



# HIDDEN COSTS OF PRIVATIZATION

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## SUMMARY

Georgia adopted the law regulating state property privatization in 1997. 34 amendments were made to the law in a period between the dates of its adoption in 1997 and its cancellation in 2010. Till now, 22 amendments have been made to the law adopted in 2010 (the Law on State Property). Quite different types of amendments were approved, but none of them provided for more transparency of the privatization process and creation of the possibility for public involvement in a decision making process. Most amendments were directed to increasing the number of facilities subject to privatization that is not surprising, taking into consideration the Georgian government's desire to increase state revenues as soon as possible. The legislative amendments do not represent an outcome of the state privatization policy built on public consensus. It is confirmed by a large number of amendments approved in a short period of time.

The issue of public access to information related to privatization process is still quite problematic. Green Alternative has witnessed a lot of cases, when the organization was refused to receive a privatization agreement, while the document is available on the public registry's website.

The laws regulating privatization issues do not envisage the possibility of public involvement in the process of making decisions on privatization of this or that facility.

When analyzing the cases, which Green Alternative has come across, one important circumstance is quite obvious and we think that this circumstance will create serious problems to both the Government and Georgian population in future, particularly to the communities affected by those privatized facilities, which have adverse effects on the environment and human health. Frequently, it is impossible (or it requires much time) to identify the owner of the privatized (large) facility – most of the new owners are registered in offshore zones. Probably, this problem is not considered so acute today, but as a result of any harm caused by operation of such facility, the problem becomes quite obvious. The problem is not less important in the context of protection of rights of those persons who are working at a privatized facility (and/or those who were dismissed after privatization).

As for the fulfillment of obligations envisaged by the privatization agreement and Georgian legislation by privatized enterprises, the public has no access (or limited access) to information about whether the owners of privatized enterprises fulfill the obligations and how they fulfill the obligations envisaged by relevant agreements and legislation. Several important trends can be highlighted here: if the agreement is confidential, as a rule, the state agencies do not reveal information about fulfillment of the agreement conditions (if any such information exists at all). However, there are some cases, when the agreement is open to the public, though the information about the state of its fulfillment is closed (or it is difficult to obtain such information). We have to deal with such situations in case of Madneuli and Quartzite. The situation is absolutely illogical in case of privatization of water supply and sewerage systems of Tbilisi, Mtskheta and Rustavi: the public has access to the presidential decree, which sets buyer's obligations (purchase conditions), but the purchase agreement (which also involves the conditions set by the presidential decree) as well as the information about the state of fulfillment of obligations is closed.

- ! The situation is unfavorable in the sphere of fulfillment of environmental obligations too. Besides the fact that new owners of enterprises are exempted from responsibility for any harm caused to the environment before privatization, there is no control over the compliance of enterprises' activities with environmental legislation.

### Recommendations

- ! It is an urgent task to adopt relevant legislative amendments to ensure relevant mechanisms for real transparency of privatization process and public involvement in a decision making process.
- ! It is important for the relevant state agencies to study the legality of privatization of large facilities.
- ! It is essential that the public has access to certain information, including names of new owners of privatized large facilities, obligations undertaken in frames of privatization agreements and state of fulfillment of these obligations.
- ! The Ministry of Environment and Natural Resources Protection of Georgia should raise the issue of cancellation of those agreements concluded in the sphere of environmental protection and utilization of natural resources, under which all the actions committed/carried out by RMG Gold, RMG Copper, Saknakshiri Ltd, a Georgian subsidiary of Polat Yol Yapı Sanayi ve Ticaret in this sphere were considered legal.
- ! It is vital for the Georgian Parliament to intensify control over the fulfillment of legislative requirements by the state agencies in the sphere of public information confidentiality.
- ! It is also important to study the legality of confidentiality of those privatization agreements, which are made confidential by these very agreements.
- ! It is very important to implement the programs aimed at building capacities of controlling authorities. These programs should involve the development of human resources and providing them with technical resources as well as empowering the controlling authorities.

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# INTRODUCTION

The process of state property privatization was launched in Georgia in 1992. According to the official data, over 15 000 enterprises were privatized till 2003. The process was passing in extremely grave and unstable social, economic and political situation that created favorable conditions for corrupt deals and money laundering in both local and foreign currency. It should be noted that non-transparent privatization of the state property was one of the major accusations leveled by the authorities, which came to power as a result of the Rose Revolution, against the previous government. Respectively, ensuring transparent and fair privatization process was one of the promises, which the Georgian population received along with launching a new "aggressive" wave of privatization in 2004.

Thus, in 2004, after the Rose Revolution, a new wave of state property privatization was launched in the country, which, according to the government of reformers, should have lasted for 18 months and unlike previous stages, should have been "utterly objective and transparent." However, like many other government promises, the reality proved absolutely opposite – the renewed privatization process has not been completed even 10 years after its commencement; probably, the quality of transparency has slightly increased, but it is still unsatisfactory that has largely contributed to the inefficiency and drag-out of the process.

The state property privatization, which is currently underway in Georgia and which many foreign countries have passed through, is a result of globalization process ongoing in the world. According to the World Resources Institute, state property privatization brings both financial and practical benefits. The goal of privatization is to promote investing of private capital in the facilities with frequently grave financial and physical condition. As a rule, just the managed process brings better and enhanced services, increased capacities and financial efficiency. Unfortunately, the experience of many countries in privatization is quite different from this theory and it frequently becomes the reason for mass discontent and disobedience.

In addition, it is acknowledged that privatization brings both wealth and increased environmental and social expenses in the countries with low level of democracy and weak environmental governance system. Decisions on state property privatization are rarely made through consultations with the public, or at least through taking into consideration the attitude/needs of local population; frequently, such decisions trigger grave social consequences, including loss of jobs and growth of prices.

Since 2005, Green Alternative has been watching closely over the privatization of several large facilities as well as the process of "improvement" of legislation to ensure transparency in this sphere. Unfortunately, our experience clearly shows that an entire cycle of decision-making on privatization of an enterprise – from announcing a decision on planned privatization of a facility to selection of particular buyers and imposing certain obligations on them - is closed to the public. The grave environmental situation in several large privatized enterprises and frequent strikes of workers clearly demonstrate the consequences of the above mentioned.

## LAW ON STATE PROPERTY PRIVATIZATION

Georgia adopted the law regulating state property privatization in 1997. 34 amendments were made to the law in a period between the dates of its adoption in 1997 and its cancellation in 2010. Till now, 22 amendments have been made to the Law on the State Property, which was adopted in 2010 and which cancelled the Law on State Property Privatization adopted in 1997. Quite different types of amendments were approved, but none of them provided for more transparency of the privatization process and creation of the possibility for public involvement in the decision making process.

Most of those 34 amendments (27), which were made to the 1997 Law on State Property Privatization, were implemented after the Rose Revolution. The first amendment<sup>1</sup>, which was made to the law in 2004, after the new authorities came to power, did not seem to be especially important and was only meant "to revise" the objective of direct sale of the state property. Before the amendment, according to the law, the purpose of direct sale of state property was "to attract investments based on the business plan in view of the specifics of the property on sale." After the amendment, "the purpose of direct sale is to give the right of ownership on property to that buyer, who will fully and honestly fulfill conditions set for privatization of state property through direct sale." Thus, it means that if before 2004 it was possible to select a new owner based on the proposed business plan, the new authorities focused on honesty of a buyer – however, it was unclear how the Georgian President<sup>2</sup>, upon making a decision on direct sale, was defining in advance, whether a potential buyer would fulfill conditions fully and honestly. According to the 2010 law, decisions on direct sale after the 2013 presidential elections are made by the Government of Georgia. The criteria for making decisions remained unchanged.

One of the important amendments made to the law in 2005 is related to the price of the property, which was put up on sale, but was not sold. Before the amendment, according to the law, if the state property was not privatized through an auction twice, it was sold at a half price (50%) at the third auction. This rule had frequently become an issue of disputes with opponents arguing that this rule served to sell state property at a miserable price and created favorable conditions for corruptive deals in the process of privatization. The new amendment aimed to eliminate this practice. According to the amendment made in 2005<sup>3</sup>, the initial cost of property may (but not obligatory) be reduced by 50% even after the very first unsuccessful attempt to sell it, if the property is not sold at a reduced price, "the price can be reduced further" (this time, no limit is set). This norm has been included in the 2010 Law on State Property in its unchanged form and respectively, it is still in force.

However, it seems that because of increased altruist aspirations of the Georgian population and frequent cases of "voluntary transfer" of property to the state, it became necessary to make amendments to the definition of "state property"<sup>4</sup>. So, the following was added to the definition of the law: "Residential houses and apartments voluntarily transferred to the state ownership; ownerless property transferred to the state ownership pursuant to the Civil Code of Georgia (residential houses and apartments)". Luckily, this definition is not included in the new law on state property.

Another amendment to the law in 2005<sup>5</sup> made frontier zone eligible for privatization. Before the amendment, frontier zone was included in the list of state property and was not subject to privatization. This norm is still in force.

Another important amendment to the law was made in 2006<sup>6</sup>. On the basis of this amendment, in agreement with the Ministry of Culture, Monument Protection and Sport and pursuant to the conditions defined by the ministry, monuments of historical-cultural and artistic values and art buildings became eligible for privatization. Before the amendment, the following state property was not eligible for privatization: religious and hieratical buildings, historic and cultural state archives, state fund of film, photo and phono materials, archives and funds of the

<sup>1</sup> The Law of Georgia on Making Amendments to the Law of Georgia on State Property Privatization, August 13, 2004, No 371-rs

<sup>2</sup> According to the law, decisions on direct sale of state property were made and relevant conditions were set by the President of Georgia.

<sup>3</sup> The Law of Georgia on Making Amendments to the Law of Georgia on State Property Privatization, March 22, 2005, No 1133

<sup>4</sup> The Law of Georgia on Making Amendments to the Law of Georgia on State Property Privatization, June 30, 2005, No 1849

<sup>5</sup> The Law of Georgia on Making Amendments to the Law of Georgia on State Property Privatization, July 8, 2005, No 1897

<sup>6</sup> The Law of Georgia on Making Amendments to the Law of Georgia on State Property Privatization, December 8, 2006, No 3937

Georgian ministries, scientific-research institutions, museum collections, funds, house museums of national value. The initiators gave the following arguments to justify the necessity of making legislative amendment: "Since the State does not have relevant budgetary resources to look after all monuments on the territory of Georgia and the owner (who is not a proprietor) does not have enough interest and relevant funds to look after and protect the monument owned by him/her, actually a lot of monuments in Georgia face the risk of being damaged or in most cases, being totally ruined<sup>7</sup>."

Subsequently<sup>8</sup>, based on the agreement with the Ministry of Culture, Monument Protection and Sport and pursuant to the conditions defined by the ministry, land plots located in the archeological protection zone also became subject to privatization. Moreover, the world heritage sites were added to the list of property not subject to privatization.

According to the current formulation of the Law on State Property, the law does not apply to transfer of printed and electronic editions issued with the support of the Ministry of Culture and Monument Protection to individuals and legal entities of private law with the purpose of popularization of Georgian culture<sup>9</sup>. Furthermore, according to the current law, historical-cultural and art facilities, cultural and artistic buildings, as well as land plots, where the above mentioned facilities are placed, can be privatized on the basis of relevant conditions through the agreement with the Ministry of Culture and Monument Protection.

Against the background of almost daily promises to settle employment problems and eradicate poverty, on May 11, 2007 another amendment was approved to the Law on State Property Privatization, as a result of which two major requirements (in this respect) were abolished. In particular, before making the amendment, by the moment the enterprise was formed into the joint stock company, almost 10% of the total authorized capital (but no more than hundred as much as minimum salary in Georgia) was granted to its workforce. The mentioned benefit was given to workers for whom the enterprise was the main place of work; for people, who were allowed by the Georgian legislation to return to this enterprise, pensioners, who retired after working for the company for no less than five years and people, who were dismissed from this enterprise a year earlier and were registered as unemployed. Moreover, the old law considered the obligation of concluding contracts with workforce of the privatized enterprise within three months after registering the right on ownership. The contracts included obligations related to labor organization, reimbursement and protection. All the above mentioned requirements were cancelled due to the amendments made on May 11, 2007.

As a result of legislative amendment approved on July 11, 2007, the list of state property subject to privatization has further extended. Thus, today the following types of property are subject to privatization:

- Special economic zone;
- Mobilization reserve, state reserve, reserve of precious metals;
- Railway of state importance;
- State mail communication, TV and Radio Broadcasting, international-intercity telephone communications, governmental communication means;
- State cemeteries;
- United state system of water supply and sewerage;
- State medical institutions of vital importance;
- Administrative buildings of state agencies.

This new amendment to the law has obliged the Government of Georgia to approve "the list of property of special importance", i.e. a list of that property, which cannot become subject to privatization. However, neither the law, nor any other regulation defined when and how and based on which criteria the property of special importance were selected. Respectively, almost a year after making this legislative amendment, due to the lack of clear criteria and vagueness of legislative requirement, the Government of Georgia issues a regulation on approving the list of

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<sup>7</sup> Explanatory note of the bill.

<sup>8</sup> The Law of Georgia on Making Amendments to the Law of Georgia on State Property Privatization, May 8, 2007, No 4716

<sup>9</sup> 5.06.2012. N6377

property of special importance<sup>10</sup>. It included five facilities:

- Senaki airdrome runway;
- Marneuli airdrome runway;
- New (military) port in Poti (dock, hydro-technical buildings, light signals, defined water areas);
- Lighthouse, light signals and defined water areas of Poti marine port;
- Lighthouse, light signals and defined water areas of Batumi marine port.

It should also be noted that current norms of the law come into conflict with the constitution of Georgia. For instance, article 4 of this law (both abolished and current ones), where property not subject to privatization is enlisted, does not include "frontier zone" anymore; it means that now frontier zone is eligible for privatization. On the other hand, according to article 3 of the Georgian constitution, boundary regime and defense of the state frontiers shall fall within the exclusive competence of higher state bodies of Georgia. Also according to the constitution, protection of exclusive economic zone, communication, airports of state importance, railway and motor roads of state importance shall also fall within the exclusive competence of higher state bodies of Georgia. Pursuant to the law, all of the enlisted objects can be privatized.

New amendment made on July 11, 2007 annulled "the remaining" requirements in the law related to social guarantees and privileges for the workers of privatized enterprises. Before the amendment, for the purpose of defending workers' interests, after submitting an application on privatization and obtaining the ownership right by a buyer, it was prohibited to change a manning table and reduce or increase the staff without agreement with the Ministry of State Property Management; it was also envisaged to provide one-time financial assistance to the workers dismissed on initiative of the new owner. These requirements were also cancelled as a result of the July 11, 2007 amendment.

As a result of the same legislative amendment, competition and leasing-redemption forms of state property privatization were cancelled. Inefficiency of these forms became the ground for their cancellation, as claimed by the initiators<sup>11</sup>. Under conditions of economic crisis, lots of arguments can be provided in favor of leasing-redemption, but when efficiency is measured in a short-term perspective (which, as a rule, is defined by the election term), this form of privatization will turn to be ineffective.

As for the form of privatization competition, it was substituted by direct sale rule, which is based on competitive selection, i.e. kind of mixture of competition and direct sale form.

The 2009 amendment to the law<sup>12</sup> is not much compatible with the above-mentioned understanding of legislators on "economic efficiency." In accordance with this amendment, when buying the property of state or local self-government unit through direct sale procedure, the buyer has to pay the cost of the property within the period set by the President. This term shall not exceed one year.

At the same time, the law makes one exception, if privatization is important for avoiding possible damage to the state/self-government unit or for avoiding the current/arbitrage case processing and/or termination of the case, Georgian President has the right to set five years for the buyer to pay the property cost.

Before adoption of the new law, the last important amendment<sup>13</sup> released buyers of state property from penalties/sanctions charged before April 1, 2010 for not fulfilling the obligation to periodically report to the Ministry of Economy and Sustainable Development of Georgia about meeting the privatization agreement conditions and/or obligation of the property insurance. Moreover, buyers of the state property were given the right to apply to the Ministry of Economy and Sustainable Development with request to change/review conditions of the agreement.

<sup>10</sup> Decree No 93 of the Government of Georgia dated April 8, 2008

<sup>11</sup> Explanatory note of the bill.

<sup>12</sup> The Law of Georgia on Making Amendments to the Law of Georgia on State Property Privatization, November 3, 2009, No 1932

<sup>13</sup> The Law of Georgia on Making Amendments and Additions to the Law of Georgia on Privatization of State Property and Property of Local Self-Government Units and Granting the Right of Use," March 26, 2010, No 2878

## **LAW ON STATE PROPERTY PRIVATIZATION**

Pursuant to the new law adopted in 2010, it was allowed to privatize the forests of former collective farms and Soviet farms existing within the territorial borders of settlements. The list of the state property not subject to privatization was further extended by the following:

- Recreation areas defined by the Government of Georgia and/or specific construction regulation zones (however, privatization is possible by the government's decision);
- Motor roads (in case of absence of alternative roads);
- The following state-owned agricultural lands:
  - Pastures, except of those leased before July 30, 2005 as well as those, which belong to the private property of physical and/or legal entities and/or state-owned buildings by the act issued by the relevant state or local self-government (government) body;
  - First belt of the sanitary protection zone (strict regime zone); however, it can be allowed only with observance of sanitary protection norms;
  - Land of the protected areas, except of protected landscape and multiple-use lands;
  - Agricultural lands used by budgetary agencies and legal entities of public law by usufruct;
  - Stock routes; lands designed for historical, cultural, natural and religious monuments; land plots adjacent to Georgian rivers, where the construction of new renewable energy sources is planned - such lands will be eligible for privatization only in case of implementation of important projects; relevant decisions in this respect are made by the Government of Georgia upon the nomination of the property manager.

The Law on State Property adopted on July 21, 2010 is much more complex and not only it regulates the issues related to the Georgian state property privatization, but it also settles the relations related to the management, disposal and transfer of state property into ownership. However, the law does not involve any mechanisms and procedures for public participation in the decision making process and transparency of the entire process.

## GENERAL INFORMATION ON PRIVATIZATION

The National Agency for State Property Management is an official source of information about the state property privatization ongoing in Georgia. However, the website ([www.privatization.ge](http://www.privatization.ge)) of the agency, which has pledged to be a guarantor of transparency of privatization process and a comprehensive source of information, proved useless both in terms of searching information on the process of privatization of various enterprises and obtaining information on the results of state property privatization, as a whole. Moreover, as Green Alternative found out, the agency has no information either about the number of privatized enterprises per year or about the total number of privatized enterprises. Respectively, the agency has no information about how many enterprises have been privatized by using separate forms of privatization.

At the request of Green Alternative to provide information about number of enterprises privatized by using separate forms of privatization, the National Agency for State Property Management responded<sup>14</sup>:

Let us inform you in response to your letter (to the National Agency for State Property Management, registration number 7378/09 dated February 20, 2014) that since there had been no uniform information database on privatized enterprises with the state share in the capital, we send the information at our disposal, which is not comprehensive. In particular, since 2010, 96 enterprises have been privatized with 3 privatized in 2010; 41 – in 2011; 46 – 2012; 5 – in 2013 and 1 – in 2014.

Respectfully

Irakli Shengelia

A person authorized to ensure the availability of public information  
of the National Agency for State Property Management

<sup>14</sup> Letter No 3/7537 dated February 28, 2014 sent by the person authorized to ensure the availability of public information of the National Agency for State Property Management.

### WHO ARE THE OWNERS OF PRIVATIZED ENTERPRISES?

Frequently, it is impossible to obtain information about the owners of large privatized enterprises. If an enterprise is registered as a joint stock company, this information is closed, because Georgian legislation does not provide for the publicity of information about the owners of shares. But if an enterprise is registered as a limited liability company (LLC), as a rule, its shares are owned by the companies registered in offshore zones. It is practically impossible to obtain information about real owners. For example:

- Tbilisi, Rustavi and Mtskheta water supply and sewerage company 'Georgian Water and Power' Ltd is owned by the company Georgian Global Utilities registered in the British Virgin Islands.
- The company Energo-Pro Georgia, electricity generation (15 small and medium hydro power plants and Gardabani gas turbine electricity station ) and distribution (covers 70% of Georgian territory) company – according to the information posted on the company's website, the company registered in Georgia is a subsidiary of Czech company Energo-Pro AS. However, in Georgia the company is registered as a joint stock company, while the information about its shareholders is unknown.
- Telasi, electricity distribution company of Tbilisi, is registered as a joint stock company. An extract from the public registry provides no information about the company's shares; however, according to the information posted on the company's website<sup>15</sup>, 75.108% of the company's shares are owned by a subsidiary of JSC RAO EES registered in Amsterdam, Silk Road Holdings B.V. (information about its founder is classified); 24.529% of shares are owned by JSC Partnership Fund– presently State Investment Fund; and 0.363% of shares are owned by unknown shareholders.
- Since 2006, the largest industrial complex of Georgia – Zestaponi Ferro-Alloy Plant, Chiatura manganese processing plant and Vartsikhe HPP Cascade – has been owned by GM Georgian Manganese Holding Limited, the company registered in Cyprus offshore zone; since 2013 – by Georgia American Alloys, also registered in offshore zone of Luxemburg.
- Since 2005, one of the largest industrial complexes of Georgia – gold-copper-polymetal extraction and processing company has been owned by Stanton Equities Corporation (later GeoProMining), the company registered in the British Virgin Islands; since 2012 – by Rich Metals Group, also registered in offshore zone.
- After the bankruptcy of JSC Tkibulnakhshiri, the Tkibuli coal mines are owned by Georgian Industrial Group Holding; this latter is owned by Chemexim International, the company registered in Marshall Islands. The same company owns the Kutaisi Auto Mechanical Plant opened in 1945, a number of hydro power plants, Gardabani thermal power plant, Tkibuli thermal power plant, etc. The Georgian Industrial Group manages a 25% share of Heidelberg Cement Georgia.
- The ownership of the Rustavi Metallurgical Plant is disputable between the two companies – JSC Georgian Steel and Rustavi Steel LLC; this latter is owned by the company registered in Amsterdam.
- According to the information posted on the website of Batumi oil terminal, "in February, 2008, JSC KazTransOil, a subsidiary of the Kazakh state company KazMunaiGaz,, became the owner of the Batumi Oil Terminal and obtained an exclusive right to manage the Batumi seaport." According to the public registry's extract, Batumi Oil Terminal LLC is owned by the company Batumi Terminals registered in Cyprus.
- Ksani Glass Container Factory is owned by JSC Mina. According to the information posted on the company's website, "since 2003, 99.98% of the company's shares have been owned by a group of companies Anadolu Cam Sanayii A.Ş." The names of other shareholders are unknown.
- JSC Sakkabeli (Sakcable) – according to the company's website, it is the leading manufacturer of cable products in Georgia. The company was established in 1958 to advance the country's industrialization ambitions through the manufacture and distribution of copper and aluminum cable products. Since 2006 the company has been managed by the company Sket. Information about shareholders is unknown.

<sup>15</sup> <http://www.telasi.ge/ge/shareholders/structure>

- Zahesi 2007 Ltd is the owner of Avchala hydro power plant "Zahesi". According to the public registry's information, 10% of Zahesi 2007 Ltd is owned by Zaza Gugava; 37.5% - by Rezo Kurasbediani (citizen of Ukraine) and 52.5% - by the company International Terminal Service registered in the Panama offshore zone.
- JSC Elmaivalmshenebeli– the public registry's extract provides no information about shareholders; however, the company's statute (in Georgian, Russian and English languages) is approved by Ramon H.M. Zuketto, the director of Allied Corporate Management BV, the management company of LOKO TRANS HOLDING BV registered in Amsterdam. Information about other shareholders is unknown.
- The Ocean Crewing Company LLC, which was separated from Georgian Navigation LLC, is owned by Georgian Tankers Limited, the company registered in Marshall Islands.
- Information about the shareholders of Electric Car Repair Works is unknown.
- The Tbilisi jewelry factory Zarapkhana Ltd is owned by Zarapkhana Development Ltd, which in its turn is owned by FLORINE LIMITED, the company registered in the British Virgin Islands.

Offshore zone is "a country or a part of its territory, which offers preferential tax treatment and/or where the requirements towards identification of persons participating in a deal do not meet international standards and which are recognized as such by international organizations<sup>16</sup>".

Registration of a company in offshore zone brings numerous "benefits" to its owner and respectively, there are a lot of companies ready to assist interested persons to undergo registration in the so called "tax heaven". While providing such services, clients are given explanations about general advantages of these services, particularly:

- Anonymity
- Offshore Asset Protection
- Protection from Legal Action
- Reduction in Taxes
- Ease of set up / operation
- Complete Financial Privacy

Besides the possibility of tax evasion, the company registered in offshore zone is the best means for legalization of unreported assets and/or property, i.e. for the so called "money laundering". Confidentiality of the owner of a company/bank account enables to conceal a real source of income and a real purpose of the deal.

Leaked information about real owners of the companies registered in offshore zones has caused international scandals for multiple times. Georgia was among participants of the world scandal in one of the latest cases of information leakage. In April 2013 the International Consortium of Investigative Journalists released a new report<sup>17</sup> concerning the hidden taxes in offshore zones. Secret records obtained by the International Consortium of Investigative Journalists revealed tens of thousands of people in more than 170 countries and territories linked to offshore companies and trusts, through which leaders of various countries, politicians, artists and other influential persons managed to conceal their incomes<sup>18</sup>. According to the same report, then Prime Minister Bidzina Ivanishvili was the director of the company Bosherton Overseas Corp. registered in the British Virgin Islands in 2006. The Government of Georgia reacted on the information provided in the report in writing. The explanation noted: "The Georgian Government is aware about some allegations that there were business links between Bidzina Ivanishvili and one of the companies registered in the British Virgin Islands.

<sup>16</sup> The Law of Georgia on Promoting the Eradication of Illicit Income Legalization, Article 2; the current formulation of the law does not contain this definition anymore as a result of the amendment approved on March 27, 2007, No4518.

<sup>17</sup> SECRECY FOR SALE: INSIDE THE GLOBAL OFFSHORE MONEY MAZE, <http://www.icij.org/offshore>

<sup>18</sup> <http://www.icij.org/offshore/who-uses-offshore-world>

## WHO ARE THE OWNERS OF PRIVATIZED ENTERPRISES?

According to Georgian legislation, the Georgian Prime Minister has to declare about all assets owned by him. Bidzina Ivanishvili has said for multiple times that in order to ensure transparency he will observe firmly all the requirements and make the information related to his own assets public. For the reporting period of 2011-12, Prime Minister Ivanishvili had no interest in the company and therefore there was no obligation to report it in his financial declaration. As far as his current assets are concerned, this information is reported in his declaration with full observance of law<sup>19</sup>.

Unlike the former Prime Minister, the leaked information about the offshore registered company triggered serious consequences for ex-Defense Minister of Georgia (2006-2008) Davit Kezerashvili. Georgian media reported citing the report by Deloitte Audit Company that after Kezerashvili moved to business sector, total incomes of the holding company founded by him in offshore zone amounted to hundreds of millions of USD in 2009-2012. The Georgian chief prosecutor's office immediately reacted on this information and launched a probe into the fact of alleged malfeasance and illicit income legalization<sup>20</sup>.

The fact of offshore registration of privatized enterprises has frequently dragged out court disputes. Green Alternative has experienced such cases for multiple times.

Consideration of Green Alternative's lawsuit<sup>21</sup> filed at the Tbilisi City Court, in which the organization demanded access to the privatization contract between the Government of Georgia, Ministry of Economy and Sustainable Development, Tbilisi Government and Multiplex Energy Limited Ltd on deed of purchase of 100% of shares in Rustavtskalkanali Ltd, Mtskhetatskalkanali Ltd, Saktskalkanali Ltd and Tbilisi Water Ltd, was dragged out significantly. The court's preliminary hearing was postponed for seven times during ten months. The reason for postponement was the failure to involve the third party to the dispute – Multiplex Energy Limited registered in offshore zone in the process. As it turned out, the Ministry of Economy and Sustainable Development had no information about the location of the company or the whereabouts of any of its representatives. The court failed to obtain relevant information from the public registry. Green Alternative managed to find the company's registration address and handed it over to the court. Finally, based on the submitted information the court managed to involve the third party after three postponed hearings and managed to proceed further into the trial on the merits only a year after filing the lawsuit. It should be noted that during a year Georgian Water and Power Company (formerly Tbilisi Tskali) was claiming that it had no contact information of the owner.

After unsuccessful attempts to obtain the privatization contract on Vartsikhe HPP Cascade from the Ministry of Economy and Sustainable Development, Green Alternative applied to the Tbilisi City Court and demanded it to study the legality of contract confidentiality and ensure the publicity of the document<sup>22</sup>. The court found Green Alternative's lawsuit admissible and decided to involve the new owner of the property - G.M. Georgian Manganese Holding Limited - as the third party. The court sent a judgment to the company to the address provided by the Ministry of Economy and Sustainable Development (Zestaponi, 9, Sakarkhno Str.). As it turned out, the office of Georgian Manganese Ltd was located at the mentioned address; the management of the enterprise refused to receive the judgment citing that the enterprise was only managing Vartsikhe 2005 Ltd and did not represent the party to the dispute. It should be noted that before launching the court dispute, the Ministry of Economy and Sustainable Development was claiming that it had sent a written notification to G.M. Georgian Manganese Holding Limited for the latter to decide whether it was possible to disclose the contract to Green Alternative.

Finally, the judgment was sent to the address indicated in the contract of G.M. Georgian Manganese Holding Limited in Cyprus (it should be noted that this address was revealed only after the court demanded it from the Ministry of Economy and Sustainable Development with the purpose of studying it). G.M. Georgian Manganese Holding Limited did not appeal against its involvement as the third party. Neither did it file a counterclaim, nor did it deem necessary for its representative to attend the trial.

<sup>19</sup> Bidzina Ivanishvili's Connection with Offshore Company", Radio Liberty, 05.04.2013

<sup>20</sup> Statement by the Chief Prosecutor's Office in regard with Davit Kezerashvili

<sup>21</sup> Green Alternative is demanding a copy of the contract on privatization of Tbilisi, Mtskheta and Rustavi water supply systems, May 22, 2009 [http://greenalt.org/ka/disputes\\_complaints/](http://greenalt.org/ka/disputes_complaints/)

<sup>22</sup> Green Alternative is demanding a copy of the contract on privatization of Vartsikhe HPP Cascade, April 13, 2007 [http://greenalt.org/ka/disputes\\_complaints/](http://greenalt.org/ka/disputes_complaints/)

The third case is also related to Georgian Manganese Holding Limited; this time dispute hearing was underway at the Court of Appeals. The Tbilisi Court of Appeals, pursuant to legal requirements, sent a copy of complaint to the Ministry of Economy and Green Alternative's counterclaim to the parties. As it turned out at the court's preliminary hearing, the court sent materials to the same address of G.M. Georgian Manganese Holding Limited in Zestaponi. It should be noted that it was the Ministry of Economy and Sustainable Development again to have sent the address to the court. In June 2008 Green Alternative received a copy of the letter sent by A. Zilberman, the director of Georgian Manganese Ltd, to the Tbilisi Court of Appeals (another copy of the letter was also sent to Deputy Minister of Economy, Vakhtang Lezhava). It should also be noted that on January 5, 2007 Minister of Economy and Sustainable Development Giorgi Arveladze handed over the document on ownership of Vartsikhe 2005 Ltd to A. Zilberman, as to the director of G.M. Georgian Manganese Holding Limited. In response, A. Zilberman, as the director of Georgian Manganese LLC, wrote: "We reiterate that the dispute is about the fact of confidentiality of the contract on direct sale between the Ministry of Economy and the company G.M. Georgian Manganese Holding Limited (which we have not seen at all) and this latter is involved as the third party and its legal address is: Cyrus, Nicosia, 10, Egypt Str.; the company is registered in Cyprus. As for us, we represent Georgian Manganese LLC; our legal address is Zestaponi, 9, Sakarkhno Str., and we are registered in Georgia. Presently, neither we have any desire and right, nor we are obliged to represent any third party at court... Please, send relevant materials related to the case to a real addressee that, in our opinion, should not be difficult for the court."

The court decided that it was not obliged to send a notification to the company in Cyprus and considered the case without the third party.

As it seems, the Government of Georgia sees nothing alarming in a large number of companies registered in offshore zones and/or absence of information about real owners of particular companies. This is confirmed by the fact that the Government trusted the fate of an unprecedented project - construction of Khudoni hydro power plant - to Trans Electrica Limited, the company registered in the British Virgin Islands in 2008.

The company Trans Electrica Limited underwent registration in the British Virgin Islands on January 25, 2010 and it is a successor of Continental Energy Limited founded on May 2, 2008. Before November 4, 2011 it was known that all the shares of the company were owned by Trans Electrica Limited. During a consultation meeting held in the village of Khaishi on November 4 the Georgian director of the company, Paata Tsereteli, said that the shares of Trans Electrica Limited were owned by the companies, whom he refrained to name, as he was not authorized to do it. Later, the information about three shareholders (World Energy Limited; SGGS INFRASTRUCTURE LIMITED; Olney Assets s.a) was posted on the website of Trans Electrica Limited. As it appeared, two out of three companies are registered in offshore zones. No websites of any of these companies are available in the Internet. Furthermore, the companies are not mentioned in any news or any types of documents.

- World Energy Limited – according to the British registry, the company with this name really underwent registration on May 8, 2000. However, according to the same registry, the company ceased functioning on February 11, 2003. No information can be searched about the company with similar name; thus, we can conclude that one of the shareholders of Trans Electrica Limited is the company liquidated in 2003<sup>23</sup>.
- SGGS INFRASTRUCTURE LIMITED – this company, unlike the first one, still exists, though it was founded on July 29, 2011 in the Jersey offshore zone<sup>24</sup>.
- Olney Assets s.a. – the company was registered in Panama offshore zone on September 24, 2010<sup>25</sup>.

Excess trust by the state agencies towards some companies registered in offshore zones, the facts of making unjustified exceptions to legal requirements and/or loyal attitude towards them arouses doubts about the possibility of unofficial influence of anonymous owners of these companies and existence of corrupt deals.

<sup>23</sup> <http://www.cdrex.com/world-energy-limited-7536425.html>

<sup>24</sup> <https://www.jerseyfsc.org/registry/documentsearch/NameDetail.aspx?id=281565>

<sup>25</sup> <https://opencorporates.com/companies/pa/713419>

# PRIVATIZATION CONTRACTS

The availability of privatization contracts is one of the major factors in terms of public access to the information related to the process of privatization of large industrial enterprises. Green Alternative has certain experience in this respect. There were some cases when state structures disclosed privatization-related documentation; for instance, upon the request of Green Alternative's request, ministry of economy sent a copy of privatization agreement conducted in 2007 between the ministry and JSC Energy-Pro on procurement of assets of 8 Energy facilities. At the same time, Green Alternative failed to get privatization contracts of JSC HydroEnergoMontazh, JSC Sakhydroenergomsheni, JSC Tbilisi Jewelry Plant, LTD Batnavtobimpex, LTD Batumi Oil terminal, LTD Batumi Marine-trade harbour, JSC Tkibulnakhshiri, JSC Rustavi Metalurgy Mill, Rustavi Cement Factory, Kaspitsemi and other enterprises.

In case of refusal to provide a copy of the privatization contract, the organization was receiving the following notification: "The contract is a commercial secret and "buyer's" written consent is needed to disclose it; in this connection, the ministry has sent a written notification to JSC/Ltd..."; however, in most cases Green Alternative failed to obtain a copy of the letter sent to the buyer and/or the latter's response to this letter.

The practice of classifying privatization contracts is also extremely interesting. As it appeared, privatization contracts are considered buyer's commercial secret pursuant to one of the articles of the contract itself. For instance, the contract on privatization of Tbilisi, Mtskheta and Rustavi water supply systems concluded with Multiplex Energy Limited contains an article (14.1) according to which "none of the parties shall make a statement on procurement of "a share" and any other related issue without prior written consent of other parties." According to article 12.4 of the agreement concluded on December, 2009 on making amendment to the contract, "the information, proposals and agreements provided in this document shall be confidential and, respectively, without prior written consent of the other side, the sides shall not release any information, related to this agreement, to another physical person."

The situation is identical with respect to the contract on transfer of 100% of state-owned shares of Vartsikhe 2005 LLC to G.M. Georgian Manganese Holding Limited.

The Ministry of Economy and Sustainable Development claims that the full text of the contract is classified under one of the articles of the contract. The ministry explains it by the fact that this article represents a decision of administrative body on classification of information.

The procedure of classification of information is set by General Administrative Code of Georgia<sup>26</sup>, according to which when submitting particular information, a person shall indicate whether it constitutes commercial secret. A public agency shall within 10 days decide to classify public information (categorize or not the information as commercial secret).

According to General Administrative Code of Georgia<sup>27</sup>, commercial secret means any information concerning the plan, formula, process, or means that constitute a commercial value, or any other information that is used to produce, prepare, or reproduce goods, or provide service, and/or which represents an innovation or a significant technical accomplishment, or any other information, disclosure of which could reasonably be expected to cause competitive harm to a person. It can hardly be imagined that the purchase contract may contain any information with such value or else the entire text may have commercial value. Furthermore, privatization contracts contain a number of data, classification of which is inadmissible or simply it is senseless - for instance, procurement conditions, which are set in the decision on privatization of this or that facility (in relevant legal acts) and which are public.

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<sup>26</sup> Paragraph 3 of article 27<sup>2</sup> of General Administrative Code of Georgia

<sup>27</sup> Paragraph 1 of article 27<sup>2</sup> of General Administrative Code of Georgia

According to article 30 of General Administrative Code of Georgia, “the decision designating public information to be classified may be rendered if law provides express requirement to protect such information from disclosure, establishes concrete criteria for such protection, and provides exhaustive list of classified information.” With respect to the contracts on privatization of large industrial enterprises, not only the law does not set direct requirement against its disclosure, but on the contrary, it directly establishes that such contract should be public. In particular, according to the Law of Georgia on Environmental Protection<sup>28</sup> and the Aarhus Convention<sup>29</sup>, the Georgian government is obliged to provide all necessary information to the public and ensure public participation in decision-making (including development of contracts) on privatization of similar facilities.

Another situation is important – clauses of privatization agreements, providing for classification of full texts of documents, as a rule, ignore the requirement of Georgian legislation on openness of the information. However, administrative agencies, as well as the courts (for an unknown reason) are guided only by regulations providing for classifying the information; they ascribe to commercial secret any information about privatized enterprise and do not meet the requirement of separating non-commercial information.

It should also be noted with respect to classification of privatization contracts that along with intensification of electronic service (website) of the Registry of Entrepreneur and Non-Entrepreneur Legal Entities, most privatization contracts are now available on the registry’s website. It should be noted that submission of contracts is compulsory for registration of property right. Thus, the registry’s website offers a number of privatization contracts, which Green Alternative had been unsuccessfully trying to obtain through long court disputes. In this situation, the fact of classification of contracts by the Ministry of Economy and Sustainable Development is absolutely illogical. However, the ministry does not issue contracts citing their commercial value for a buyer.

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<sup>28</sup> Paragraph “f” of article 6 of the Law of Georgia on Environmental Protection: “A citizen shall have the right to participate in the process of discussing and making important decisions in the sphere of environmental protection.

<sup>29</sup> Article 7 of the Convention on Access to Information, Public Participation in Decision-Making and Access to Justice in Environmental Matter (Aarhus Convention): “Each Party shall make appropriate practical and/or other provisions for the public to participate during the preparation of plans and programmes relating to the environment, within a transparent and fair framework, having provided the necessary information to the public.”

### REPORTS ON FULFILLMENT OF PRIVATIZATION CONDITIONS

Like in case of privatization contracts, Green Alternative's experience in obtaining the reports on fulfillment of conditions set by the contracts on privatization of large industrial enterprises also causes concern.

For instance, Green Alternative was trying during two years to obtain the report on fulfillment of conditions set by the contract on privatization of Rustavi, Mtskheta and Tbilisi water supply and sewerage systems.

The Rustavi, Mtskheta and Tbilisi water supply and sewerage systems were transferred to Multiplex Energy Limited on a number of conditions, which are directly linked with the state of the environment and human health. Respectively, the document reflecting the fulfillment of conditions, according to the Aarhus Convention, is environmental information<sup>30</sup> and should be available<sup>31</sup> to the public. Also, this is information about the measures, which should definitely have adverse effects on human life and health and the classification of which is inadmissible under the Georgian General Administrative Code<sup>32</sup>. What is most important, this is information, which, according to the Georgian constitution<sup>33</sup>, should be available to any citizen.

Despite the above mentioned, the Ministry of Economy and Sustainable Development refused to disclose information to Green Alternative without the owner's written consent. Green Alternative received the same response from the Tbilisi Government, one of the parties to the contract. The attempt to obtain the document grew into a two-year court dispute. Subsequently, the courts of all instances shared the position of public agencies claiming that reports on fulfillment of privatization conditions were classified under the relevant article of privatization contract, according to which "none of the parties shall make a statement on procurement of "a share" and any other related issue without prior written consent of other parties."

The experience in obtaining the reports on fulfillment of conditions set by Madneuli JSC (presently RMG Copper) and Quartzite Ltd (presently RMG Gold) privatization contracts was quite different. In response to the request to get the report on fulfillment of conditions set in the privatization contract between the Ministry of Economy and Sustainable Development and Stanton Equities Corporation, Green Alternative received already "traditional" answer from the ministry, which noted that according to the concluded contract, "buyer's" written consent was needed to disclose information; therefore, the ministry would make a decision on disclosing the information to Green Alternative only after written consent of Stanton Equities Corporation. After several months of correspondence, finally Green Alternative obtained the letter sent by the Director General of Madneuli JSC to the Ministry of Economy. It was clear from the letter that the Ministry of Economy was not monitoring the fulfillment of obligations set by the contract and Madneuli JSC (apparently, based on Green Alternative's request) was demanded to submit relevant information only in May 2009. Green Alternative's expectations were not justified again – instead of the report, the organization received a letter from Mr. Devadze, in which the director general of Madneuli JSC was arguing that the company had fulfilled all the obligations envisaged by the contract duly.

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<sup>30</sup> Article 2

<sup>31</sup> Article 4

<sup>32</sup> Paragraph (a) of article 42

<sup>33</sup> Paragraph 5 of article 37

## HISTORIC POLLUTION

As a rule, large privatized industrial facilities are so called large polluters. Therefore, Green Alternative was trying to ascertain, whether the privatization contracts envisaged an obligation to mitigate/eradicate the damages caused to the environment as a result of operation of these facilities as well as to avoid environmental pollution in future.

As it turned out, instead of imposing an obligation to eradicate the pollution, privatization contracts provided for exempting buyers from the responsibility for environmental pollution.

The term "historic pollution" was established in Georgia in 2004, in the process of state property privatization; it is connected with exempting investors from any liability for the harm caused by the privatized enterprises to the environment in the past (prior to privatization).

We should also note the practice based on which this term (which is informal, but frequently used by officials) contradicts Georgian legislation, particularly the Law of Georgia on Environmental Protection, according to which<sup>34</sup> "the owner of the privatized industrial facility is not released from meeting the commitments on environment protection, which were undertaken by the former owner of the industrial facility. Compensating the damage caused by activities violating the Georgian legislation on environment protection, prior to the privatization of the industrial facility, is the obligation of each new owner of the industrial facility, if not otherwise stated by the legislation."

If we take into account the fact that "otherwise is not stated by the legislation," exemption of new owners from the responsibility for previous pollution is a rough violation of the law. Despite it, we come across similar conditions in a lot of contracts. For example:

According to article 6 (Environmental Liability) of the contract signed between the Ministry of Economy and Sustainable Development and G.M Georgian Manganese Holding Limited on December 8, 2006 on privatization of Vartsikhe HPP Cascade, "the sides agree that the seller will assist the buyer within its competence to eradicate the facts of historic environmental pollution on public-owned land plots, also land plots received from the State by usufruct and their adjacent territories, as well as any future facts of environmental pollution if any such exist."

According to presidential decree No 245 issued on April 10, 2008 on transferring 100% of shares in Rustavtskalkanali Ltd, Mtskhetatskalkanali Ltd, Saktskalkanali Ltd and Tbilisi Water Ltd to Multiplex Energy Limited LLC through direct sale and setting relevant conditions, the Georgian Ministry of Environment Protection and Natural Resources was instructed to develop a plan on environmental measures within its competence in order "to exempt an investor from the historic pollution liability." Although the formulation of the ministry's obligation was quite obscure and unclear (particularly, the basis for preparing the plan, its timeframes and relevant funds), the purpose was absolutely clear – no responsibility for "historic pollution" should have been imposed on the investor. If we judge proceeding from the purpose, such plans should have been prepared before transferring the enterprises to the new owner. It should also be noted that not only the Ministry of Environment Protection and Natural Resources did not participate in preparation of the draft presidential decree, but it learnt about the existence of such obligation only after Green Alternative requested the plan developed in line with the decree. No plan has been developed either then or later.

The contract between the Ministry of Economy and Sustainable Development and Stanton Equities Corporation contains the following article: "'The vendor" undertakes the commitment that "the vendee" is not responsible and will not be obliged to clean or otherwise redress or pay any fee for cleaning or otherwise redressing "till the end date"<sup>35</sup> of any harmful material emitted on the territory of the "company groups" or any other pollution of environment on the land and premises owned by the "company groups."

Besides the fact that the Ministry of Economy concluded an illegal agreement, by releasing Stanton Equities Corporation from responsibility for past damage to the environment, the Ministry added one more violation to the tender<sup>36</sup> which was conducted with lots of other violations.

<sup>34</sup> Article 21. Environmental Requirements in the Course of Privatization

<sup>35</sup> According to the agreement "end date" means the date of payment and transfer the property to the owner

<sup>36</sup> For detailed information, please see the report of Green Alternative issued in 2007: Aggressive State Property Privatization policy or "Georgian-Style Privatization". Available on the web-site: [www.greenalt.org](http://www.greenalt.org)

The point is that the responsibility for damage made to the environment in the past by "Madneuli" and "Quartzite" is connected with solid expenses<sup>37</sup>, and the conditions of the tender did not imply possibility of release from the commitment. So, the participants of the tender were to present their offers taking into consideration these expenses. It is unknown whether the offer presented by Stanton Equities Corporation implied undertaking commitment for damage to the environment in the past. One thing is obvious - the action of the Ministry of Economy is in any case illegal, as: if the company allowed for these expenses when participating in the tender and the Ministry of Economy released it from undertaking the responsibility for past pollution when signing the agreement, the ministry caused an unjustified loss to the state budget. But if the company did not allow for this commitment from the beginning, then while identifying the winner the Ministry of Economy put Stanton Equities Corporation into unequal conditions with those participants of the tender who provided for these expenses in their offers. Besides, in this case the offer of Stanton Equities Corporation should not have been reviewed in the tender because it did not meet the conditions of the tender.

In the process of state property privatization, the practice of releasing the new owner from the responsibility for past damage made to the environment by operating the enterprises, is exercised in many countries and is justified by the circumstance that often by undertaking responsibility for this damage the enterprises become so unprofitable that selling them becomes impossible. If this is the case the environment protection audit evaluates the damage to the environment and strict differentiation of commitments between the owner and the state occurs. Such practice, on the one hand, simplifies state control of the current pollution of the enterprise and, on the other hand, enables timely planning of measures necessary for redressing of environment condition.

As a result of wrong practice established in Georgia, we face the situation where no one (neither the state, not the owners of the privatized enterprises) undertakes a commitment to redress and compensate the damage caused by the factories to the environment prior to privatization. Such practice causes other problems as well, due to the fact that damage and pollution are not evaluated prior to privatization, the owner of already privatized enterprise is given a possibility to ascribe "the current pollution" to the "past pollution" and thus escape the commitment imposed by the legislation to avoid, decrease or moderate "current pollution".

As already mentioned above, after privatization of the enterprises neither the state considers itself responsible for redressing and compensating the damage to the environment caused by operating the enterprise; accordingly, the authorities do/plan nothing to redress damage caused to the environment. The clear example of it is the selling of Madneuli and Quartzite, when the state, after selling the factories did not start looking for funds to redress damage made to the local environment and population by the operations of the enterprise, but, on the contrary, demanded transferring to the central budget of those funds which Stanton Equities Corporation owed to the local budget.

According to the conclusion<sup>38</sup> made by the Chamber of Control about inspection of planning-performing local budget in Bolnisi region local administration, liability towards local budget covered by Stanton Equities Corporation (GEL 5 million) was granted by the local administration "as financial aid to the state budget." It is indicated in the report that: " The funds were granted to the state budget on the basis of the letter from the Ministry of Finance of March 6, 2006 N 04-03/1972, by which the Ministry informs the head of the Bolnisi municipality that according to the agreement signed between the Ministry of Economy and Stanton Equities Corporation (by which full package of JSC "Madneuli" shares and "TGR" authorized capital were purchased) the latter should cover tax liabilities of JSC Madneuli and Quartzite Ltd before December 31, 2006 part of which will be transferred to the local budget. According to the main principle of implementing local self-government – general-unity of state interests and article 6 of Organic Law on Local Self-Governance and Governance, the Ministry requested the local administration to transfer funds received as liabilities to the local budget to consolidated receipts account of the state budget of Georgia."

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<sup>37</sup> In spite of the fact that calculations have never been done due to that simple reason that the government has never thought of solving this problem, taking into account the scale and duration we can presume that the amount will be significant.

<sup>38</sup> Inspection-control act N1/47, of January 5, 2009 of Georgian Chamber of Control about complex inspection of planning-performing local (regional) budget of Bolnisi region local administration and financial service for the period from October 1, 2005 till January 1, 2007.

## ILLEGAL LAW AND AGREEMENTS

For years privatization of large industrial facilities was carried out without environmental impact assessment. Besides the fact that new owners were released from responsibility for the damage caused to the environment prior to privatization, environmental impacts and compliance of ongoing operations of enterprises with environmental legislation were not controlled. Even special laws were adopted to meet the interests of such facilities and justify the inaction by public agencies.

After the Rose Revolution in 2003, the government policy directed to economic liberalization exerted its influence on the legislation regulating the environmental protection and utilization of natural resources. Most of the legislative amendments were related to the government policy aiming at full economic liberalization and deregulation as well as the willingness to increase the budgetary revenues by all possible means (including through maximum utilization of natural resources). Besides the fact that these amendments were implemented non-transparently and without consultations with all stakeholders, they were aimed at minimizing the existing possibilities of raising public awareness and their participation in a decision making process.

Furthermore, proper law enforcement has remained an insuperable obstacle, as under conditions of strong patronage in the state structures, it provided the enterprises with an opportunity of environmental pollution without assuming any responsibility for it. After March 2011, when the environmental monitoring functions were distributed between the Ministry of Environment Protection and the Ministry of Energy and Natural Resources, this sphere descended into deep chaos.

In March 2012 the Parliament of Georgia adopted the law, according to which in exchange for paying compensation in favor of the state, a person would be discharged from liability for the violations committed in the sphere of environmental protection and natural resources. While adopting the law, the public agencies were arguing that agreements could only be concluded on minor violations and that it was the only solution to protect small enterprises against bankruptcy. However, as it turned out later, the very first agreement was concluded with one of the largest enterprises of the country (that, simultaneously, are the largest environmental polluters) – Madneuli JSC (presently RMG Copper) and Quartzite Ltd (presently RMG Gold).

Based on the agreement concluded on May 15, 2012, all the actions carried out by Madneuli JSC and Quartzite Ltd in the sphere of environmental protection and natural resources from April 1, 1994 to May 14, 2012 were considered lawful and respectively, no civil and/or administrative liabilities before the state and/or local self-government bodies shall be imposed on the enterprises.

The agreement envisages only two types of obligations: (1) payment of GEL 13 million by Madneuli JSC and Quartzite Ltd jointly before March 2014 under the agreed scheme, and (2) implementation of coordinated environmental measures before expiration of the term of license. It should also be noted that the agreement envisages a liability for violating a scheme of payment of compensation. If the total number of days overdue is 10, the agreement shall be considered unfulfilled and canceled, whereas the agreement envisages no sanctions for unfulfilled plan of environmental measures attached to the agreement. Thus, we should suppose that attaching this so called plan to the agreement is a mere formality. The same is confirmed by the list of measures envisaged by the plan. Besides the fact that the enterprises had been instructed to fulfill all the actions enlisted in the plan, description of measures is quite general, overlapping and in some cases, absolutely senseless. For example, 10 paragraphs in the list are about the issue of waste management. One out of ten paragraphs is "waste management", which should be fulfilled by 12.04.2014. It is unclear, how the fulfillment of this paragraph should be expressed, if according to the plan "waste separation" and "liquid waste management" should also be fulfilled by the same period.

One more circumstance is also interesting in respect of this agreement. As we have already mentioned above, according to the agreement on privatization of the enterprises signed between the company Stanton Equities Corporation and the Ministry of Economy on November 11, 2005, the company was released from any liability for the harm caused to the environment in the past (before sale). In particular, the agreement notes: "A seller' assumes an obligation that 'a buyer' will not have to answer and will not be obliged to clean or otherwise redress, or pay a certain amount for cleaning or redressing otherwise 'before the date of completion' for any harmful substances emitted on the territory of 'the companies of the group' or for other environmental pollution on the

adjacent territory.” Considering this circumstance, it is unclear why the company decided to pay compensation for the violations committed in a period between 1994 and 2005.

Moreover, in a month after signing the agreement, on May 15, 2012, then owner of the enterprises, GeoProMining, made a statement on selling its assets in Georgia<sup>39</sup>. According to the statement, the company was carrying out negotiation on the sale of its assets for several months. Taking this fact into consideration, we should suppose that the agreement was signed in order to ennoble the history of activities of the enterprises on the part of GeoProMining, to be exempted from the responsibility for environmental damages and subsequently, sell them profitably. Strange as it may seem, the new owner of the enterprises declares<sup>40</sup> today that when buying the enterprises, he knew nothing about the agreement and respectively about the obligation to pay a certain amount envisaged by the agreement. It is hardly believable that the company participating in a 120-million deal signed the agreement without studying the obligations thoroughly or maybe the deal does not envisage any sanctions concerning newly discovered obligations. However, the statements made by the new owner do not change anything in this respect. The agreement has been signed and before complete payment of the sum by Madneuli JSC and Quartzite Ltd before May 14, 2102, all the actions carried out in the sphere of environmental protection and natural resources will be considered lawful – that cannot but be profitable for the new owner of the enterprises.

As we have already mentioned above, imposing an obligation of implementing the above mentioned measures is a mere formality and no sanctions are envisaged in case of non-fulfillment of this condition. Moreover, as Green Alternative clarified<sup>41</sup>, the Ministry of Energy and Natural Resources did not have any information about the fulfillment of the plan envisaged by the agreement and neither had it implemented any measures to obtain this information. The situation has not changed even after October 2012, when the new authorities came to power in Georgia. According to the Ministry of Environment and Natural Resources Protection, the Ministry has no information about the fulfillment of obligations undertaken by the agreement.

Thus, the agreement concluded on May 15, 2012 with Madneuli JSC and Quartzite Ltd in the sphere of environmental protection and natural resources has further strengthened the situation created by the state when privatizing the enterprises in 2005 by exempting the new owner from the responsibility for the damages caused to the environment in the past – the situation, where nobody (neither the state nor the owners of the enterprises) assume the responsibility for recovering and compensating for damages caused to the environment.

It should be noted that one of the first initiatives of the new government which came to power as a result of the 2012 October parliamentary elections was cancellation of those amendments to the Law of Georgia on Environmental Protection, which allowed concluding an agreement in the sphere of environmental protection and natural resources. Green Alternative hoped that the law would be cancelled on the basis of a relevant assessment and conclusion in order to establish the practice of substantiating the need and legality of making legislative amendments, on the one hand, and to avoid the possibility of initiating similar legislative amendments in future, on the other. However, on March 25, 2013 the Parliament of Georgia abolished the law without any specific discussions.

It should be noted that by its decision No2/1/524<sup>42</sup> dated April 10, 2013, the Constitutional Court, citing paragraphs 3 and 4 of article 37 of the Georgian constitution<sup>43</sup>, recognized the norm already abolished by

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<sup>39</sup> <http://www.geopromining.com>; Statement on the sale of assets of GeoProMining in Georgia; June 14, 2012, Moscow

<sup>40</sup> <http://liberali.ge>, “Environment Lost in Calculation”, 08.02.2013

<sup>41</sup> On December 6, 2012 Green Alternative received an answer from Irakli Khmaladze, the head of the Law Department of the Ministry of Energy and Natural Resources; the organization was requesting information about the fulfillment of the plan of actions agreed on the basis of the agreement signed with Madneuli JSC and Quartzite Ltd on May 15, 2012 in the sphere of environmental protection and natural resources (most part of actions envisaged by the plan should have been fulfilled already).

<sup>42</sup> The composition of the board: Zaza Tavadze – chairman of the hearing, reporting judge; Otar Sichinava – member; Lali Papiashvili – member; Tamaz Tsubutashvili – member. Name of the case: Georgian citizen Giorgi Gachechiladze vs. the Parliament of Georgia. The subject of dispute: compliance of paragraphs 1 and 3 of article 57<sup>10</sup> of the Law of Georgia on Environmental Protection with paragraphs 3 and 4 of article 37 of the constitution of Georgia and the compliance of paragraph 4 of the same article with paragraph 5 of article 37 of the constitution of Georgia.

<sup>43</sup> Article 3. Everyone shall have the right to live in healthy environment and enjoy natural and cultural surroundings. Everyone shall be obliged to care for natural and cultural environment. Article 4. With the view of ensuring safe environment, in accordance with ecological and economic interests of society, with due regard to the interests of the current and future generations the state shall guarantee the protection of environment and the rational use of nature.

the Parliament as unconstitutional. Unlike the Parliament and the Ministry of Environment Protection, the Constitutional Court held a lengthy discussion on the incompatibility of the norm subject to cancellation.

It should be noted that while considering the case at the Constitutional Court, Neli Korkotadze, head of Mineral Resources Management Department at the Agency of Natural Resources, and Konstantine Khachapuridze, deputy head of the same Department, who were invited to court hearing as witnesses, claimed that “even in the period of inspection, it is almost impossible to identify whether a particular violation was committed in the period envisaged by the agreement or after this period; as a result, it is difficult to receive impartial information. The witnesses explain that disputable norms do not enable controlling authorities to obtain reliable, substantiated and comprehensive evidence that hampers collection and dissemination of complete and impartial information about the environment. In addition, the witnesses suppose that the disputable norm is problematic as when signing the agreement a person has no obligation to disclose what kind and amount of harm was caused to the environment; respectively, the above mentioned can become the basis for corrupt deals, the process will become non-transparent that will cause harm to the environment and violate basic human rights.<sup>44</sup>”

It should be noted that despite abolition of this norm, the agreements concluded in the period of operation of the law still remain in force. The Ministry of Environment and Natural Resources Protection saw the risks of corrupt deals and causing damages to the environmental and basic human rights; however, it failed to see the same risks in the agreements concluded on the basis of this norm and did not demand cancellation of these agreement (noteworthy that not only the law enabled but also obliged the ministry to act so).

Two more agreements were concluded during the period of operation of the law:

On June 29, 2012 Saknakshiri Ltd (GIG Group) applied to the Ministry of Energy and Natural Resources and requested to conclude an agreement in respect of licenses No 100752<sup>45</sup>, No 01018<sup>46</sup> and No 00885<sup>47</sup> for the period between January 6, 2010 and October 12, 2011 in the sphere of environmental protection and natural resources. In exchange of the agreement, the company was ready to pay GEL 40 000 within 20 calendar days.

It is unknown what particular violations Saknakshiri wanted to be considered lawful. We can conclude from the company’s statement that the violations were related to the extraction of minerals. However, the order issued by Georgian Prime Minister Ivane Merabishvili on July 20, 2012 and subsequently, the agreement concluded with the Ministry of Energy and Natural Resources (represented by Minister Alexander Khetaguri) on July 24, 2012 envisages considering lawful not only the license-related actions but generally all the actions carried out in the sphere of environmental protection and natural resources.

It is interesting that the agreement did not provide for the fulfillment of any additional commitments and it only envisaged payment of GEL 40 000 for all those violations committed under three licenses during almost two years to be considered lawful.

On July 24, 2012 Georgian Prime Minister Ivane Merabishvili issued order No 1135 on concluding yet another agreement in the sphere of environmental protection and natural resources. According to the order, the Ministry of Energy and Natural Resources was instructed to sign an agreement with the Georgian branch of the company Polat Iol Iapi Sanaii ve Tijareti (Turkey). The order defined agreement period – from July 8, 2011 to July 20, 2012; GEL 20 000 was defined as the sum of compensation for all the violations committed in the sphere of environmental protection and natural resources to be considered lawful.

On August 6, 2012 the Ministry of Energy and Natural Resources (represented by Minister Alexander Khetaguri) and Georgian branch of the company Polat Iol Iapi Sanaii ve Tijareti signed an agreement under the conditions defined by the Prime Minister’s order. Like in two other cases, the essence of violations is again unknown.

<sup>44</sup> <https://matsne.gov.ge>, Ruling of the Constitutional Court 2/1/524, registration code 000000000.00.000.016012

<sup>45</sup> License No 100752 on the use of minerals was issued to Saknakshiri Ltd on October 24, 2007 for underground processing of the Tkibuli-Shaori coal deposit. The Mindeli and Dzidziguri mines should have been rehabilitated under license conditions.

<sup>46</sup> License No 01018 on the use of minerals was issued to Saknakshiri Ltd on December 25, 2007 for extracting coal on the territories of Tkibuli and Ambrolauri. Construction of a new mine is planned under license conditions.

<sup>47</sup> License No 00885 on the use of minerals issued to Saknakshiri Ltd on October 24, 2007 for partially open-pit coal mining.

It should be noted that the Georgian branch of the company Polat Iol Iapi Sanaii ve Tijareti underwent registration in Georgia on July 8, 2011. Actually, all the actions carried out by the company in the sphere of environmental protection and natural resources since the day of launching operation in Georgia have been considered lawful by the agreement.

It should be noted after the new government came to power as a result of the October 2012 parliamentary elections, the new owner of Madneuli and Quartzite voiced an initiative to direct the amount envisaged by the agreement (GEL 13 million) to settlement of environmental problems<sup>48</sup>. On July 16, 2013 the director general of RMG Copper (JSC Madneuli), on behalf of RMG Copper and RMG Gold, submitted an indicative action plan on environmental protection to the Ministry of Environment and Natural Resources Protection, which noted: "The new management of the company realizes the grave problems inherited from the previous enterprise as well as the scales and essence of historic environmental pollution. Therefore, the key vector of the company's environmental policy is to implement purpose-oriented measures based on the results of a detailed expert research of the enterprise and its adjacent territory that should finally bring a long-term and sustainable result concerning significant reduction of environmental impacts." In connection with the agreement concluded on May 15, 2012, the plan notes that "the new owners were not informed about the fact of concluding this agreement and especially about its contents. Thus, the new management of the company was presented with a fait accompli. Unfortunately, as we found out later, the plan of measures, which was developed hastily by the previous management of the

At this stage, it has been studied and ascertained that the main source of environmental pollution from the industrial territory (enrichment factory, industrial sites, etc.) is wastewater, while the main pollution components are heavy metals and acid waters. Pollution recipients are the following rivers: Kazretula, Mashavera, Poladauri, as well as the soils in river groves and irrigation areas. It should be noted that accumulation and dynamics of heavy metals in the soils of river groves and irrigation areas are not studied on a regular basis. They need additional research and specification. It is also essential to study background parameters of the above mentioned rivers and soils in view of one-year dynamics.

The data received in the period of wastewater monitoring are in most cases illogical and do not fall under any patterns; thus, the existence of hidden, unstudied factors of environmental impact is quite apparent.

Industrial area covers various elements of industrial infrastructure with one part being an identified polluter and another part being a potential polluter.

companies, does not adequately reflect the real situation in the enterprises and is not directed towards the key priorities of improvement of the state of environment." As it turns out from the document, based on the above mentioned, the company tried to make amendments to the annex of the agreement (which sets a schedule of implemented measures); however, according to the same document, "it was impossible to implement it from legal point of view."

Although the plan submitted by RMG Copper did not focus on the environmental problems related to the activities of RMG Gold (Quartzite Ltd) and generally, it was not a high-quality document, the report described a number of environmental problems, which were not admitted by the companies previously.

Extract from RMG Copper/RMG Gold indicative action plan on environmental protection (2013):

As Green Alternative found out, on August 27, 2013 the Ministry of Environment and Natural Resources Protection submitted its remarks and recommendations to RMG Copper concerning the indicative plan and by this, the activities of both the ministry and the company over this issue came to an end. We have no information about what where the conditions set by RMG in terms of directing the amount envisaged by the agreement towards settlement of environmental problems. However, we can suppose that the company is not ready to reject the condition of the agreement, according to which all the actions carried out by the enterprises in the sphere of environmental protection and natural resources from April 1, 1994 to May 14, 2012 were considered lawful.

<sup>48</sup> Environment Lost in Calculation, 19.12.2012, [www.liberali.ge](http://www.liberali.ge)

Otherwise, the company would have demanded abolition of the agreement and the state agencies would have been forced to agree on this demand. In this situation, inaction by the Ministry of Environment and Natural Resources Protection further aggravates the situation - on the one hand, the Ministry does not take the initiative to abolish the agreement (that is the ministry's obligation based on the decision of the Constitutional Court), and on the other, under conditions of considering lawful the harm caused by the companies to the environment for years, it does not seize the opportunity to use the sum envisaged by the agreement for settlement of environmental problems on the ground and does not enter into active negotiations with the companies.

### CONCLUSION AND RECOMMENDATIONS

As already mentioned above for multiple times, despite numerous amendments to the legislation regulating state property privatization, the legislation does not envisage the possibility of public participation in the process of making decisions on privatization of a facility. The issue of public access to the information related to privatization process is also quite problematic. Green Alternative has witnessed a lot of cases, when the organization was refused to receive a privatization agreement, while the document is available on the public registry's website.

Frequently, it is impossible (or it requires much time) to identify the owner of this or that privatized (large) facility – most of the new owners are registered in offshore zones.

As for the fulfillment of obligations envisaged by the privatization agreement and Georgian legislation by privatized enterprises, the public has no access to information about whether the owners of privatized enterprises fulfill the obligations and how they fulfill the obligations envisaged by relevant agreements and legislation.

The situation is unfavorable in the sphere of fulfillment of environmental obligations too. Besides the fact that new owners of enterprises are exempted from responsibility for any harm caused to the environment prior to privatization, there is no control over the compliance of enterprises' activities with environmental legislation.

#### Recommendations

It is an urgent task to adopt relevant legislative amendments to ensure relevant mechanisms for real transparency of privatization process and public involvement in a decision making process.

It is important for the relevant state agencies to study the legality of privatization of already privatized large facilities.

It is essential that the public has access to certain information, including names of new owners of privatized large facilities, obligations undertaken in frames of privatization agreements and state of fulfillment of these obligations.

The Ministry of Environment and Natural Resources Protection of Georgia should raise the issue of cancellation of those agreements concluded in the sphere of environmental protection and utilization of natural resources, under which all the actions committed/carried out by RMG Gold, RMG Copper, Saknakshiri Ltd, a Georgian subsidiary of Polat Yol Yapı Sanayi ve Ticaret in this sphere were considered legal.

It is vital for the Georgian Parliament to intensify control over the fulfillment of legislative requirements by the state agencies in the sphere of public information confidentiality.

It is also important to study the legality of confidentiality of those privatization agreements, which are made confidential by these very agreements.

It is very important to implement the programs aimed at building capacities of controlling authorities. These programs should involve the development of human resources and providing them with technical resources as well as empowering the controlling authorities.

Association Green Alternative is a non-governmental, non-commercial organization that was founded in 2000. The mission of Association Green Alternative is to protect the environment, biological and cultural heritage of Georgia through promoting economically sound and socially acceptable alternatives, establishing the principles of environmental and social justice and public involvement in the decision making process.

Since the day of its foundation, the organization has monitored the activities of the international financial institutions in Georgia; moreover, the organization works on particular issues, such as: the improvement of environmental policy and instruments; the conservation of biodiversity; energy/climate change and poverty reduction; the protection of environmental, social and economic rights of the local population in the state property privatization process; the eradication of illegal wood cutting and illegal trade in fauna species; the promotion of the availability of environmental information and full public involvement in the process of making important decisions.

Association Green Alternative cooperates with non-governmental organizations both in Georgia and outside Georgia. In 2001 Green Alternative, along with other local and international non-governmental organizations, founded a network of observers devoted to developing a poverty reduction strategy in Georgia. Since 2002 Green Alternative has been monitoring the Baku-Tbilisi-Ceyhan oil pipeline project implementation, its compliance with the policies and guidelines of the International Finance Corporation and the European Bank for Reconstruction and Development, the project's impact on the local population and the environment. Since 2005 the organization has been a member of the Monitoring Coalition of the ENP (European Neighborhood Policy) Action Plan. In 2006 Green Alternative founded an independent forest monitoring network. Green Alternative is a member of CEE Bankwatch Network; it closely cooperates with Friends of the Earth International, an international network of environmental organizations, as well as Central and Eastern European Network of Climate Change, International Network for Sustainable Energy, and various international and national organizations working on environmental, social and human rights issues; Green Alternative is a member of the Coalition Transparent Foreign Aid to Georgia, which was founded in 2008. In 2009 Green Alternative started setting up the Georgian Advocacy Network for Environmental and Social Justice.

In 2004 Green Alternative was awarded with the Goldman Environmental Prize for successful activities conducted for environmental protection, social justice and equality related to the Baku-Tbilisi-Ceyhan oil pipeline campaign.