

# INFORMAL PRACTICES OF BIG BUSINESS IN THE POST- SOVIET PERIOD: FROM OLIGARCHS TO “KINGS OF STATE ORDERS”

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**Abstract:** This article traces the transformation of informal relations between the government and big business due to the changing financial and administrative capabilities of the state, comparing the situations in the 1990s, 2000s, and 2010s. The oligarchic capitalism of the 1990s arose when a weak state was forced to seek the help of those with financial capital in exchange for political rights. Economic development in the 2000s, the budget surplus, and Putin’s policies changed the situation: “milking” the country’s budget and arranging “payoffs” became the main forms of informal cooperation between the government and business. However, the economic difficulties of the 2010s sharply aggravated competition for access to budget resources. Under the slogans of legalizing the economy and fighting corruption, the administration found new informal ways to manage and control big business, assigning the “kings of government contracts” to implement projects as a marker of loyalty to the President’s administration and a precondition for continued business success.

Russia has a reputation for unwritten rules. Although informal business practices are found in countries all over the world, in Russia they are not merely decorative but provide the basis for many economic and

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political processes. All kinds of entrepreneurs actively use informal practices to build relationships with their partners and the state, and they are a key feature of Russians' everyday lives.<sup>1</sup>

Informal practices are both plastic and stable. On the one hand, they change quickly in response to external conditions, playing the role of springs absorbing the collision between formal rules and social norms.<sup>2</sup> On the other hand, informal practices are extremely stable and inert. That is, first they help to adapt to the formal order and then they become an informal standard of behavior.

The focus of this article is: *how have informal practices in relations between big business and the government changed in the post-Soviet period?* Inevitably, we will have to refer to the 1990s for comparison, but the main focus is the period after 2000, when Vladimir Putin came to power.

I deliberately avoid the term “informal economy,” which is usually defined as a system of trade or economic exchange that exists outside state-controlled venues or money-based transactions the income from which is not typically included in gross domestic product (GDP) computations. There are various ways to recalculate GDP taking the informal economy into account.<sup>3</sup> According to official data from the Federal State Statistics Service, the “non-observed economy” accounted for about 15% of Russian GDP in early 2018, which significantly differs from the IMF estimate (33.5%).<sup>4</sup>

The focus here, however, is not quantitative assessments of the informal economy so much as the qualitative characteristics of informal practices that have been established in the relationship between the government and big business in Russia. Corruption, payoffs and “milking” the budget are all examples of such practices. We are interested in how these informal practices shape the behavior of market participants, how they

<sup>1</sup> Svetlana Barsukova and Alena Ledeneva. 2018. “Are Some Countries More Informal than Others? The Case of Russia.” In Alena Ledeneva, ed., *The Global Encyclopaedia of Informality: Understanding Social and Cultural Complexity*, Volume 2. London: UCL Press, 487-492; Svetlana Barsukova and Vadim Radaev. 2012. “Informal Economy in Russia: A Brief Overview.” *The European Electronic Newsletter “Economic Sociology”* 13: 2: 4-12; Elena Denisova-Schmidt and Olga Kryzhko. 2015. “Managing Informal Business Practices in Russia: The Experience of Foreign Companies.” *Mir Rossii* 24: 4:149-174.

<sup>2</sup> Alena Ledeneva. 2006. *How Russia Really Works: The Informal Practices that Shaped Post-Soviet Politics and Business*. Ithaca, NY: Cornell University Press.

<sup>3</sup> 2002. *Measuring the Non-Observed Economy*. Paris: OECD; Michael O’Higgins. 1980. *Measuring the Hidden Economy: A Review of Evidence and Methodologies*. London: Outer Circle Policy Unit.

<sup>4</sup> The head of Rosstat said, “It is very difficult for me to say about these figures, because according to our estimates, this is approximately two times less.” See “Rosstat otsenil doliu tenevoi ekonomiki” [Rosstat Estimated the Share of the Shadow Economy]. *RIA Novosti*, February 27, 2018, At <https://ria.ru/economy/20180227/1515368247.html>, accessed January 9, 2019.

interact, and channels of influence, rather than the value of “the hidden GDP.” Corruption is certainly linked to the informal economy,<sup>5</sup> but bribes are not included in the GDP of any country since they create no unrecorded product and simply redistribute income.

Informal practices dynamics analysis (“what it was and what it has become”) is a favorite methodological method for studying informality. The Soviet period was marked by a variety of practices that can be described in short as “stealing from the state.”<sup>6</sup> The shortages of everyday goods that the Soviet people experienced were compensated for with “pull” (“blat”) and profitable connections.<sup>7</sup>

After the collapse of the USSR, in the 1990s, so-called market reforms began. The speed and intensity of the transformations and their destructive nature has been embodied in the metaphor of “market Bolshevism.”<sup>8</sup> Business began to move en masse into the informal sphere, ignoring all the laws that the “weak” state attempted to impose on it. Some of the erstwhile functions of the state were taken over by gangsters.<sup>9</sup> Commodity abundance made *blat* obsolete, but informal relationships continued to be important for solving private and business problems alike.

In 2000, Vladimir Putin became president of Russia. Although he rhetorically proclaimed adherence to Boris Yeltsin’s policy, the political course gradually began to change. Whereas the essence of Yeltsin’s policy had been emergency and orthodox liberal reform of the economic and political systems, Putin began the process of “restoring the Russian state” by gradually reorienting it toward national conservatism.<sup>10</sup> If the early Putin era was described as the “road to democracy,”<sup>11</sup> it later became clear that the road was a dead end; Russia became an “authoritarian market” or “hybrid” regime.”<sup>12</sup>

<sup>5</sup> Axel Dreher and Friedrich Schneider. 2010. “Corruption and the Shadow Economy: An Empirical Analysis.” *Public Choice* 144: 1-2: 215–238; Jay Choi and Marcel Thum. 2005. “Corruption and the Shadow Economy.” *International Economic Review* 46: 3: 817-836; Stephen Dobson and Carlyn Ramlogan-Dobson. 2012. “Inequality, Corruption and the Informal Sector.” *Economic Letters* 115: 1: 104-107.

<sup>6</sup> Gregory Grossman. 1977. “The Second Economy in the USSR.” *Problems of Communism* 26: 5: 25–40; Konstantin Simis. 1982. *USSR—The Corrupt Society: The Secret World of Soviet Capitalism*. New York: Simon and Schuster.

<sup>7</sup> Alena Ledeneva. 1998. *Russia’s Economy of Favours: Blat, Networking, and Informal Exchange*. Cambridge and New York: Cambridge University Press.

<sup>8</sup> Peter Reddaway and Dmitri Gliniski. 2001. *The Tragedy of Russian Reforms: Market Bolshevism Against Democracy*. Washington, DC: United States Institute of Peace.

<sup>9</sup> Vadim Volkov. 2002. *Violent Entrepreneurs: The Role of Force in the Making of Russian Capitalism*. Ithaca, NY: Cornell University Press.

<sup>10</sup> Vladimir Gel’man. 2015. *Authoritarian Russia: Analyzing Post-Soviet Regime Changes*. Pittsburgh, PA: University of Pittsburgh Press.

<sup>11</sup> Tom Bjorkman. 2003. *Russia’s Road to Deeper Democracy*. Washington, DC: Brookings Institution Press.

<sup>12</sup> Daniel Treisman. 2011. “Presidential Popularity in a Hybrid Regime: Russia under Yeltsin and Putin.” *American Journal of Political Science* 55: 3: 590–609; Steven Levitsky and Lucan

How did the relations of big business and the government transform in the context of these changes? Quite a lot has been written about the difference between the 1990s and the 2000s, mostly in terms of the opposition between the “freewheeling” 1990s and the “stable” 2000s. However, there has been less work done on how informal practices continued to evolve after Putin’s rise to power. Much of the literature suggests that with the advent of Vladimir Putin, Russia entered a period of stability, as if “the end of Russian history” had come.

But it has not. Changes continue, even if they are less noticeable. The political and economic situation in which Russia finds itself today is significantly different from the one in which it was at the beginning of Putin’s rule. Accordingly, informal practices in the relationships between big business and the government are also changing. This is due to the changing administrative and financial capacity of the Russian state. The short presidency of Dmitry Medvedev did not affect this trajectory, since his election was purely symbolic.

This article describes changes in the informal practices of interaction between big business and the state during the post-Soviet period—that is, high-level, “elite” informal practices. On the one hand, these practices do not affect the everyday experience of ordinary people. On the other hand, it is these “high-level” informal practices that provide indications of the real nature of the regime and answer the question “Whither Russia?”

### **Informal Practices of Big Business in the 1990s: The Formation of an Oligarchy**

We might say that big business was born in Russia in 1992-1993. It was then that the government of the Russian Federation privatized the former Soviet enterprises and identified their assets. These companies included the largest raw materials enterprises (Gazprom, Yukos, Rosneft, LUKoil, Surgutneftegaz) and the country’s electricity complex (RAO UES of Russia).

Privatization began in 1991 and swiftly got under way. Initially, however, it was only trade and service enterprises that were privatized, as well as relatively small industrial and agricultural enterprises—what can be called “small privatization.” The essence of Russian privatization was not the search for new owners for “no-man” enterprises but the transfer of legal property rights to those who already possessed them informally. These owners were the so-called “red directors,” high-ranking bureaucrats and shadow entrepreneurs. In other words, privatization formalized the de facto reality, providing the final proof of what the Soviet people already

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Way, 2010. *Competitive Authoritarianism: Hybrid Regimes after the Cold War*. Cambridge: Cambridge University Press.

vaguely suspected: that they were not the owners of the enterprises. Perhaps because this was already widely understood, privatization did not cause large-scale protest among the population.

However, the government was in no hurry to transfer the largest state assets to private businesses. These were the state's trump card, to be held in reserve for the crucial moment. This moment came in late 1995. With the presidential elections, scheduled for June 1996, on the horizon, Yeltsin was facing the fact that he had little chance of being re-elected. Shortly before the election, his favorability rating was about 3%.<sup>13</sup> At that point, the government turned to bank capital with a request for large loans. In exchange, they offered shares in the largest industrial enterprises in the country. This scheme, implemented in November-December 1995, was called "loans for shares" or "mortgage auctions."

Formally, the government took a loan against collateral. But this belied the informal reality: the government did not plan to repay the loans, essentially gifting industrial assets to the banks. A special piquancy is added by the fact that the commercial banks issued loans with money from the Ministry of Finance, which opened an account in each of the banks and placed funds in it. That is, banks credited the government of the Russian Federation with state money.

However, the government's scheme could only be brought to fruition if Yeltsin won the 1996 elections. The victory of communist Gennady Zyuganov, who was polling much better than Yeltsin, would have deprived these banks of the promised shares in state enterprises.

Thus, big business put its colossal financial resources into ensuring Yeltsin's re-election in 1996. Thereafter, informal arrangements were made to convert bank capital into industrial assets received at below market cost. Vladimir Potanin's Onexim Bank became the owner of Norilsk Nickel, while Mikhail Khodorkovsky's Menatep Bank gained control over the oil giant Yukos. Boris Berezovsky, meanwhile, paid just \$100 million for the oil giant Sibneft, valued at \$3 billion.<sup>14</sup>

All in all, the formal procedure of "loans for shares" was used as a tool to reach informal agreements that provided financial support for the Yeltsin regime. In exchange for political support, the government provided these bankers with *carte blanche* for development and was forced to put up with their enormous political influence. An oligarchic model of governance was established.<sup>15</sup> However, there was no unanimity within the

<sup>13</sup> Daniel Treisman. 1998. "Dollars and Democratization: The Role and Power of Money in Russia's Transitional Elections." *Comparative Politics* 31: 1: 1-21.

<sup>14</sup> Marshall Goldman. 2004. "Putin and the Oligarchs." *Foreign Affairs* 83: 6: 33-44.

<sup>15</sup> David Hoffman. 2002. *Oligarchs: Wealth and Power in the New Russia*. New York: Public Affairs Books; Paul Khlebnikov. 2000. *Godfather of the Kremlin: Boris Berezovsky and the Looting of Russia*. New York: Harcourt; Sergei Guriev and Andrei Rachinsky. 2005. "The Role of Oligarchs in Russian Capitalism." *Journal of Economic Perspectives* 19: 1: 131-50;

oligarchic corps and wars over spheres of influence erupted, making the usual thesis of the “seizure of state governance by business” an unnecessary oversimplification of the situation.<sup>16</sup>

The oligarchs certainly did not own all big business. But it was the oligarchs who became the hallmark of the 1990s. Informal channels of influence over the government gave them unprecedented wealth. The activities of the federal government, sectoral ministries, and regional authorities hid the informal influence of big business.<sup>17</sup>

Notably, some key business figures actually hid their role in decision-making. Roman Abramovich, for instance, was formally only head of the Moscow office of Sibneft and an ordinary member of the company’s board. Formal workflow safely hid his actual role in the business. Such “fouling the trail” was a common business practice in the 1990s, when intricate and changeable formal property relations protected real owners against the revision of privatization.

The opacity of formal business structures hid real property relations and made it difficult to understand who owned given assets. Enterprises often belonged to “shell companies,” which were created only to register assets of a real enterprise. The owners of the “shell companies” were similarly euphemistic firms. As a rule, they were offshore companies. Formal business organization resembled a Russian nesting doll in which the real owners were hidden deep inside. Thus, not only were the channels of big business’ influence over the government informal, but so too were its internal structure and the boundaries of large business empires.

The change in relations between big business and the government is usually associated with the arrival in power of Vladimir Putin. This is a fair assessment, but it is also true that big business was also keen to formalize relations with the authorities. This was due to the 1998 financial crisis, which saw the disappearance of many large Russian banks. It became extremely difficult to find domestic sources of funding, forcing big business owners to turn to the global financial market. To do this, however, they had to formalize their business practices, bringing their financial statements into line with the real state of affairs and showing capitalization and dividends. It was not possible to say, “I control regional authorities” or “I have the right person in the Kremlin” and get foreign credit. In addition to cosmetic measures, such as assigning independent members of the board

William Tompson. 2005. “Putin and the ‘Oligarchs’: A Two-Sided Commitment Problem.” In Alex Pravda, ed., *Leading Russia: Putin in Perspective*. Oxford: Oxford University Press, 179-203.

<sup>16</sup> Janine R. Wedel. 2003. “Clans, Cliques and Captured States: Rethinking ‘Transition’ in Central and Eastern Europe and the Former Soviet Union.” *Journal of International Development* 15: 427-440.

<sup>17</sup> Yakov Pappe. 2000. *Oligarhi. Ekonomicheskaya Khronika 1992-2000* [Oligarchs. Economic Chronicle 1992-2000]. Moscow: HSE Press.

of directors, some essential changes began: formalization of business management procedures and rejection of non-transparent, “matryoshka-like” business architecture. Thus, the default of 1998 and the forced reorientation of business from the domestic to the global financial market resulted in a drift toward the formalization of business activities.

Interactions with the global financial market revealed that close informal connections between big business and the government were a negative in the eyes of potential investors. After all, the authorities who “patronized” the business could lose their position or influence at any time. In addition, informal relations were not sold together with assets; the more important they were for doing successful business, the greater a risk they posed to lenders and buyers. To conform with the preferences of the world market, Russia’s big businesses tried to distance themselves from informal relationships with government authorities and adhere more closely to the formal rules of interaction—at least to a certain degree.

Yet the government, to the utter surprise of big business, did not just seek to correct the course charted by Yeltsin, but proposed completely new rules of the game. On February 25, 2000, presidential candidate Vladimir Putin penned an open letter to Russian voters in which he presented his election program. He announced that he was committed to “making oligarchs equidistant from the government,” explaining, “No economic progress is possible if an official depends on capital. Some wonder how to build relationships with the so-called oligarchs in this case. On a common basis! Just like with an owner of a small bakery or a shoe repair shop.”<sup>18</sup> A month later, on March 26, 2000, Putin won the election and became president of Russia.

Perhaps his experience as a professional intelligence officer fostered in Putin a special concern about the political ambitions and economic power of big business. A policy of “consolidation of statehood” was announced, but at that time no one could have guessed how fast this process would go. Putin was completely unknown in business circles, a true “dark horse.”

### **“Milking” and “Payoffs” as a Leitmotif of Dialogue: Between Business and Government in the 2000s**

Putin embarked on a decisive struggle against the oligarchs, gradually distancing big business from important political decisions.<sup>19</sup> The Yukos case (2003) was a landmark event, proving that the Putin regime was prepared to destroy any big business if it did not submit to the supreme

<sup>18</sup> Vladimir Putin, “Otkrytoe pis'mo Vladimira Putina k rossiiskim izbiratel'iam” [Open Letter of Vladimir Putin to Russian Voters]. *Kommersant*, February 25, 2000, At <https://www.kommersant.ru/doc/141144>, accessed January 9, 2019.

<sup>19</sup> However, it is believed that Putin’s clan has become the core of the new Russian oligarchy: Leonid Kosals. 2007. “Essay on Clan Capitalism in Russia.” *Acta Oeconomica* 57: 1: 67-85.

power.<sup>20</sup> The state's tax claims were based on the admissions of a number of firms, which in fact concentrated profits affiliated with Yukos. Of course, there were no formal signs of the affiliation because Yukos had highly qualified lawyers. The court was therefore forced to demonstrate the elasticity of legal norms under distinct informal pressure from the authorities. This increased the loyalty of the rest of the large firms operating in the oil market, since all of them engaged in the same tax evasion schemes. It is important to note that the state did not need to change the letter of the law, just prevent the judiciary from deviating from the "power vertical."

This signal was heard. The oligarchs quickly turned into "petitioners," willing to do favors for the government in exchange for preferential treatment. For example, the state made it clear that it wanted to dominate "strategic industries" and regain the "key positions" in the economy. In response, Gazprombank redeemed Atomstroiekspor's shares from Kakha Bendukidze and transferred them to the state, giving the latter a controlling stake in nuclear construction in foreign markets. At that time, the state did not yet own a controlling stake in Gazprom and therefore lacked the formal power to dictate to Gazprombank what it should do. But big business leaders understood in which direction the informal rules of the relationship between the government and business were shifting and sought to please their "Big Brother." All links and levels of state governance increased pressure on business: "the seizure of the state by business" gradually changed to "the seizure of business by the state."<sup>21</sup>

As Putin eliminated the oligarchs, he headed for a "strong" state with a powerful repressive system and controlled the media.<sup>22</sup> Mass media played a huge role in creating a positive background for the perception of Putin's policies.<sup>23</sup> Regions were strictly subordinated to the center.<sup>24</sup> The

<sup>20</sup> Vadim Volkov. 2008. "Standard Oil and Yukos in the Context of Early Capitalism in the United States and Russia." *Demokratizatsiya: The Journal of Post-Soviet Democratization* 16: 3: 240–64.

<sup>21</sup> Andrei Yakovlev. 2006. "The Evolution of State-Business Interactions in Russia: From State Capture to Business Capture?" *Europe-Asia Studies* 58:7: 1033–56; Vladimir Gel'man. 2010. "The Logic of Crony Capitalism: Big Oil, Big Politics, and Big Business in Russia." In Vladimir Gel'man and Otar Marganiya, eds., *Resource Curse and Post-Soviet Eurasia: Oil, Gas, and Modernization*. Lanham, MD: Lexington Books, 97–122.

<sup>22</sup> Gerald Easter. 2008. "The Russian State in the Time of Putin." *Post-Soviet Affairs* 24: 3: 199–230; Brian Taylor. 2011. *State Building in Putin's Russia: Policing and Coercion after Communism*. Cambridge: Cambridge University Press.

<sup>23</sup> Scott Gehlbach. 2010. "Reflections on Putin and the Media." *Post-Soviet Affairs* 26: 1: 77–87; Maria Lipman and Michael McFaul. 2003. "Putin and the Media." In Dale R. Hespington, ed., *Putin's Russia: Past Imperfect, Future Uncertain*. Lanham, MD: Rowman and Littlefield, 63–84; Olessia Koltsova. 2006. *News Media and Power in Russia*. London: Routledge.

<sup>24</sup> Vladimir Gel'man. 2009. "Leviathan's Return? The Policy of Recentralization in Contemporary Russia." In Cameron Ross and Adrian Campbell, eds., *Federalism and Local Politics in Russia*. London and New York: Routledge, 1–24; Paul Goode. 2011. *The Decline of Regionalism in Putin's Russia*. London: Routledge.

political process lost the element of surprise. The state's monopoly of legitimate violence was restored.<sup>25</sup> Gradually, the country began to emerge from economic crisis: between 1999 and 2008, Russia's GDP almost doubled. In the 2000s, people saw real changes for the better: economic growth,<sup>26</sup> and reduction of "everyday" corruption serving the relations of the population and government (albeit compensated for by the growth of "business" corruption in the relationship between government and business).<sup>27</sup> This move from decline to development was welcomed by the majority of the population,<sup>28</sup> which was tired of "shock therapy," the degradation of the economy and the weakness of state power. Eventually, the government gained widespread electoral support: Vladimir Putin's re-election in 2004 expressed the real will of the citizens. Protest sentiments would not appear until the next decade.<sup>29</sup>

Two circumstances that are characteristic of the 2000s had a serious impact on the dialogue between the government and business. First, the state apparatus grew numerically and professionally.<sup>30</sup> In the 2000s, the share of the working population employed in the management and provision of military security grew annually—from 4.8% in 2000 to 5.8% in 2010.<sup>31</sup> For every 1,000 people employed in the economy, the number of employees of state bodies and local governments was 17.6 people in 2001 and 24.9 in 2009, an indicator that likewise showed annual growth.<sup>32</sup> Control over the activities of the lower levels of the "power vertical" increased and personnel changes took place in key positions in the control

<sup>25</sup> Vadim Volkov. 1999. "Violent Entrepreneurship in Post-Communist Russia." *Europe-Asia Studies* 51: 5: 741-754.

<sup>26</sup> For an overview of Russia's economic development in the 2000s, see, for example Anders Aslund, Sergei Guriev, and Andrew Kuchins, eds. 2010. *Russia After the Global Economic Crisis*. Washington, DC: Peterson Institute for International Economics.

<sup>27</sup> Svetlana Barsukova. 2009. "Corruption. Academic Debates and Russian Reality." *Russian Politics and Law* (July – August): 8-27.

<sup>28</sup> Richard Rose, William Mishler, and Neil Munro. 2011. *Popular Support for an Undemocratic Regime: The Changing Views of Russians*. Cambridge: Cambridge University Press.

<sup>29</sup> Graeme Robertson. 2013. "Protesting Putinism: The Election Protests of 2011–2012 in Broader Perspective." *Problems of Post-Communism* 60: 2: 11–23; Samuel A. Greene. 2013. "Beyond Bolotnaya: Bridging Old and New in Russia's Election Protest Movement." *Problems of Post-Communism* 60: 2: 40–52.

<sup>30</sup> 2015. *Trud i zaniatost' v Rossii—2015: Statisticheskii Sbornik* [Work and Employment in Russia—2015: Statistical Compilation]. Moscow: Rosstat.

<sup>31</sup> During this period (i.e., 2000–2009), the share of people employed in health care remained virtually unchanged (up from 6.8% to 7.0%), while in education it decreased (from 9.3% to 8.8%). See Federal State Statistics Service. 2011. *Srednegodovaia chislenost' i struktura zaniatykh v ekonomike po vidam ekonomicheskoi deiatel'nosti* [Average Annual Number and Structure of Employed in the Economy on Types of Economic Activity]. At [www.gks.ru/bgd/regl/B11\\_36/IssWWW.exe/Stg/d1/03-10.htm](http://www.gks.ru/bgd/regl/B11_36/IssWWW.exe/Stg/d1/03-10.htm), accessed January 9, 2019.

<sup>32</sup> Data from the Federal State Statistics Service. n.d. *Gosudarstvo, obshchestvennye organizatsii* [State, Public Organizations], At [www.gks.ru/wps/wcm/connect/rosstat\\_main/rosstat/ru/statistics/state/#](http://www.gks.ru/wps/wcm/connect/rosstat_main/rosstat/ru/statistics/state/#), accessed January 9, 2019.

and repressive organizations. This did not mean that corruption disappeared among *siloviki*—security, defense, and law enforcement chiefs. On the contrary, their inclusion in the shadow economy became systemic.<sup>33</sup> Yet the Russian power structures had eliminated competitors and monopolized the ability to either solve business problems or deliberately create problems that they were then ready to help get rid of for a bargain price. The state became a machine capable of punishing the unwanted. All in all, the “stick” in the hands of the state was hard to miss.

Second, the state showed big business a “carrot.” In the 2000s, the federal budget of the Russian Federation began to run a surplus, giving government agencies and organizations massive amounts of funds to play with. This situation, a stark contrast from the chronic deficits of the 1990s, was occasioned by the new system of taxing commodities introduced in the 2000s. This system significantly increased payments from oil and gas production, allowing Russia to run a budget surplus of a record 7.5% of GDP in 2005.<sup>34</sup> The surplus persisted until 2009, earning the decade the moniker of the “fat noughties.”

It is quite clear that the strengthened state became not only a source of threats but also a solvent and extremely profitable customer for some businesses, such as construction of infrastructure facilities, equipment supply for municipal hospitals and schools, development of software products for government agencies, etc. The total value of government contracts doubled in the period from 2006 to 2010 (from 2.1 to 4.8 trillion rubles),<sup>35</sup> and this amount did not include the procurement of state-owned enterprises, which became obliged to enter into contracts on a competitive basis only in 2011. Undoubtedly, there was a huge market extremely attractive for business.

Big business’ response to the solvency of the state was quite pragmatic. Shadow schemes for “milking the budget” became widespread as companies found various ways to make corrupt deals with government officials and thus charge state and municipal authorities inflated rates for services. Formally, everything took place in strict accordance with the law and the contract was awarded on a competitive basis. However, auction organizers rather quickly invented technologies that guaranteed the victory to a pre-selected participant.

Often, officials did not even bother to simulate competition. Reference to an “emergency” could exempt officials from the need to hold a competition. Suppose rain flooded a basement. Treating this as an

<sup>33</sup> Anastasiya Maksimova and Leonid Kosals. 2013. “Russian Police Involvement in the Shadow Economy.” *Russian Politics and Law* 51: 4: 48-58.

<sup>34</sup> Federal State Statistics Service. 2008. *Konsolidirovannyy biudzhet Rossiiskoi Federatsii* [Consolidated Budget of the Russian Federation], At [www.gks.ru/bgd/regl/b08\\_51/IssWWW.exe/Stg/02-01.htm](http://www.gks.ru/bgd/regl/b08_51/IssWWW.exe/Stg/02-01.htm), accessed January 9, 2019.

<sup>35</sup> Federal State Statistics Service, *Gosudarstvo, obshchestvennyye organizatsii*.

emergency, officials would contract with a “lapdog” company specially created for such situations to overhaul the building. As the Anti-Corruption Foundation (headed by Alexey Navalny) showed, the average life of companies involved in “emergency situations” was no more than a year.

An official’s remuneration (“payoff”) became an indispensable element in gaining access to government contracts. The state representative who awarded the contract was given a payoff as an informal reward from the company. This reality added a new nuance to Russian historian Nikolai Karamzin’s famous phrase about the specificities of Russia, “They keep stealing!” In the 2000s, it became “They keep stealing but in full accordance with the law.” Payoffs and milking the budget are among the “paradoxical phenomena” that do not contravene the law but comply with it. In print media, “payoffs” were mentioned most frequently in the 2000s.<sup>36</sup>

Over the course of the decade, big business began working with the powers-that-be to collectively “milk the budget.” Shadow tandems of officials and businessmen allowed mutually beneficial use of the law as a tool for implementing informal agreements.<sup>37</sup> Access to government contracts became the way to quick and guaranteed enrichment. According to experts, payoffs made up 30-40% of the value of state contracts, and up to 60% of Ministry of Defense contracts.<sup>38</sup> The caricature of this situation was the image of the two-headed eagle of Russia, which was cut in half by a huge saw.<sup>39</sup>

### “Kings of Government Contracts”: New Roles in the 2010s

Like all things, this situation, too, eventually came to an end. The crisis of 2008 heralded the end of “the fat noughties.” With the exception of 2011, the Russian Federation has had a budget shortfall since 2009. In 2016, it reached 3.4% of GDP. Government departments and lobbying groups found themselves in an intense struggle for access to budget money. Public disclosures and compromising materials became a tool in this competition, as isolated but loud scandals led to the arrests of major officials: governors, mayors and ministers.<sup>40</sup>

For example, in 2012, a corruption scandal broke out in the Ministry

<sup>36</sup> Markku Lonkila. 2011. *Networks in the Russian Market Economy*. Basingstoke: Palgrave.

<sup>37</sup> Vladimir Gel'man. 2004. “The Unrule of Law in the Making: The Politics of Informal Institution Building in Russia.” *Europe-Asia Studies* 56: 7: 1021- 40.

<sup>38</sup> <http://novayagazeta-nn.ru/2011/191/reiting-korrumpirovannostiministerstv-i-vedomstv-rossii-ot-novoi-gazety.html>

<sup>39</sup> See the website of the Anti-Corruption Foundation run by Alexey Navalny. The Fund’s project for controlling the use of budget funds is called “RosPil” (<https://fbk.info/>), a play on the word “raspil.”

<sup>40</sup> Michael Mesquita. 2018. “Kompromat.” In Alena Ledeneva, ed., *The Global Encyclopaedia of Informality: Understanding Social and Cultural Complexity*, Volume 2. London: UCL Press, 435-438.

of Defense of the Russian Federation that led to the resignation of Defense Minister Alexander Serdyukov. The repression machine began to gain momentum. The governor of the Bryansk region was arrested in 2014. The governor of Sakhalin and the head of the Komi Republic were arrested in 2015. The governor of the Kirov region, as well as Minister of Economic Development Alexey Ulukaev were arrested in 2016.<sup>41</sup> The latter was the first arrest of a federal minister in the history of post-Soviet Russia. In 2017, the heads of Udmurtia and Mari-El were arrested. The list goes on; there are dozens of vice-governors, mayors, and heads of regional governments on it.<sup>42</sup>

The population considered these processes evidence that order was being restored in the country. Intriguingly, despite Putin's public condemnation of Stalin's mass repressions and Yeltsin's rhetoric of continuing the Gorbachev reforms, the population thinks about the current president quite differently. In the mass consciousness, Vladimir Putin is perceived as a figure close to Stalin and Lenin and an antagonist to Gorbachev and Yeltsin, who are extremely unpopular in modern Russia.<sup>43</sup>

The rollback of liberal reforms and his self-positioning as a strong and tough politician increased Putin's standing with the public. This is perhaps because Putin's repressions, unlike Stalin's, did not extend to the public at large, but were limited to personnel "shake-ups." Of course, Putin was not exactly in control of these processes—increasing competition for state, financial and administrative resources became an internal driver of repression—but he was able to capitalize on them to gain popular support. According to the Public Opinion Foundation, in 2015 his favorability rating hit its highest mark (72%) since 2000.<sup>44</sup>

In 2013, a new federal law was adopted that tightened the procedure for procurement of goods and services for state and municipal needs (a market valued at about 7 trillion rubles). Control over the use of budget money was greatly strengthened. In 2017, the Accounts Chamber of the

<sup>41</sup> The governor of the Bryansk region was sentenced to 4 years in a penal colony. The Governor of Sakhalin was sentenced to 13 years in prison in a strict regime colony and the Governor of the Kirov region to 8 years. The court sentenced the Minister of Economic Development to 8 years in a penal colony.

<sup>42</sup> The increase in the number of sentences involving deprivation of liberty concerns not only high-ranking officials, but also ordinary citizens. Frequent amnesties are a means of saving the penitentiary system from overcrowding. See: Ella Paneyakh. 2016. "No Room: What Has Changed in Russia's System of Repression During the Past Year." *Russian Politics and Law* 54: 4: 404-413.

<sup>43</sup> Aleksandr Zhavoronkov. 2018. "K probleme obrazov politikov v massovom soznanii (opyt izmereniia za 1999-2016 gg.)" [On the Problem of Images of Politicians in the Mass Consciousness (Measurement Experience for 1999-2016)]. *Sotsiologicheskaya Nauka i Sotsial'naya Praktika* 6: 3: 77-98.

<sup>44</sup> "Elektoral'nyi reiting Putina za 15 let" [Putin's electoral rating for 15 years]. *Argumenty i Fakty*, March 25, 2015, At <http://www.aif.ru/dontknows/infographics/1475392>, accessed January 9, 2019.

Russian Federation found 2.5 times more violations of this law than in the previous year, due not to the deterioration of the situation but to the growing number of audits and the development of audit methods.<sup>45</sup>

Accordingly, the risks of corruption schemes perpetrated with the assistance of officials increased sharply. Some continued to “milk the budget” within the framework of small contracts, hoping that a negligible amount would not be carefully controlled. Others who continued to do it relied on a high degree of administrative protection. But periodic scandals/revelations indicated that businessmen and the officials working with them overestimated the degree of protection. The repressive machine was gaining momentum, spurred by competition for access to budget money.

The general deterioration of the economic situation, caused by the sanctions imposed against Russia, exacerbated the competition for budget funds. Fighting for a place in the sun, the companies actively “poured dirt” on their competitors. This made the previous schemes of “payoffs” and “milking the budget” even more risky for business and state authorities alike.

Gradually, major government contracts moved beyond the market logic of “payoffs” and “milking.” Large state contracts began to be given to business structures close to the government because of their special merits or personal connections with top state officials. Moreover, formal contests and tenders were canceled for particularly large contracts and the contractors were appointed by government decrees.

Such contracts required high-level administrative support. This did not mean that there were no “payoffs” within the framework of such cooperation. Rather, this meant that firms were chosen exclusively among confidants and “trusted” structures close to the government. The administrative resource started superseding the market one.

A kind of contractor club for distributing large state orders was set up, of which one could become a member for providing special services in the political sphere or due to personal relations with President Putin. For example, in 2016, the state obliged owners of large trucks to pay for the wear and tear their trucks caused to the roads. The “Platon” system was created for the collection of fees. The operator of this system was appointed without any competition: it was a company in which a large stake belonged to the son of Arkady Rotenberg, a personal friend of Putin since their days in youth sports. Drivers began to call this fee the “Rotenberg tax”; their strikes were to no avail.

As for Arkady Rotenberg, his company Stroigazmontazh celebrated a milestone in the fall of 2017, when the total amount of the government

<sup>45</sup> Accounting Chamber of the Russian Federation. 2018. *Kontraktnaia sistema v sfere zak-upok trebuetsia optimizatsii* [Procurement Contracting System Requires Optimization], At [http://audit.gov.ru/press\\_center/news/32996](http://audit.gov.ru/press_center/news/32996), accessed January 9, 2019.

contracts it had been awarded since 2011 exceeded 1 trillion rubles. And this is not even counting all the contracts awarded to firms in which he has a stake.<sup>46</sup>

Another, even more ambitious example is associated with the system of labeling products to monitor their turnover. All manufacturers and importers will be required to mark their products. The operator of this system, again appointed without competition, is Alisher Usmanov's company. Usmanov has repeatedly rendered important services to the authorities, such as taking on the funding of the gymnastics program, which regularly wins gold medals in international competitions.

As such, Rotenberg Jr. and Usmanov's companies are allowed to control a huge market with guaranteed profitability. Note that the risks to them are minimal, since the state itself will force drivers to pay for wear and tear to roads or compel manufacturers to apply a label. In other words, the government makes a decision that creates a huge market and appoints these companies to benefit from the market thanks to certain personal relations with representatives of the supreme power. As long as this logic dominates, it will be almost impossible for other players to break into this market. The one-time logic of "milking the budget" with the help of "payoffs" has been transformed into a long-term rent granted by the state.

A new term—"Kings of State Orders"—has appeared in the lexicon of the Russian media. However, the names of these "kings" will soon be hidden from the public, since in 2017 Prime Minister Dmitry Medvedev allowed government customers not to disclose contractors.

One gets the impression that the modern Russian state distributes large orders as generous gifts to especially close firms, guaranteeing these "kings of state orders" huge profits and easy business. This conclusion is extremely common in the opposition media, yet it is erroneous. The situation is more complicated.

The fact is that there are many economically unprofitable and technically complex projects among the government orders, and "the kings" cannot refuse to take them on lest their failure be interpreted as disloyalty to the system. These include projects with a symbolic and political component, such as the Olympic facilities in Sochi, stadiums for the World Cup, or the Federal University on Russian Island in the Far East, where there had previously been nothing but a military base. The companies involved in these contracts may incur losses, the projects are technically complex, and their schedules are demanding. The aforementioned Far Eastern Federal University needed to be designed and built in time for the APEC summit—that is, within three years. Thus, the implementation of such projects is a duty and burden rather than a sinecure. Yet it is a burden that these firms are

<sup>46</sup> For comparison, the annual expenditure of the federal budget for education in 2017 was about half a trillion rubles and for defense about a trillion rubles.

willing to take on in order to remain part of the narrow circle of firms that the government allows to actively develop and be a leader in their industry.

Recall the largest state contract in the history of post-Soviet Russia: for the construction of the Crimean bridge, which cost 228 billion rubles (in 2015 prices). This contract went to Arkady Rotenberg's company, prompting the opposition to reproach the authorities for once again giving money to "the confidants." But what the opposition failed to mention is that there were no others who wanted to build the Crimean Bridge. Presumably, the other major construction firms breathed a sigh of relief upon learning that this task had not been assigned to them. In addition to the enormous technical difficulties and tight deadlines, participation in this construction meant a "black spot" on one's global record, as the international community does not recognize Russia's right to Crimea. No wonder, then, that this contract was awarded on the orders of the government; likely no one would have entered a competition for it.

Another example is the construction of stadiums for the World Cup. These stadiums were built by the Crocus Group company in Rostov-on-Don and Kaliningrad, which specialized in the construction of shopping and entertainment complexes and had built sports facilities before. In an interview with the business channel, the head of the Crocus Group, Aras Agalarov, said that he could not refuse those projects since his partnership with the state was formalized as a government order. A public-private partnership was mandatory for his business.

The businessman described these contracts as "Lenin's *subbotnik*" (voluntary unpaid work performed on a Saturday). The stadiums were built on time; Crocus Group did not receive any financial benefits. The businessman publicly expressed the hope that he would not be forced to take control of these stadiums, since he estimated that they would be unprofitable.<sup>47</sup> However, he is unlikely to dare to refuse if this happens.

Evidently, the state determines important objects (sports facilities, the Crimean bridge, a university on a distant island, etc.), and then, under the guise of a public-private partnership, it transfers part of the costs to business. In the best-case scenario, some costs will be compensated later, but there will be no profit, of course. The mobilization of business to solve one task or another takes place in the form of a non-competitive "order" or "appointment." "Kings of State Orders" cannot refuse when the government wants to enter into a public-private partnership with them.

Any large business engages in many practices that teeter on the edge

<sup>47</sup> As the head of the company that built the stadiums for the World Cup said: "I only get into such situations on some errands. I don't take part in state tenders... It's just another break-even clean-up ... it's impossible to make money on it." See "Agalarov-RBK: 'Stroitel'stvo stadionov bylo ochen' riskovannoi istoriei'" [Agalarov-RBK: The Construction of the Stadiums Was a Very Risky Business]. *RBK*, April 9, 2018, At <https://www.rbc.ru/interview/business/09/04/2018/5ac4c8869a79472ab1f1b3e0>, accessed January 9, 2019.

of legality or even cross this line. Thus, a motive for repression is easy to find. But it is impossible to simultaneously punish all the businesses that are breaking a law. Sanctions are therefore applied selectively and according to criteria that are outside the legal system. These criteria are often political, relating to the business-government relationship. The refusal to participate in a public-private partnership can cause major problems for any business. It will be punished on strict formal grounds and there will not be not a single formal document indicating that this repression is due to the failure to execute a state contract. A public-private partnership is therefore becoming a kind of tax that big business has to pay in order to get the green light in its business sphere. Government contracts can be a burden for a business, but they guarantee the preservation and development of other, more profitable parts of the business.

Businesses who execute unprofitable government contracts may also be rewarded with preferential treatment or profitable contracts with guaranteed returns. Arkady Rotenberg built the Crimean bridge and his son was given the lucrative contract for servicing the “Platon” system. It can be assumed that in the event that Rotenberg Sr. had refused to participate in the construction of the bridge, the state authorities would quickly have found grounds for withdrawing the “Platon” system from his son.

Thus, government contracts are divided into two groups: contracts-obligations, which are a kind of tax on big business and contracts-rewards, bestowed for loyalty to the system. The former give individuals the right to remain in the group of successful entrepreneurs. The latter provide an opportunity to enter a profitable market created and patronized by the state.

The logic of coercive public-private partnerships is operational not only at the federal level. It is also reproduced at the regional level. The projects involved in the partnerships at this level are less well-known, and smaller businesses are in charge of implementing them. But the general model of relations between the regional authorities and local business is a wholesale copy of relations at the federal level. Governors gather representatives of local businesses and announce to them what projects they should implement in the region, in what time frame, and with what budget funds. Sometimes such offers of cooperation are beneficial for business, sometimes businesses break even, and sometimes they are entirely unprofitable. But businessmen almost never refuse to participate in such projects either as investors or as direct executors, aware as they are of the consequences of such a refusal.

We have therefore delineated three distinct stages in the relationship between government and big business in the post-Soviet history of Russia. These correspond broadly to the 1990s, 2000s, and 2010s, with their main “heroes” being the oligarchs, the participants in “milking” the budget, and “Kings of State Orders,” respectively (see Table 1). Of course, the division

**Table 1. Change in informal relations between the government and big business**

	Oligarchs	Participants in “milking” the budget	“Kings of State Orders”
Period	1990s	2000s	2010s
Type of business	Govern the state in the interests of their own business	“Milking” budget money (implementation of contracts at inflated prices)	Executing big government contracts within the framework of a public-private partnership
Relations with state authorities	“State Capture”; reduction of the state authorities to the role of puppets	Shadow collusion with the state authorities; “payoffs”	Demonstrative loyalty and participation in economically unprofitable projects
Degree of voluntariness for business	Voluntary	Voluntary	Voluntary-compulsory
Profitability for business	Unprecedented opportunities for enrichment at the expense of “privatization of the state”	Profitability of “milking” a budget depends on the value of the contract and the agreed “payback” amount	Government contracts may be unprofitable for business, but their implementation is a necessary condition for good relations with the authorities. That may result in a reward in the form of profitable contracts. But the main reward is heading off state repression.
Formal procedure	Lobbying laws and appointing “loyal” people to state positions	Formal execution imitating contests, where the winner is determined in advance during a shadow conspiracy or a contract is given to a firm without competition by reference to an “emergency” situation	The government appoints contractors
Dominating subject (business or state)	Business	Equal	State
Way to join the group	Financial support of Boris Yeltsin’s regime	Social relations with government authorities; market competition based on the amount of “payoff”	Personal ties with Vladimir Putin and a narrow circle of the most influential officials

into decades is conditional: “tipping points” did not necessarily fall on the eve of each decade. For example, the 1998 default and the 2008 global financial crisis played a significant role in further changes. However, with some nuance, such a division is justified, since the combination of factors gave these decades clear distinctions in terms of relations between government and business.

## Conclusion

Changes in the informal practices governing the business-state relationship in post-Soviet Russia not only took place during the transition from Yeltsin to Putin but have also occurred over the course of Putin’s long reign.

In the 1990s, under Boris Yeltsin, the “seizure of the state” by a large oligarch class led to disastrous consequences. A weak power unpopular with the population handed over political management to big capital in exchange for financial support. The population was disappointed in the reforms and supported the new course of “consolidation of statehood” charted by Vladimir Putin.

The changes of the 2000s are associated not only with the political will of Vladimir Putin, but also with the new administrative and financial capabilities of the state. GDP growth and budget surplus created a favorable background for strengthening the state’s position in its dialogue with business. The state apparatus grew numerically and professionally. The oligarchs were distanced from important political decisions. However, the growth of the administrative and financial capabilities of the state opened the floodgates to “milking the budget.” The practice of “payoffs” became the main form of cooperation between big business and the state.

In the 2010s, economic growth slowed and federal funds once again became limited. Russia’s international isolation led to a deterioration in the business climate and a bitter struggle for access to budget resources. One form of competition was accusations of corruption, which made the practice of “milking the budget” more risky for officials and business alike. The arrests of governors, mayors, and high-level officials became regular occurrences. The people associated these arrests with the uncompromising Vladimir Putin, making him even more popular.

As a result, big state orders began to be handed out outside the framework of “milking,” given to a narrow circle of trusted firms, the so-called “Kings of State Orders.” Such companies are not selected during a competitive process but are appointed by government decree. These projects may be extremely profitable or extremely unprofitable, but the business almost always agrees to carry out the task entrusted to it. Public-private partnership has become a duty for business, in gratitude for which the government refrains from repressing them and even rewards them with

more profitable projects.

Big business has evolved from the omnipotent oligarchs to the “kings of state orders” with whom the state shares the burden and profit of a public-private partnership. If the oligarchs dictated their requirements to the state authorities, then the “kings of state orders” obediently implement the projects they are appointed by government decree.

In general, modern Russia is struggling to legalize the economy. The external attributes of this process are all in evidence: the growth of repression, the expansion of the powers of the tax service, legislative innovations that facilitate the legalization of business, etc. In a textbook paradox, the result of the latest round of the struggle for legalization has been the formation of a new set of informal rules.<sup>48</sup> The tightening of requirements for the legal activities of big business has generated new informal practices for cooperating with the authorities. Big business in Russia is forced to admit that the formal ownership of private property does not guarantee anything; state power alone disposes of everything and everyone.<sup>49</sup>

Periodically, the government needs the potential of the market and allows it to develop. But as soon as market initiative begins to bear fruit in the form of an increase in the resource base, the authorities return their positions. In Russia, the principles of a market and administrative economy coexist diachronically—that is, the periodic and brief triumph of the market gives way to a long-term and controlled distribution of resources by the authorities.<sup>50</sup> Formally, the existing market institutions mutate from the inside and change their content, retaining only the facade. This cyclical nature of Russian history causes it to resemble a kind of “Groundhog Day.”

<sup>48</sup> Alejandro Portes. 1994. “The Informal Economy and Its Paradoxes.” In N.J. Smelser and R. Swedberg, eds., *The Handbook of the Economic Sociology*. Princeton, NJ, and New York: Princeton University Press and the Russell Sage Foundation, 426–49.

<sup>49</sup> Simon Kordonsky. 2016. *Socio-Economic Foundations of the Russian Post-Soviet Regime*. Stuttgart: Ibidem-Verlag.

<sup>50</sup> Svetlana Kirdina. 2014. “Institutional Matrices Theory, or X&Y Theory: The Main Provisions and Applications.” *Journal of Institutional Studies* 6: 3: 15-33.

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