

# Fragmentation of Authority and Privatization of the State: From Gorbachev to Yeltsin

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In 1991, when the Soviet Union collapsed, state authority in Russia collapsed with it. State authority was associated with violence, the KGB, and party privileges. Discredited and despised, it was cast out and replaced not by the rule of law but by liberation from restraint. As happens in most revolutions, fear of the state evaporated. Instead of harmony and democracy, what ensued was a free-for-all—a rise in crime, theft of state assets, and a redivision of property comparable only to that under the Bolsheviks. Central authority, the ability of Moscow to enforce its will, weakened. In some places, local authority moved in to pick up the pieces; in others, criminal networks stepped in to usurp taxation and provide security. Louise Shelley has called the rise of organized crime and its domination of the economy and the ruling structures the new form of authoritarianism.<sup>1</sup>

This was the culmination of the fragmentation of Russian state authority that had started under Gorbachev during the so-called parade of sovereignties in 1990–91. Authority was no longer based on fear of Moscow's sanctions, but on what the local authorities could get away with. As one researcher put it, the nomenklatura freed itself from Communist Party control.<sup>2</sup> Gorbachev's rivalry with Yeltsin, and later Yeltsin's rivalry with the Supreme Soviet, stimulated the fragmentation of state authority in Russia. The provinces tried to acquire more and more power, defying Moscow at every opportunity. Some government ministries were disbanded, others were reorganized, and still others privatized.

Portions of the state structure were turned over to private hands, usually to former executives of those structures. An amalgamation of former state, current state, and private entities occurred. Some former state agencies became private companies, such as Gasprom from the Ministry of Oil and Gas, and those that remained state entities, such as the Ministry of Rail or the Ministry of Defense,

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created affiliates staffed by relatives and friends whose only purpose was to milk the state agencies and siphon off revenue. This process led one Russian scholar to conclude, "It is a state in which attempting to ascertain where gangsterism ends and the government begins is impossible, a state where in the laws of criminal clans turn out to be higher than human lives."<sup>3</sup>

### **Privatization of State Assets**

The privatization of state property in 1992–95, took place under conditions of fragmentation of state authority and in an atmosphere of "what one could get away with." Moscow was greatly weakened, and the local elites were strong; no legal infrastructure, strong middle class, or moral impediments stood in the way of the dividing up of property. Local elites, managers, soviet executives, party officials, police, and KGB networks used the situation to obtain as much real power and real assets as they could in the shortest time possible. Some did it by buying shares and vouchers and grabbing assets; others by selling off assets of the state under their custody, such as weapons, buildings, raw materials, and so forth.

"Factories to Workers!" was the Bolshevik slogan in 1917. What happened in 1992–95 can be summarized as "Oil to the Oil Ministry," "Factories to Managers," "Weapons to the Army," and "Railroads to the Railwaymen!" Custodians seized property under their custody. The people's property became the *nomenklatura's* property. Everything was divided by the civil servants, managers, and others representing the state.

The main outline of this story is well known. When the so-called price liberalization and shock therapy hit Russia in 1992, the existing monopoly networks that nominally still belonged to the state, but in fact were controlled by private interests, could hike up the prices on anything. During this hectic and virtually unregulated stage, no one knew what was worth what and who owed what to whom. The *nomenklatura* bought up the vouchers of their enterprises, enterprises themselves set up banks, which merged with other banks and acquired stakes in other enterprises. Banks and businesses that had something to export were doing well. Those tied to unsalable Soviet-era products were nearly bankrupt.

In August 1995, the country was sick of the shock therapy; most people suffered from it, and only a few exporters of raw materials flourished. The government desperately needed money. Yet there were few buyers for the to-be-privatized giants of the Stalin era. It was in this situation that Yeltsin signed what may turn out to be his most important *ukaz*, although at the time it did not appear to contain anything extraordinary. It allowed banks that loaned money to the government to receive as collateral shares of the enterprises to be sold—the "shares for loans" scheme. When the time came to auction the enterprises, those who held shares as collateral had a built-in advantage. Competitors were not admitted to the so-called auctions, prices were fixed, and state agencies in charge of the auctions had links to banks that were the sole participants.<sup>4</sup> As a result, state property passed to private owners at bargain-basement prices with the direct complicity of state agents who benefited from the transactions. Most of the auctions of real assets that took place in Russia in 1995 and 1996 were insider trading. It

was plain for all to see that in Russia rules and laws were not the same for everyone. It was whom you knew in Moscow that was important.

As Yegor Gaidar pointed out, the nomenklatura “acted gropingly, step by step, exploring what it could get away with, not in accordance with a well-considered plan, but obeying a deep instinct. It followed the scent of property as a predator pursues its prey.”<sup>5</sup> The nomenklatura, the ruling class under Brezhnev, had finally come to power by appropriating the real assets into its own hands as property. The nomenklatura as a social entity in the late Gorbachev and early Yeltsin periods acted coherently to “change the facade of the decrepit system, to legalize property relations that had formed spontaneously within the system and to build (or to bring to the surface) out of the shadows the edifice of nomenklatura state capitalism.”<sup>6</sup>

What Yegor Gaidar omits in his observations is that not all of the nomenklatura came to power through the privatization of assets. More important is that its well-being still derived from its proximity to the state; it still depended heavily on protection by those in high places. To get state agencies to deposit funds in one’s bank, to obtain an export license, or to represent the state in export operations, one needed friends in high places, as in Soviet times. Private capital in postcommunist Russia was born out of corruption and shady dealings of the nomenklatura.

Yeltsin probably did not realize the full implications of his actions, which had the effect of legalizing insider trading. He made it possible to create post-soviet monopolies; he established a climate of state favoritism in business, which tied the state to private monopolists and their protectors in government. He made it possible to create political-corporatist criminal networks that did not pay taxes, disregarded laws, and used state resources for private purposes. Those networks were soon to show their power in financing Yeltsin’s reelection campaign.

As this was happening, most observers in the West were applauding the rise of a class of owners in Russia that would become the bastion of democracy, the guarantor of the rule of law whose very foundation would be private property.<sup>7</sup>

### **Privatization of the State**

Privatization of the state is a system under which a state functionary has replaced the law, and different rules are applied to different people. Civil servants use the offices of the state for their personal enrichment and state functions are either not performed at all or performed for the benefit of those who use the state for illicit purposes.

The privatization of the state was a direct consequence of the privatization of state assets: If buildings and factories that used to belong to the state could become private property, why not state offices as well? If a factory manager privatized his factory and turned from a custodian to the owner, why could not an army commander treat his units and his materiel in a similar fashion? If a minister of gas and oil industries used his position to privatize oil and gas in a company in which he had a stake, why could not countless others—governors, mayors, and presidents—treat assets under their custody as if they were their own? In the West, such actions would qualify as abuse of authority and corruption. In Russia, it was merely the next stage of the nomenklatura privatization.

The Ministry of Railroad Transport did not own Russian railroads. As an office of the Russian state, its job has always been to regulate rail traffic and collect appropriate dues for the treasury. As a recent scandal revealed, high-ranking officials of the ministry used their influence so that part of the rail network and stock was sold to a private company whose owners were wives, nephews, and sons of those ministry officials. This private company was given preferential treatment in fulfilling contract work for the ministry and controlled 90 percent of the profitable western sector routes. It had exclusive rights in export of coal and many other perks. Hundreds of millions of dollars were made and divided up, much of it bypassing the treasury.<sup>8</sup>

State funds have been used by ranking state officials not only for personal enrichment but for political ends as well. According to Amy Knight, Korzhakov's security service was not accountable to anyone. It had been acting as a private KGB successor, selling arms abroad and using the revenue for Yeltsin's reelection campaign.<sup>9</sup> Similarly, in June

1996, Korzhakov's men arrested two of Chubais's men walking out of a government building with half-a-million dollars in cash. Despite subsequent scandals, no trial or account has been given. Accusations of misappropriation of funds, embezzlement, and private use of state funds appeared in the press but were hushed up.<sup>10</sup>

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### **Taxation and Extraction of Tribute**

Any modern state fulfills some basic functions, such as providing law enforcement, defense, and social services. In all of these areas, the state has been either weakened to impotence or taken over in part or in whole by criminal elements. It is common knowledge that the modern Russian state is not capable of collecting taxes. Tax evasion is pervasive. Because of its inability to collect more than a third of taxes, the state increased taxes to such high levels that even those willing to pay would be ruined if they did so. This pushes them into the ranks of tax evaders. Tax collectors siphon off some of the money into their own pockets, as do people in the customs service and local authorities issuing permits.

The use of public office for personal gain is so pervasive in today's Russia that virtually any transaction in any sphere requires a bribe or an extra tax, a tribute that goes into the hands of those who are supposed to perform their duties. Every traffic violation, every registry of apartments, every visa issued, and every day of trading activity is subject to tribute, not to the state, but to those who privatized state functions for personal enrichment. Doctors, judges, teachers, and clerks at all levels accept “presents” while performing their duties.

In Vladivostok, customs officials receive a cut of the proceeds of criminal cartels' importing goods without paying taxes to the state. In theory, they must enforce the customs regulations; in practice they use their offices to collect tribute into their own pockets. This is an example of a state agency turned into an appendage of a criminal organization, a state agency privatized and criminalized.

### Law and Bribe Enforcement

On paper, law enforcement in Russia is run by powerful institutions. The Ministry of Internal Affairs has a huge army at its disposal comparable to if not better equipped than the regular army. Yet in reality, in a typical Russian city, the militia is underpaid and understaffed, powerless to combat organized protection rackets.<sup>11</sup> The local city militia knows very well which groups control which businesses, which criminal groups have expanded to neighboring districts and cities. Data on major organized crime groups are systematically compiled.<sup>12</sup> The militia go through the motions of fighting them and in the process help themselves. Bribery has become a part of the system.

Organized crime groups have taken over functions of the state by providing protection, security, and insurance, coupled with extortion, racketeering, and money laundering.<sup>13</sup> Twenty-five thousand private security firms employing 800,000 people have privatized contract fulfillment by their own methods.<sup>14</sup> The Solntsevo criminal group, by means of violence, threats, and extortion, extracts a tribute from 30 percent of Moscow businesses. The press is flooded with reports of contract killings, usually reported as *mafioznye razborki*—mafia settling of accounts.<sup>15</sup> In fact, these are not only punishment for undelivered services or unpaid debts, but also part of endless turf wars or cases of revenge for refusal to pay tribute.

The temptation is enormous, noted a journalist, to let a vehicle go through without inspection if a reward is ten years' worth of your salary. The price of a Kalashnikov automatic rifle in Moscow—\$2,000—reflects all the fees one has to pay en route from the Caucasus, where it could easily be obtained for a bottle of vodka.<sup>16</sup> The former Minister of Internal Affairs, Kulikov, staged an experiment by sending a group of undercover agents into south Russia with a bus full of weapons. They were able to transport their cargo everywhere by paying officers at checkpoints, who "privatized" them. It is common knowledge in the streets what costs what. Everything has a price, from a parking violation fine to a residence permit or a release from custody. To get an arrested person released costs \$2,000 in most districts of Moscow, and to obtain release from Petrovka 38 headquarters is \$4,000.<sup>17</sup> Dropping of charges and suppressing evidence would cost more. In some areas, criminal groups control retail trade and small businesses and are more powerful than the local police.

Some observers have suggested that because the state was failing to perform duties such as enforcing contract fulfillment, paying wages, and providing security, people had to turn to criminal networks to fulfill those functions of the state; therefore, there was nothing wrong with it.<sup>18</sup> In reality, the customs officials in Vladivostok and the militia officers who release offenders for a fee have been turned into an extension of the criminal networks. Not only are the organized

crime groups not a private alternative to failing state services, but they have contaminated the state agencies with criminal cultural practices and taken over some of them altogether. The very expression “law enforcement” sounds like a joke in the Russian context: it is, in fact, bribe enforcement.

### **An Army of Traders**

The privatization of the state by corrupt officials took particularly ugly forms in the armed forces. Like the oil and railroads ministers and the traffic policemen who had turned assets in their custody into sources of revenue, army officers began to regard military hardware as “theirs.” Unlike oil or railroads, the army was a state institution that could not be privatized overtly. In reality, however, the army’s top brass, while remaining in state service, turned hardware, equipment, airfields, and airplanes into a source of personal enrichment. Hidden behind the checkpoints of military bases, unaccountable to anyone other than their military superiors, these officials were free to exploit opportunities that presented themselves after the collapse of the USSR. According to an expert study:

The frequent pilfering of unit equipment and supplies by military personnel of all kinds and the routine misuse of manpower and material resources rapidly became a sophisticated multidimensional ubiquitous series of criminal enterprises fostered and sustained by systematic corruption.<sup>19</sup>

One can distinguish three main levels of privatization of the state by the elements of the armed forces. The first was regular equipment pilfering, falsifying of accounts, and sale of military hardware by soldiers, junior officers, and unit commanders. Underpaid officers in many districts had to fend for themselves. They were not paid for months, and their only means of survival was to sell the hardware in their custody.<sup>20</sup> This form of embezzlement, theft, and abuse of authority was particularly widespread in the North Caucasus during the Chechen war.

Commanders of the Russian forces in Germany were notorious before their withdrawal in mid-1994. Illegal sale of military hardware ran into millions of dollars. Similarly, in the Baltics, the commander of the Baltic Military District was involved in large-scale, illegal sale of fuel, metals, and explosives. Even after withdrawal of the Russian troops, the networks that had been established continued to function, mostly in the areas of smuggling and illegal exports.

The second level of privatization was the systematic and prolonged operations involving numerous commanders in illegal trafficking of weapons and other materials, using army bases and resources. A case in point was the operation run by Major General Rodionov, commander of the Long Range Aviation base in the Far East.<sup>21</sup> The base was turned into a transportation hub for moving commercial goods into China, bypassing customs, of course. Bomber pilots and crews were involved in this money-making venture. Similarly, military buildings and equipment that had belonged to the construction troops were privatized by a civilian company staffed by relatives and friends of a group of officers. What all of these cases have in common is the transformation of the military command hierarchy into criminal-commercial networks that usurped state assets and functions.

The third level was the creation of nominal state agencies or companies that, in the course of their operations, turned into criminal and privatized enterprises with direct involvement of top government officials. The case in point was the affair with *Rosvooruzhenie*. Created in 1994 on the orders of Yeltsin, *Rosvooruzhenie* was supposed to be a state company in charge of Russia's export of military hardware. Viktor Samoilov of the Defense Ministry cadres department, a friend of then Defense Minister Pavel Grachev, was named the director. Most Bank was one of the banks officially authorized to handle transactions, and Yeltsin's bodyguard, Korzhakov, was given some supervisory functions over export operations. Deputy Prime Minister Oleg Soskovets became chairman of the Interdepartmental

Commission, which was also involved in *Rosvooruzhenie* operations.<sup>22</sup>

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In 1995, reports began to appear of improprieties with *Rosvooruzhenie* exports. Transactions were not recorded, money disappeared, and attempts to investigate were cut short. A state company was privatized. State bureaucrats of the highest level diverted some

of the revenue into foreign accounts and used the export operation for personal enrichment and political ends. Military hardware that had disappeared without a trace during the previous five years was worth hundreds of millions of dollars. A large portion of it was sold on international markets. Nuclear smuggling pops up on the pages of the press now and then as a concern of various international agencies.<sup>23</sup> Illegal activity of the Russian military—smuggling, diversion of equipment, illegal business ventures, and weapons trafficking—has earned them the name “mafia in uniform.”<sup>24</sup>

### **Social Services for a Fee**

The pride of socialism, the social services, were the cornerstone of Soviet achievements. The official ideology maintained that only in the country of the victorious proletariat could every person receive free medical care, free education, and a pension in old age. After 1991, social services became the most neglected area of Yeltsin's government. The shock therapists argued that if a few grandmas were unhappy with the forces of the market, that was their problem. Expenditures on education, medical care, and social benefits have been steadily falling. Schools are in need of repair; teachers are paid some \$40 a month, which has triggered a flight from the previously prestigious profession. Only those who had nowhere else to go remained teachers. Hospitals and clinics are overcrowded, understaffed, and without medicines. In most Russian cities, salaries have not been paid for months. The state has no money or inclination to support this colossus of the Soviet era and essentially has let the social services fend for

themselves. The state itself pushed parts of the fallen system to privatize themselves to survive.

Almost totally dependent on budget allocations, secondary and high schools and colleges were totally lost.<sup>25</sup> Colleges and universities realized that they had to rely on themselves, so they started subletting parts of their premises and charging tuition for foreign students and, increasingly, for domestic students as well. Some of these institutions managed to survive, others made money and invested it well, and therefore were able to expand and hire more faculty. The problem with most of these transactions was that they were based on a “what one-could-get-away-with” principle. Few people knew where the money received from foreign students went. Where did Yurii Afanasiev, president of the Russian Humanities University, obtain the money to buy a villa in France? From his official salary or from foreign students’ fees? The line dividing private and public spheres was blurred. No board of trustees, no faculty meetings, and no tax inspector could oversee most of those transactions. Those who founded genuinely private educational institutions could run them as businesses, paying appropriate taxes to the state, tributes to mafia, and bribes to state educational officials. But those that remained state institutions in theory and private in reality fit our definition of the privatization of the state. They generate autocratic practices, shady financial deals, and unethical if not criminal conduct.

By any measure, the Russian state has failed to deliver the most basic functions of the state in recent years: to provide social services, defense, and law enforcement on the basis of collected taxes. In many of these areas, criminal networks have taken over. In some, the state agencies aid the criminal networks. Not only has the Russian state been weakened and fragmented, its has been rotting as well.

#### **The Local Level: From Obkom Secretaries to the Feudal Lords**

By 1995, one could no longer speak of the national political scene in Russia. Politics became regionalized. Poor provinces of the so-called “Red belt” held on tenaciously to the “good old days” of Soviet rule, trying to retain the remnants of state subsidies, and those provinces identified as reformist embarked on various forms of new authority building. The diversity of Russian politics across the country is enormous. Successful autonomists, such as Shamiev, president of Tatarstan, skillfully managed to wrest from Moscow much of the taxing power over their republics. President Dudaev of Chechnya chose a more direct approach, which ended in a protracted war. Yet for the purposes of this discussion it is important to emphasize that virtually everywhere the local leaders gained in power in relation to Moscow. Local apparatchiks seized the opportunities that presented themselves after 1991. The process has been explained succinctly by Kimitaka Matsuzato:

Disgusted with Gorbachev’s incompetent leadership, a significant portion of the *khoziaistvenniki* supported Yeltsin. In 1992 Gaidar’s “shock therapy” pushed them toward opposition. Accelerated privatization changed their mood once again. . . . because the dubious procedures of privatization put the new property owners under the yoke of local administrations—of nomenklatura democrats. As always in Russian history, here also, the state created the estate.<sup>26</sup>

Consider the activities of famous “reformers” such as Sobchak in St. Petersburg, Luzhkov in Moscow, and Rossel in Yekaterinburg. They all have been or still are regional leaders with the reputation of being pro-Western reformers and democrats; all played the autonomy game against the Kremlin with varying degrees of success; all presided over privatization processes in their respective provinces and cities; and all made fortunes for themselves in the process.

As governors or mayors, these people had enormous powers during the process of privatization in their respective provinces or cities. They had the power to determine the value of land, buildings, permits, licenses, regulations, and taxation. They had to power to negotiate the share of taxes to be delivered to Moscow and the share for their regions. As Lynn Nelson has indicated, Rossel confronted the same kind of devastation as did much of the industrial region. The giants of the military-industrial complex came to a grinding halt. Hundreds of thousands of people were not being paid. City and provincial budgets could not hold out for long. In this situation, Rossel, then chair of the Soviet executive committee, encouraged the rhetoric of the Urals republic. Moscow did not fulfill its obligations, and the Urals was going to do better on its own. Popular sentiment was roused to bring pressure on Moscow to allow the Urals to export some of its nonferrous metals and raw materials and to buy food abroad to feed hungry workers. Moscow gave in. The conglomerate Interural made millions of dollars in the process. Rossel skillfully used local patriotism to play the autonomy card against Moscow while at the same time creating companies with direct links to Yeltsin. Rossel’s daughter works at the Interural office in Germany, and Yeltsin’s son-in-law at the Interural office in Moscow. Is Rossel’s case that of building a new, pro-Western, market-oriented democracy? Or is it an example of the military-industrial complex adapting to the new and, in the long run, more advantageous conditions—more freedom of action, access to world markets, and opportunities of enrichment? Lynn Nelson defined it as

a process in which business interests depend heavily on the favor of officials for privileges and benefits that range from securing buildings and equipment to receiving necessary permits and licences and being granted special tax considerations. These debts are sometimes repaid with lucrative jobs for relatives of officials sometimes with payments in money or goods and sometimes in “currency” of other types.<sup>27</sup>

These people used their offices as civil servants to create personal property out of public assets. They differed though from others in that while taking a cut for themselves they cared about their public image and tried to create a populist image. Yuriy Luzhkov went out of his way to pay pensions and wages and to provide city services to Moscovites. The popular attitudes toward people such as Luzhkov are remarkable. Widespread corruption is common knowledge, yet there has been no public outcry because “he cares.” Others only steal, but he steals and delivers something to the people. He became a popular mayor and, like Rossel, an example to others of a successful post-Communist leader. Sobchak, on the other hand, took too much *perebral*. His legacy is that of endless scandals and

revelations about misappropriations of funds, bogus foundations, favoritism, and outright theft and embezzlement.<sup>28</sup>

The successful bureaucrats have learned how to manipulate public opinion; influence, buy, or silence the media; and deliver votes, even more votes than there could possibly be voters. Those who have tried to oppose Moscow or stay in opposition persist in their poverty or have learned that the centralizing process would force them to pay homage to Moscow at some point. Neither side, however, has achieved complete victory. In summer 1997, when Yeltsin attempted to remove Nazdratenko from office in Vladivostok, Yurii Luzhkov of Moscow openly spoke out against Yeltsin, jealously guarding the prerogatives of elected local officials. Detailed studies suggest that a pattern of new politics is emerging in provincial Russia. New politics is a process of the rise of a new oligarchy based on newly privatized property and the intertwining of political and financial elites. A Russian sociologist put it this way:

An oligarchy of influential officials, new entrepreneurs and members of the former "directors' corps" as a group constitute a political corporation with opportunities for essentially unlimited control of all resources of power in the regions.<sup>29</sup>

No law governs what a ruler of a post-soviet *khanate* takes for himself. Luzhkov, Rossel, and Sobchak acted as rulers of little countries called Muscovy or Piter or the Urals republic. Major transactions in real estate and in imports and exports needed their approval and they required a cut. Banks involved in the businesses had to support the rules, and media outlets had to create a populist image of a nice guy playing football, like anyone else. The former Soviet executives now feudal lords effectively taxed businesses for a favorable contract or a permit and took an unspecified portion of the money as their personal gain. The line between public property and private property has been blurred because it was not defined. What was the city's was now theirs to exploit—for the city, for themselves, and for their friends. Luzhkov, Sobchak, and Rossel have been acting as feudal lords who could afford to disobey the khan on occasion and use the state for personal enrichment.

To a student of Russian history, this provides a sense of *deja vu*; there is something familiar about this system. In some way, it is a modified version of the Soviet political system of patronage networks and Obkom secretaries (*krysha*) in Moscow, in the Central Committee, and in the Politburo. It also reminds one of lucrative state contracts obtained through the intervention of Grigorii Rasputin at the imperial court for a hefty fee. By Western standards, what Luzhkov, Sobchak, and Rossel were doing would qualify as corruption pure and simple. In the Russian context, it is but another example of what we call the privatization of the state.

The new oligarchy is not monolithic. What they have in common is their skill in grasping the opportunities that presented themselves in the wake of the Soviet collapse. In the future, their clans, backed by their own media, banks, and enterprises, will clash over raw materials, markets, power, and influence, and ultimately over the crown in Moscow. How different are they from the medieval *Kniaz'ya* vying for the throne of all Muscovy?

### Government and Criminal Networks

Extortion and racketeering gangs, trade in stolen weaponry, cross-border illegal import-export operations, and pervasive bribery of civil servants at all levels are all manifestations of Russia's failing state. In many countries, criminal activity coexists with regular business. But in Russia most of today's big banks and corporations are big because they were parts of state industry privatized by the bureaucrats who ran them, or because they made their fortunes from special tariffs, privileges, and tax breaks denied to others. Russia's big business is a product of corrupt practices, unfair dealings, and abuse of authority: by Western standards it is criminal in its very origins.

Consider two types of criminal actions—fixed brokering and insider trading. Fixed brokering is defined as companies' securing state contracts by bribes and kickbacks to government officials. In the West, dirty brokers are usually the initiators of fixed brokering, but in Russia, it is the state agencies that are offering contracts to companies on condition of a bribe. According to *Gas and Oil Journal*, in the Russian gas and oil industry these practices affect 100 percent of the contracts.<sup>30</sup> The way to do business in Russia is to fix deals behind closed doors with those empowered to act on behalf of the state. Influence peddling and insider trading are practices that involve leaking privileged information to commercial entities that would lead to their enrichment and to the transfer of certain funds to the source of the privileged information. According to a Russian scholar, 70 percent of state officials take bribes. All of the auctions in 1995–96 were, by Western standards, insider trading.

Most of Russia's banks are connected to some *krysha* (roof protector) in government on whose influence and patronage they depend for their well-being and survival. It is a system of clans of politicians and bankers controlling certain sectors of the economy and certain sectors of state power.<sup>31</sup> Political parties, laws, and law enforcement agencies are secondary in this system. Primary is the patronage network between government officials and the banks and industries that these networks control. One observer has called such networks "gangster bureaucrats."<sup>32</sup>

Property is just as elusive as it was in Soviet times. Today's owners may well discover that their property is gone or threatened once they or their protectors are out of favor. Everything hinges not on law but on having protection in high places—*krysha*. The loss of the *krysha* for a company in Moscow may mean a change in taxation rate, revision of the statutes under which it operates, revision of ownership, denial of government contracts, or outright liquidation. This is exactly what is happening now in St. Petersburg. With the fall of Sobchak, some of his subordinates wound up accused of corruption, misappropriated funds, and bribe taking. As insurance against such a turn of events, billions of dollars in seized assets have been leaving Russia to safe havens abroad.<sup>33</sup>

The new owners are acting like thieves, not owners. They know that the terms of their ownership can be questioned and reconsidered. This, in turn, creates an incentive to rely not on the rule of law but on the continued practice of influence peddling, insider trading, and bribery. As a result, the difference between honest and legitimate

businesses or banks and the corrupt and criminal ones is blurred. Honest businesses and factories are bought by corrupt banks, which involve them in their operations. The result is the strengthening of the criminal-corporatist networks.<sup>34</sup>

With this background, the big magnates approach the state as something to be used for their purposes. For them, state office is a means of self-enrichment. The magnates constantly seek to increase their power and strengthen their representation in Moscow. In recent months, the big seven banks have been buying up Russia's major newspapers. Editors were changed, and policies and objectives were redefined. Some courageous Russian journalists have been protesting against new censorship, outright manipulation of the press, and its shameless use for the benefit of the new owners.<sup>35</sup> One Russian political observer put it this way:

An unseen bureaucratic overturn has taken place in Russia. And the massive buying up of the newspaper is only its last stage. We have lost without noticing not only the freedom of the press but freedom generally. Russia is entering a new political epoch which is somewhat similar to Brezhnev's stagnation. Everything will be determined by the interests of the financial-bureaucratic oligarchy.<sup>36</sup>

The ultimate objective is to become so powerful that no state regulation could threaten them. For this reason, the huge banks have been diversifying their holdings; cultivating support in geographic areas where their presence is high; incorporating local politicians, mayors, and Duma members as consultants and board members; and fostering special relationships with appropriate bureaucracies in Moscow. The super rich magnates strive to maximize profits, evade paying taxes, and enjoy confidential relations with the corrupt bureaucracy. They are engaged in empire building, or, to put it in other words, in creating corporate-political criminal networks. The product is the system of corporate-bureaucratic clans that act as monopoly producers and link corrupt state officials and criminal elements.<sup>37</sup>

### Conclusions

Russian government is the conglomeration of criminal-corporatist political clans engaged in a constant struggle for power. Government officials are not strictly the agents of the state but are representatives of private interests, which they defend in the state apparatus for a fee. They preside over state agencies that have in fact been privatized.

Customs, police, and the army are sick elements of the Russian state. They are underpaid, and are encouraged to fend for themselves by illicit contacts with organized crime. In some parts of the country, they have fused with organized crime groups.

Banks, corporations, and holding companies' control over their assets is still tenuous and reversible, because it is still dependent on the big *krysha* providers in government. Any change in the balance of power between the kingmakers may cause the fall of some banks and companies and the rise of others, but not the destruction of the system of corrupt capitalism.

Governors and mayors are feudal lords despite appearances of populist democracy because the line between private and public is blurred. They treat their provinces as their *votchina*, patrimony where they are the patrons. They define

the tribute they extract for themselves, they define the rules and regulations of the so-called economic reform, and they represent their regions in Moscow in the federation council. In some respects, their power is superior to that of the *obkom* secretaries, from whom they inherited the system of bribe taking and the patronage networks of the Brezhnev days.

It is extremely naive to believe that because there is private property in Russia, there will automatically be democracy and rule of law. On the contrary, private property appeared in Russia as a result of a hectic redivision of wealth conducted by and in the interests of the corrupt nomenklatura. Private property was added to the Soviet system. In the end, it may well be that private property will not democratize the Soviet system, but that the Soviet system will absorb and modify private property. Privatization of property led to the privatization of state, which in turn, led to the strengthening of criminal networks of monopoly magnates and government agencies.

The true division in Russia today is not between reformers—democrats and retrograde Communists—but between networks who grabbed real assets using the state and those who feel they were deprived of their fair share. Political struggle is not between reformers and conservatives but between those who seized parts of the state for their own benefit and those who were left behind, striving for a place under the sun. The rule of law is as distant in Russia as it was seven years ago. Democracy is a propaganda ploy as it was in the days of Stalin. Behind the facade of democracy, no longer are there commissars and *obkom* secretaries, but networks of bankers, corrupt executives, bureaucrats, and mafia bosses. In the last seven years, Russia has made enormous strides toward creating a criminal corporatist oligarchy.

#### NOTES

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2. Lynn D. Nelson and Irina Y. Kuzes, "Interest Representation in Sverdlovsk and the Ascendancy of Regional Corporatism," *Demokratizatsiya* 5 (spring 1997): 236.
3. Yuriy Voronin, "The Emerging Criminal State: Economic and Political Aspects of Organized Crime in Russia," *Transnational Organized Crime* 2 (summer/autumn 1996): 53.
4. "Going, Going, Gone. Russia Auctions off Stake in Oil Company to the Only Bidder," *Wall Street Journal*, 24 December 1996, 2.
5. Yegor Gaidar, "How Nomenklatura Privatized Its Power," *Russian Politics and Law* 34 (January-February 1996): 35.
6. Ibid.
7. See for example, Anders Aslund, "Russia's Success Sory," *Foreign Affairs* 73 (September-October 1994): 58–71.
8. "Ministerstvo zhen, plemiannikov a synovey," *Izvestiya*, 24 October 1997.
9. Amy Knight, "Internal Security and the Rule of Law in Russia," *Current History* 95 (October 1996): 311–15.
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16. "Proshchai Oruzhie," *Mir Novostei*, 12 May 1997, 5.
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18. Jim Leitzel, Clifford Gaddy, and Michael Alexeev, "Mafiosi i Matreshki," *Brookings Review* 13 (winter 1995): 26.
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20. Galina Mashtakova, "Ordered To Steal," *Moscow News*, 24–30 July 1996, 12. See also Victoria Tripolskaya-Mitlyng, "A Parade of Troubles," *Bulletin of the Atomic Scientist* 52 (November 1996): 17.
21. Graham H. Turbiville, "Organized Crime and the Russian Armed Forces," *Transnational Organized Crime* 2 (winter 1995): 75.
22. *Ibid.*, 74.
23. See for example, Rensselaer, "Recent Trends in Nuclear Smuggling," *Transnational Organized Crime* 2 (summer/autumn 1996): 109–122.
24. Turbiville, "Organized Crime and the Russian Armed Forces," 62.
25. On machinations in the education administration, see "Mafiya: luchshii podarok - kniga," *Novaya Gazeta*, 7–13 July 1997, 6.
26. Kimitaka Matsuzato, "The Split and Reconfiguration of Ex-Communist Party Factions in the Russian Oblast Chelyabinsk, Samara, Ulyanovsk, Tambov, and Tver (1991–1995)" *Demokratizatsiya* 5 (winter 1997): 53–89.
27. Lynn D. Nelson and Irina Y. Kuzes, "Interest Representation in Sverdlovsk and the Ascendancy of Regional Corporatism," 222–39.
28. "Ten' Sobchaka," *Novaya Gazeta*, 21–27 July 1997, 5. See also Vadim Nesvizhsky, "Thorough Purge of Petersburg Police Begins," *Current Digest of Post-Soviet Press*, 19 March 1997, 23.
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