

**STATE-BUILDING
vs. RESOURCE MANAGEMENT**
*(The Case of Azerbaijan
and Its Oil Fund Management)*

Mehmet KALYONCU

*Graduate fellow at the Center for Eurasian,
Russian and East European Studies,
Edmund A. Walsh School of Foreign Service,
Georgetown University
(Washington, U.S.)*

***D**ependency is what the state elite, be it government officials or the political leader, of the developing countries at the periphery make of it. That is, whether the economic ties of the periphery with the center lead to modernization and prosperity or dependency and underdevelopment depends on the development policies of the periphery states.*

In that sense, analysis of the economic policies of a given government gives us insights about whether the country is heading to democracy and prosperity, or authoritarianism and underdevelopment. Such analysis is especially crucial for countries undertaking state-building process and development of their vast natural resources simultaneously. Azerbaijan provides a perfect example.

Introduction

Multinational corporations may lead either to satellite-center relationship and hence underdevelopment of the periphery, or to prosperity and modernization at the periphery. What determines the outcome out of these two is the attitude of the government, specifically of the leader, of the host country. I argue that the dependency is what the state elite, be it government officials or the political leader, of the developing countries at the periphery make of it. That is, whether the economic ties of the periphery with the center lead to modernization and prosperity or dependency and underdevelopment depends on the development policies of the periphery states. In other words, *ceteris paribus*¹ the state has the control to determine the legal framework in accordance with which the foreign capital operates within the country. As such, it can control the impact of the foreign capital on economic development of the country. This is especially so in extractive industries. Since the extraction site has a fixed location, the resources are not easily transferable and the state rather than private parties has the ultimate control over the extraction sites, the government can be very demanding in terms of establishing the operative regulations of the foreign extraction and related companies.

There are several crucial tasks that the host countries need to fulfill in order to have the multinational companies contribute to their overall development. First they need to understand what they can expect from the multinational corporations and what they cannot, in other words, they need to accept the multinational corporations as self-interested actors working to maximize the profit of their shareholders. As the commercial director of the BP, which is the largest shareholder and operator of the oil and gas related projects in Azerbaijan, notes, “we are not an aid agency or a charity. Our purpose is to create wealth on behalf of our shareholders. Our interests will thrive if the societies in which we invest also thrive.”² Namely, the multinational corporations and the host country may first have mutual benefits and can achieve these benefits as long as they cooperate. Second, they need to grow a middle class as large as possible by involving the local small businesses in the extraction related industries. Third, they need to grow a human capital by gaining know-how about the industry. Fourth, they must build institutions independent of political influence and protected by the constitution. These institutions must oversight the activities related to the development of the natural resources. Fifth, they must accumulate the natural resource income in a fund which is under the control of not the government and hence the president but of the private management council. Sixth, they must transform the income into long-term income-generating mechanisms for the national economy. The quintessential to managing natural resource wealth, which is predominantly oil in the Azerbaijan case, is to keep in mind that that particular resource sooner or later will have depleted. Therefore, in order to maintain the pace of the economy based on the natural resource development, the government must ensure that the resource income is being invested in new institutional arrangements and income-generating mechanisms that are capable of replacing the depleting natural resources. Joseph Stiglitz suggests that the government must build natural resource fund with stabilization and savings functions so that it can prevent the negative impacts of oil price volatility on the domestic economy. Lastly, they must ensure maximum transparency, accountability, and the involvement of the citizens in the decision-making process about how to spend the natural resource income.

Yet the first and foremost requirement, which must precede these seven tasks, is the willingness of the government to do so. After all, it is the government leader who is supposed to take initiative and start the whole process. Rather than seeking sources of legitimacy for his authoritarian tendencies, the

¹ Unless the home countries of the multinational corporations coerce the host countries through diplomatic or military means to adopt normally-unacceptable regulations.

² A. McAuslan, Panel: “Caspian Oil Windfalls: Who Will Benefit?” hosted by the Open Society Institute and the Center for Strategic and International Studies, 12 May, 2003. Conference Proceedings, available at [http://www.osi-az.org/cow_docs/osispeechbaku.pdf].

president must be willing to deprive his/her post of the authority to control the natural resource income, and let constitutionally protected institutions take that responsibility. It is also important for such institutions to establish through constitutional amendments rather than governmental legislation, because the latter makes such institutions still vulnerable to the president or the government's control. In a developing country, especially that whose economy is mostly based on the export of the natural resources, the level of observance of these tasks and the president's attitude with respect to giving up such authority can give us insight about whether the country is heading to authoritarianism and underdevelopment or democracy and modernization.

The Case of Azerbaijan: Neither Democracy Nor Authoritarianism

Economic development does not necessarily entail political development, but democracies better survive in economically developed countries,³ concludes Adam Przeworski. Regarding the same correlation between economic development and political development, Huntington contends that a certain level of initial authoritarianism is necessary and beneficial in order to establish the institutions necessary for the maintenance of long-term political stability. Having not yet fulfilled what these two theories imply, Azerbaijan seems to be a viable model in order to test both theories. Ever since its independence after the collapse of the Soviet Union in 1991, authoritarianism and democracy have come along hand in hand in Azerbaijan. Before advancing in detail to the political development of Azerbaijan, it is important to note that one should differentiate his/her approach to the regime during both Heydar Aliev and his son Ilkham Aliev administration while evaluating both in terms of democratization and political openness. The main reasons for differentiating between the two are the time frame and the associated regional, international, and domestic conditions concerning Azerbaijan. Moreover, I argue that Heydar Aliev had to be authoritarian in a sense, and could not afford to be more democratic since the maintenance of both regional and internal stability was crucial to attract foreign direct investment and start a long-term development project. The presence of multiple strong opposition parties would delay, if not prevent, the accomplishment of such policies. On the other hand, Ilkham Aliev has taken over the administration once the regional stability was maintained, the conflict with Armenia over Nagorno-Karabakh has been at least cooled down, and maximum number of foreign investors have already come in and started their projects to process the natural resources of Azerbaijan. Therefore, the Ilkham Aliev administration's challenge is the management of the natural resource development and transformation of this natural resource wealth into long-term income-generating instruments as well as ensuring that the citizens are equally benefiting from this wealth.

It is difficult to make a clear definition about the political system of Azerbaijan when it comes to authoritarianism versus democracy. Azerbaijan has experienced and keeps experiencing both simultaneously. As Swante Cornell notes, "Today, Azerbaijan is neither a democracy nor a clear-cut authoritarian state of the sort found in the Central Asian republics, with which Azerbaijan shares cultural, linguistic, and religious affinities. An active and diverse opposition, a relatively free press, and a vibrant political life exist in Azerbaijan. Opposition leaders (and the press) criticize the regime openly and harshly; they even organize demonstrations and rallies, something that would be unthinkable in

³ See: A. Przeworski, *Democracy and Development: Political Institutions and Well-Being in the World, 1950-1990*, Cambridge University Press, 28 August, 2000.

Central Asia.”⁴ In that sense, Azerbaijani people enjoy wide freedoms to articulate their dissent with the policies of the ruling party. However, the ruling party has also been marked by its similarly harsh counteract against the opposition activities. For instance, opposition leaders have been sued and banned from politics, sent to exile. Media channels, be it radio and TV stations or press, were closed. After all, the elections and democratic process have never reached the international standards. Moreover, the major problem in Azerbaijan regarding its democratization has not been about the legislation allowing democratic methods but about the conduct of them. For instance, before the second parliamentary elections in 2000, mainly in response to the international pressures, Azerbaijan have revised and improved the electoral legislation in order to allow the opposition parties to run in the elections. “Yet serious irregularities,” maintains Cornell, “in both the conduct of the elections and the subsequent counting of the votes have obliterated this progress and have cast serious doubt not only on Azerbaijan’s development in the direction of a more pluralistic society but also on its political stability.”⁵ In that sense, Azerbaijan’s political system has swayed between opposition’s quest for democratization and the ruling party’s somewhat authoritarian tendencies.

Sources of Legitimacy for the Current Regime

There are several factors which help the Ilkham Aliev administration consolidate its power to the extent that it violates democratic values and carries out a suspicious vote-count, and yet is not held accountable. The factors providing legitimacy to the policies of the Heydar Aliev administration are slightly different than those pertinent to the Ilkham administration. As noted above, there used to be both domestic and international concerns which made the former administration’s authoritarian tendencies somewhat legitimate, such as the need to find an urgent solution to severe poverty, and the insurance of land integrity against Armenia. However, in the latter case, international factors provide more legitimacy to the administration, even to the extent that regional and international concerns outweigh the domestic concerns. What are these domestic concerns which are outweighed? Today, as David Case reports, poverty is still severely affecting the Azerbaijani people. Non-oil economy dramatically has shrunk through the late 1990s; half the population lives at \$26 per month, and throughout the last decade millions of refugees from Karabakh region have lived in railroad wagons. In that regard, Case stresses, “The boom in Azerbaijan’s oil fields has remade Baku’s skyline but has left the majority of Azerbaijanis desperately poor.”⁶ Similarly the watchdog group, Transparency International, describes Azerbaijan, after the suspicious 2003 elections, as one of the world’s most crooked countries. In addition to this economic underperformance, there is a major bribery scandal about the Aliev government, which consequently heated the citizens’ dissent about Ilkham Aliev administration, and increased public support for opposition groups such as Musavat. Furthermore there has not been much development in terms of political freedoms either. For instance, there is still suppression on the opposition activities; the presidential candidate and the chairman of Azerbaijan Democratic Party, Resul Guliev, is in exile, and ran the campaign over phone from New York. Similarly the co-chairman of the same party, Serdar Jalaloglu is in prison since the elections, and the public believes that the courts are highly influenced by and take orders from the regime.⁷ Moreover, the international organizations that monitored the 2003 election described it as a sham, replete with voter intimidation, violence, ballot

⁴ S. Cornell, “Democratization Falter in Azerbaijan,” *Journal of Democracy*, 12 February, 2001, pp. 181-191.

⁵ Ibidem.

⁶ D. Case, “Azerbaijan’s Crude Doctrine,” *Mother Jones Magazine*, July 2004.

⁷ See: Ibidem.

box stuffing, and brutal repression. So to what extent do these domestic concerns impact the legitimacy of the Ilkham Aliev administration in the minds of the citizens? Given that he does not have his father's charisma, and will always be seen, at least by some, as not an elected but selected president, what factors contribute to his legitimacy? Or how does he justify the over-consolidation of power in his hand? Even though he does not have the reasons that his father used to justify his authoritarian policies, he has something more influential: international legitimacy.

It is international legitimacy in the sense that the ongoing oil and natural gas production projects, the pipeline projects involving several regional countries, the amount of investment already made, the role of Azerbaijan in "war on terror" etc., all these factors make a government change in Azerbaijan highly risky and undesirable to the states involved in these projects and to neighboring countries. They rather become willing to ignore human rights violations or undermining democratic process in Azerbaijan for the sake of having a solid, reliable administration. Especially the U.S. support constitutes the most important source of legitimacy for the Aliev administration. Starting in the early years of his government, Heydar Aliev had successfully used the oil companies and his Washington connections to establish reliable relations with the U.S. government and resumed the U.S. aid to Azerbaijan. In the maintenance of these good relations, Richard Armitage, the former Deputy Secretary of State, has played a crucial role. He initiated and co-chaired the U.S.-Azerbaijan Chamber of Commerce, maintained very close personal ties with the Aliev family dating back to the early years of independence. More importantly he remained the key person who established the business contacts between the Aliev administration and the oil companies for which he also provided consulting service. The personal connections transformed into \$7.4 billion project, "the contract of the century," with ten companies, including prominent Western oil companies: BP, Unocal, Conoco-Phillips, ExxonMobil, Chevron, and Pennzoil. These companies formed a consortium called Azerbaijan International Operating Company (AIOC) in partnership with the State Oil Company of Azerbaijan Republic (SOCAR). The consortium aims to extract the reserves amounting up to 7-13 billion barrels. AIOC has already invested \$4 billion for this purpose and is planning to invest \$10 billion more in the next few years. The amount of its oil and natural gas reserves and its geopolitical situation make Azerbaijan appealing for these companies and countries that they belong to. Caspian Sea oil reserve almost seems to be an alternative to Saudi Arabia in oil production. Their capacities are, respectively, 200 billion barrels (equal to \$4 trillion) and 250 billion barrels. Azerbaijan itself will be producing 1 million barrels of oil per day by 2008. Furthermore, the U.S. wants the oil flow through Azerbaijan rather than riskier routes crossing Russia and Iran. Besides its oil and natural gas production capacity, Azerbaijan's role in "war on terror" has also increased its importance. Heydar Aliev helped the U.S. in "war on terror" immediately opening Azerbaijan's air space to the U.S. jets, and in return received military aid. To the international community, Azerbaijan is a major oil producer and a good ally in war on terrorism. Case notes, "Azerbaijan's pipelines are regarded by the U.S. government as vital to America's oil supply." And he further stresses, "The war in Iraq further improved the Aliev regime's standing in Washington: Azerbaijan was one of the few Muslim nations that supported the war." When all these international factors put together, they provide a good amount of legitimacy for the Ilkham Aliev administration and a good chance of toleration (or ignorance by the international community) for its prospective authoritarian policies.

Ilkham Aliev at the Crossroads

The analysis of both regional and domestic context for Azerbaijan indicates that the conditions that the Heydar Aliev administration faced and the Ilkham Aliev administration has been facing are quite different. In parallel the expectations from these two are quite different as well. The simplest way of articulating this difference is as follows: Heydar Aliev had to start up a national enterprise

which would make use of the country's natural resources; such an enterprise was crucial in order to ensure a sustained regional stability and economic development, to attract foreign investment, and to eradicate the severe poverty; and in order to achieve that goal, Heydar Aliev had to sometimes suppress opposing voices that might endanger the formation of that enterprise. However, Ilkham Aliev is supposed to manage the enterprise that has already been started up. The challenges waiting for him are respectively ensuring the best return on investment possible, maintaining the optimal public spending and investment policy, providing maximum transparency on the government activity, and public involvement in decision-making on how to use the natural resource income. Despite the contextual difference between Heydar and Ilkham Aliev administrations, they yet share one crucial thing in common: availability of sources of legitimacy for their, respective, governments and their authoritarian tendencies. It was dominantly domestic source for Heydar Aliev. National security vis-à-vis Armenia in Nagorno-Karabakh, the severe level of poverty, and the necessity to urgently utilize the oil-gas resources are the essential elements in tolerating the authoritarian tendencies of Heydar Aliev. For Ilkham Aliev, the international context provides quite sources of legitimacy in case he cannot find it domestically through ballot boxes. Azerbaijan's crucial role in helping the U.S. in war on terror, the amount of already invested foreign capital, the expected return on oil and gas investment, the Caspian's capability to be an alternative world energy resource to Saudi Arabia; these are sufficient reasons for the international actors and especially for the U.S. to look the other way in case there are human rights violations or policies of the government conflicting with democratic values. At this point, Ilkham Aliev has to make a decision about the source of legitimacy he would seek for his government. Will it be through strong international connections or through the ballot box?

Whether to respond to these expectations or not is quite up to the will of Ilkham Aliev given that he possesses a strong international legitimacy. Basically he, I believe, would be still fine to many countries and especially to Western oil companies if he practiced a sort of authoritarianism as long as the fates of oil and gas projects are secured. Given the power accumulated in his hand, his preference at this point will have crucial implications on the future of Azerbaijan with regards to its political and economic development.

In order to trace prospective implications on political and economic development, it will be quite informative to analyze the oil income investment policies of the government. How does the government manage the oil income? Does it allow public participation in decision-making? Does the government allow maximum transparency about its activities with the natural resource income? Compared to the natural resource income management models, which were applied in the oil-rich countries from Alaska to Kuwait, what are the strengths and weaknesses of the natural resource income management plan of Azerbaijan? The analysis of the structure and operations of SOFAZ (The State Oil Fund of Azerbaijan) will provide important insights about, respectively, the government's tendencies toward democracy or authoritarianism; the prospects of the oil income, whether it will fade away or the government will be able to transform the depleting natural resources into income-generating mechanisms; and whether the government will seek to maximize its control over the natural resource income, or transfer the authority to the institutions which will be easily monitored and controlled by the citizens.

The Management of Natural Resource Income in Azerbaijan

In order to avoid the past mistakes of the oil-rich, in this case oil-cursed, countries, Azerbaijan has committed to avoid extreme spending by establishing an oil resource fund, SOFAZ. Doing

so Azerbaijan seeks to control inflation which otherwise increases by the influx of the oil income into the market, and maintain exchange rate stability. Moreover Azerbaijan has employed a Poverty Reduction Policy in order to better use its oil and gas resources to alleviate the severe poverty in the country. In this regard, Azerbaijan is considerably prepared for managing its oil wealth with solid projects and policies, and it maintains continuous consultation with the IMF and the World Bank.

The current government in Azerbaijan believes that restoring energy production should precede reforming the society. In contrary to the reputable rentier states, or in other words, the oil-cursed countries in the Middle East, Azerbaijan is cautious not to distribute the oil income among the citizens based on their kinship with the ruling party or the government officials. The main policy regarding the oil income is to accumulate it in the SOFAZ after covering production-related expenses, and to use the dividends accruing from the fund in general infrastructure related development, concrete projects in economic transition, and country specific projects like alleviating the suffering of the refugees. The State Oil Fund carries out these projects, and in order to do so it gathers its income from different resources such as: revenues generated from the country's share of sales of crude oil and gas after deduction envisaged by the appropriate legislation; bonus payments; royalties, accrued payments from the PSA operators⁸; rental fees, for the use of state property by the foreign companies under oil-gas contracts; revenues generated from the sale of assets transferred to Azerbaijan; and lastly revenues generated from the investment of the fund assets.

Furthermore, Azerbaijan has launched a Poverty Reduction Policy through which it aims to use the oil and gas income to maintain a balanced economic growth for all industries. Despite a rapid growth in oil-related sectors, the foreign investment in these sectors has created relatively low number of employment opportunities. As noted in the project, "In 2002, about 5,000 people were employed in foreign oil companies in Azerbaijan (mostly living in Baku), and about 61,000 for SOCAR (of which 74% were men and 26% women) out of total labor force of about four million. Oil and gas sector development plays an important role in increasing state revenues but only creates a limited number of employment opportunities."⁹ Recognizing such a bottleneck in the oil sector, the government has been dedicated to strengthen the non-oil sectors for job creation and to promote regional development programs, privatization, developing the financial and banking sector, and encouraging the growth of small and medium businesses. As Svetlana Tsalik noted before, Azerbaijan took advantage of being able to evaluate the previous experiences of the oil producing countries and take lessons from their mistakes.

However the authority issue, in other words, the control power over managing the oil wealth, be it accumulating the oil income in the SOFAZ, spending it for infrastructural renovations or for public needs, still seems to be problematic. Even though both Aliev governments have employed various economic policies such as Poverty Reduction Policy, and undertaken institutional changes such as the establishment of SOFAZ for managing the oil income through continuous consultations with IMF and the World Bank, they as a ruling party or political figures have been highly criticized by the area specialists and human rights organizations for having tremendous power to influence these policies and institutions. In this regard, Nazim Imanov, Azerbaijan Parliamentary Budget Committee member, argues that "right now in Azerbaijan, the oil fund under the current law is under the control of one person; the president of Azerbaijan," and "regardless of whether we are talking about today's President or future Presidents, it is basically an unacceptable situation for the oil fund to be under the control of one person."¹⁰

⁸ These are the companies which partner with the SOCAR in Production Sharing Agreements.

⁹ "Poverty Reduction Policy," in: *Azerbaijan: Poverty Reduction Strategy Paper (PRSP)*, World Bank, p. 108 [http://poverty.worldbank.org/files/Azerbaijan_PRSP.pdf].

¹⁰ N. Imanov, Panel: "Findings and Recommendations of the Caspian Revenue Watch" hosted by the Open Society Institute and the Center for Strategic and International Studies, 12 May, 2003.

Similarly Tsalik points to the importance of decentralization of power among the institutions and transparency of government operations in order to insure the country against the oil curse. She argues that the resource fund may have an excellent investment strategy and yet may collapse if it is completely subordinated to the President. Moreover, the fund can generate excellent returns and yet not benefit the citizens if there is no complete transparency regarding how the income is being spent.¹¹ She further argues that avoiding the resource curse requires further reforms that give a greater role to other branches of government, and making information and opportunities available for the citizens to observe and shape government fiscal policies. In regard to such criticisms, Azerbaijan's U.S. Ambassador Pashaev shed light on the issues such as transparency of the SOFAZ activities and the accountability of the fund. He noted, "To bring more public control to the Oil Fund, the government of Azerbaijan after intensive consultation with the IMF and the World Bank agreed to make changes in the law on the state budget and include the State Oil Fund expenditures as part of the state investment program in the consolidated, parliament adopted budget of Azerbaijan."¹² Apparently it is a big step in terms of making the information about the fund activities accessible to the public. Yet it is still questionable whether the citizens possess the means and knowledge to influence the fund's spending policies. Similarly in regard to the accountability of the fund's governing body, he notes that SOFAZ publishes quarterly reports on its revenues and expenditures and undertakes annual audits. These audits are carried out by the Parliamentary Chamber Accounts which is the supreme audit institution of the country. Yet again there is always the possibility for SOFAZ not to reveal information about its every activity. Moreover, given the power of the ruling party in the parliament, the supreme audit institutions would always be vulnerable to the influence of the ruling party. Therefore, the international community and the area specialists are still hesitant about the fate of democratization process in Azerbaijan.

***What Could Be Done
in Terms of Decentralization of Power,
Increasing Transparency and
the Public Involvement?***

The Alaska Permanent Fund presents a good example for successful oil fund management. What distinguishes the Alaska Permanent Fund from its counterparts in the Middle East or Latin America is its fulfillment of three requirements which are as follows: transparency, checks and balances, and public involvement. Transparency is the key element to prevent the secrecy of the fund management that otherwise might lead to abuses and misappropriations by the government officials. Checks and balances aim to ensure power separation among the different branches of the government or institutions that are in charge of managing the country's natural resource development. Decentralizing the authority over the control of the natural resource funds, checks and balances seek to prevent the government officials from wasting the funds on unreliable and weak projects, channeling the funds into the businesses that they have personal connections with. Besides, it helps the government resist the temptation to spend heavily in the short run, at the expense of future generations, Tsalik maintains. At this point one particular point must be clarified: is the exhaustion of the natural resource funds in short

¹¹ See: S. Tsalik, Panel: "Findings and Recommendations of the Caspian Revenue Watch" hosted by the Open Society Institute and the Center for Strategic and International Studies, 12 May, 2003.

¹² H. Pashaev, "Government Plans and Challenges in Managing Petroleum Wealth" hosted by the Open Institute Society and the Center for Strategic and International Studies, 12 May, 2003.

term something that should be avoided absolutely? Rather than in how much time the fund exhausted, the most important concern must be what the funds are spent for. As long as the funds are transformed into different types of income-generating mechanisms, the governments should be able to spend the funds regardless of time. At this point another crucial question arises: who will decide on what project is worth to spend the funds for? The third requirement, public involvement, seeks to ensure public participation in decision-making on what to spend the funds for. It aims to make the public an active player in decision-making process so that an overarching consensus can be reached about the use of the natural resource funds.

From the beginning the State of Alaska emphasized the decentralization of the control over the Alaska Permanent Fund. For this purpose, a separate non-political entity, the Alaska Permanent Fund Corporation (APFC) was created to manage the fund.¹³ Doing so, the state isolated the management of oil funds from any possible political influence. Moreover, the State of Alaska provided an institutional protection to the fund by a constitutional amendment. From that point on, the fund activities had to be undertaken according to the guideline specified with the constitutional amendment rather than the legislation which could be influenced by the ruling party. Moreover, although independent of any political influence in its investment decisions, the APFC was accountable to both the government of Alaska and to Alaskan Citizens.¹⁴ Furthermore, in order to provide public involvement in the fund management, the Governor Jay Hammond established the State Investment Advisory Committee, composed of representatives from consumer groups, business, government, and the public, to conduct hearings to gauge public opinion on the use of oil income.¹⁵ Along with these hearings, the committee also organized public seminars in order to inform the citizens about the development of the state oil resources. The governor Hammond believed that people rather than government should decide how to spend the money, and encouraged the public participation to decide on how to spend the oil income. For this purpose the state encouraged public discussion through media and asked for comments directly from the citizens through the press channels.¹⁶ After extended discussions about whether to use the Fund's income for economic diversification, for public works, or to provide annual dividends to Alaskan citizens, the citizens chose the dividend program.¹⁷ Doing so, as the real owners of the state's natural resources the Alaskan citizens ensured that every individual directly benefits from the natural resource wealth.

By several aspects, the Alaska Permanent Fund could be a benchmark for Azerbaijan. The Aliiev government keeping the natural resource income in off-shore banks has already eliminated potential suspicions about misuse or misappropriation of the natural resource income by the government officials. Going beyond that, the administration should be willing to bring the SOFAZ under constitutional protection, and limit the government's elevated control over the funds. Doing so, it would primarily invalidate the arguments that the fund is absolutely subordinated to the President no matter what institutions seem to control it. Secondly it would provide more transparency and give chance to the citizens to better monitor the activities of the fund. However making the information available is not sufficient in order to ensure public involvement in the decision-making process. The citizens must have a basic knowledge about the fund activities and alternative investment strategies. At this point it is crucial to distinguish between transparency and informed public participation. As Steiner notes,

¹³ See: S. Tsalik, *Caspian Oil Windfalls: Who Will Benefit?* Chapter 2: Natural Resource Funds, The Open Society Institute, The Caspian Revenue Watch Program, 2003, p. 22.

¹⁴ See: *Ibid.*, p. 22.

¹⁵ See: J. Kasson, "The Creation of the Alaska Permanent Fund," *Trustee Papers*, Vol. 5, Alaska Permanent Fund Corporation, 1983.

¹⁶ See: "Alaska is Still Looking for Ways to Spend Its Revenues from Oil," *New York Times*, 14 December, 1980.

¹⁷ See: S. Tsalik, *Caspian Oil Windfalls: Who Will Benefit?*, Chapter 2: Natural Resource Funds, p. 22.

whereas transparency is an access to information, informed public participation means that the public has the capacity to synthesize that information, form rational public opinion on it, and then advocate this in the public policy process. In order to inform the citizens in this regard, just like the State of Alaska could, the Aliev administration establishes public advisory councils which would consist of the representatives from the different segments of the Azerbaijani society. Arranging public hearings and seminars, this advisory board can educate the citizens about the natural resource development as well as advocate the citizens' views in negotiations with the industry and government representatives. The efficiency of the Regional Citizens' Advisory Councils established in Alaska after Exxon-Valdez oil spill proves the benefits of such councils in getting the citizens involved in decision-making. Through these councils the citizens had a chance to negotiate with the oil companies about their environmental concerns. Going beyond the mere environmental issues, the administration should also form a citizens' council to monitor the activities of SOFAZ, which would be mediator between the citizens and the government on how to utilize the natural resource funds. Such an involvement would also give more confidence to the citizens about what the fund is used for as well as more confidence in the Aliev administration.

C o n c l u s i o n

When we look at Azerbaijan, we see a growing country which is equally likely to be either an authoritarian or democratic. What will determine the outcome is the preference of the political elite of Azerbaijan. It is their preference because they have always possessed the sufficient sources of legitimacy for their regime. That is, they could manage to be in the office and yet authoritarian in the absence of the citizens' consent. Heydar Aliev had his reasons to be authoritarian and suppress the opposing voices because the country's land integrity was at risk; the war with Armenia had to be ended; in order to insure long-term regional stability and development, foreign investors had to be attracted; and the opposing voices within the country would slow down the whole process. Therefore the Azerbaijani people were consent with the authoritarian policies of the administration as long as it worked to overcome the severe problems of the country such as land security and poverty.

Similarly Ilkham Aliev possesses the sufficient sources of legitimacy for his government, which would give him the luxury of being authoritarian despite the absence of the citizens' consent. However this legitimacy comes not from the domestic context but from the international community, western oil-gas companies and hence the Western states, somehow involved in the oil-gas development in the country. Relying on these strong connections, he could ignore the criticisms and become another authoritarian. Obviously the short period of time he has been in the office is not sufficient to judge about his tendencies toward either democracy or authoritarianism, however his policies regarding the vast oil wealth of the country give us the chance to predict about it. His administration has undertaken important progress in order to avoid the oil-curse that other oil-rich countries have been inflicted with. He established the necessary institutions for better management of the oil wealth. However he needs to go further and deliberately strengthen these institutions by transferring the power to manage this wealth from the Presidency to them.