**Russia’s Oligarchs and the Case of Mikhail Khodorkovsky**

Olivia K. Leonard

**Abstract**

The fall of the Soviet Union led to a rapid introduction of privatization and emergence of market economy. The absence of clear rules for privatization, a weak government and the dizzying pace of change led to a narrow group of politically connected entrepreneurs taking full advantage of the opportunities and concentrating much of the wealth in their hands. Many of the Oligarchs were mangers of enterprises or other well-connected officials during the Soviet era. They used their political connection and knowledge to earn vast fortunes.  By focusing on the rise and fall of the politically ambitious Yokos chief, Mikhail Khodorkovsky, I want to highlight the complex relationship between the Russian government and the Oligarch.  I show that the weak government under Yeltsin was more dependent upon the Oligarch but under Putin’s rule the state has asserted its control over the Oligarchs.

**Russia’s Oligarchs and the Case of Mikhail Khodorkovsky**

After the fall of the Soviet Empire, Russia experienced a sudden and rapid transition to capitalism and democracy. Observers expected Russia to develop a “unique” form of democracy and open-markets but did not expect a concentration of power to be in the hands of the few. The relationship between the Russian tycoons and the suits in the Kremlin developed during the end of the Soviet era and strengthened under President Boris Yeltsin. Government dealings with the entrepreneurs were legal in a system that lacked clear economic policies and means of enforcement.

Oligarchy, as defined by Aristotle is the rule of a wealthy few and is the least stable and desirable form of government because they constantly promote their private and political interests (Wegren and Herspring, 159). For Russia, the term oligarch is used to describe a group of individuals who used their political connections to enhance their economic interests. Many of the Oligarchs were mangers of enterprises or were other well-connected officials during the Soviet era. They used their political connection and knowledge to earn vast fortunes.

The rise of the Oligarchs emerged during the chaotic shift from communism to capitalism in which power transitioned from formal political institutions to informal networks of individuals who had economic resources or political connections at their disposal. Corruption and mutual favors rather than transparent rules and regulations drove this process of privatization (162). Russia had never experienced a form of democracy or open market system before and had to re-invent the wheel as to how they would implement this new system.

During the early stages of transition to capitalism in Russia, rapid voucher privatization between 1992 and 1994 gave managers of former state owned enterprises’ and employees the opportunity to become legal owners of it. There was no set of technical rules and procedures in place which privileged the insiders- mangers of insiders of the Soviet rules- and those who had the cash for privatization. Although the government had introduced private property, it failed to draft institutions and laws that protected and specified the rights of ownership (Volkov, 250). The conditions were ripe for a few well-connected insiders to become the new ruling elite. Rather than opening opportunities for wider section of society, privatization ended up replacing the previous party apparatchik with another set of oligarchs.

As state institutions, including law enforcement, collapsed the private sector became in charge of the developing markets. Private businesses paid off private and state enforcers as the government failed to develop any significant policy. The breeding grounds for a new system were in place; the absence of laws, moral and institutional collapse, and the state’s withdrawal from it all made the rise of the Oligarchs possible (250).

The “loans-for-shares” auctions in 1995-1995 were a key stepping stone in the transition to Oligarchy. Key firms, such as the Sibneft Oil Company and Norilsk Nickel, were sold off cheaply to businessmen with strong political ties. These auctions were rigged: those who could offer financial and organizational resources for his re-election bid in 1996 were sure to win the bidding process (Wegren and Herspring, 164). The future of the Oligarchs was at the mercy of Yeltsin. The opposition Communist Party leader, Gennady Zyuganov a former Soviet propagandist, was leading the polls and there was a grave threat of reversing privatization (Hoffman, 310-313). Yeltsin was pulled through victory with the help of the Oligarchs. For example, Boris Berezovsky mobilized his media empire to help Boris Yeltsin win the elections, (Wegren and Herspring, 164).

The beauty behind the “loans-for-shares” auctions was that it was carefully planned out by some of the same tycoons who benefited from these auctions. The banks would give the government a loan and “…take some of the factories as collateral” (Hoffman, 307). This is how some of the Oligarchs ended up owning some of Russia’s largest state owned enterprises. One of two deputy Prime Ministers, Anatoly Chubais, met with Vladimir Potanin who drafted the plan along with bank owners Mikhail Khodorkovsky and Alexander Smolensky. Chubais knew that the plan was rigged and that the winners of the auctions were ultimately being hand-picked by the Kremlin (Hoffman, 309-110). In order to ensure the help of Oligarchs to the re-election bid of Boris Yeltsin, Chuabis created a:

“…dual key system, in which the first key for each factory would be given out before the 1996 presidential election, but the second key-the one that allowed the businessmen to lock up and keep their property-would be distributed only after the 1996 election” (Hoffman, 313).

The banks were allowed to take over and manage the factories that they had as collateral until the loans were repaid by the government. If the government defaulted, “…the banks could sell the shares in a second phase, paying back the loans but keeping 30 percent of the proceeds as a commission” (Hoffman, 314). The loans-for-shares auctions put the Oligarchs in a chokehold. They could only obtain the collateral from the government if Yeltsin was re-elected. Berezovsky had to give Yeltsin media time and campaign ads to ensure his re-election as President so that the Oligarchs that were involved wouldn’t lose everything.

A key feature outlined in the plan allowed the Oligarchs to be the auctioneer and bid on their company of choice. For example, Menatep Bank, owned by Khodorkovsky, organized the auction for Yukos Oil Company. Khodorkovsky bought 45 percent of the shares for $150 million and another 33 percent in an investment tender for $150 million with the promise of another $200 million to invest into the company under one of his shell companies. It was unclear where Khodorkovsky got the money to buy Yukos. He had various international political and financial connections and claimed that most of the money was borrowed from various sources. One former bank official stated that he was buying Yukos with the money Yukos had accumulated from not paying their taxes. It is believed by insiders that Khodorkovsky exploited the connection he had with Yukos by using their money in return for “…future oil deliveries for loans” (Hoffman, 314-318). Regardless of where Khodorkovsky obtained the money from, lack of transparent privatization process and procedures permitted such behavior to occur without the risk of repercussions from the State.

Out of these auctions emerged some of the most powerful Oligarchs such as Boris Berezovsky, Roman Abramovich, and Mikhail Khodorkovsky. The first generation of Oligarchs primarily owned banks, media, natural resources, and other enterprises. They “…obtained their wealth and influence by controlling financial and information flows” while exchanging favors with politicians, such as giving media time to them in return for expanding their power and maintaining their property in the case for Yeltsin’s re-election (Volkov, 251).

While the first group of Oligarchs relied heavily on political ties from the Soviet era, the second group of Oligarchs aggressively competed for control over thousands of enterprises. The latter took advantage of the laissez- faire policies and induced hostile takeovers after the August 1998 financial crisis. Along with laissez-faire policies between 1998 and 2002, “…Moscow focused on reducing the excessive regional sovereignty, leaving the oligarchs to compete for assets” (Volkov, 252).

The 1998 financial crisis was caused by the massive debt that the Russian government had obtained to pay for budget deficits:

“First the government borrowed money to defend the ruble at an exchange rate that was overvalued against the dollar, and second, it issued $40 billion of short-term debt to cover its yawning budget deficit instead of trying to cut government spending…In August 1998 the Russian government defaulted on its debts, the ruble lost 75 percent of its value, and most private banks collapsed, wiping out much of the savings of Russia’s nascent middle class” (Herspring, 165).

Many Oligarchs were seriously weakened by the financial crisis but those who had investments in industries such as oil and gas were virtually unaffected. The Oligarchs who were unaffected mostly kept their money that they had stripped from the government and other enterprises offshore, which added to the draining of the Russian economy. The new laisser-faire policies were once again legally exploited, this time however they also sought help from the courts.

A new generation of Oligarchs exploited the financial crisis by taking over enterprises as either “…legal actions in defense of the minority shareholder’s rights” or by framing them as bankruptcy proceedings through the courts. These procedures were typical and allowed advancement for the new camp of Oligarchs. Newer laws which were meant to facilitate the privatization process also made it easy to overthrow the current management team. For example, the 1998 “Law on Bankruptcy” and the latter “Law on Joint-Stock Companies”, allowed the courts to:

“…initiate bankruptcy procedures against enterprises when their outstanding debts exceeded the equivalent of 500 minimum-wage payments –about 42,000 rubles in 1999 (about $15,000), and were not repaid within three months of the due date” (Volkov, 252).

The aftermath of the 1998 financial crisis left the country with a tremendously low debt threshold that allowed the more powerful actors to push out weaker actors’ and seize their assets.

The practice of these “contract bankruptcies” amounted to approximately 1,400 cases in 2001. The term “contract bankruptcy” implies a hidden economic agenda and about half of the 1,400 cases “…were connected with hostile takeovers and attempts to avoid repaying debts to outside investors or taxes to the state” (252). The enterprises that were targeted were mainly the large and medium ones with the most prominent cases from the natural resources sector such as oil and gas (252-253).

**The Oligarchs: A Closer Look**

“By the beginning of 1999 two groups of oligarchs had formed to claim power over Russian and the Kremlin” (Khrushchev, 4). The first group could be comparable to America’s robber-barons and not considered to be as mischievous as the later group of Oligarchs. The former focused mostly on their expansion in Russia and the rest of the world while ensuring that future ties would still be in Russia. The other more aggressive group of oligarchs formed in the Kremlin:

“They had acquired billions, mainly through financial speculation, and were therefore especially dependent on the powers that be, just as the corrupted government became financially dependent on them” (Khrushchev, 6).

The second group included Boris Berezovsky and Roman Abramovich.

In 1993, Berezovsky and Abramovich, a young oil engineer who was knowledgeable about the oil-rich Siberian region, formed a partnership. By 1995, Berezovksy persuaded Yeltsin “…into issuing a decree on the formation of a Siberian oil company, Sibneft, and Abramovich indicated which state enterprises should be included in it- the most profitable, naturally” (Khrushchev, 6). The plan went smoothly and “…after a mortgage auction and two monetary auctions with foregone conclusions, Sibneft was fully owned by Abramovich and Berezovsky” (Khrushchev, 6).

Berezovsky was the former executive secretary of the Confederation of Independent States and had acquired a lot of power in the Kremlin. He was well connected with the Yeltsin family but after the 1998 financial crisis tension arose. Berezovsky managed to hold complete control over companies that he only had a few shares of and appointed various members of Yeltsin’s family on the board of companies he owned (Khrushchev, 7).

Along with two other Oligarchs, Berezovsky became the co-owner of two Swiss companies in 1998. He was soon accused of money laundering by a Kremlin deputy who happened to be the husband of one of Yeltsin’s daughters. The Oligarchs began to panic as they were ordered by the prosecutor’s office to simply provide a testimony. These “witnesses” fled Russia in a panic. Prominent Oligarchs such as Alexsandr Smolenskey and Berezovsky started a political campaign once abroad against newly appointed Prime Minister Yevgeny Primakov, who led the investigation (Khrushchev, 8-9).

The Oligarchs influence ran so deep under Yeltsin that he forced the resignation of the lead prosecuting attorney and Primakov. Berezovsky’s close relationship with Yeltsin’s daughter Tatyana influenced his decision to end the investigation against Berezovsky. In the spring of 1999, power began to shift between the Oligarchs and the Kremlin when numerous governors lost an election that was fully backed by Oligarchs, such as television magnate Vladimir Gusinsky. Only months later, in July, the Yeltsin family picked Vladimir Putin to become the president (Khrushchev, 9-12)

The August 1998 financial collapse, Yeltsin’s last couple years spent physically incapacitated, and the upcoming new appointment of Yeltsin’s successor caste shadows on the future of the infant democratic market-economy of Russia. Would the Oligarchies continue to reign? Would Putin come down with new economic reforms? Soon after Putin’s appointment, it was clear that changes were about to occur.

**Vladimir Putin and Mikhail Khodorkovsky**

Under control of President Vladimir Putin, there were some key turning points in reasserting control of Russian industry. On October 2003, the richest man in Russia, Mikhail Khodorkovsky, head of the Russia’s largest oil company, Yukos, was arrested and subsequently sentenced to eight years in jail for tax evasion (Wegren and Herspring, 161). Khodorkovsky was one of the leading figures from the very beginning but now, Putin saw Khodorkovsky as a political threat. Khodorkovsky’s trial and verdict verified Putin’s power and raised new questions about the relationship between the Russian state and the Oligarchs and the fate of democracy and capitalism in Russia.

On the night of December 31st, when Putin was appointed Prime Minister, he left a hopeful impression on the people of Russia. He gave an address that focused on a new type of society that would address Russia’s social and economic problems such as ending corruption and creating a stronger state. He discussed the lack of capital investments and the fact that at Russia was very far behind world production and innovation of goods, Russia accounted for less than 1% of world’s commodities at that time. In Putin’s address, he urged the need for market reform as a bulwark against the inheritance of a Soviet style economy. He stated the following in his address:

“We are paying for the Soviet neglect of such key sectors as information science, electronics, and communications….and today we are reaping the bitter fruit, both material and mental, of the past decades” (*The Modern Russia*, Putin).

Putin followed this up by admitting that the Soviet system had set Russia back economically and ultimately into a “blind alley” far away from mainstream civilization. He further stated that Russia had used up its limit for political and socio-economical upheavals and ultimately the limit of tolerance for a new radical break up that would lead to an economic, moral, political, psychological, and moral collapse (Putin, Vladimir).

Putin wanted to continue market reform without revisiting Yetsin’s privatization program. Putin kept many key figures from Yeltsin’s family and appointed Chubais to privatize electricity monopoly Unified Energy System. He drove Berezovsky and Gusinsky into exile and obtained control of the two national TV stations by sending in the tax police. The other Oligarchs had assumed that as long as they kept away from mass media, they would be fine.

In spring of 2003, it was rumored that Khodorkovsky intended to run for president in 2008 with the possibility of running as early as 2004. Yukos had the loyalty of Duma deputies and used “…its leverage to black legislation it disliked, such as higher oil excise taxes and revisions to the 1995 law on production and sharing (an arrangement that allowed approved foreign companies to recoup their investments in oil and gas fields before they started paying taxes)” (Wegren and Herspring, 166).

Khodorkovsky poured money across various political parties during the December 2003 State Duma election. As he became more and more successful in the public’s eyes by funding international charities and opening his business to the West and China, he became more of a threat to Putin. After Putin had Khodorkovsky arrested in the summer of 2003, his party had received a sweeping victory in the December 2003 election (Wegren and Herspring, 166, 167).

**The Rise and Fall of Khodorkovsky**

Mikhail Khodorkovsky had a rare advantage as a young man because while attending university he served as deputy chief of Komsomol and made connections with Communist Party bosses, including the KGB (Hoffman, 100). Khodorkovsky was a very determined young man who recognized the shortcomings and even the loopholes in the Soviet system. He obtained a degree in chemistry, served on his university’s economic debate team, and studied law for a few years finding it “necessary to be able to understand and exploit decrees issued by the government” (Hoffman, 111). His knowledge of science, economics, the law, and his ties with Komsomol would later become necessary for his advancements as a businessman in the newly reformed state.

In the late 1980’s, the Communist Party felt that they had to do something drastic in order to salvage Komsomol as membership was drastically declining. They decided to conduct an experiment where they introduced some capitalist elements into the organization by allowing the youth to own their own businesses that would be funded by Komsomol or through loans. The enterprises were allowed to keep their own profits and soon enough printing shops, cafes, discos, bars and other small businesses popped up. Khodorkovsky’s first business was a café inside of the university, which was unsuccessful. His second venture focused on young scientists, like himself, that gave technical support to industry and factories. His private ventures annoyed his superiors at Komsomol who in 1987, just a year after he graduated, presented him with only two choices: he could either climb the Komsomol ladder or leave and go on with what they referred to as his “self-financing tricks” (Hoffman, 101- 107). Khodorkovsky energetically chose the latter which was a gamble considering that he could lose a chance to obtain a powerful and prestige position in order to try for a risky Soviet experiment.

One of Khodorkovksy’s first stops was at The Institute of High Temperatures, which was an enormous and highly sophisticated lab that studied high-temperature physics, lasers, and rocket propulsion. The head of the company, Alexander Sheindlin, recalled his impression of Khodorkovsky and his business partner as energetic and that they carried good merit as former Komsomol workers. Sheindlin admits that they had nothing to offer him but were good guys and he wanted to give them money because they said that they would work honestly and just needed some “start-up capital” (107-108). He gave them about 170,000 rubles and had them agree to doing “some kind of scientific research” (108). Sheindlin also reflected that he doesn’t know the details of what they did with the money but he does know that they used “this money to increase the money many, many times” (108). Khodorkovksy’s deal with the institute was just one small step as he “discovered how to exploit the way money was controlled and used-and turn it into more money” (109).

In the Soviet system, there were two kinds of money. There was simple cash and there was non-cash, or beznalichnye. Simple cash was scarcer in factories and enterprises and was hard to obtain from the State while non-cash was widely distributed as virtual cash as subsidies to factories. Beznalichnye only existed as a unit for accounting and could not go into your pocket. It was prohibited for a factory manager to change the virtual money into real money. This was a major dilemma for factory managers who always needed more cash from the State while the nearly useless supply of beznalichnye was very abundant. Khodorkovsky took advantage of this imbalance and figured out how to turn the virtual cash into real cash (109-110).

In December 1987, a new set of financial rules was issued by the central committee of the Komsomol which allowed them to set up their own bank accounts and raise and spend as they wished. An extremely significant rule that came out of this was that the organization could mix the simple cash and non-cash for certain cases. The youth had attempted a strategy that no factory director had dared do: “turn the useless noncash into cash and pay more people with it or build a nice dacha in the woods outside of Moscow” (110). `

One of Khodorkovsky’s privileges as a Komsomol man allowed him to set up “temporary creative collectives” which is a group of workers who worked inside of the institute or outside of it and could legally be paid in cash. He could draw up contracts to have them write software, build something for the institute, or perform a research project. This is where the money machine comes in to the picture: “Khodorkovsky could take the noncash from the institute and turn it into cash to pay the ‘temporary creative collective’” (111). As Hoffman puts it, “This was not just peanuts, but real money churning from idle state subsidies into hard cash” (111).

Khodorkovsky was constantly hustling and coming up with new ideas to draw out more money from thin air. He was able to find “some enterprises that would exchange the noncash for valuable foreign hard currency” (114). This export companies were primarily timber with plenty of hard currency for Khodorkovsky to exchange with the virtually worthless noncash. His “financing tricks” were now reaching new heights and with his ties to the Komsomol he was able to practice this type of business unlike other young hustlers who couldn’t take as many risks because of the KGB (115).

Khodorkovsky was protected by his connections at Komsomol and by the powerful State Committee on Science and Technology, which cosponsored youth science centers when he was questioned by Soviet militia. With all of the changes taking place, law enforcement didn’t really understand what perestroika was as entrepreneurship was gradually being taken into the system. When questioned by the militia, Khodorkovsky appealed to the chairman of the State Committee in detail about what he was doing and asked to be left alone. The next two years were the most crucial two years of Khodorkovsky’s money machine and he had the authorities off his back (115).

Khodorkovsky next venture was in computers. He bought personal computers with hard currency from abroad, sold them for virtual cash, and then changed the noncash back into hard currency again. Due to the enormous price differences inside of the Soviet Union along with scarcity and high demand, personal computers was one of the most profitable turnovers Khodorkovsky could have taken. Khodorkovsky once stated that “it is possible to find loopholes in every law, and I will use them without an instant of hesitation” (118). The fact of the matter is that Khodorkovksy wasn’t really doing anything illegal at this time. He had the full backing of the reformist in Soviet State in not one, but two departments along with vague perestroika laws that were often overridden by whenever the party apparatchik found them to be inconvenient. Khodorkovsky was intelligently seizing opportunities but was cautions because he did not know how much longer glasnost and perestroika might survive.

When the main bank of the Soviet Union, Gosbank, split into five different banks specializing in different areas such as agriculture and foreign trade, Khodorkovsky sought them out for a loan to create his own bank. Although they couldn’t give him a loan because he was not a state enterprise under an official state plan, they could help him set up his own commercial bank. Khodorkovsky’s old friend Sheindlin, who was very eager to help sponsor him as he was concerned about connections and status. Khodorkovsky brought in Vladislav Surkov, who he knew from the youth science center to help him market his new bank Menatep, the marketing strategy was so successful that Menatep soon turned into a household name. They did all sorts of catchy television ads and celebrity appearances on talk shows in order to get thousands of shareholders. This way, if the authorizes tried to end their play time; they would encounter resistance (118-123).

Khodorkovsky and his business partner Nevzlin decided to that there wasn’t enough money to be made in the emerging private sector. They decided to milk the largest source of capital, the State owned enterprises. During the escalated chaos in the Kremlin at this time, Khodorkovsky roamed the corridors of the Kremlin and became an adviser to Ivan Silayev, Yeltsin’s prime minister. The government was issuing enormous amounts of credits to enterprises to keep them from closing. One of the first chosen banks to transfer government money to enterprises was Menatep. “…Khodorkovsky could parlay the state credits-which came practically free, like water from a tap- into good profits” (124). Similar to what he did with computers he did with credit: he “…took money from the state, gave it to state enterprises, and then took money from state enterprises and returned it to the state” (124). The State did not understand the time value of money and the turnover that Khodorkovsky made was extremely profitable. He and Nevzlin understood the importance of connections with the State and made millions in a very short period of time.

By 1997, Khodorkovsky was on top of the world. He was expanding internationally and was very optimistic. That year he had “…unabashedly told a business crowd in Washington that he wanted to be among the top ten world oil companies within decades” (397). At only thirty-four years old, Khodorkovsky was in charge of an oil company that had Russia’s largest oil reserves and won another auction obtaining another Russian oil prize, Eastern Oil Company. His control of “an ocean of oil” allowed him to borrow loans from a variety of Western banks, including Goldman Sachs and Credit Lyonnais. Khodorkovsky demanded the oilfield extraction companies to sell him the oil at very cheap prices to parent company Yukos. He then exported the oil at much higher prices to secure his loans. He cleverly stripped the value of the extraction companies, now left with debt, while he reaped the benefits of the new loans (398).

On January 19, 1998, he announced that he would combine Yukos with Berezovksy’s oil company, Sibneft. The new oil giant would be called Yuksi and would be the largest integrated oil company in the country. Sitting shoulder to shoulder at the announcement were media giant Vladimir Gusinsky, “banking king” Alexander Smolensky, Berezovsky, and Khodorkovsky. The banks owned by Khodorkovsky and Gusinsky would be folded into Smolensky’s SBS-Argo, thus making him “the banking king” (400-401). This merger fell apart after only five and a half months as oil prices began to drop and while Russia’s economy was faced with devaluation and debt (402, 419).

The case against Yukos started to build up in 1998. In the early years of Khodorkovsky’s banking career he “built an offshore financial network” (446). Millions of dollars from Menatep could be found in safe havens in the Caribbean, Switzerland, Gibraltar, Isle of Man and other secret locations around the world. Khodorkovsky used Jurby Lake Ltd., “a well-known offshore tax haven” to handle Yukos’ exports and deposit earnings to other Khodorkovsky controlled companies and his partners (447). Eventually, he came up with an elaborate plan that would take all of Yukos offshore leaving Western investors and small shareholders dry (448).

Khodorkovsky’s next step in the scheme was “to issue millions of new shares in the subsidiaries” (448). This specifically stripped the value from Yuko’s extraction companies. After this, he sold all of the millions of new shares in the oil extraction subsidiaries to offshore companies, believed to be Khodorkovsky-affiliated. Khodorkovsky also decided to purchase the millions of additional shares “with veksels, or promissory notes, issued by the other Yukos extraction subsidiaries” (449). In turn, this created a paper chase with one company issuing millions of shares; selling them to offshore companies, and then collected promissory notes for the shares they just sold (449). Khodorkovsky was able to sell these shares with promissory notes because they were coming from *his* companies.

By the time 1998 rolled around, the State was paying more attentions to which of its Oligarchs were playing fairly. Dmitri Vasiliev, former chairman of the Russian Federal Securities Commission expressed concern that Yukos was trying to dilute minority shareholders. He received a written pledge from them stating that they would follow the rules but only a year later investor complaints began to stack up against Yukos (453).

In the spring of 1999, Khodorkovsky brazenly launched his plan to take control over the entire oil company. The Kremlin’s response was to have Vasiliev announce a “full-fledged investigation into whether Yukos had violated minority shareholders rights” (453). Just a month prior, three emergency shareholder meetings, one per oil extraction subsidiary, was held. One of the shareholder’s representatives for Yuganskneftegaz was not admitted into the meeting and learned that the shares were being frozen for his client, American businessman Kenneth Dart, due to a technicality. Seventy-seven million new shares were being issued inside; dramatically shrinking Dart’s holdings (449).

Dart and Khodorkovsky engaged in a long legal battle. Khodorkovsky had to shake off Dart and Western creditors simultaneously. “The three banks that had loaned Khodorkovsky’s Bank Menatep $236 million could, under terms of the deal, claim a total of about 30 percent of Yukos when Menatep defaulted on the loan” (451). This was a sizeable chunk of the company and could make Khodorkovsky vulnerable. The Western banks were aware that investing into an economically and politically weak country such as Russia was a big risk and they would have little leverage inside the weak courts of Russia. Khodorkovsky sent the “…Yukos-owned shares in the oil-extraction subsidiaries” and new diluted shares offshore. Thus, the banks were left with an empty shell (Hoffman, 452).

Chairmen Vasiliev was warned privately by a Yukos’ vice president to get out of Khodorkovsky’s way. The World Bank had lent Russia $89 million to help improve its capital markets. Some of this money was used by Vasiliev “…to pay for the commission’s press office and computers that allowed outsiders to read reports about its regulatory decision on the Internet” (454). Global public relations firm, Burson-Marsteller, was contracted to run the press office. “The goal of the World Bank program, which paid the bill for Burson-Marsteller’s work, was to improve ‘transparency’ and to provide more ‘complete and reliable’ information about companies in the stock market” (454). As Vasiliev strived to improve his credibility and image abroad, he soon discovered that Burson-Marsteller was playing both sides.

In 1999 Vasiliev discovered that Burson-Marsteller was representing Yukos at the same time the commission was investigating. The PR company claimed that they were building transparency but were defending Khodorkovsky’s abrasive measures to hide shares. Vasiliev needed the funds from the World Bank and couldn’t throw out his relationship with Burson-Marsteller. Mark D’Anastasio, managing director of the international development practice at Burson-Marsteller, even proposed to Vasiliev that he could be the peacemaker between Yukos and the Russian government. D’Anastasio admired Khodorkovsky and agreed that he was going too far (454,455). Vasiliev was virtually powerless. The capital markets were being weakened by the very firm that was hired to improve it.

Vasiliev expressed that Yukos “…was running into a brick wall” at a news conference on June 29, after a complaint from the trade association of stockbrokers got the Russian Trading Systems to halt the trading of Yukos and the oil extraction companies (455). The investigation was going nowhere. On August 18, the same vice president who warned Vasiliev to back off quietly filed a complaint against Vasiliev on the grounds of slander which was illegal under Russian law. The discouraged Vasiliev resigned in October laminating that “the system here doesn’t protect investors” (456).

Khodorkovsky was winning everywhere he went. Vasiliev resigned, he settled with Dart, he defeated creditors, and most importantly he was gaining more control of his oil company. Khodorkovsky’s bank had collapsed in the crash and he told top officials of West LB, parent bank of West Merchant which suffered losses from the Russian crash and lent Menatep $135 million, that it was not possible to pay back the loans due to the collapse. However, Yukos was still strong. Instead of the West LB pressuring him to pay back the loans, the bank sold off the assets for half of what was originally loaned to Khodorkovsky. After the lenders “threw in the towel” Khodorkovsky bought back 23.7 percent of the 30 percent of shares Yukos had pledged. Thus, Khodorkovsky got back most of his shares “…for less than half the cash he had originally borrowed” (456,457). By the end of 2000, Yukos amassed an estimated $2.8 billion in cash (457).

A politics shifted at the dawn of a new century, so did Khodorkovsky’s business practices. In 2002, Khodorkovsky became the first major owner of a Russian company “…to break with the climate of secrecy in which Russian capitalism was born in the 1990s, and this pioneering step forward was even more surprising because of Khodorkovsky’s own history of murky deals” (495). He revealed the ownership structure of Yukos and it was becoming evident that he was now leaning toward openness and Western business practices.

According to New York Times article, *Mikhail Khodorkovsky’s Plea for Russia*, Khodorkovsky “…brought in Western board members who understood the principles of good corporate governance.” This was unheard of in Russia but Khodorkovsky understood the importance of transparency in a market based economy. He also needed to create an image of what the Russian businessman looked like. The article goes on to say that Khodorkovsky used PricewaterhouseCoopers to create “…an accounting structure that allowed Yukos to report earning that met Western accounting standards, while satisfying Russian tax authorities, no mean feat.”

The article further describes how former chief financial officer of Yukos, American Bruce Misamore, explained that in October of 2003, when Khodorkovsky was arrested, “…he was in the process of selling a stake of the company to either Exxon Mobile or Chevron, both of which were eager to make an investment.” Khodorkovsky was also ready to list Yukos on the NYSE and was reported to be worth $15 billion at the time.

In Western media, Khodorkovsky is portrayed as a hero while Putin is the villain. His arrest, conviction, and treatment by the government have raised serious concerns about Russia’s due process of law. It is true that there has been a lot of corruption conducted by the Russian government in handling the questionable business practices of the Oligarchs. Russian businessman, journalists, lawyers, etc. who speak in opposition of the government may find their houses broken into and may even end up “disappearing” or found “mysteriously dead”. Given the fact that these Oligarchs formally had no clear laws to abide by and have now tried to implement Western business practices into their firms to legitimize them, it leads to the belief that Oligarchs like Khodorkovsky have only faced imprisonment because he was seen as a threat to Putin. However, I have reason to believe that the case is much more complicated than this. I am hampered by the fact that I cannot read Russian which has prevented me from being able to read opposition to the belief that Khodorkovsky is only in prison because of trumped up charges conducted by Putin.

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