-owned companies controlled 90 percent of Armenia's energy sector, including all electricity generation, and distribution networks (Karapetian 2006). *Gazprom* gained a controlling stake in the Iran-Armenia gas pipeline by raising its stake in the Russian-Armenian company *ArmRosGazprom* from 45 to 58 percent (Socor 2006d). Azerbaijan was also reliant on Russia for power generation, importing Russian gas and buying electricity from *United Energy Systems* (*UES*) (Muradova and Abbasov 2006). Under the leadership of Chubais, *UES* expressed designs on ownership of the CIS electricity generating facilities and transit grid in order to dominate the export to Europe (Drankina and Klasson 2003).

The domination of non-transparent activities of the stakeholders in trans-territorial networks limited the role that Georgia could play as a transit corridor from Central

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[19] Interview with David Darchiashvili, Director, Soros Foundation, Tbilisi, Georgia, April 2005.

Asia to Europe. The major rail transit from Baku to Batumi was hindered by delays, rents, and diversions. During the Shevardnadze era, it took 7 to 12 days for rail transit from Baku to Batumi, which could have been reduced by 4 days through proper investment and management (Ollivier, et al. 2003). Further, the potential of the Batumi oil terminal was never realised due to a lack of investment. The manager of Batumi's oil terminal, Jan Bonde Nielson, and his company, *Greenoak*, invested US$ 39.8 million in modernising the terminal in the late 1990s, and an additional US$ 24 million was expected to be invested. From 1997 to 2000, Chevron sent 60,000 barrels of oil per day by rail from Baku to Batumi, employing the company Caspian Transco, a Turkish company owned by the billionaire, Okan Tapan, to coordinate the effort (International Crisis Group 2004a). However, due to the instability in Georgia in the late Shevardnadze era, the Overseas Private Investment Corporation (OPIC) postponed providing additional funding for the Batumi terminal. As a result, Georgia experienced an 11 percent decrease in petroleum shipments from Baku to Batumi from 2001 to 2003. The decrease was also related to increased competition from oil terminals in Iran and Makhachkala, Daghestan.

Perhaps the primary reason behind the lack of a regional energy programme was that the South Caucasus lacked a security framework upon which to base cooperation. Various attempts were made to formulate and codify such a security framework, but the efforts remained on paper. On March 8, 1996, Presidents Shevardnadze and Aliyev signed a 'Declaration on Peace, Security and Cooperation in the South Caucasus'. At the April 1999 Washington NATO summit, the US tabled the idea of a Caucasian Cooperation Forum, but it did not materialise. In November 1999, at the Instanbul OSCE summit, President Aliyev invited the US, Russia, Turkey, and the South Caucases states to sign a 'Pact on Security and Cooperation in the Caucasus' as a basis for relations among the states in conflict settlement. It called for a regional security system that included all actors plus the EU. Then, on January 15, 2000 while visiting Georgia, Turkish President Suleyman Demirel suggested a 'Stability Pace for the Caucasus' to be guided by OSCE principles. Meanwhile, Moscow was supporting a series of meetings of the Caucasian Four (Russia plus the three South Caucasus states). Despite all of this shuttling between capitals, documents, and promises to move forward as a region in resolving conflicts and deciding on mechanisms for greater cooperation, none of these projects came to fruition. In actuality, official relations were undermined by the predominance of the grey market activity.

7.5 Trans-Caucasus Pipelines

Map 7 - Trans-Caucasus Pipelines

Source: (Energy Information Administration 2007)

Given the difficulties faced by foreign companies investing in Georgia's energy sector, it may seem paradoxical that the most successful and lucrative foreign investment project in Georgia during the Shevardnadze era was the construction of two new hydrocarbon pipelines traversing its territory. These were the Baku-Tbilisi-Ceyhan (BTC) oil pipeline and the parallel Baku-Tbilisi-Ezerum (BTE) gas pipeline, more often referred to as the South Caucasus Pipeline (SCP) (see Map 7 above). In November 1997 President Clinton announced the idea of a 'Eurasian Transportation Corridor' to enhance the Caspian-European hydrocarbon transit route. This project came to be known as the 'East-West Transit Corridor', as opposed to the Russian-dominated northern routes that monopolised energy transit from the Caspian to Europe (Elkind 2005). One of the strategic motivations behind this policy was an effort to reduce the West's over reliance on tankers carrying crude oil through Turkey's Bosphorus Straits, estimated to handle 3.5 percent of the world's daily oil transport, as well as to prevent Iran from becoming a major transit country for

Caspian hydrocarbons to global markets (Hill 2001). With the BTC, oil would go directly from the Caspian Sea to the Mediterranean Sea over land. British Petroleum (BP) and its partners in these projects gave formal approval for the BTC pipeline in August 2002 and the SCP pipeline in February 2003.

Despite the monopolisation of major investment projects in Georgia's energy sector by *elite* groupings and the potential for trans-territorial networks to divert resources from the state, the Trans-Caucasian pipeline project remained relatively free from spoilers. The pipeline project is an interesting case on which to test the parameters of trans-territorial networks. Why was it that this project survived the *elite* network interests and was able to unite several South Caucasus states, all the while operating in a generally transparent mode? There were several converging circumstances that kept the pipeline project relatively free from deal-breaking schemes. The first was that, in Georgia, President Shevardnadze was the patron of the BTC project. After a meeting in Tbilisi with the Chief Executive of BP, President Shevardnadze told a Georgian radio programme,

> Mr. John Brown once again formally confirmed the final decision taken by the BP management that the company would undoubtedly implement both the Baku-Tbilisi-Ceyhan major oil pipeline and the Baku-Tbilisi-Erzerum gas pipeline projects. For my part, I said that Georgia would continue to provide as much assistance as possible to British Petroleum and other companies involved in the implementation of these projects. There is no exaggeration in saying that the Georgia president is the main guarantor of this. I personally have been watching closely all the negotiations on the oil and gas pipeline issues and I will take the final decision on behalf of Georgia so that there will be no need for the parliament to adopt a law on the issues. I have also been personally coordinating all the large-scale work being done in this respect (Georgian Radio 2001)

Shevardnadze assigned primary responsibility for this project to the Georgian International Oil Company (GIOC), established in 1995. He named Giorgi Chanturia, one of his closest allies, to preside over GIOC and act as his special envoy on every aspect of the pipeline project. Prior to this, Chanturia had served as Ambassador to Azerbaijan and had befriended the son of the president, Ilham Aliyev, who headed Azerbaijan's state oil company (SOCAR) from 1994 until 2003, when he was elected to succeed his father as president of Azerbaijan. Shevardnadze also personally selected members of a special working group to coordinate the pipeline project overseen by Chanturia.

The second factor that protected the pipeline project was that Shevardnadze's *elite* clientelistic network in the energy sector was not threatened by the construction of the pipelines. This allowed him to sustain their continued loyalty while ensuring the success of the project. No oil and relatively little gas from these pipelines were meant for the Georgian internal market. That is, there was no threat to the Georgian-Russian distributors of oil and gas who monopolised the Georgian market. None of the estimated 148,000 barrels of oil per day pumped through BTC was meant for Georgian consumption. Even with the increase gas volumes from SCP, it was only expected to supply Georgia with 5 percent of its overall gas volume by winter 2007. (Georgia received 3 billion cubic meters (bcm) of gas per year from Russia, half of which it transported on to Armenia.) Georgia could explore options to buy more gas from SCP at a special price (US$ 55 per 1,000 cubic meters) for 20 years. There were periodic attempts by *Gazprom* to secure control over the transit rights of all gas transit within Georgia, including the SCP pipeline, but a vigorous campaign by the US government thwarted such efforts each time.

The third factor that kept the pipelines free from spoilers was the anticipated boost to Georgia's economy this project would provide, rewarding stakeholders in the *bureaucracy, business groups*, and *consumers* in Georgia. A macro-economic assessment conducted by the EBRD stressed the importance of the pipeline construction and related investment for Georgia's overall economic activity (EBRD 2004). The total cost of the BTC pipeline was almost US$ 4 billion, while that of the SCP was US$ 3.2 billion. Approximately 70 percent of BTC costs were funded by finances from third parties. The BTC project brought unprecedented levels of revenue, local employment opportunities, and initially raised investment perspectives in Georgia. More than US$ 200 million was spent in Georgia, making the BP consortium the largest single source of foreign expenditures. At its peak, more than 6,000 people were employed in construction, more than 75 percent of them Georgian nationals. Additionally, more than 3,000 landowners received over US$ 18 million in compensation. Transit revenues were projected to exceed US$ 700 million and average annual income at its peak throughput was expected to be around US$ 50 million. Ongoing annual expenditures of BP were expected to be US$ 35 million a year, with the continuing employment of around 300 persons. The pipeline project was also accompanied by US$ 80 million in social and economic investment commitments in Georgia (Digings 2005). Moreover, BP made US$ 1 million available to pay for electricity supplies for vulnerable citizens in the winter months (Sarke Information Agency 2004). As a result of the project, unemployment was projected to diminish by around 33 percent overall, and GDP growth rates were estimated to reach 6.6 percent (Tvalchrelidze 2003). The IMF anticipated that if both pipelines (BTC and SCP) were filled to capacity, Georgia could expect to receive around 1 percent of GDP in additional revenues, which would significantly contribute to the country's low tax revenue (Billmeier, et al. 2004).

The fourth circumstance that kept the pipeline projects free from illicit activity was the participation of a consortium of European and American banks and western oil companies. This meant that the process was tightly controlled, well managed, and relatively transparent. According to a BP consultant, the problem with doing business in Georgia was a contradiction between various laws, combined with a weak legal structure (e.g. efficacy of the courts, clear regulatory systems, and clear licensing processes). In dealing with the Georgian government, BP took precautions to avoid a scandal. There was not only a corporate image to uphold, but there was pressure from banks to ensure that there was no corruption associated with the project.[20] The major lenders — the EBRD and the IFC — insisted that the participating banks and companies operate efficiently and according to strict legal requirements.[21] Hence, a variety of mechanisms were established to reduce, if not eliminate, the potential for illicit activity. A 'ring-fence' was placed around the projects in the form of intergovernmental agreements (treaty law) and host government agreements concluded with each of the three countries. In practice, this meant that a lot of power was taken out of the hands of the Georgian government and placed with BP. In Georgia, the Host Government Agreement ceded sovereignty over the details of

[20] Interview with Jonathon Elkind, independent energy consultant and former Director for Russian, Ukrainian, and Eurasian Affairs, National Security Council, US Government, 1998-2001, London, UK, June 2005.

[21] The group providing loans, export credits and risk insurance to BTC was composed of export credit agencies of seven countries and a syndicate of 15 commercial banks. British Petroleum had the lead over 11 oil company partners from Azerbaijan, France, Italy, Japan, Norway, Turkey, and the US. Companies involved in the SCP were from the UK, Norway, France, and Azerbaijan.

project management to BP, with the company acting as the primary consultant to GIOC. Compared with Azerbaijan, where the state company SOCAR was the regulator and owner of the pipeline, GIOC had only a minor financial stake. BP also signed a detailed Memorandum of Understanding with Eurasia Foundation in Tbilisi that gave it the right to oversee a consortium of NGOs with monitoring responsibilities over the pipeline regarding social issues in the communities affected by the project, including land ownership issues, environment protection, historical preservation, local business content, and protection of the rights of workers involved in the project (British Petroleum 2004). This was complemented by a region-wide initiative by George Soros' Open Society Institute to monitor the project.

A fifth factor that protected the pipeline project was that the legal and regulatory mechanisms related to the BTC project were isolated from the rest of the political and business climate in Georgia. Despite hopes that the construction of the pipelines would lead to 'an anti-monopoly, open, transparent, and competitive environment in Georgia', as expressed by delegates to the annual 'Georgia International Oil, Gas, Energy and Infrastructure Conference' in Tbilisi in 2003, in fact the pipeline project did not impact on the conduct of business in Georgia (Gladchenko 2003). The western oil companies and financiers had very little influence over Georgian politics, the management of the broader energy market, or the overall investment climate in Georgia. In fact, at the same time as the pipeline projects were getting underway, foreign investors in Georgia's market, *GAOR* and *AES Telasi*, were being forced out of the country. Further, BP limited its long-term investments in the region. It had the opportunity to take an even larger stake in the oil field in Azerbaijan, for example, or it could have carried GIOC as a financial partner, thereby investing more in the future viability of the Georgian state oil company. BP could also have invested more in the other aspects of Georgia's energy infrastructure, such as buying *Telasi* from American *AES*.[22] Instead, BP and its partners determined to stay out of Georgia's broader energy market. That said, the project did have an impact on the socio-political dynamics, for example, by negotiating with local groups for land use, transferring skills in technical and civil areas, employing conflict resolution in accordance with

[22] Interview with Robert Corzine, former journalist for the Financial Times, consultant to British Petroleum, Istanbul, Turkey, August 2005.

local practices, expanding the scope and depth of non-governmental organisations in terms of monitoring, and enhancing cooperation between Azerbaijan, Georgia, and Turkey (Starr and Cornell 2005).

Finally, noticeably absent from the pipeline project were the Russian *elite* and Georgian-Russian *business groups*. When the US government and western oil companies started actively pursuing the goal of diversifying hydrocarbon transit routes from the Caspian region away from Russian dominated pipelines, there was a negative response from the Russian government. In particular, President Boris Yeltsin considered the Caspian Sea to be Russia's energy domain. Prime Minister Viktor Chernomyrdin was associated with the powerful Russian oil lobby, led at that time by *LUKoil*, and was also initially opposed to US involvement. However, the US government devised a package envisaging multiple pipelines and Vice President Al Gore conducted regular consultations with Prime Minister Chernomyrdin about the package, leading eventually to the Russian government's acquiescence.

They agreed that the first stage would include the construction of a new Caspian Pipeline Consortium pipeline, known as the Northern Route, carrying 'early oil'. Chevron would take the lead in securing links between Tengiz and Atyrau in Kazakhstan with the Russian Black Sea port of Novorossiysk. Chevron came away with the largest holding within the consortium of 15 percent and *LUKoil-ARCO* (Russian-American joint venture) had the second largest holding of 12.5 percent. *LUKoil* was put in charge of constructing the pipeline and appointing the Caspian Pipeline Consortium's general director. The first stage would also involve the AIOC, a BP-led consortium, sending oil from Azerbaijan's Chirag field north through the Russian pipeline to Novorissysk, and west to Supsa on Georgia's Black Sea coast in a rehabilitated pipeline. Eventually, over 70 percent of pipeline oil exports from Azerbaijan were routed through the Baku-Supsa pipeline, as the Russian route was subject to higher fees. There were also quality issues related to blending the oil with a lesser grade from Siberia, and frequent closures, in part due to instability in Chechnya (Ollivier, et al. 2003). The second stage would be the AIOC's development of the Azeri-Chirag-Guneshli fields (ACG), with *LUKoil* holding a 10 percent share, which it relinquished in 2004. *LUKoil* also obtained a 10 percent interest in the Shah-Deniz field in the southeast Caspian in a consortium led by BP. Finally, when the decision was taken in 2002 to build a new oil pipeline from Baku to Ceyhan through Tbilisi, Russian companies did not compete for the contracts (Karagiannis 2002).

The relative freedom of the business framework from trans-territorial networks does not mean that there was no local illicit activity. Chanturia, the head of GIOC, was thought to have set up his own devices for profiting from pipeline construction, including side companies from which he took a percentage of business deals made with locally contracted companies in Georgia.[23] One BP senior manager explained that the 'right amounts of money were channelled into the right networks in terms of management, development, and construction.' In return, Chanturia 'delivered' the necessary networks to BP.[24] The process was also not free from profiteers, particularly among stakeholders in the *bureaucracy* and *business groups* along the pipeline route. There were problems regarding regional politicians buying up tracts of land along the pipeline route from unsuspecting citizens and then making a large profit in the resale of this land to BP. For example, BP bought land in Alkhakalaki area for US$ 50,000 per acre, but Chanturia is alleged to have paid the families only US$ 5,000 per acre. Moreover, a network of local politicians and businessmen forced those compensated for the use of their land to hand over a percentage of their reparations.[25] The *gamgebeli* of Borjomi was fired in spring 2003 for a scandal related to land sales for the BTC pipeline track. There were also plans by some local networks to establish facilities to tap into the BTC pipeline, much as they did with the Baku-Supsa pipeline, to extract crude oil and sell it. BP found newly constructed storage tanks along the Turkey-Georgian border at Vale, between the pipeline route and the train station. From these storage tanks a 15 inch pipe ran to the Turkish border. It appeared that some businessmen were determined to tap into the BTC pipeline and transport oil from it via railcar for sale elsewhere.[26]

However, the geo-political factors in support of the pipeline project seem to have overridden the factors in favour of potential spoilers. One regional energy expert refers to the 'politicisation of pipeline routes in the South Caucasus' (Adams 2000).

[23] Interview with Jonathon Elkind, June 2005.
[24] Interview conducted off-record with energy company employee, Tbilisi, Georgia, April 2005.
[25] Interview with Gia Kopadze, Chairman of the New Rights Party. He was the Gamgiabeli of Alkhakalaki from 1991 to 1995, Samskhte-Javakheti, Georgia, July 2003.
[26] Interview conducted off-record interview with energy company employee, Tbilisi, April 2005.

That is, the importance of the pipeline to Europe's future energy supply, to America's push to diversify supply routes from Russia whilst isolating Iran, and to Turkey's efforts to bolster its position as a hydrocarbon hub whilst finding alternatives to the use of the Bosphorus straits, all worked in its favour. In particular, the alliance between the leaders of Azerbaijan, Georgia, and Turkey, with the backing of President Clinton and EU member states, meant that there was too much to lose for it not to succeed. For Heydar Aliyev, an export route for Azerbaijan's Caspian hydrocarbons was essential to the state's future development. For Eduard Shevardnadze, the pipeline cemented Georgia's status as a reliable transit route and bridge between Central Asia and Europe. For Suleyman Demirel, it enhanced Turkey's configuration in regional politics, in particular its influence over events in Azerbaijan and Kazakhstan. It also enhanced Turkey's role as a responsible energy hub for Europe. The success of this project suggests that only a large-scale foreign investment project of geo-strategic significance, protected by a 'ring fence' of documents ceding state rights to the consortium that did not compete with family business, could succeed in Shevardnadze's Georgia.

The Trans-Caucasus pipelines were a visible symbol that the region was of strategic importance to western security organisations, NATO and the EU, as well as being a pivotal geo-strategic area for the US, Russia, Iran, Turkey, and European states. The South Caucasus provided the only corridor connecting NATO member states with Central Asia, Afghanistan, and Iran. In the post-September 2001 campaign to impede global terrorist networks, the region served both as a staging ground for the military campaign in Afghanistan (air over flight and refuelling rights), as well as a place for terrorists to find a safe haven in Georgia's Pankisi gorge, as discussed in Chapter 3. After 2001, Georgia's weakness was viewed not just as a liability to strengthening the security of the South Caucasus, but also as an obstacle in the longer campaign against international terrorism. Preserving strategic access to this region, as well as securing the energy transit corridor, became the strategic priorities of NATO in the South Caucasus. However, for most of the first decade of Georgia's independence, reform plans sponsored by the EU and NATO did not seem to enhance the security of Georgia, nor were these organisations able to provide a security framework for the region. President Shevardnadze's periodic calls for Georgia's membership in the EU and NATO went unheeded. However, this is likely to have had as much to do with the organisations' 'expansion fatigue' and, in particular, the EU's lack of design for Eurasia. The European Neighbourhood Policy only included the Caucasus after active lobbying by the governments of the South Caucasus, and it was not until after the Rose Revolution in 2003 that the EU appointed a Special Representative for the South Caucasus.

After the 1998 and 2001 clashes between Abkhaz and Georgians in Gali and the escalation in violence in South Ossetia, the Trans-Atlantic organisations engaged in conflict resolution efforts in Georgia grew increasingly concerned about the possibility of an outbreak of war. After construction on the BTC pipeline began, security concerns about the separatist regions were linked to the energy security of Europe. Nevertheless, Georgian officials were unable to get the UN Security Council to consider expanding the peacekeeping mandate in Abkhazia beyond the CIS mandate. Nor was it able to break out of the perceived imbalanced 'peacekeeping' arrangement in South Ossetia in which Georgia had to deal with the 'troika' of Russia, North Ossetia, and South Ossetia. In the absence of a regional security framework, the Armenia-Russia-Iran triad (with participation from Greece) increasingly competed with the Georgia-Turkey-American triad (with participation from Azerbaijan) in terms of political, economic, and military assistance provided to the South Caucasus countries. While the CIS and other regional organisations struggled to effectively implement economic policies in the region, Russia was able to increasingly dominate the business sectors in the post-Soviet states, in particular the energy sector. This manifested itself in Russia's control over much of the CIS gas and electricity supply and export markets to Europe and Turkey by 2003.

7.6 Conclusion

The alternate force created by trans-territorial networks had a negative impact on Georgia's inter-state relations. Trans-territorial networks significantly weakened development prospects for Georgia. The networks were also a major contributing factor to the separatist tendencies in the state and the overall level of increasing violence and instability. The pipeline projects served as the exception to the rule that Russia was the only successful investor in Georgia in the Shevardnadze era. The energy sector was perhaps the most visible aspect of Georgia's decline and it played a role in the increasing perception of Georgia as a trouble spot in the region. For a decade, grants, loans, and technical assistance had been lost in non-transparent deals conducted in the grey market. Georgia's neighbours, however, could not stop cooperating with it. Turkey and Azerbaijan relied on Georgia as a critical link in the transit corridor for hydrocarbons. Georgia provided Armenia's only access route to Europe. In the end, however, the idea of a common energy market among the South Caucasus states and Turkey was made impossible by the lack of transparent mechanisms. Each state was left to establish independent relationships according to specific needs, resulting in often competing and inefficient arrangements.

What most scholars of Eurasia, and of Georgia in particular, find ironic is that while it was consistently rated the most corrupt and fiscally irresponsible government of the former Soviet states by international organisations, it continued to receive the most foreign assistance. So, in fact, the trans-territorial networks did not appear to have much effect on external actor's willingness to provide assistance to Georgia until almost the very end of the Shevardnadze era. That is, from 1995 until mid-2001, Georgia continued to receive assistance from the American and European governments, as well as the IFIs. This actually sustained the trans-territorial networks in Georgia, as was seen in the case of the American company's investment in Georgia's main electricity distribution company discussed in Chapter 5. This is now attributed, with hindsight, to the 'aura of Shevardnadze', the hero who had brought an end to the Cold War as Gorbachev's Foreign Minister. For the US government, it could also have had to do with an unspoken, and yet very evident, game of securing various transit routes across the Caucasus, as well as getting the post-Soviet states 'in their corner', away from the reach of Moscow.

There is speculation about whether Shevardnadze was the grand patron of this alternate force and whether he deliberately weakened the state for the gains of his family and elite clients, or whether he was too weak to control the numerous stakeholders. During his presidency, no direct evidence was ever made available linking him to corrupt acts. It is difficult to determine how much the alternate force relied on Shevardnadze and how much he was just another stakeholder, albeit one of the most influential ones. Did he directly order the undermining of *AES Telasi* and *GAOR*? Did he personally gain from selling state assets to *Gazprom* and *RAO-UES*?

Stefes explains that the truth about Shevardnadze lies somewhere between his allies, who said that the President inherited the system and had to rely on these structures for political support, and his opponents who believed that he was the cause of state weakness (Stefes 2005). Based on information gleaned from a series of interviews with members of his presidential administration who were also his friends over the years, it would seem that he placed most emphasis on preserving power through balancing various potential opponents. Thus, while his primary aim was not monetary gain (although the bank accounts of his family have never been publicly disclosed), nor undermining the state, he did manipulate the political system for the purpose of preserving power. As Stephen Jones observed in 1997,

> Shevardnandze's most surprising failure – given his reputation as a reformer and 'new thinker' – has been his passivity in the field of economic and political reform…[H]is adherence to the principle of balance between opposing political forces and loyalty to discredited colleagues has stalled reform, perpetuated the disintegration of institutional power, and undermined his credibility (1997, page 527).

It is clear that at some point he knew well what was happening, and he even appointed young reformers to serve as a check on the *elite* and *bureaucracy*. However, he would only intervene and punish some of the more flagrant violators of the law when the most egregious acts were exposed by the media or raised by western donors. His leadership style was a fluid process that relied very much on his personal well being. After the attempted assassinations on his life, and as he naturally aged, his level of control over situations ebbed and waned according to his mental faculties. It is not clear whether, by the early 2000s, he was completely in charge. Some believe that he was being told half-truths by his inner-circle, in particular the heads of the power ministries, who manipulated their positions to gain increasing power and assets. One of the best explanations for Shevardnadze's ultimate ruin was suggested by one of his closest confidants,

> Shevardnadze was ultimately discredited because he lost the moral right to address opponents in his government. He was implicated in allowing the undeserved to gain too much privilege. Shevardnadze got to the point where he was threatened by his own security services not to touch certain criminal persons operating on his territory. He was threatened [by the security services] with chaos, instability, and a return to the early

> 1990s turf battles between militias if he attempted to curb the power of criminal branches operating within Georgia.[27]

The next chapter will draw conclusions broadly from the thesis, focusing on theoretical implications of trans-territorial networks for Georgia's sovereignty, and discuss potential applications of the socio-political network model to other post-Soviet states.

[27] Interview conducted off-the-record with Georgian government official, February 2007.

Chapter 8: Conclusion

> President Saakashvili's 2006 Address to Parliament: We started with everything in ruins. We started when Georgia's existence as a state was finished. Our country was deprived of any dignity and people were deprived of their rights. We started from hopelessness, despair, injustice, the absence of electricity, the absence of salaries and pensions, and the absence of public order. We started from a point at which countries and nations usually cease to exist (Saakashvili 2006).

8.1 Introduction

The basic objective of the research conducted for this thesis was to discern the underlying reasons for persistent state weakness in post-Soviet states, despite over a decade of significant international assistance. Noting that the western security dialogue was increasingly naming weak states as a major threat to international security, the second objective of this research was to discern just how this threat manifested itself. To this end, I identified Georgia as an excellent example of a weak state because, despite receiving the largest per capita foreign assistance in the region, it was consistently rated among the worst performing economies and most corrupt governments. In particular, the thesis queried *why the Georgian state remained persistently weak, and what impact Georgia's weakness had on its inter-state relations.* Rather than follow conventional approaches to state weakness, which omitted features that appeared significant to understanding a weak state, a framework of analysis was devised, borrowing terms and references from the trans-national and globalisation literatures, as well as tools employed in network analysis. The state was reconceptualised as an arena of conflict, caught between local and global factors, traversed by state and non-state actors, who operated between the informal and formal economies. This created a new lens through which to understand how a variety of stakeholders operating in Georgia's energy sector could eventually undermine the strengthening of the state. For the most part, the trans-territorial networks that were identified as operating in Georgia negatively impacted on both the state's internal resources of supply, as well as hampering its ability to effectively use external support mechanisms.

This concluding chapter will begin with a review of what the thesis has demonstrated. Following from this, specific theoretical implications regarding the sovereignty of a weak state will be explored. The next section will address the limitations of the research presented in this thesis. In particular, it will examine whether this single country study can be applied to other post-Soviet states and, if so, what the variable factors will be that may differ among, for example, the South Caucasus states. It will also examine whether the fact that trans-territorial networks tend to serve as enablers in stronger states challenges the premise of this thesis. Finally, a future research agenda will be proposed, applying the network model to post-Rose Revolution Georgia, with some preliminary analysis of the operations of trans-territorial networks after Shevardnadze's presidency.

8.2 Main Findings and Conclusions

Most academic analyses of the phenomenon of weak states have been either subjective and tautological in nature, blaming weak institutions for weak states, or they have been objective taxonomical accounts measuring states according to the idealised Weberian model. These approaches have included works by institutionalists (Brock 2005; Sørensen 2004), post-colonialists (Clapham 1996; Reno 2000), and taxonomists (Rotberg 2004b). The other main approach to weak states has been ideational, in which the state has been viewed as constituting an arena of conflict between the government and its citizens (Buzan 1991; Holsti 1996). However, none of these approaches have adequately delved into the complexity of the causal factors of state weakness, in particular the intersection of actors in networks. Nor have they moved away from the predominant view that state and society are either cohesive or non-cohesive, and instead conceived of a state in which state and society act as a conspiratorial unit in their actions to undermine the state. The literature and policy reports on the weak state appear have been framed by the stronger states' agenda in addressing international terrorism, which prescribed a combination of democratisation and development to overcome weakness. Efforts to account for varying dynamics among states, such as historical, political, economic, and regional conditions that may perpetuate weakness have been minimal.

Georgia received unprecedented high levels of foreign assistance, yet it was paradoxically marked by extreme levels of abuse and neglect of the state's energy sector for much of the first decade of independence. Three periods of Shevardnadze's presidency were analysed, during which the economy and energy sector declined, rallied, and then deteriorated again. The first period saw the destruction and dilapidation of the energy sector during the war years (1991-1994). This was followed by a hopeful period of some deregulation and privatisation of small hydropower plants and Tbilisi's electricity distribution company (1995-1998). However, the 1998 Russian rouble crash led to a period of instability, from disinvestment and perpetual energy shortages (1999-2003), to mass protests on the streets of Tbilisi. The only positive development was agreement among a consortium of international energy companies, with the sponsorship of western governments, to build parallel gas and oil pipelines from Azerbaijan to Turkey, traversing Georgia. Throughout the three periods, the lethal combination of economic malaise, a perpetual energy crisis, and increasing reliance on Russian companies for energy supply not only left President Shevardnadze very unpopular with Georgian citizens, but also compromised the survival of the state.

Thus, rather than consolidating the empirical reality of a modern bureaucratic state, independent Georgia moved towards the creation of a personalised, kleptocratic, patrimonial regime with little interest in developing the state as such. Many Georgians viewed the internationally recognised 'state' as a medium through which to pursue operations that would gain them economic advantage in a resource starved market. This system allowed a variety of actors, including former Soviet *nomenklatura* from across the post-Soviet region, members of the security services, and trans-national *business groups* to act as vital sources of social, political, and economic authority in Georgia. Soviet structural and ideational factors and their post-Soviet manifestations served to support the interconnectivity among actors throughout the post-Soviet states. These included the practice of *blat* or providing services in exchange for favours, patrimonialism as a management tool within the governing structures, and the predominance of the informal economy. The common feature shared by all three factors was that they undermined the effectiveness of the state, while also compensating for its deficiencies.

The weak state was reconceptualised as a web of actors comprising networks that traversed the state. The networks consisted of stakeholders from some or all of the following four groups: *elite* (ruling family, key power ministers, and international partners), *bureaucracy* (state and local), *business groups* (politicians, paramilitary groups, and criminals), and *consumers* (the marginalised majority). The networks were *semi-permanent,* set up for one operation or a fixed period of time and then disbanded. This made them *unique,* their configurations and rules dependent on the mission. Every network's operation was *sponsored,* usually by someone in the *elite.* The practice of selecting members of a network resulted in highly *personalised* structures. The networks were also *non-transparent,* governed by a set of unwritten and yet binding rules. The actors in the networks were *multi-sectoral,* covering a variety of state and non-state offices, as well as simultaneously operating in different business sectors. Finally, the networks operated according to a certain *logic,* for profit accumulation or welfare maximalisation.

The relationships within the networks neither resembled a hierarchical nor a horizontal pattern, but were more likely to form web-like *heterarchical* structures. Networks traversed both defined and undefined territorial and financial zones, and thus were *trans-territorial.* The system was neither directly sponsored as an official state function, nor was it part of an unofficial or shadow economy, but instead comprised the *grey market*. All actions were *conditioned* by current socio-political and economic factors. Ultimately, the networks created an *alternate force*, which challenged governmental institutions as the primary inter-state actor.

The functional networks operated in natural gas imports, electricity distribution, production of petrol, transportation of petrol, and electricity transmission. Their actions created a non-competitive and inefficient energy sector that monopolised commodity exchanges and financial transactions. The regional networks traversed Georgia and its separatist and quasi-autonomous regions – Abkhazia, South Ossetia, Adjara, and Javakheti. These networks strengthened local fiefdoms within Georgia, which could act counter to the state in their efforts to capture an aspect of the energy market. Both the functional and regional networks challenged the credibility and effectiveness of western companies and donors operating in Georgia. Within less than a decade, Georgia went from independently managing its gas and electricity infrastructure, to being heavily in debt to numerous neighbouring states for gas and electricity, and ceding control of most of its supply and distribution system to the state controlled Russian companies. The embezzlement of foreign assistance by the Georgian *bureaucracy* meant that infrastructure upgrades were not completed, leaving Georgia unable to exploit its potentially most abundant source of electricity – hydropower. Georgia's relationships with neighbouring states were based on the knowledge that a significant percentage of the energy sector was relegated to the grey market, and that many of the business relationships were non-transparent and semi-permanent. This alternate force prevented the creation of an integrated and efficient regional energy arrangements.

There is also a self-perpetuating symbiosis among the various stakeholders in networks. In Georgia, there came a point in the early 2000s when the interests of individual stakeholders, whether it be for personal or group gain, were overtaken by the alternate force of networks. That is, new members received the same benefits as others who were already participating in the networks. The alternate force replaced the state, as transactions occurring within networks traversing the state were more sustainable than anything the state provided. This intra-state phenomenon of an alternate force of networks replacing the state was compounded by the fact that the network system was also the primary medium of doing business among stakeholders in the post-Soviet space. Thus, cooperation among regional adversaries was sustained through the alternate force, despite political conditions which might otherwise have prevented the states from cooperating. None of this was officially sanctioned, documented, or discussed openly. And yet, the alternate force of trans-territorial networks was the main source of income, interaction, and communication among numerous groups.

This was due, in part, to the centrifugal tendencies in the former Soviet space and the failure to institutionalise post-Soviet regionalism in the form of the Commonwealth of Independent States, the Collective Security Treaty Organisation, or the Eurasian Economic Community. Despite the difficulties in creating functioning regional institutions at the official level, the less tangible factors related to a shared identity among elites resulted in a system in which various modes of regional cooperation were sustained through trans-territorial networks. As discussed in Chapter 4, political networks created when the Soviet Union existed did not dissolve in 1991, but were retained and transformed. This was due to at least three factors. First, *elite* networks stemming from Soviet times (e.g. peer groups, cohorts, and friendships) were maintained. Second, some of the more practical aspects of cooperation related to the formerly integrated system among the Soviet republics remained, despite the new states' varied political paths and the fostering of nationalist cultures. Third, an influx of foreign capital and technology created new business opportunities, in particular in the energy sector, which led to lucrative partnerships across the region. The political *elite* networks followed one of two patterns: between Russia and the new states (centre-periphery), or among the new states (periphery-periphery). At first, the former was the more prevalent arrangement. However, as Russia increasingly exercised its power through state-owned hydrocarbon companies, the post-Soviet states looked for alternate arrangements with other actors.

Since the mid-1990s, Russian private and state-owned companies have steadily regained control over much of the Eurasian energy sector through the use of trans-territorial networks. As Russian state-owned companies operating in the former Soviet states have taken over smaller private companies, such as *Gazprom's* acquisition of *Itera's* operations in Georgia, the Russian government has gained economic and political leverage in these states. This has happened primarily within the context of business deals arranged among members of the former Soviet *nomenklatura.* The Russian government has pursued a multi-prong strategy: buying up the rights to sell and distribute gas from Central Asia to the rest of the post-Soviet states and Europe, arranging debt-for-equity swaps for the states' strategic energy assets, investing in energy infrastructure across the region (e.g. oil refineries, electricity transmission systems, and pipelines), and creating third-party companies with states to negotiate agreements that favour Russian companies. The impact of this was evident during negotiations in 2005-2007 between energy suppliers (Russian companies and Central Asian governments) and transit states (Ukraine, Belarus and Moldova), which ended up favouring Russian companies in terms of pricing, barter arrangements, transit rights, and securing storage facilities and pipelines (Stern 2006).

These trans-territorial networks have challenged the ability of the Trans-Atlantic liberalisation agenda to implement transition plans effectively in post-Soviet states. The EU and the US government have had to balance energy demand from post-Soviet states with their political, economic, and social reform agendas. According to the EU, energy policy reform in Eurasian states is essential for 'their [Eurasian states] economic and political future, as well as for the safe and efficient transit of energy to the EU' (European Commission 2002). Thus, the effectiveness of the EU's energy strategy in Eurasia presupposes the strengthening of state institutions. The European Commission has increased its assistance to policies designed to enhance the energy sectors in its 'New Neighbourhood'. However, the extent to which EU efforts have been able to challenge the Russian-driven trans-territorial networks is debatable. This thesis has argued that the large-scale European funded projects, such as the construction of east-west pipelines (Baku-Supsa and Baku-Tbilisi-Ceyhan/Ezerum), upgrades to rail and road transit corridors along the Silk Route through the TRACECA and INOGATE programmes, and public (TACIS) and private investment have not significantly contributed to the strengthening of the Georgian state. Nor have the projects served as the impetus for integrating the South Caucasus energy sector. This is due, to a large extent, to the agenda of the political elites gaining access to financial rewards from these projects, rather than using them to strengthen the energy security of the state. This leaves the trans-territorial network as the primary actor in the regional energy market.

Ultimately, the lens of trans-territorial networks makes it clear that rather than inter-state relations being between states, they are a web of networked relations locked in a struggle for resources in the grey market. All of the neo-institutional parameters normally accorded a state are ambiguous: territory, authority, and legitimacy. Traditional government-to-government relations are usurped and are often just a disguise for the actual activities happening within trans-territorial networks. This involves illicit activity with actors whose purpose is to undermine the ability of the state to adequately protect the external means of support for strengthening the state. The functioning of the networks can also invite external actors whose purpose it is to obtain access to strategic state assets for political manipulation of the state. This affects not just the two states involved in the network, but those who are trying to operate in the same economic sector, those who are supporting the strengthening of the state with their own competing projects, and those who need to transit the state for legitimate business purposes. Moreover, trans-territorial networks change the dynamics of authority among populations across a region. Regions outside the control of central authorities tend to develop their own supply lines separate from the centre, which can perpetuate allegiances to other authorities both within, and without a state. Irredentism can lead to calls for autonomy, eventually inciting conflict. As for the security of the state and its region, the trans-territorial networks test the ability of the state to protect its borders from incursion and trafficking. Rather than guard the territorial integrity of the state, security services team up with paramilitaries and other criminal groups to transit materials. This leaves large swaths of areas across states unprotected and open to outside and sometimes threatening forces.

8.3 Linking Empirical Conclusions with the Theoretical Framework

As power and politics have moved away from the strict definitions of state institutions towards the process of engaging in political activity, and as the community of actors has expanded with forces of globalisation, then so too should the empirical sovereignty of a weak state transform. The same post-modern concepts used in Chapter 2 to reconceptualise the state are useful for examining sovereignty in a weak state given the inapplicability of the conventional frameworks for addressing the causes of weakness. The concept of trans-territorial networks creates a different lens through which to analyse the sovereignty of a weak state. In a weak state, the traditional notion of sovereignty as either residing in the sovereign or in the polis is challenged by the networks of stakeholders traversing multiple territories, defying both physical and financial boundaries. As the weak state undergoes a transformative process, its empirical sovereignty is in flux for a certain period of time. Moreover, in the weak state, the absence of will by the authority to act as a responsible sovereign leads to a crisis of legitimacy. Jackson (1990) began the discussion on the weak state's sovereignty dilemma just as the Soviet Union was dissolving, and this study will now return to his depiction of two forms of sovereignty and explore the nature of empirical versus juridical sovereignty in a post-Soviet weak state.

The debate on problematic sovereignty originated from the general conception in the political science literature that the prime feature of sovereignty is juridical recognition by other states (i.e. international legal sovereignty). As discussed in Chapter 2, Jackson, followed by Kaplan, suggested that post-colonial states possess neither internal coherence nor credible governments to be granted the status of full sovereignty. In fact, Jackson reversed the neo-neo consensus on the role of anarchy in International Relations. Contrary to the neo-neo view that the international system is characterised by anarchy, Jackson argued that there was stability in the international system through the acceptance of the juridical sovereignty of the state, while anarchy reigned within weak states at the domestic level. This domestic anarchy, Jackson explained, had less to do with the capacity of institutions and more to do with a lack of will to govern effectively. Thus, one of the most important challenges to the traditional notion of sovereignty emanating from this discussion was the idea that empirical sovereignty could be linked to the government's will to govern, a quality that varied among states regardless of their legal sovereign status and institutional capacity.

Cynthia Weber (1995) applied a post-modern approach to capture the debate on empirical sovereignty and the weak state. She argued that sovereignty could be 'simulated' by state elites, or the regime, for the purposes of survival. State and society could also 'simulate' sovereignty in their efforts to undermine the state. Moreover, sovereignty could be constructed from the bottom-up; from the inter-connections among societal formations and the trans-national forces that penetrate them. Weber suggested analysing state sovereignty through a series of questions (1995: 30). Who or what is the foundational authority figure for each interpretive community? Where, if anywhere, does sovereignty reside in each distinct historical period and for each particular inter-subjective community? What, if anything, does sovereignty mean for each community? Answering these questions within the context of a weak state, in which the normal channels of communication have been usurped by trans-territorial networks, presents interesting insights for the study of sovereignty.

Of particular interest is the previously mentioned notion that perhaps sovereignty can be constructed from the bottom-up. Granted, of the networks discussed in this thesis, many were either created by, or obtained sponsorship from, a higher authority in the *elite* and *bureaucracy.* Further, decision making was most often made by a central clique. However, some networks, particularly those formed in outlying regions of

Georgia, primarily composed of the *business groups* and *consumers* and sponsored by a member of the local *bureaucracy*, did function separately from the central authorities. In Georgia, regional fiefdoms in Javakheti and the Samegrelo regions, for example, operated locally generated businesses. These networks were sustained through their trans-territorial connections, shifting the site of empirical sovereignty from the centre to the periphery, and from the top to the bottom.

Weber explained that simulated sovereignty was the result of the act of constituting a state. Like Walker, she argued that it should therefore be viewed as a continual process, 'repeated in various forms at numerous spatial and temporal locales' (1995: 3). In a later work, Weber clarified how the study of sovereignty should be approached,

> While the word sovereignty denotes a state of being – an ontological status – sovereignty in fact expresses a characteristic way in which being or sovereign statehood may be inferred from doing or practice. It is not possible to talk about the state as an ontological being – as a political identity – without engaging in the political practice of constituting the state (Weber 1998: 3).

If, as the post-modernists argue, sovereignty is problematic and continually being constituted, then empirical sovereignty is constantly changing as well.
For the weak state, in which myriad trans-territorial networks are at work, the foundational authority figure for the community can be conceptualised as shifting, often unidentifiable, and even illegitimate. Sovereignty for a community can be irrelevant if the community does not identify with the state, the regime, or the nation. When one examines empirical sovereignty through the lens of trans-territorial networks traversing a weak state, one observes that empirical sovereignty is simulated under the guise of juridical or international sovereignty, first and foremost, for the purposes of benefiting the *elite*. This perpetuates a system in which others, including the *bureaucracy* and *business groups*, also simulate sovereignty to participate in trans-territorial networks for the benefit of gaining resources. Finally, in the absence of adequate provisions of goods and services by the state, the *consumers* simulate sovereignty as citizens of one state, operating across borders with various actors in a second or third state.

By its very nature, domestic sovereignty in a weak state is undeveloped, manipulated, and often simulated. Considering the relationship between simulated sovereignty and territory generates interesting insights. In the case of Georgia, for some communities, such as the Abkhaz and Ossets, simulating empirical sovereignty has been a survival mechanism; gaining juridical recognition from the international community has been deemed critical for the survival of the nation. On the other hand, for some groups, such as the Armenians living in Javakheti, territorial demarcations have been less important. The Javakhs have relied on their neighbours in Armenia and Russia for subsistence and for them, therefore, there are several centres of authority other than the state in which they reside. Finally, the role of the international community in granting weak states sovereignty and providing developmental assistance can be viewed as simulating sovereignty and granting recognition to those who simulate sovereignty. In the first case, by granting diplomatic recognition and financial assistance to empirically weak states in which the challenges to reform are well known, the international community could be understood to be simulating sovereignty in the hope of developing stronger states. In the second case, by supporting empirically weak states, the international community could be seen to be supporting the practice of regimes simulating sovereignty. This should begin to address the critics of Jackson who argue that a western notion of sovereignty fluctuates according to the context (Walker 1992), and by Africanists who believe that global historical processes effecting empirical sovereignty have been largely ignored (Grovogui 2001).

8.4 Limitations of the Research

There are two limitations of this research. The first is the application of the socio-political model of networks to only one weak state. Within the confines of this thesis, I was not able to carry out a comparative study of several post-Soviet states and isolate factors which may or may not affect the ability of these networks to impact negatively on the development of the state. However, given that the networks analysed in this thesis are multi-state, and include several of Georgia's neighbours, which share many common Soviet legacies, there are grounds for offering preliminary comments about the applicability of the model to other states. The second limitation of this research is the absence of an examination of why trans-territorial networks strengthen some states, while they weaken others. Each of these limitations will be addressed below.

8.4.1 Comparative Application of the Network Model

Much of the literature used in the process of conducting this research came from Sovietologists and transitoligists whose work refers to other post-Soviet states. These states share structural, ideational, and historical factors which emanate from their existence within a single integrated country. The legacies discussed in Chapter 4 included the importance of personal connections in making it possible to survive economic crises, patrimonial power structures, and the prevalence of the second economy. The similarities among the post-Soviet states was confirmed in the formation of trans-territorial networks by multi-state stakeholders from Russia, the Caucasus, and Central Asia for the conduct of business in Georgia's energy sector. Field research conducted in Russia and Armenia to explore the links with Georgia provided some opportunities to gather information on their respective energy sectors, and to assess the degree to which trans-territorial networks operate. This section will provide a preliminary analysis on the validity of applying the network model to other post-Soviet states.

The two post-Soviet states that had the most in common with Georgia before the Rose Revolution were its South Caucases neighbours – Armenia and Azerbaijan. All three states suffered from persistently low levels of investment, high levels of abuse of public office for personal gain, and unresolved conflicts. Armenia is a state in which strong networks usurped state functions, and for which the energy sector played a role in strengthening the power of *elites,* in particular, President Kocharian's circle of former school friends and colleagues from Stepanakert (the administrative capital of the unrecognised separatist entity Nagorno Karabakh). This group included one of the most powerful actors in the energy sector and potential heir to the presidency – the Minister of Defence, Serge Sarkissian. As with Georgia, Armenia and Azerbaijan also had ambiguously defined borders surrounding a separatist territory, Nagorno Karabakh, which provided a conduit for smuggling. Azerbaijan also has a territory, Nakhichevan, physically separated from the rest of the state by Armenia and Iran. As we have seen in this thesis, Armenian stakeholders participated in the trans-territorial networks traversing Georgia smuggling petroleum from Russia and Azerbaijan for sale in Armenia. Further, Armenian authorities provided electricity to southern Georgia.

However, there were several differences between Armenia and Georgia. Armenia was the hardest hit of the South Caucasus countries by the economic downturn, as it struggled with the economic embargo imposed by Turkey and Azerbaijan, an absence of energy resources, and the lowest wages in the former Soviet Union, aside from Tajikistan. In contrast to Georgia, however, Armenia had a significant external source of funding from the Diaspora, some of it transparent and some not. This funding was sometimes able to compensate for the lack of government spending on infrastructure and welfare programmes. Moreover, unlike Georgia, Armenia had a homogeneous population; from the mid-1990s, nearly 98 percent of Armenia's population of almost 3 million were ethnic Armenians. Another difference was that the Armenian government *willingly* sold nearly all of its strategic assets in the energy sector to Russia. By 2006, Russian state-owned companies controlled all of Armenia's electricity generation facilities, as well as the electricity and gas distribution network. Russia even gained ownership of Armenia's pipeline from Iran (Karapetian 2006). This is linked to Armenia's strong political and military alliance with Russia. Finally, since the mid-1990s, Armenians have been spared the energy crises experienced in Georgia. This has been partially attributed to decisions made by the Armenian authorities to make the system more efficient, including continuing to operate the Metsamor nuclear power plant despite European objections.

In Azerbaijan, there were at least three differences from Georgia. Power was consolidated in one cohesive family – the Aliyevs – and their closest associates from among the *nomenklatura*. The Aliyevs maintained tight control over all aspects of the state, in particular management of the energy sector and its revenues. The current president of Azerbaijan, Gaidar Aliyev's son, Ilham, was the vice president and then first vice-president of the State Oil Company of Azerbaijan (SOCAR) from 1994 until 2003. He was actively involved in directing the state's energy strategy, while holding leadership positions in his father's New Azerbaijan Party from 1999. This overt domination of the Aliyev family was further supported by an authoritarian style of governance that ensured loyalty among all sectors of the state. This then meant that in

Azerbaijan, the networks resembled more of a pyramid, with the *elite* having greater control over most of the transactions, whereas in Georgia the networks were more heterarchical in structure, with authority more widely dispersed throughout the state. The second difference is that Azerbaijan is a resource rich state and therefore, since independence, it has been able to gradually provide for not only its internal use, but export surplus as well. In 1995, oil production in Azerbaijan out measured oil consumption, resulting in a net export margin, although most of this was initially sent by pipeline through Russia. Nonetheless, Azerbaijan remained reliant on Russia for power generation, importing Russian gas from November 2000 until January 2007, and buying electricity from *RAO-UES* (Muradova and Abbasov 2006). Finally, as a resource rich state, the Azerbaijani government was expected to increase social welfare spending. The recovery of the Azerbaijani economy started in 1994 after several Production Sharing Agreements (PSA) with leading Western oil companies were signed for the exploration of the nation's hydrocarbon resources. In 1999, President Heydar Aliyev created the State Oil Fund, designed to spend oil windfalls on education, poverty reduction, and raising rural living standards. However, in 2006 after the oil and gas from Azerbaijani fields had started to flow through the newly constructed pipelines to Turkey, western organisations remained concerned as to whether Azerbaijan would convert the hydrocarbon windfalls into sustainable areas of economic development and welfare maximalisation of the citizens.[1]

From this preliminary discussion of the South Caucasus states, there appear to be at least three variables that would need to be taken into account if the network model were to be applied to other post-Soviet states. First, there are cultural variations, which are often difficult to identify. One example is the deference to authority in Azerbaijan, which allows the regime to maintain a higher degree of control over subordinates within state structures; there is less deference to authority in Armenia and far less in Georgia. Second, the scope of trans-territorial activity will differ in each state, as a result of the number and types of actors traversing the state. In Azerbaijan, it is probably the case that the networks are less penetrable by external

[1] Over a 20-year span, Azerbaijan is projected to receive as much as $230 billion in revenue from energy development and export ventures, including the Baku-Tbilisi-Ceyhan (BTC) pipeline and the South Caucasus gas pipeline. The credibility of the oil fund has been questioned because of the appointment of its members by the President, despites advice from the IFIs to the contrary.

actors and are more tightly controlled. This could vary, however, in the case of people living near Nagorno Karabakh and Nakhichevan. There is also the interesting dynamic of 25 million Azeris living in northern Iran. Armenia is the most isolated state, with the least number of options, and it is the state in which Russia has the most influence. At the same time, this isolation presents opportunities for lucrative smuggling networks, not only with Georgia and Russia, but also with Iran and Turkey. Third, the timing, decisions, and investment made towards enhancing energy efficiency will determine the necessity to rely on trans-territorial networks to compensate for a lack of supply. By the late-1990s, Georgia had fallen behind both Azerbaijan and Armenia in terms of making the necessary adjustments to its internal energy sector in order to make maximum use of its current and planned resources. Nevertheless, if account is taken of these varying factors among the states, it would appear that the network model could be applied to the three states' energy sectors during the period 1993 and 2003, and that many of the same conclusions would be reached regarding the role of trans-territorial networks in weakening the state and preventing the development of a regionally integrated security framework.

8.4.2 Strong States and Trans-territorial Networks

The second limitation of this research is the absence of a thorough analysis of why trans-territorial networks have a paralysing effect on the weak state and not on the strong state. All of the networks analysed in this thesis operate in the grey market and, therefore, they operate outside of the law. Trans-territorial networks that operate in strong states, on the other hand, are, for the most part, operating within legal parameters as defined by the state and international law. Thus, trans-territorial networks do not *per se* cause state weakness; it is non-transparent networks operating in the grey market that do this. However, limiting the explanation to a matter of legal versus illegal parameters of trans-territorial networks does not account for the broader conceptualisation of the weak state provided in this thesis. That is, the ability of trans-territorial networks to operate so effectively in the grey market is the result of the lack of will on the part of the authority in the state to act as a responsible sovereign. From this comes a cascade of actions taken by various stakeholders within and beyond the state, which combine to undermine the strengthening of the state.

Eventually, there is little to distinguish between the official and unofficial sectors; the former is the basis of the strength of the latter.

It would appear important to determine the point at which trans-territorial networks go from being a hindrance to becoming a benefit to the state. In stronger states, trans-territorial networks are often praised for their development-enhancing capacities in terms of moving goods, people, and capital. Trans-national corporations, while not immune to controversy, can be the vehicles of economic development. As was discussed in Chapter 7, even Georgia was strengthened by a trans-territorial network involving a consortium of energy companies in the construction of two pipelines across its territory. However, this was deemed the result of a 'relinquishing of sovereignty' on the part of the Georgian government to the consortium through a Host Government Agreement. Paradoxically, trans-territorial networks in weak states both facilitate and restrict cooperation. As was seen in the case of Ergneti market in Chapter 6, the networks brought the conflicting parties together in trade regimes. At the same time, however, competition led to violence, which prevented the development of greater confidence among the parties engaged in conflict resolution efforts. Invariably, it is the type of state that determines the type of trans-territorial networks that operate within it. This provides some explanation as to why strong states benefit from trans-territorial networks and weaker states suffer. It is less the trans-territorial networks themselves, and more the state through which they traverse that determines whether they assist or harm the state.

In a stronger state, an effective economy and the formalisation of the role of state institutions governed by an independent and transparent rule of law create a barrier through which very few disruptive trans-territorial networks are allowed to penetrate. The rules of engagement for trans-territorial networks that wish to operate within stronger states are often strictly regulated and, if manipulated, are subject to penalties. In a weak state, by contrast, networks become the system; they are the norm in most activity, public and private. The trans-territorial networks that manipulate the regulations in stronger states are aberrations, whereas in the weak state they are the norm. In addition, the incentives for participating in networks in a weak state are different. For *consumers*, the incentive is survival; networks compensate for the inability of the state to perform certain services and provide goods. For the *bureaucracy*, the first incentive is to hold onto their positions, and the second incentive is to convert their positions as clients of the *elite* into financial rewards for themselves and their groups. For the *elite*, the incentive is to make millions of dollars in personal wealth, and to convert this personal wealth into power over the state. In stronger states, the stakeholder's incentives for participating in trans-territorial networks can also relate to revenue generation, both for the government and private entities. However, it is done, for the most part, towards strengthening organisations for the purposes of generating even more public and private revenue in the future. Moreover, the national security interests of the strong state are usually placed above the considerations of trans-territorial networks, whereas in the case of Georgia, state security was compromised for the sake of obtaining private financial gains from trans-territorial networks. Whether trans-territorial networks can go from weakening to strengthening a state is examined in the next section on prospects for future research.

8.5 Prospects for Future Research

In an ironic twist of history, as a result of natural disasters in the Sochi region in winter 2007, Russia appealed to Georgia for deliveries of electricity. Allegedly, Russia began to take electricity from Georgian sources before the Georgian government had agreed. President Saakashvili told a Georgian audience that at first he was upset by this news, but then he changed his mind, explaining, 'As it turns out, we have something to be proud of. We tried for many years to get something from Russia, and now Russia was forced to use our electricity' (Gordienko 2007). It would appear that something had changed in Georgia's energy sector since President Saakashvili came to power that made it possible for Georgia to export electricity to Russia. The obvious extension of this research, therefore, would be to examine what has happened to the trans-territorial networks in Georgia's energy sector since the start of Saakasvhili's administration in January 2004. Do the trans-territorial networks continue to conduct most transactions in the grey market, or has the new government been able to push the exchanges among stakeholders into legitimate channels of business? If the latter, has this improved inter-state cooperation?

A preliminary study of the Georgian economy from 2004 until the winter of 2007 shows that it had begun to develop, and that measures were being put into place to enhance future growth. Georgia was rated first in making itself more 'business friendly' than any other country in 2006, leaping from number 122 to 37 in the World Bank's rankings of the ease of doing business (World Bank 2007). Since Saakashvili took over, GDP growth (which was 1.8 percent in 2000 and 4.8 percent in 2001) has increased from 5.5 percent in 2002, to 11.1 percent in 2003, 5.9 percent in 2004, 9.3 percent in 2005, and 7.8 percent in 2006. The budget has jumped from less than US $500 million per year for much of the Shevardnadze era to US$ 2.2 billion by 2006 (TACIS 2006). The perception of corruption, however, has remained steady; Georgia's rating for Transparency International in 2006 was the same as in 2005, placing it towards the bottom of most corrupt states at number 130 out of 158 (Nodia 2006). Thus, there appears to be a divergence between the strengthening of the economic performance and the improvement of the legal framework for conducting business, on the one hand, and the persistence of corrupt practices, on the other hand.

President Saakashvili made it a top priority to enhance the state's energy security. The emerging agenda had four objectives: to replace and repair obsolete equipment; to construct new power plants and transmission infrastructure; to diversify imported energy resources; and, to create a commercially viable economic model to attract investment (Government of Georgia 2006). And yet, after one year in power, in his February 2005 State of the Nation address, Saakashvili admitted that the inability to provide a regular power supply had been 'the biggest failure of our government.' Energy sector reform followed a similar pattern to the rest of the post-Revolution agenda. First, former energy officials were fined or jailed, in part to raise much needed funds to pay off debts and increase procurements. However, the use of plea bargains and confiscations of property led to allegations of human rights abuses, and the tactics were used much less after 2005. Next, the government implemented a strategy to draw the energy sector out of the grey market through regulatory and financial mechanisms, including the reform of the tax code and lowering the rate of value added tax. In 2004, General Inspectorates were opened in each of the ministries and hotlines were established for the public to report abuses. This was followed by the privatisation of state assets. Taxes were lowered, obtaining licenses and permits was made easier, and the process of tenders was meant to be more transparent and competitive. Then, when an energy supply crisis from Russia hit Georgia in the winter of 2006, discussions increased on the need to diversify energy sources, including the construction of more hydropower plants. The notion of an integrated South Caucasus energy system was briefly reintroduced, as was increased cooperation with Kazakhstan, Iran, and Turkey. Each of these will be discussed in turn.

Approximately a year after Saakashvili became President, there were several arrests and formal investigations were opened of former energy officials. At that time, the law-enforcement bodies arrested Gia Jokhtaberidze, Shevardnadze's son-in-law, in February 2004 for tax evasion. He was released in April and paid US$ 15.5 million to the state budget. Shevardnadze's nephew, Nugzar Shevardnadze, purportedly sold his assets in Georgia, but there have been varying accounts as to whether he has left the country. The father of the former president's daughter-in-law, Guram Akhvlediani, was questioned for misappropriating funds at Poti port, including trade in petroleum products. However, he maintained his assets in the port and was never accused of any crime. Other former officials in the energy sector were investigated, but only the former Minister of Fuel and Energy, Mirtskhulava, was sentenced to 12 years in prison. The charges related to his signing a contract without President Shevardnadze's approval that resulted in a US$ 600 million debt to Armenia for the provision of electricity through the Ashrot-Ninots'minda line, as well as negligence in numerous other incidents. The former Head of the Railway, Akaki Chikhidze was arrested for his role in the trans-Georgia petroleum smuggling from Azerbaijan, but he was released after paying a mere US$ 3 million.

Curbing contraband trade was the second major initiative undertaken in the first days of the Saakashvili administration. The purpose was to increase state revenue by disrupting the trans-territorial networks. Efforts were made to improve the capacity of the security forces manning the borders and transit corridors, and to decrease the level of influence of regional politicians on either side of the separatist zones. This was the idea behind the closure of Ergneti market on the border with South Ossetia and the withdrawal of Georgian Ministry of Defence sponsorship of guerrilla groups operating on the Abkhaz border in the Gali district, such as the *Forest Brothers*. However, there are allegations that new paramilitaries are taking their place, tasked with protecting the Georgian citizens in the separatist zones. Further, while there are now approximately 80 fuel importers in Georgia, which enhances competition, they must split profits from a relatively small market. The high cost of petroleum in

Georgia has meant that smuggling continues, particularly from Russia and Azerbaijan. Georgian economist Gia Khukhashvili explained that 'without the government's more active participation, fighting smuggling is nearly impossible. It is very organised' (Alkhazashvili 2007).

In June 2004 a Russian tycoon of Georgian origin, Kakha Bendukhidze, was appointed by the Prime Minister, Zurab Zhvania, to head the Ministry of Economy and he was tasked with privatising Georgian enterprises. Russian investors were initially given guarantees that their present investments were safe and that projects worth several billion dollars would potentially be open to their investment (Ultanbaev 2005). Over the next year, three energy enterprises were offered for sale. The Kazakh state company *KazTransGaz* won the tender for *Tbilgaz*. *Azoti* chemical plant was transferred to a new 'Energy Invest Group' that appears to be a joint Russian-Georgian venture with *Gazprom.* Russia's *Evraz Holding* and an Austrian-Georgian company *DCM-Ferro* took ownership of the majority shares in *Zestaponi*, *Chiatura* manganese mines, and the *Vartsikhe* hydropower plant for US$ 132 million (Corso 2006). The *Kakheti* distribution company was sold to a Georgian company *TBC Group*. In September 2006, a Czech company *Energo-Pro* offered US$ 312 million for *United Distribution Company of Georgia* (UDC) (which supplies 70 percent of Georgian electricity), the Adjara distribution company, and six hydropower stations (Galt and Taggert Securities 2006). Foreign investments also enhanced Georgia's role as a petroleum transit corridor, including the purchase by Kazakhstan's *KazMunaiGas* of the controlling block of shares of Batumi port and subsequent investments in the oil terminal. Exxon Mobile and Chevron agreed to increase their use of the Baku to Batumi rail transit for petroleum products.[2] The use of Poti port was also increased as a result of the private Swiss-registered company *Silk Road Group* leasing Poti terminal from Turkey's Channel Energy and shipping oil from Turkmenistan via Baku and then rail to Poti (Menas 2006).

An examination of these sales and leases reveals, however, that many of the companies were backed by Russian investors, certain investors were excluded, and the process lacked transparency. The Industrialist and Democratic Front factions in

[2] Interview conducted off-the-record with energy company representative, September 2006.

Parliament expressed concern that the Russian government might have been involved in the acquisition of *Tbilgaz* through a consortium of the Kazakh bank *TuranAlem* and the *Silk Road Group* (Channel 1 2006). President Saakashvili told a conference in Tbilisi sponsored by the International Energy Agency that the Czech company, *EnergoPro,* originally offered US$50 million to circumvent the tender process along with unspecified future investments. The Georgian government apparently rejected that offer and then the same company came back and offered US$ 312 million in the tender. Minister of Fuel and Energy, Nick Gilauri, admitted that he had been given assurances that *EnergoPro* was a reputable company, but that he had heard rumours that one possible investor was *RAO* – the Russian state-owned electricity company (Roberts 2006). When *EnergoPro* finally signed the contract 9 months later, the company only paid US$ 132 million for the distribution company and hydropower stations. The government explained that the additional US$ 285 million would be spent in investments (Corso 2007). A Georgian energy expert, expressing an opinion anonymously, suggested that the privatisation process was not very transparent. 'The whole sector was well wrapped and presented. What the [energy] sector needs is not an investor that pays a lot but the one that will invest a lot.'[3] Turkish companies attempted to participate in the privatisation process, but the pricing was not made clear and data on the companies offered for sale was unavailable. It appeared to most Turkish businessmen that the deals were pre-arranged.[4]

One of the main efforts of the Saakashvili government was to spend loans and grants efficiently on improving the electricity generation and transmission system. In 2004, 6 power plants, 5 high-voltage transmission lines, and the natural gas pipeline in the Kazbegi region were rehabilitated, and an effort to re-meter major cities in western Georgia was launched. In 2005, Georgia's energy sector received around US$ 132 million in state and international financing towards enhancing electricity supply. The Saakashvili government pledged that US$ 70 million out of an expected US$ 200 million from state property sales would be spent on securing electricity supplies in 2006. Plans included the construction of a new electric power line between Georgia and Armenia, the conclusion of repair work at *Gardabani* thermal plant and

[3] Interview conducted off-the-record with energy expert, London, June 2006.
[4] Interview with Zeyno Baran, Hudson Institute, Cambridge, UK, September 2006.

hydropower generation plants, and the improvement of energy efficiency in the country (RIA Novosti 2005). The biggest electricity supplier, *Inguri* hydropower plant, once again received an EBRD grant for US$ 38 million. Meanwhile, Georgia's Ministry of Fuel and Energy was finalising deals with foreign contractors to build over 30 new hydropower stations in the next 3 to 4 years, with Chinese, European, Turkish, and Kuwaiti investors. The EU also provided Georgia with a 7.5 million Euro (US$ 9.87 million) grant for South Ossetia to rehabilitate the gas and water distribution network, and to construct a hydropower plant and waste management system. In 2006, Russia began building a gas pipeline from North Ossetia to reach South Ossetia; however, it is unclear what percentage of the population has received gas from Russia.

Within these four areas of development, there are some situations in which the role of trans-territorial networks has diminished, but in others the networks remain strong, albeit with new stakeholders. For the largest and most marginalised group – the *consumers* – the trans-territorial networks were temporarily disrupted, but not blocked. This is due in large part to the continued necessity to rely on networks for energy supply, as reform plans have yet to adequately change the situation in the regions. Thus, some low level smuggling of petroleum and electricity diversion remains common practice in outlying regions of Georgia. Several measures taken by the Saakashvili government have probably diminished the activities of *business groups*, including the government's withdrawal of support for guerrilla groups transiting the separatist regions, the new law banning *thieves-in-law*, the arrests of several former businessmen/politicians, and the agreement with Russia to close its military bases. The government's efforts to legitimise business practice through new incentives (e.g. lower taxes, decreased tariffs, and improved licensing procedures) have perhaps been the most influential in weakening the networks.

As for the *bureaucracy,* the government's efforts have likely had the most significant impact in diminishing the power of networks. Reforms in the law enforcement agencies, tax administration, prosecutor's office, and financial regulations have all led to a more transparent system. Regional governors are no longer as personally involved in the electricity sector, and the manipulation of regional distribution centres has decreased. However, in some of the regions, the staffing policy has been chaotic and this has hampered reform efforts. Many local administrators from Shevardnadze's patron-client networks remained, particularly in the western Samegrelo region (Wheatley 2005a: 200). In some of the western regions, so-called 'commercial lines' established for businesses were still diverted for personal consumption with the participation of officials (Rimple 2006). Moreover, the anti-smuggling operations at the South-Ossetian border revealed some limits in the government's strategy. While poor traders had been deprived of their livelihood, some officials, members of the law enforcement bodies, and businessmen remained unaffected (di Puppo 2005). As for the *elite,* the ambiguous and erratic nature of the privatisation process causes concern as to whether these deals were made for Georgia's long-term energy security or for short-term political or personal gain. There is also concern over Russia's ownership of Georgia's strategic assets, particularly given that relations between the two states reached the lowest point since 1991.[5]

Thus, an initial review would suggest that trans-territorial networks are still active, but their role in weakening the state is decreasing. The best sign of constructive inter-state relations is to assess energy developments in the region. As of January 2007, Georgia no longer purchased electricity from Russia and only one-half of its gas demand was supplied by Russia. In late December 2006, an agreement signed by Azerbaijan, Georgia, and Turkey redistributed the quotas of gas from Shah-Deniz for transit through the Baku-Tbilisi-Ceyhan gas pipeline for 2007 among the three countries. Turkey lent its quota of 800 million cubic meters to Georgia, at the unofficially reported price of US$ 120 per 1,000 cubic meters. This was a far better price than Russia's offer of US$ 235 (Socor 2007). There were also new developments in the regional electricity system, such as the construction of a new high voltage electricity line between Armenia and Georgia, assisted by the US government's Millennium Challenge Fund (US-Azerbaijan Chamber of Commerce 2005). Georgia and Azerbaijan began planning the synchronisation of their electricity

[5] The problem began with the Russian government's embargo on Georgian wine, spirits, and water. This was followed by the arrest of four alleged Russian GRU spies in Tbilisi in September 2006. Russia responded by withdrawing its ambassador from Tbilisi, imposing a total economic blockade of Georgia, and implementing a systematic programme of checking all Georgians residing in Russia and immediately deporting those with inadequate documentation. At the same time, the steady decline in relations pushed Georgia to decrease its economic dependency on Russia, seeking alternative import and export markets.

systems based on a joint study, swapping electricity when Georgia produced excess in the summer and Azerbaijan in the winter. Georgian Prime Minister Noghaideli proposed a joint Georgia-Turkey high voltage power line after Turkey provided emergency electricity to Adjara in February 2006. Instead, Georgia arranged emergency supply contracts with Azerbaijan and Iran in preparation for winter 2007. There were also developments concerning the petroleum industry. The Azerbaijan state oil company, SOCAR, agreed to pay US$ 3 million for land plots on which to construct a network of petrol stations in Georgia (Trend 2006). Thus, while there was still no regionally integrated plan, there was more bilateral cooperation in the South Caucasus.

Based on the example of Georgia's pre- and post-Revolution energy sector developments, future research could usefully include several of the post-Soviet states. The 'coloured revolutions' in Eurasia, which saw civil action defeat entrenched Soviet *nomenklatura* regimes, occurred in energy dependent states: Georgia, Ukraine, and then Kyrgyzstan. In all three states, persistent energy shortages and non-transparent sales of major state energy assets to Russian companies were factors in moving the masses to protest. The 'governance resource curse' theory argues that large revenue windfalls from hydrocarbons should allow entrenched political regimes to suppress political opposition. This would be the case in Russia, Turkmenistan, Kazakhstan, and Azerbaijan. In the absence of such revenues, one would expect that the reverse would occur.[6] However, in Ukraine, Georgia, and Kyrgyzstan, entrenched power structures manipulated the state's dependency on foreign energy supply for almost a decade to strengthen their power base. This was partly the result of collusion among *elite* stakeholders across the region to devise electricity and gas import schemes generating personal profit to the detriment of state development programmes. Building on the evidence from Georgia, a comprehensive analysis of post-Revolution developments in these three states' energy sectors, in particular whether or not trans-territorial networks continued to play a role in supporting the new regime, and whether the state weakened as a result, could provide useful insights into state-building in Eurasia.

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[6] Interview with Dr. Paul Stevens, BP Professor of Petroleum Policy, University of Dundee, Cambridge, UK, September 2006.

8.6 Re-examining the Threat of the Weak State

The western security discourse would have us believe that the weak state is one of the biggest threats to international security. I believe that it is wrong to pose the weak state as a threat to international security. Viewing state failure as a threat to global security is problematic because it focuses the debate on the impact of local forces on the international system rather than on either the impact of global forces on the state, or, even more appropriately, the intersection of local and global forces. The premise of this thesis is that some states are purposely kept weak for the benefit of a combination of trans-territorial actors, local and global, state and non-state, operating between the formal and informal economies. Thus, the real action is taking place within a complex heterarchical pattern of multiple actors, creating variable causes of weakness. Nonetheless, outside of African studies, the causes of state weakness are not adequately addressed. Moreover, outside of globalisation studies, the state is not reconceptualised in any meaningful way so as to understand how it relates to other states. Until international relations moves beyond its traditional assumptions and consistently applies sociological and other approaches to the state, it will continue to suffer from less than adequate prediction and problem-solving capabilities.

At some point the international community has to take responsibility for the operations of the trans-territorial networks that are undermining the strengthening of states. After all, the effectiveness of many crippling trans-territorial networks depends on sustenance from international grants, assistance programmes, off-shore registration of companies, and money laundering through foreign banks. The notion of the 'First World' being complicit in the weakening of the 'Third World' is certainly not new. It is present in the international security and development studies literature regarding global arms sales, proxy wars waged by the superpowers during the Cold War, current economic debates regarding the protectionist policies of developed countries in the agricultural sector, and international organisations and trans-national corporations implicated in bribe scandals in developing countries. However, assessing the role of the international community in the post-Cold War transition process in the former Soviet Union has not been the subject of thorough research.

Rather than just looking at the weak state, perhaps it is the trans-territorial networks that traverse weak states, supported by stakeholders from stronger states, which are a threat to international security. I am not disputing that when a state fails, there are negative repercussions for international security. However, I am claiming that limiting the discussion about the impact of the weak state on international security to an analysis of the weak state within the neo-institutional framework tells only part of the story. I am suggesting that it would be more useful to view weakness within the framework of trans-territorial networks, including the interface between the international community and weak states. This would involve clearly defining the stakeholders in trans-territorial networks and the types of systems that evolve from their interaction. Moreover, holding onto the neo-liberal Wilsonian belief that weak states are actually aspiring to become Weberian-like in terms of strengthening their bureaucratic structures, their economies, and their control over territory is misguided for two reasons. First, it is an inappropriate starting point for shaping international discourse between stronger and weaker states. Second, this line of reasoning increasingly is a liability in effectively implementing the Trans-Atlantic development programmes.

If it is not in the interests of the regime to strengthen empirical sovereignty, or if the programmes directed towards the states actually strengthen the trans-territorial networks that undermine the state, then the effectiveness of the international community's efforts to deal with weak states should be questioned. There is a critique of the American-led invasion of Iraq in 2003 that the US government did not take into account the power balance within the state, state-societal relations, and trans-territorial networks within, for example, the Shia and Kurdish communities, before it began state building efforts. What about indigenous forms of power and authority wielded in more 'traditional' cultures, such as the Chechens, within the confines of demarcated states, who may grant authority to a different sovereign other than that chosen for them? Failed efforts to strengthen Iraq or Chechnya should make political leaders in Moscow and Washington question what it is that is weak; is it the state institutions, the legitimacy of the state, the efforts by the international community, or all three?

And this suggests one final problematic aspect of international relations concerning the weak state – the approach to finding a resolution to the non-recognised entities in Eurasia. As with weak states, international relations treat the *quasi-state* entities, and the regimes that run them, as threats to international security. In the case of Georgia and Moldova, the territorial integrity of these states is regarded as inviolable. Although not expressed officially, many people working in non-governmental organisations in the separatist regions tend to sympathise with the grievances of those residing in the separatist regions. Increasingly, the international discourse (e.g. western governments, media, and think tank analysis) depicts the separatist regions as threats to international security; porous vacuous spaces ruled by criminal regimes rife with illicit activity. To some extent, this is true. There have been problems of counterfeiting operations originating from South Ossetia, money laundering through banks in Abkhazia, and incidents of narcotics, arms, and even enriched uranium being trafficked through the separatist zones. However, the blame is almost always placed on the separatist authorities and their Russian sponsors. And the justification for restoring territorial integrity is tied to the necessity to combat the threats to international security emanating from these regions. That is, Moldova must regain Transnistria in order to stop the production and trafficking of small arms.

Rarely are the titular states (Georgia, Armenia, Azerbaijan, and Moldova), not to mention neighbouring states other than Russia (Turkey, Ukraine, and Romania), blamed for the trafficking. How does traffic traverse the separatist zones, if not via the trans-territorial networks detailed in Chapter 6 of this thesis? How do isolated economies gain the financial means to engage in trans-national business? It is well known, even now, that Georgians are cooperating with Abkhaz in smuggling operations, that products are still transported from Russia down the TransCam through South Ossetia and into Georgia, and that the smuggling of petroleum from Azerbaijan into Georgia follows multiple routes. As with the weak state, placing the blame on the weak *quasi-states* neither helps the conflict resolution process, nor does it stop the trans-territorial networks from operating. Thus, exposing the trans-territorial networks traversing the South Caucasus, and discussing the implications of these operations, would provide a wider, and more realistic, lens for assessing the separatist conflicts and finding avenues for compromise among the parties.

Ultimately, the political network model of socio-economic relations is best suited for area studies and security studies. In terms of area studies, applying the trans-territorial network model to the transactions among stakeholders traversing a region locked in a struggle for resources, for example, could reveal new perspectives on why certain states remain weaker. By applying one model to several regions, and by taking account of the multiplicity of stakeholders, including global and local, there would be the potential to strengthen the role of area studies in International Relations concerning the study of the weak state. As for security studies, applying a political network model of socio-economic relations to conflict-prone states would allow for a more sophisticated understanding of the reasons for conflict, and the intransigence of some parties in resolving disputes. Finally, in terms of foreign security assistance and foreign intervention in weak states, analysing the implications of external actions on trans-territorial networks traversing a state and region, and the impact these events have on the shifting balance of authority among locally competing groups, could enhance the understanding of why foreign intervention so often does not strengthen states. Of course, none of this is new to researchers residing in the regions composed of weaker states; however, it is hardly ever applied by the majority of those from stronger states engaged in the study and practice of International Relations.

Appendix 1: Attributable (Cited) Interviews

Georgia

Tbilisi

Asli, Vadi, President of the American Chamber of Commerce, April 2005.

Botcheridze, Iraqli, Service of Regional Management, Office of the President, July 2003.

Darchiashvili, David, Member Executive Board, Caucasus Institute for Peace, Democracy, and Development, July 2003 and April 2005.

Gadjan, Gadjiev, Ambassador of Azerbaijan to Georgia, April 2005.

Glonti, Giorgi, Research Director, Transnational Crime and Corruption Center, October 2003.

Jervalidze, Liana, independent energy analyst, April 2005.

Losaberidze, David, Caucasian Institute for Peace, Democracy and Development, April 2005.

Mamradze, Peter, former Chief of Staff to President Shevardnadze and first Head of the Government Chancellery under Saakashvili, April 2005.

Meskhidze, Giorgi, President, Civitas non-governmental organisation, April 2005.

Metreveli, Eka, Fellow, Georgian Foundation for Strategic and International Studies, November 2003.

Nadareishvili, Tamaz, President, Abkhaz Government-in-Exile, July 2003.

Nakaidze, Vano, Director, Group of States Against Corruption, American Chamber of Commerce, August 2003.

Nodia, Ghia, Chairman of the Board, Caucasian Institute for Peace, Democracy and Development, November 2003.

Ramishvili, Levan, Director, Liberty Institute, April 2005.

Rondeli, Alex, President, Georgia Foundation for Strategic and International Studies, June 2003 and April 2005.

Shatirishvili, Tea, VIP Manager of CanArgo and former employee of GAOR, April 2005.

Targamadze, Givi, Chairman of the Parliamentary Committee on Defence and Security Issues, April 2005.

Wright, John, Political Advisor, European Centre for Minority Issues, April 2005.

Zakareishvili, Paata, Independent Political Analyst, June 2003.

Abkhazia

Artoba, Giorgi, *de facto* Deputy Minister of Foreign Affairs, July 2003.

Kvarchilia, Liana. Programme Coordinator for the Centre for Humanitarian Programmes, July 2005.

Tuzhba, Konstantin, *de facto* Minister of Finance of Abkhazia, July 2003.

Adjara

Chapiashvili, Hamlet, Member of Parliament from Adjara and Deputy Head of Foreign Affairs Committee, Revival Party, July 2003.

Gogiashvili, Dato, Minister of Finance of Adjara, July 2003.

Samskhte-Javakheti

Chingilashvili, Zura, Channel 9 producer in Akhaltsikhe, July 2003.

Kopadze, Gia, Chairman of the New Rights Party. Gamgebeli of Alkhakalaki from 1991 to 1995, July 2003.

Mosiashvili, Temur, Governor of Samtskhe-Javakheti February 2002-August 2003, July 2003.

Zugdidi

Gunava, Bezshan, Member of Parliament from Zugdidi, April 2005.

Istanbul, Turkey

Corzine, Robert, former journalist for the Financial Times, consultant to British Petroleum, August 2005.

Yerevan, Armenia

Voskanyan, Arsot, Government of Armenia Ministry of Foreign Affairs, Policy Planning Staff, July 2003.

United Kingdom

Babukhadia, Mikheil, former Chairman of the Supervisory Board of *InguriHES* and former commercial manager for *AES Telasi,* September 2006.

Baran, Zeyno, Director, Center for Eurasian Policy, Hudson Institute, September 2006.

Bhatty, Robinder, formerly of Cambridge Energy Resource Associates, June 22, 2004.

Cohen, Jonathan, Co-Director of the Caucasus Programme, Reconciliation Resources, April 2003.

Elkind, Jonathon, independent energy consultant, and former Director for Russian, Ukrainian, and Eurasian Affairs, National Security Council, US Government, 1998-2001, June 2005.

Galeotti, Mark, Director Organised Russian & Eurasian Crime Research Unit Keel University, Spring 2005.

Gambar, Isa, Chairman of the Musavat Party, May 2005.

Grigoryan, Mark, Journalist, BBC, London, May 2004.

Robson, David, Managing Director and Chief Executive Office CanArgo, February 2007.

Stevens, Paul, BP Professor of Petroleum Policy, University of Dundee, 2006.

Wallace, Lord William, Member of the House of Lords and Professor (Emeritus) London School of Economics, London, 2004.

Zureishvili, Nini, investigative journalist for '60 Minutes' new programme, Rustavi television station, August 2004.

United States

Lordkipanidze, Gorcha, Deputy Head of Mission, Georgian Mission to the United Nations, New York, April 2003.

Appendix 2: Background Interviews

Georgia

Tbilisi (Summer 2003, November 2003, April 2004, April 2005)

Adeishvili, Zurab, Member of Parliament, Chairman of the Committee for Legal Affairs, Rule of Law and Administrative Reforms, May 2003.

Badridze, Giorgi, Director of the Americas Office, Ministry of Foreign Affairs, April 2005.

Batonishvili, Zurab, General Director, Air BP Georgia, April 2005.

Bolkaria, Roman, Prosecutor General's Office, June 2003 and April 2004.

Christ, Mathew, Second Secretary, Political and Economics Affairs, Embassy of the United States of America, May 2003.

Clark, Lance, UN Resident and Humanitarian Coordinator, UNDP Resident Representative in Georgia, May 2003.

Denman, Amy, Executive Director, American Chamber of Commerce in Georgia, May 2003.

Dunn, Jonathon. Resident Representative, International Monetary Fund, June 2003.

Gegeshidze, Archil, Senior Fellow at the Georgia Foundation for Strategic and International Studies, July 2003, November 2003, and April 2005.

Giorgadze, Khatuna, Development Section Assistants, Department for International Development, British Embassy, June 2003.

Glonti, Giorgi, Director, Transnational Crime & Corruption Center, July 2003 and April 2004.

Gogia, Giorgi, Caucasus Analyst, International Crisis Group, November 2003.

Gotsiridze, Roman, Head, Budget Office, Parliament of Georgia, June 2003.

Japaridze, Ambassador Tedo, National Security Advisor to the President of Georgia, April 2004.

Kandelaki, Otar, Deputy Head, Budget Office, Parliament of Georgia, June 2003.

Kbilashvili, Rusudan, Editor-in-Chief, The Georgian Times, April 2005.

Khechinashvili, Devi, Chairman, Partnership for Social Initiatives, November 2003.

Khideshili, Tina, Board Member, Georgian Young Lawyers' Association, July 2003 and April 2004.

Khomeriki, Temur, Chairman of State Procurement Agency, June 2003.

Khutsishvili, George, Professor of Peace and Conflict Studies, Chairman of Board and Founding Director, International Center on Conflict and Negotiation, June 2003.

Kikodze, Zaaliko, Anthropologist and Conflict Resolution specialist, April 2005.

Kukainashvili, Lado, former Deputy Director, Georgian Gas International Corporation, April 2005.

Kvashilava, Gela, Ministry of Interior, Summer 2003 and April 2005.

Kvelashvili, Dimitri, Head of Financial Audit, United Energy Distribution Company of Georgia, April 2005.

MacKenna, Rod, First Secretary, British Embassy in Georgia, June 2003.

Marshania, Nino, electricity expert, PA Consulting, April 2005.

Melikidze Nikoloz, Director, The Strategic Research Centre, August 2003 and April 2005

Militauri, Joseph, World Bank energy expert, April 2005.

Morchiladze, David, General Director, Tbilgaz, March 2005.

Mukbaniani, Zviad, Chairman, Foreign Affairs Select Committee, Parliament of Georgia, June 2003.

Mullen, Mark, Head, National Democratic Institute and Transparency International, July 2003, November 2003, April 2005.

Muskhelishvili, Marina, Head, Centre for Social Studies, November 2003.

Nikoleishvili, Levan, National Security Council of Georgia, Director of Defence Issues Department, May 2003.

Papava, Tamuna, former employee GNERC, then Project Coordinator for gas programmes at TACIS, April 2004.

Papava, Vladimir, Senior Fellow, Georgia Foundation for Strategic and International Studies, July 2003, November 2003, and April 2005.

Parsons, Rob, BBC Journalist residence in Tbilisi, June 2003.

Salia, Korneli, Head of Border Guards, June 2003.

Saridze, Giorgi, Administration for Fighting Against Corruption and Economic Corruption, Ministry of the Interior, March 2004.

Sekania, Givi, Assistant to the Minister of Fuel and Energy, April 2005.

Siladze, George, TBC Group and Petrofag, April 2005.

Staszewski, Marian, Senior Political Advisor, United Nations Observer Mission in Georgia, July 2003.

Sunel, Yonca, First Secretary, Embassy of the Republic of Turkey, April 2005.

Tarkhan-Mouravi, Professor George, Co-Administrator, Institute for Policy Studies and professor at Tbilisi State University, July 2003 and April 2005.

Thornton, David, PA Consulting Group, Energy consultant for USAID projects, April 2004.

Tsirekidze, Buba, Advisory Assistant to the Ministry of Energy, Core International, USAID, April 2005.

Tugushi, Giorgi, Assistant to the Deputy Chairman, Parliament of Georgia, May 2003.

Tugushi, Lasha, Editor of Resonance Newspaper, April 2005.

Turnava, Natia, First Deputy Minister, Georgia Ministry of Economy, Industry and Trade, June 2003.

Usuparishvili, David, Senior Legal and Policy Advisor, IRIS-Georgia, Rule of Law Programme, April 2005.

Utiashvili, Shota, International Section Editor, 24 Hours newspaper, Tbilisi November 2003.

Vashakidze, Ambassador Nikoloz, Deputy Secretary, National Security Council, May 2003.

Vashakmadze, Sergo, Economist, World Bank in Tbilisi, June 2003.

Abkhazia (July 2003 and July 2005)

Akaba, Natilla, President, Association of Women in Abkhazia.

Atubaeva, Roza. Deputy Representative to the Secretary General of the United Nations in Abkhazia.

Gugulia, Manana. Director of Media Club and Abkhaz Press Agency.

Gvinja, Max. Assistant to the Minister of Foreign Affairs, *de facto* Ministry of Foreign Affairs.

Mukhail, Chalmaz, President of Grant Bank.

Shamba, Sergei, *de facto* Minister of Foreign Affairs.

Adjara

Mamuladze, David, Senator of the Adjarian Parliament, July 2003.

Phutkaradze, Eduard, Deputy Chairman of the Government of the Autonomous Republic of Adjara, September 2005.

Samskhte-Javakheti (July 2003)

Arzumanian, Rafael. Gamgebeli of Ninotsminda.

Buchukuri, Brigadier General Otar, Head of Akhaltsikhe Division, Border Guards.

Ezkuziani, Samvel. Border Guard, Ninotsminda

Mosiashvili, Teimur, Governor of the Samskhte-Javakheti Region.

Kopadze, Gia, Chairman of the New Rights Party, Akhaltsikhe.

Lagvilava, Nino, UNDP Integration Programme, Samtskhe-Javakheti.

Murjikneli, Marina, Akhalkalaki University, Department of Georgian Language.

Petriashvili, Tamazi and Zaza, Directors of the TV Company Lomisia and Gamgebeli (Zaza) of Akhaltsikhe.

Rastakian, David, Leader of Virk, Akhalkalaki.

Tsalenjikha (April 2004)

Gelava, Zurabi, Chief of Police of Tsalindjika.

Kvaratskhelia, Igor, Chairman of the Electoral Commission of Tsalenjikha.

Russia

Moscow

Krilov, Alexander. Chief Researcher, Institute for Eastern Studies, Russian Academy of Sciences, October 2003.

Lichfield, Gideon, Moscow Bureau Chief, The Economist, October 2003.

Malashenko, Alexei, Scholar-in-Residence, Carnegie Moscow, October 2003.

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United Kingdom

London

Broers, Laurence, School of Oriental and African Studies, Caucasus expert, 2004-2005.

Champlain, Phil, Director of Programmes, International Alert, February 2005.

Clogg, Rachel, Co-Director of the Caucasus Programme, Conciliation Resources, Spring 2003.

Corboy, Ambassador Dennis, Director, Caucasus Policy Institute, King's College London, Spring 2005.

de Waal, Thomas, Caucasus Editor, Institute for War & Reporting, Spring 2004.

Hewitt, George, Head of Department of Languages and Cultures of the Near and Middle East, School of Oriental and African Studies, May 2003.

Kavadze, Ambassador Amiran, Georgian Ambassador to the UK, February 2005.

Matveeva, Anna, Head of Arms & Security, Eastern Europe Programme, Saferworld, Fall 2003.

Nash, Ambassador Stephen, former British Ambassador to Georgia, Spring 2006.

Naysmith, Peter. Author and conflict resolution specialist on Georgia, Summer 2003.

Roberts, John, Energy Security Specialist, Platts, The McGraw-Hill Companies, September 2005 and 2006.

Rood, Elizabeth, Foreign & Commonwealth Office, Research Assistant, Eastern Research Group, April 2006.

United States

Hardin, Katherine, Director, Caspian Energy Russia and Caspian Energy, Cambridge Energy Research Associates, Boston, MA, October 2005.

Joyal, Paul, National Strategies Inc., Vice President, 2003.

Larabee, Stephen. RAND Corporation, Corporate Chair in European Security, 2003 and 2005.

Smith, Ambassador David, Senior Fellow, Potomac Institute for Policy Studies and US Member of the International Security Advisory Board (Georgia), 2003 onwards.

Welt, Cory, Deputy Director and Fellow, Russia and Eurasia Program, Center for Strategic and International Studies, Washington, DC, July 2006.

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