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*The review provides a detailed analysis of main trends in Russia's economy in 2009. The paper contains five big sections that highlight single aspects of Russia's economic development: the socio-political context; the monetary and credit and financial spheres; the real sector; social sphere; institutional challenges. The paper employs a huge mass of statistical data that forms the basis of original computation and numerous charts.*

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## Alexander Radygin, Georgy Malginov

### Property Relations and Role of the Public Sector and Privatization

#### 5.1.1. The size, integral components and main features of the public sector

Last year the Russian economy developed in a crisis situation, and this resulted in a delay in passing a successive privatization program. In 2009 this document was approved as late as the end of November while during six previous years privatization programs were usually approved late summer – early autumn<sup>1</sup>.

The Forecast privatization plan (program) of federal property for 2010 and the main trends of federal property privatization for 2011 and 2012 approved by the respective Resolution of the RF Government of November 30, 2009 No 1805-r, as the previous similar documents contained data on the number of unitary enterprises in federal ownership (FGUPs) and joint-stock companies with the share of the Russian Federation in their capital at the beginning of the calendar year only. Therefore we do not have sufficient information yet to assess objectively the dynamics of these components of the public sector in 2009. Let us review in detail the changes that occurred in the key categories of the business entities in federal ownership.

#### *Federal government unitary enterprises*

Dynamics and the sector structure of FGUPs in 2004 – 2008 are tabled below. In 2008 the total number of unitary enterprises in federal ownership reduced by 1/3 (almost 2,000 enterprises) and amounted to 3.8 thousand entities by early 2009. Such reduction of the sector was the largest one during recent years (for comparison: the number of the unitary enterprises reduced by 1/10 or by less than 1,500 from June 1, 2006 to January 1, 2008).

Table 1

#### Dynamics and the sector structure of the federal government unitary enterprises in 2005 – 2008

Sector	As of June 1, 2005		As of June 1, 2006		As of January 1, 2007		As of January 1, 2008.		As of January 1, 2009	
	units	%	units	%	units	%	units	%	units	%
Non-productive sectors	3617	43,6	1817	25,3	1670	25,6	1151	20,2	988	26,25
Industry	1870	22,55	1624	22,6	1539	23,55	1744*	30,5	476	12,65
Agriculture	1111	13,4	913	12,7	826	12,65	618	10,8	611	16,2
Construction	903	10,9	752	10,5	668	10,2	...	...	300	8,0
Transport & Communications	725	8,75	612	8,55	536	8,2	409	7,2	249	6,6
Forestry	67	0,8	53	0,75	49	0,75	37	0,65	...	...
Other sectors	–	–	1407	19,6	1245	19,05	1750	30,65	1141	30,3
Total	8293	100,0	7178	100,0	6533	100,0	5709	100,0	3765	100,0

\* –industry plus construction .

Source: 2006 Forecast plan (program) of federal property privatization and the main trends of federal property privatization for 2006 – 2008; 2007 Forecast plan (program) of federal property privatization and the main trends of federal property privatization for 2007–2009; 2008 Forecast plan (program) of federal property privatization

<sup>1</sup> The Forecast plan (program) of federal property privatization for 2008 was the only exception as well the main trends of development of federal property privatization for 2008 – 2010 approved in spring 2007.

zation and the main trends of federal property privatization for 2008 – 2010; 2009 Forecast plan (program) of federal property privatization and the main trends of federal property privatization for 2010 and 2011; 2010 Forecast plan (program) of federal property privatization and the main trends of federal property privatization for 2011 and 2012; calculations made by the authors.

Early 2009 the enterprises in the category of “other sectors” that were not included in the base classification (30.3% of the total number of FGUPs) remained the most numerous category in the FGUP sector structure. The non-productive sectors (26.3%), agriculture (16.2%) and industry (12.7%) were largely represented; 8% of FGUPs represented construction and 6.6% - transport and communications.

In 2008 a sharp decline of the absolute number and share of enterprises in the industry and construction manifested a major trend of changes in the FGUP sector structure. If early 2008 30.5% of the federal unitary enterprises were in the industry and construction, a year after this figure dropped to 20.7%. The reduction of the share of the transport and communications sector was insufficient: from 7.2% down to 6.6%. The specific weight of the non-productive sector and agriculture increased by 5-6 per cent points.

The dynamics of FGUPs number by sectors illustrates well the size of the shift in the FGUP sector structure. Thus, for two years between January 1, 2007 and January 1, 2009<sup>1</sup> the absolute number of the unitary enterprises in the industry reduced by 3.2 times, in the construction, transport and communications sectors by 2.2 times while in the non-productive sectors by 1.7 times, in agriculture – by 1.35 times and in other sectors (outside the base classification) by 1.1 times.

#### *Joint-stock companies (JSC) in federal ownership*

It is worth noticing that by early 2009 the number of JSC which shares were owned by the federal government reduced by more than 9% (or by 337 companies) vs early 2008; thus their number was 3,3337 companies which is the lowest figure for the entire period 1999 to 2008.

Now let us review the dynamics of the number of JSC which shares were owned by the federal government for the last years, by sectors (see *Table 2*).

*Table 2*

#### **Dynamics and sector structure of the joint-stock companies which shares are in federal ownership or in relation to which a special “golden share” right is used, in 2005 through 2008**

Sector	As of June 1, 2005		As of June 1, 2006		As of January 1, 2007		As of January 1, 2008		As of January 1, 2009	
	unit	%	unit	%	unit	%	unit	%	unit	%
Non-productive sectors	685	18.1	356	9.6	405	10.1	638	17.4	383	11.5
Industry	2078	54.9	1772	47.6	1797	44.95	1878*	51.1	1583	47.45
Agriculture	287	7.6	380	10.2	404	10.1	...	...	234	7.0
Construction	459	12.1	396	10.6	353	8.9	397	10.8	280	8.4
Transport & Communications	229	6.1	363	9.7	534	13.35	761	20.7	522	15.65
Forestry	45	1.2	99	2.7	88	2.2	–	–	...	...
Other sectors	–	–	358	9.6	416	10.4	–	–	335	10.0
Total	3783	100.0	3724	100.0	3997	100.0	3674	100.0	3337	100.0

\* – including industry and construction (695 units or 18.9%), fuel and energy complex (597 units or 16.25%) and military industrial complex (586 units or 15.95%).

Source: 2006 Forecast plan (program) of federal property privatization and the main trends of federal property

<sup>1</sup> The selection of the two-year interval between January 1, 2007 and January 1, 2009 was justified by that early 2008 the industry and construction were quite pronounced in the FGUP sector structure; this impedes making correct comparison of the FGUP structure as of early 2008 and early 2009. Besides in the 2009 data forestry is not segregated.

privatization for 2006 – 2008; 2007 Forecast plan (program) of federal property privatization and the main trends of federal property privatization for 2007–2009; 2008 Forecast plan (program) of federal property privatization and the main trends of federal property privatization for 2008 – 2010; 2009 Forecast plan (program) of federal property privatization and the main trends of federal property privatization for 2010 and 2011; 2010 Forecast plan (program) of federal property privatization and the main trends of federal property privatization for 2011 and 2012; calculations made by the authors.

As of the beginning of 2009, in the JSC sector structure (federally owned) the largest weight was that of industrial enterprises (about 47.5% of all the JSC). The industry was followed by agriculture (15.7%), non-productive sectors (11.5%) and other sectors (10%). The total weight of the construction, transport and communications sectors was less than 10%.

While speaking about changes in the JSC sector structure which shares are federally owned, one can notice a pronounced increase of the share of industry and agriculture (2.5 and 2.4 per cent points accordingly) in 2007-2008.<sup>1</sup> The specific weight of the non-productive sectors was somewhat less pronounced (by 1.4) while the share of construction, transport and communications, and other sectors in the general JSC structure with federally owned stocks decreased; mostly in construction (by more than 3 points).

Distribution of JSC with the state participation depending on the federally owned share is another important feature of such JSC (*Table 3*).

*Table 3*

**Dynamics and the structure of joint-stock companies with the government participation in 1999 – 2008 (including the use of the “golden share” right) with account of the government share size**

Date	Total		by 25%		25 to 50%		50 to 100 %		100%		«Golden share»	
	unit	%	unit	%	unit	%	unit	%	unit	%	total	No shares
1999 г.	3316/ 3896*	100	863	26.0	1601	48.3	470	14.2	382	11.5	580**	
January 1, 2001	3524***	100	1746	49.55	1211	34.4	506	14.35	61	1.7	...	...
August 2001	3949 ****	100	1843	46.7	1393	35.3	625	15.8	88	2.2	542**	
January 1, 2002	4407	100	2270	51.5	1401	31.8	646	14.65	90	2.05	750**	
January 1, 2003	4222 *****	100	2152	51.0	1382	32.7	589	13.95	99	2.35	1076	118
June 1, 2003	4205	100	2148	51.1	1339	31.8	600	14.3	118	2.8	...	...
October 1, 2003	4035	100	2051	50.8	1308	32.4	552	13.7	124	3.1	640	148
January 1, 2004	3704	100	1769	47.75	1235	33.35	540	14.6	160	4.3	591	251
June 1, 2004	3905	100	1950	49.9	1183	30.3	499	12.8	273	7.0	...	...
March 1, 2005	4075/ 3791#	100	1697	44.8	1154	30.4	487	12.85	453	11.95	...	284
June 1, 2005	3783/ 3524##	100	1544	43.8	1093	31.0	474	13.5	413	11.7	...	259
June 1, 2006	3724/ 3481###	100	1063	30.5	885	25.4	397	11.4	1136	32.6	...	243
January 1, 2007	3997/ 3816###	100	932	24.4	814	21.3	368	9.6	1702	44.6	...	181
January 1, 2008	3674	100	771	21.0	645	17.6	269	7.3	1989	54.1	...	...
January 1, 2009	3337	100	769	23.0	510	15.3	200	6.0	1858	55.7	...	...

<sup>1</sup> The selection of the two-year interval between January 1, 2007 and January 1, 2009 was justified by that at the beginning of 2008 in the JSC sector structure (with federal ownership of stocks) the group of other sectors was absent; at the same time the industry and construction (jointly), fuel and energy complex and military industrial complex were quite marked. This makes difficult reasonable comparison of the JSC structure with federal blocks of stocks as of early 2008 and early 2009. Besides forestry ceased being shown separately after 2007.

\* – The Concept of management of the state property and privatization in 1999 mentions 3,896 business entities (including 3611 OJSC, 251 CJSC and 34 LTD and LLC), in which capital the federal government participates. 3316 units is an estimate and a result of summarizing the blocks of shares of various size mentioned in the Concept;

\*\* – total number of JSC using the “golden share” special right; JSC with no government share are not shown separately;

\*\*\* – JSC without consideration of 48 interests and blocks of shares in foreign companies; data are available that Russia owns 119 interests, shares and blocks of shares in foreign companies which book value is \$1.4 bln;

\*\*\*\* – the data from the draft Privatization program for 2002 presented by federal Ministry of Property to the federal government; according to the data of the Ministry of Property Register, 4308 blocks of JSC shares were federally owned as of September 1, 2001;

\*\*\*\*\* – only open joint-stock companies with no account of 118 OJSC where the special “golden share” right was used (no shares available), blocks of shares of 102 JSC transferred to FGUP Rosspirtprom for operational management, 75 CJSC and interests in the LLC charter capitals, transferred by the RF Government Regulation of April 2, 2002 No 454-r “On the termination of state participation in the charter capitals of credit organizations” or received in the form of succession, gift or on other grounds;

# 3791 units is an estimated number of JSC which shares are federally owned, with no account of 284 JSC where the special “golden share” right is used (with no block of shares available). The weight of a JSC with a particular share in the capital for comparison with the previous period data is calculated based on this number. For reference: as of January 1, 2005, the shares of 3767 JSC were federally owned not considering the above 284 JSC with the “golden share” and interests in the charter capitals of 24 LLC companies transferred to the treasury following the RF Government Regulation of April 2, 2002 No 454-r “On the termination of state participation in the charter capitals of credit organizations”;

## – the calculated number of JSC which shares are federally owned; with no account of the JSC where the special “golden share” right is used. The weight of a JSC with a particular share in the capital for comparison with the previous period data is calculated based on this number.

*Source:* www.mgi.ru; Russian economy in 2001. Trends and prospects (Edition 23) Vol. 2 M, IEPP, March 2002, p. 62; A. A. Braverman. On measures to improve efficiency of federal property management and the criteria of its evaluation. //Bulletin of the Ministry of Property of Russia. 2003. No 1, p. 13-14. Enterprises with the state participation. Institutional and legal aspects and economic efficiency. Series “Scientific reports: independent economic analysis. № 155. M.: Moscow Public Research Foundation.; Association of Researchers of the public sector economy, 2004, p. 47; 2004 Federal Property Privatization Program and main trends of federal property privatization by 2006// Bulletin of the Ministry of Property of Russia. 2003. No 3. p. 4–5. Key problems of improving management efficiency of federal property and main directions of the dividend policy of the Russian federation// Bulletin of the Ministry of Property of Russia. 2003. No 4. p. 8; V, Andrianov. Russia in global economy// Society and Economy 2003, No 11, p. 84.; 2005 Federal Property Privatization Program// Materials for the RF Government meeting on March 17, 2005 “On measures to improve management efficiency of federal property; 2006 Forecast plan (program) of federal property privatization and the main trends of federal property privatization for 2006 – 2008; 2007 Forecast plan (program) of federal property privatization and the main trends of federal property privatization for 2007–2009; 2008 Forecast plan (program) of federal property privatization and the main trends of federal property privatization for 2008 – 2010; 2009 Forecast plan (program) of federal property privatization and the main trends of federal property privatization for 2010 and 2011; 2010 Forecast plan (program) of federal property privatization and the main trends of federal property privatization for 2011 and 2012; calculations made by the authors.

The number of the FGUPs to be incorporated has been constantly growing, however the mid-2005 trend of increasing share of blocks of shares that would help the government to exercise a full-fledged corporate control due to a sharp growth of the number of full (100% shares) blocks ceased gradually and did not develop further in 2008.

As of January 1, 2009, likewise early 2008, the government was able to exercise a majority or complete control in more than 61% of all the companies. The share of the minority stakes (up to 25% of the capital) has been growing in the overall structure of the federally owned stocks while the share of blocking (25% to 50%) or majority stakes (over 50% but under 100%) was decreasing.

The absolute number of minority stakes in federal ownership has changed insignificantly while the number of blocking and majority stakes reduced obviously: by more than 1/5 and 1/4 accordingly. This trend affected the full stakes to a lesser degree and the number of full stakes reduced by 6.5%.

Rosstat monitoring is another source of data about the growth of the public sector<sup>1</sup>. According to Rosstat, the growth dynamics of business entities in 2008 and in 1H of 2009 developed as follows (*Table 4*).

*Table 4*

**Number of enterprises in the public sector of economy registered by territorial divisions of the Federal Property Management Agency and the Property Management Agencies of the RF subjects in 2008 – 2009**

Date	Total*	GUPs -State unitary enterprises- including treasury enterprises	Government agencies	Business entities which charter capital has over 50% of shares in	
				federal ownership	in ownership of business entities that operate in the public sector of economy
As of January 1, 2008	80570	10598	64440	4111	1410
As of July 1, 2008	77461**	9864	62571	3930	1089
As of January 1, 2009	75878**	9144	61831	3795	1101
As of July 1, 2009	77082**	8706	63019	4007	1350

\* – including organizations which foundation documents after registration in government authorities do not specify types of activities, but excluding joint-stock companies in which more than 50% of shares (stakes) are in joint federal and foreign ownership; the total number of public sector entities can exceed the number of GUPs, institutions and business entities;

\*\* – federal property is registered under Resolution of the RF Government of July 16, 2007 No 447 “On improvement of registration of federal property”;

Source: On the development of the public sector of economy of the Russian Federation in 2007. M., ROSSTAT, 2008, p. 123. On the development of the public sector of economy of the Russian Federation in 1H 2008, M., ROSSTAT, 2008, p. 87; On the development of the public sector of economy of the Russian Federation in 2008. M., ROSSTAT, 2009, p. 7.; On the development of the public sector of economy of the Russian Federation in 1H 2009. M., ROSSTAT, 2009, p. 7.

In general the number of organizations of the public sector of economy decreased by 5.8% in 2008; however in 1H 2008 it grew by 1.6%. As a result, as of mid-2009 this number roughly corresponded to the similar indicator a year ago – July 1, 2008.

The development dynamics varies by different sub-sectors of the public sector. The number of state unitary enterprises was going down (a stable trend): in 2008 – by 13.7%, in January-June 2009 – by 4.8% (for the year and a half - by 17.9%).

At the same time the number of state enterprises having reduced by 4% in 2008 grew up by 1.9% in 1H 2009. Those business entities in which charter capital more than 50% shares (stakes) are owned by the government demonstrated a similar trend. In 2008 this figure went down by 7.7% while in January-June 2009 it went up by 5.6%. In 2008 the number of business entities in which charter capital more than 50% shares (stakes) are owned by the public business entities dropped most dramatically as compared to other categories of companies in

<sup>1</sup> According to Resolution of the RF Government of January 4, 1999 No 1, Rosstat includes the following business entities of the federal and regional levels: (1) state unitary enterprises under the right of operating and economic control; (2) state institutions; (3) business entities which charter capital has over 50% (stakes) in federal ownership; (4) business entities which charter capital has over 50% of shares (stakes) in the ownership of business entities in the public sector.

the public sector (almost by 22%), however in 1H 2009 it went up also dramatically by 22.6%.

#### 5.1.2. Mid-term privatization plans

While considering the Forecast plan (program) of federal property privatization for 2010 and the main trends of federal property privatization for 2011 and 2012 approved by RF Government Resolution of November 30, 2009, No 1805-r, certain variations from the similar documents of the previous years can be noted.

Primarily this relates to the financial and economic crisis situation where a regular privatization program was approved.

The Program did not appear by the end of summer thus breaking the established tradition, and autumn announcements by the competent Russian officials of the possibility to expand 2010 Privatization program vs the initial version with the expected budget revenues from privatization of RUR7.1 bln<sup>1</sup> in a new context of budget deficit (the first deficit since early 2000'es) demonstrated a forced backslide to using privatization tools for recharging the budget exactly as it was done in the 1990'es.

Nevertheless, in spite of the ambitious statements on the initiation of a new wave of privatization and initial optimistic estimates (the federal budget was expected to receive RUR 100 bln from sales of the state property in 2010) 2010-2012 Privatization program does not look too radical.

The following issues should be pointed out in this document.

Firstly it has another reference to the official government document that sets development shapes for the future – Main directions of activity of the Russian Federation Government for the period ending 2012 approved by Resolution of the RF Government of November 17, 2008 No 1663-r<sup>2</sup> where it states that *by 2012 the public sector will reduce, the composition of the state property will conform to the authorities and functions of the state and structural changes in the respective sectors of economy; the work will be continued to reduce the list of strategic enterprises that are not subject to privatization; the process of corporatization (converting enterprises into joint-stock companies) of federal unitary enterprises that are not necessary for exercising public authorities will be completed.*

With account of the above, in 2010 – 2012 the work will continue to remove restrictions on privatization of certain types of federal property that have lost their relevance, and to reduce the number of strategic enterprises and joint-stock companies according to the decisions of the President of Russia. A most acceptable and efficient method of management of these property and enterprises including their privatization will be determined.

Secondly, among the objectives of the government policy for federal property privatization in 2010-2012, in addition to the traditional objectives there is a target to create environment for getting off-budget investments for joint-stock companies development.

This means a much broader application of the mechanism of charter capital increase in the open joint-stock companies established in the process of privatization which 25% or more shares are owned by federal or municipal authorities, while keeping the threshold limits for

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<sup>1</sup> M. Momot. Large clearance. V. RBK, No 11, 2009, p.46-51. .

<sup>2</sup> The main directions of activity of the Government of the Russian Federation for the period ending 2012 address mainly implementation of the first stage of the Concept of the long-term economic and social development of the Russian Federation for the period ending 2020.



the state owned shares. This procedure was defined in 2006, and the effective Law on privatization was amended accordingly.

Rosgosstrakh company (the government share is 25%) is a good example of such scheme: the company was excluded from the list of strategic JSC by Decree of the President of Russia in September 2009. The Decree points out that the RF Government may well take a further decision to increase the charter capital of the company provided the government stake remains to be at least 13.1% of votes at the general shareholders meeting with a possibility to consider the use of a special right of the Russian Federation to participate in the company management (“golden share”).

Thirdly, the current Privatization program mentions major facilities in federal ownership subject to privatization as it was done in the similar documents for 2007 and 2008. Such major (budget-making) facilities subject to privatization are stakes of such open joint-stock companies as TGK-5, Rosgostrakh, Moscow Metrostroi, Iskitimcement (Novosibirsk region), Tyretsky Solerudnik (Irkutsk region)<sup>1</sup>.

Besides, to raise additional revenues to the federal budget, the RF Government may pass resolutions to privatize blocks of shares of companies that are highly attractive for investors. As the document suggests, such are the shares of sea and river ports, shipping and steamship companies including the stock of OJSC “Modern Commercial Fleet (not more than 25% minus 1 share from the federally owned stock), Murmansk Sea Commercial Port, Novorossiysk Sea Commercial Port, Anapa Airport (Krasnodar Krai) Koltsovo Airport (Ekaterinburg) (Tolmachevo Airport (Novosibirsk))<sup>2</sup>.

A necessary condition for this is Resolution of Russia’s President on termination or reduction of the participation share of the Russian Federation in management of the joint-stock companies included in the list of strategic enterprises and JSC.

The presence in the list of the airports, sea and river ports as potential objects for privatization<sup>3</sup> follows the recent trend when certain restrictions emerged to include in privatization the enterprises in traditional sectors of production (primarily in industry where integrated entities were actively built up); attempts were made to raise private capital for infrastructure development. It is enough mentioning the sale of full stakes (100%) of the Sochi and Tyumen airports, and identification of the Ufa and Salekhard airports as major targets of privatization in the 2007 Forecast plan (program) of federal property privatization and the main directions of federal property privatization for 2007-2009.

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<sup>1</sup> In the final version of the 2010 Privatization program there is no OJSC SG-Trans which is a larger railway shipper of liquid gases. It was planned to auction this company in 1H 2010 with expected revenue of RUR 8 bln.

SG-Trans privatization was planned in 2006, however it failed because a larger part of the company’s property was not registered (for ownership). At the end of 2007 RFFI assessed 100% shares of the shipper owned by the government as worth RUR14.8 bln. Moscow Metrostroi was also included in the Privatization Plan earlier.

<sup>2</sup> Tuapse and Vanino sea commercial ports and several shipping companies (Murmansk, North-West, Volga, Enisei and Sakhalin) were also mentioned as possible facilities for privatization though they were not included in the Privatization program.

<sup>3</sup> An object for privatization in such cases is the airport terminal building or the property for rendering services by the sea terminal operators since the facilities used for supporting air or sea traffic, etc. are included in the property list not subject to privatization which are used by specialized government enterprises (FGUPs “State Corporation for Air Traffic Organization in the Russian Federation”, “Administration of Civil Airports (Flying Fields), Rosmorport, Administrations of Sea Ports that are deemed agencies).

Expectations associated with allocation of budget funds for modernization and construction of airports and primarily their flying fields were a significant factor that heated up the interest of the Russian business to invest in the airports. More serious budget limitations that are expected in coming years may strongly change this motivation and complicate the government search of investors. Another incentive for inclusion of sea and river ports in the Privatization program was, possibly, the size of the government stake in the capital which in many cases does not exceed the size of control stake.

Fourthly, for the first time in recent years after the current Law on privatization was enforced in 2002, and the government began approving annual Forecasted privatization plans (programs) the document under review does not contain a nominal list of federal unitary enterprises (FGUPs) to be privatized.

As in the similar documents of some previous years, the document states that in 2010 – 2012 those FGUPs that do not support the government functions of the Russian Federation will be privatized. About 250 FGUPs are to be privatized in 2010; their privatization procedures began in 2009.

If the President of Russia takes a respective decision in 2010, FGUPs that are excluded from the list of strategic enterprises including those that are parts of vertically integrated structures in the strategic sectors of economy may be converted into joint-stock companies; moreover, newly formed JSC may be re-included in such strategic list.

Literal understanding of this aspect gives grounds to assume that in the current year the privatization process (de facto, mainly, in the form of corporatization) of unitary federal enterprises in terms of their range expansion will slow down except for the earlier initiated procedures that would be brought to their logical end.

The other parameters of the Privatization program are as follows.

In 2010–2012 the blocks of shares of joint-stock companies established in the process of conversion of federal government unitary enterprises including those incorporated under the 2009 Forecast plan (program) of federal property privatization will be offered for sale except strategic JSC that are in the list of strategic joint-stock companies or participate in the formation of integrated structures.

In 2010 the following stakes will be offered for sale:

- blocks of shares which do not exceed 50% of the charter capital of the respective joint-stock companies except blocks of shares of strategic JSC or JSC participating in the formation of integrated structures;
- blocks of shares of joint-stock companies in construction, agriculture, chemical, petrochemical and polygraphic industries, public road system, geology, water and air transport, machine engineering, etc. (except strategic companies +JSC).

The work on establishment of integrated structures in the strategic sectors of economy using as a basis joint-stock companies which shares are in federal ownership will continue in 2010–2012.

The shares of 449 JSC and 56 property facilities of the Russian Federation Treasury including real estate, sea and river vessels are included in the 2010 Forecast plan of privatization approved by the RF Government.

By comparing the data describing the 2010 Forecast plan (program) of privatization and the data results of implementation of the previous Privatization plans (*Table 5*), one can state that in general its quantitative indicators are far from their maximum values reached in the middle of 2000's.

Table 5

**Benchmarking of the privatization dynamics of the federal government unitary enterprises and federal blocks of shares in 2000 – 2008**

Period	Number of privatized enterprises in federal ownership (Federal Property Management Agency data, before 2004 – RF Ministry of Property data)	
	FGUPs privatized <sup>1</sup>	JSC blocks of shares sold
2000	2	320
2001	5	125 <sup>2</sup>
2002	102	112 <sup>2</sup>
2003	571 <sup>3</sup>	630
2004	525	596 <sup>4</sup>
2005	741	521 <sup>5</sup>
2006	...	356 <sup>6</sup>
2007	377	377
2008	213	209 <sup>7</sup>

<sup>1</sup> – all preparations completed and decisions on privatization terms made;

<sup>2</sup> – with account of stock which sale was declared in the previous year;

<sup>3</sup> – without FGUPs which property was contributed to OJSC RZhD share capital;

<sup>4</sup> – including 31 blocks of shares which sale was announced in 2004 but the sale results were summarized in 2005;

<sup>5</sup> – with no account of 273 blocks of shares which sale was announced in 2005 but the sale results were summarized in 2006;

<sup>6</sup> – estimated value based on the report data of FAUFI (Federal Agency for Federal Property Management) “On privatization of federal property in 2007”;

<sup>7</sup> – including blocks of shares of 135 JSC which sales were announced according to the 2007 Forecast privatization plan, but without 268 blocks of shares which sales were announced in 2008 with the results summarized in 2009;

Source: www.mgi.ru; Materials for the RF Government session on March 17, 2005 “On measures to improve efficiency of federal property management”; FAUFI report “On privatization of federal property in 2005”, M, 2006; FAUFI report “On privatization of federal property in 2007”, M, 2008; FAUFI progress report for 2008, M, 2009.

In 2010 the federal budget expects to gain RUR18 mln of privatization proceeds (out of those, RUR12 mln from major sales of the so-called budget-forming assets); in 2011 – RUR6 bln and in 2012 – 5 bln.

The revenues from the federal property sales can be much higher if the RF Government decides to privatize shares and other property that are highly attractive for investors.

In this context the Russian officials in their announcements made in November 2009 and related to the approval of the Privatization program for 2010 – 2012, mentioned more than RUR 70 bln of aggregated revenues of the federal budget from sales of federal property. Out of them, RUR 54–55 bln can be gained from sales of the federal stock in 28 JSC provided they are excluded from the list of strategic companies.

As for the 2009 Privatization program, its implementation, as had been expected, ran against a sharp drop of the purchasing power of the population and expectation of investors related to reduction of the assets value. Officials of the Federal Agency for Federal Property Management noticed that investors’ interest began growing only by the end of summer – beginning of autumn. Potential investors showed their interest for the property auctions in 10% of cases while in the previous years it was 30%.

As of November-end, the Federal Agency for Federal Property Management passed Resolutions regarding the terms of privatization of 173 blocks of shares, published 158 information notices about sales, summarized the results of 100 bids (the annual plan provided for

selling shares of 287 JSC)<sup>1</sup>. Major deals (over RUR100 mln) of the last year included auction sales of the government's stakes of OJSC Tobolsk River Port (25.5%, RUR188.456 mln, re-tenders, Tyumen region) and Gipromyasomolagroprom (100%, RUR188.380 mln, St.\_Petersburg), Hydrometallurgichesky zavod (HydroSteel Plant) (100%, RUR123.7 mln, Stavropolsky Krai). All the deals took place under selling and initial price parity<sup>2</sup>.

### 5.1.3. Influence of the government presence in property on the government structural policy in various sectors, issues of strengthening of the government position

After stormy events and intensive processes in 2007 and 2008, where in mergers and acquisitions companies with the government interest in their capital domineered as buyers of assets, integrated structures were actively built up, six state corporations (GK)<sup>3</sup> were established, and RAO EES was liquidated, all Russia's economy has been hit by the world financial and economic crisis, and special government programs of urgent assistance to some Russian companies and banks has come to the forefront. Besides the issue of sourcing such programs (the budget system, off-budget funds, and Central Bank funds) and the terms of programs delivery in terms of their influence on the property relations, of importance was whether the state would elect acting directly or using agents (such as banks and development institutions).

If to take the period before the Anti-Crisis Action Program of the RF Government for 2009 was announced early April at the State Duma, decisions on increasing charter capitals of the following JSC received the highest resonance: OJSC Agency for Mortgage Housing Credit-ing (by RUR60 bln, November 2008), Russian Railway Roads (by RUR41.5 bln, December 2008), Risslkhpbzbank (by RUR45 bln, February 2009), Rosagroleasing (by 25 bln, February 2009)<sup>4</sup>.

The content of the 2009 Federal Anti-Crisis Program, namely, the priority given to subsidizing interest rates and state guarantees for credits may suggest (with caution) a minimal probability of direct expansion of the government when the government stake in some problematic companies may increase at the expense of the budget funds.

However, this Program among other actions to retain and increase the industrial and technological potential proposed allocation of considerable budget funds to additional capitalization of leading companies of the defense-industrial complex; examples are the buyout by the government of additional issue of stock of OJSC RSK "MiG" for RUR150 bln, respective decisions for FGUP GKNPC named after M. V. Khrunichev for RUR8 bln, OJSC KAPO named after S. P. Gorbunov for RUR 4.128 bln, OJSC MMP named after V. V. Chernyshev for RUR2.9 bln; this follows the trend to increase share capitals. The Program provides for addi-

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<sup>1</sup> Interview of Deputy Head of the Federal Agency for Federal Property Management E. L. Adashkin, RIA Novosti, www.rosim.ru, 25.11.2009.

<sup>2</sup> www.rosim.ru.

<sup>3</sup> Federal Foundation for Assisting Housing Construction Development created in pursuit of Federal Law of July 24, 2008 No 161-FZ formally has a restricted form of incorporation (foundation) but in reality is very close to state corporations established earlier, since the Foundation and these corporations are considered non-commercial organizations. .

<sup>4</sup> The assessment of the anti-crisis actions to support the producing sector of the Russian economy. GU-VShE and MATs report for the 10<sup>th</sup> International scientific conference of GU-VShE on the issues of development of the economics and the society, Moscow, 7-9 April 2009. – M, GU-VShE Publishing House, 2009.

tional issue of shares and bonds of certain strategic enterprises with their further buyout by the authorized agencies for RUR52 bln.

In addition separate items reflect compensation (as the increase of the charter capital of OJSC RZhD) of under-received revenues due to reduced pace of railway tariff indexation for 2009 by 8% (against 14% in the plan) for goods and passenger traffic tariffs (privileged categories)(total of RUR52.3 bln); increase of the charter capital of the Agency for Mortgage Housing Crediting (by RUR 20 bln), an interest-free loan to OJSC AVTOVAZ from the federal funds designated for property contribution to GK Rostechology ( RUR25 bln) <sup>1</sup>; another contribution to this company (RUR 2 bln) was declared as a state support to the air lines.

New examples of expansion of the state business include a decision to establish a state leasing company in the transportation complex on the basis of OJSC State Transportation Leasing Company (100% voting shares belong to the government)<sup>2</sup>, which share capital was increased by RUR10 bln, and announcement of the establishment of an integrated leasing company to support coal mining enterprises with mining equipment (in this case the status and the level of government involvement has not been announced yet).

The available and announced cases of additional capitalization refer mainly to those companies where the government is the sole shareholder (e.g. Agency for Mortgage Housing Crediting, Russian Railways, Rosselkhozbank, Rosagroleasing), and the process of mergers and acquisitions is not affected. In principle the same can be said about a possible buyout of an additional issuance of shares by separate strategic enterprises of the defense-industry complex, though private shareholders are also present in some of these enterprises.

However, regardless of the significant influence of the federal budget policy on the property relations development, banks and development institutions as agents of support of the federal government have always played a more serious role in providing support to the companies.

In the context of the absence of officially announced plans of further comprehensive expansion of the state entrepreneurship sector, the scale and the format of the government support and the selected priorities in crediting the real economy and participation in the stock exchange market transactions have proved to be decisive factors.

The most urgent issue was that of the policy of Vnesheconombank (VEB) which began re-financing the external debts of the major Russian private companies in autumn 2008. Since VEB granted mainly short-term loans (for one year), in 4Q 2009 the issue of repayment of the granted loans emerged, and if no repayment, the issue of choice between granting new loans, restructuring the debts (de-facto it was renewal of the granted loans), initiation of bankruptcy procedures or obtaining property rights on the pledged assets. Formally this should not be deemed nationalization since the federal treasury is not going to receive any additional property, and VEB as a state corporation is a non-commercial entity.

Major banks with government stakes that received the government financial support face a similar choice. Mechel company, e.g. that was attacked by the federal government officials in

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<sup>1</sup> Late 2009 MinPromTorg approved the Rules for granting subsidies from the federal budget to GK RosTechnologies in the form of a property contribution to provide financial support to OJSC AVTOVAZ by way of an interest-free loan for AVTOVAZ to execute the obligations before the suppliers, intermediary entities, crediting companies and other agents with a following increase of the GK RosTechnologies share in the AVTOVAZ charter capital.

<sup>2</sup> Converted from CJSC Leasing Company of Civil Aviation in 2006

July 2008 who were displeased by the company's failure to pay taxes in full volume and the use of transfer pricing mechanism disrupted the terms of 78.9% credit agreements (the loan value) in 2008 and early 2009. Among the Mechel creditors were: Gazprombank (under a \$1.5 bln loan 35% of shares of the coal mining companies Yakutugol and Yuzhny Kuzbass were pledged); VTB (under a RUR15 bln loan part of the assets of Yuzhny Kuzbass and Chelyabinsk metal works were pledged) and Sberbank (RUR3.3 bln loan)<sup>1</sup>. The latter is also a creditor of the united chemical company Uralkhim having received for security against \$700 mln loan the control stakes of OJSC Azot (Berezniki city, Perm region) and OJSC Kirovo-Chepetsk khimcombinat (chemical plant) (Kirov region).

Possible transition of the property rights to the state-owned companies and major banks with government stakes would have obviously marked a new stage of the state property expansion.

In real life, however, the government would tend to meet the business interests by following the previous practice of debt restructuring. In the first half of October 2009 the VEB Supervisory Board extended for another year the loans issues for repayment of external debts to such companies as Gazpromneft, Citroniks, Evraz Group, Rusal, GK PIK and Altimo. The prolongation was made without revision of the main parameters of the deals earlier recorded in the loan agreements (including the size of the security) except interest rates<sup>2</sup>.

If such approach continues to be followed, the potential of possible expansion of the public sector would remain unrealized in large; however such situation would imply a certain revision of the principles of financial accountability, refusal from "soft" budget limitations in business entities' activities and consistency in application of the bankruptcy procedures which was implemented in the Russian economy from early 90'es with great difficulties and tremendous cost efforts.

The preliminary data for 2009-end results allows us making a cautious conclusion that the state has been less active in implementing the policy of integration of separate state-owned assets into holdings. An indirect sign of this is the lower number of clarifications in the list of strategic unitary enterprises and joint-stock companies vs two previous years: 12 clarifications vs 22 in 2008 and 42 in 2007 (for comparison: three clarifications were made as of 2004 end results, four – in 2005 and 12 in 2006). The bigger number of the clarifications was connected with building up integrated structures where initially the enterprises and the companies to be integrated are excluded from the list and later a newly-formed holding is re-included. As a result of this, 22 unitary enterprises and 16 joint-stock companies were excluded and 4 integrated companies were included in the list.

As a reminder, in 2008, following the decisions of the President and the RF Government, Federal Property Management Agency established 26 integrated companies, OJSC Oboronservice and GK RosTechnologies among them; these two companies integrated 440 unitary enterprises and 43 joint-stock companies. Since the Russian Government issued Resolutions on their privatization in November 2008, and these companies were included in the respective program in 4Q 2008, the procedure for their integration was to be completed in 2009.

To implement the 2008 resolutions, the first stage of the establishment of an integrated company OJSC Headquarters for Reproduction of Farm Livestock was completed on the basis

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<sup>1</sup> D. Varaskin, Banks displeased. – Vedomosti, June 24, 2009, S. B. 02.

<sup>2</sup> Development Bank extended the loans for one year. : RBK daily, 9 October 2009 г., No 185 (748). p. 2.

of the Center for Artificial Insemination of Farm Livestock; this company integrated 19 farms located mainly in the Povolzhie (the river Volga), the Urals and in Siberia (Bashkiria, Mordovia, Idmurtia, Ekaterinburg, Tyumen, Altai, Kemerovo, Novosibirsk, Krasnoyarsk and Krasnodar).

In the previous year under the government property policy, OJSC Agency for Regulation of the Product Market was converted into United Grain Company; its charter capital received the shares of 31 enterprises of cereal products (milling plants, grain elevators, etc.) including 17 control stakes in the form of placement of additional shares.

Likewise the charter capital of the earlier created integrated company called Concern of Radio Engineering Vega will be increased by adding federal stocks of 14 joint-stock companies including 100% minus 1 share of 7 joint-stock companies established as a result of conversion of the earlier FGUPs.

The establishment of Rosgeology Holding is under consideration which charter capital will be formed as a result of establishment of joint-stock companies from FGUPs in exploration and by including the stocks of operating servicing JSC (49 companies altogether)<sup>1</sup>.

In 2009 inconsistency of the government policy towards state-owned corporations became obvious, the establishment of state-owned corporations has become a new direction in the federal property and structural policies during the last two years.

Early 2009 the government began discussing extensively new plans of creation of state-owned companies (GK) and expansion of businesses of the state-owned companies in operation. Thus the Central Bank had to transfer the funds of National Wealth Fund and the Reserve Fund to a new GK Russian Financial Agency while VEB – pension deposits and also the internal and external debts of the country<sup>2</sup>. Consolidation of communications assets of VEB and integration of 11 air lines in Rosavia under Rosoboronexport was also considered as an alternative<sup>3</sup>. In the last case the situation changed early 2010: the consolidation now is to begin under the auspices of Airflot; however in terms of general federal government policy, this is not a new trend but a technical correction.

Decisions were taken to transfer GK Rostechologies as a property contribution of the federal government in addition to a large package of the federal property transferred in 2008 of shares of another 3 joint-stock companies including 18.83% of AVTOVAZ stock that had been in management of FGUP Rosoboronexport; this corporation was to act as a customer in construction of 12 federal medical centers of high technologies under the respective national project. Rostechologies was expected to receive federal budget allocations (as property input) at the expense of the respective reduction of the budget allocations to the Russia's Ministry of Health and Social Development for construction of the said centers while in future subsidies would be granted to complete the construction and commission these centers. In this light another initiative of Rostechologies to enter a pharmaceutical market by way of setting a holding with the government stakes of 35 companies looks quite logical.

In summer 2009 the Law on Establishment of the State Company Russian Motor Roads (Avtodor) was passed; Avtofor will be a national operator of the federal motor road network; simultaneously a new form of legal entity's incorporation oriented at the use of federal prop-

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<sup>1</sup> E. Korytina, The State moved to exploration// RBK daily, October 2, 2009, p. 5; E. Korytina, Sechin helped geologists//RBK daily, October 15, 2009, p. 5.

<sup>2</sup> I. Zinenko. New state corporation will control all financial assets of the government, 13.01.09. – <http://www.rb.ru>.

<sup>3</sup> A. Khazbiev. Indecent proposal, - Expert, 2009 No 11, p. 26-27.

erty by the state-owned company was added to the RF Civil Code and the Law on Non-Commercial Organizations.

Avtodor is to render state services and perform other functions in the road sector by using federal property under trust management. This company will receive for trust management the federally-owned toll motor roads or the roads in general use and federal significance that have toll areas.

Such format will inevitably cause a lot of questions starting from expediency of the new form of incorporation with a pronounced focus on commercialization of public wealth and ending with obvious restrictions in using the term “state-owned company” (public company) in the economic and political vocabulary.

The Russian Motor Roads as a non-commercial entity is very close to the state-owned companies established earlier, the only difference being the trust management; however, this form has not been widely used for other types of federal property, e.g. blocks of shares.

On the other hand, criticism of the state-owned companies that has been growing since their establishment ended in development (by summer) by the initiative of the President of Russia of the “Concept of development of the legislation on legal entities” which contained proposals on changing the legal form of all existing state-owned companies, on refusal from their use in future and on repealing a number of “specific” provisions of the law that granted these companies “special” rights.

The President’s Letter to the Federal Assembly of Russia in November 2009 pointed out that in future state-owned companies should be converted to joint-stock companies under the government control, while those companies that have specified periods of their operation should be liquidated in due time. These include Olimpstroj and Foundation of Assistance to Reform the Utility and Housing Sectors. According to A. Dvorkovich, Aid to the President of Russia, the prospects of transformation of Rosatom and Federal Agency for Deposit Insurance will depend on their long-term results. Most probable candidates for corporatization are VEB, Rosnano and Rostechologies<sup>1</sup>. However, there are no specific dates set for such transformation. It is not clear whether the new vision of the state-owned company status applies to Avtodor and Federal Foundation of Assistance to Housing Construction Development.

The first step in this direction may become corporatization of airlines that have been transferred earlier to Rostechologies and have the status of unitary enterprises, and their further transfer to Airflot – this was announced in February 2010. The airlines considered are GKT Russia, Kavminvodyavia, Orenburg airlines and Saratov airlines, Vladivostock airlines and Sakhalin Airlines where Rostechologies received federal stakes. Thus the Rostechologies plans to establish a new integrated air company Rosavia<sup>2</sup> comparable with Airflot in terms of traffic volume have not been implemented. It is quite possible that Rostechologies will receive a stake in exchange for the said assets.

As a result of the current financial and economic crisis, opportunities to act on the market of corporate control as actively as in 2004-2007 have been restricted for the majority of companies with the government stake even with account of state support granted to them under the anti-crisis program.

The emergence of this trend may refer to 2008 when in the context of \$120 bln worth M&A in Russia there was no major deal with a company having a government stake that act-

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<sup>1</sup> www.prime-tass.ru, 12 November 2009

<sup>2</sup> Initially participation in Rosavia and Atlant-Soyuz airline controlled by the Moscow authorities was expected.



ed as a buyer. Mechanical engineering is worth mentioning with acquisition by the United Avia Engineering Corporation (OAK) of 49.4% of shares of Scientific and Production Corporation Irkut (a major exporter of military and civil aerotechnics) for \$420 mln and acquisition of the entire capital of Kriogenmash and 85% of the capital of KHIMMASH (for total \$290 mln) by Gazprombank which also became the owner of 8.3% of the shares of National Telecommunications for \$128 mln. Two more deals could be possibly mentioned as having reference to the companies with the government interest but with greater specifics related to external capital markets. Gazpromneft acquired a control stake in Naftna Industrija Srbije (NIS) for \$560 mln, while Gazprom expected to receive 49% of CJSC Gerosgaz possessing 2.93% of Gazprom from German company E. ON AG that bought 25% stock minus 1 share in Severneftegazprom<sup>1</sup>.

In 2009 communications was the “hottest” sector. At the beginning of the year a possibility arose for VEB acquisition from investment bank KIT Finance<sup>2</sup> of 40% shares in Rostelecom and 25% plus 1 share in Svyazinvest ( a telecommunication holding) from AFK Systema where for many years the sale of the federal control stake (75% minus 1 share) was on the agenda; the state-owned corporation could receive this control stake directly from the federal government.

AFK Systema being the third largest private shareholder of the company since the outrageous sale by the government of the blocking shareholding in 1997<sup>3</sup>, at the end of 2008 proposed that the government buys out its block of shares for \$1.9 bln. This amount exceeded by almost 2.8 times the asset value assessed by Ernst & Young in spring 2008; this encouraged the AFK Systema to buy another 25% shares from the government thus increasing its stake in Svyazinvest up to the control stake. Some time later AFK Systema offered the government a counter-deal to exchange the blocking shareholding in Svyazinvest for the write-off of the debt (RUR26 bln) to Sberbank of a Systema daughter company, Komstar-OTS, and the Svyazinvest stake in MGTS (28% of voting shares) where Systema had already a control stake. It goes without saying that if the proposed deal fails, Systema will be able to keep its stake in Svyazinvest and will hope selling it profitably after the crisis is over<sup>4</sup>.

As for Svyazinvest, this company began considering an opportunity of merging with one of the All-Russia mobile communications operator. Minister of Communications and Mass Media of the Russian Federation I. Shchyogolev addressing the Association of European Business late June 2009 said that one of the aims of the holding restructuring was to become one of the fourth major cellular operators in Russia; this could be achieved by not only getting control in one of “Big Three” operators (e.g. in Megafon) but also by merging the cellular assets with outside regional cellular operators’ assets or with one of the second tier majors (Tele2, SMARTS, Motiv and Sky Link)<sup>5</sup>.

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<sup>1</sup> Review of the M&A market in 2008. Ernst & Young, 2009, p. 8, 22, 24, 32.

<sup>2</sup> 90 % of its capital are owned by OJSC RZHD and ALROSA from autumn 2008

<sup>3</sup> At that time 25% and 1 share of Svyazinvest were bought by Mustcom of J. Soros and V. Potanin for \$1.87 bln in expectation of further privatization. In 2004 this block of shares was sold Access Industries of L. Blavatnik and his partner V. Vekselberg for \$625 mln, and in 2006 it was bought by AFK Systema for a double price registering the acquired asset to Komstar-OTS, its daughter company.

<sup>4</sup> A. Klyuchkin. Back to the wood. www.lenta.ru, 14.05.2009.

<sup>5</sup> A. Bursak. Svyazinvest thinks about an alliance; RBK daily, 24 June 2009 , No 108 (671). p. 10.

The merge of the major Russian private companies in metal works and mining sectors (Norilsk Nickel, RUSAL and Metalloinvest) with GK Rostechologies involvement did not occur though the information about this merge appeared at the end of 2008<sup>1</sup>.

It is reasonable to ask how the processes triggered by the crisis affected the positions of the federal government in the economy as a producer of goods (services and works). Rosstat monitoring results partially confirm the increasing weight of the public sector in the economic performance indicators (*Table 6*).

*Table 6*  
**The weight of the public sector by various indicators in 2006 – 2009, in %**

Indicator	2006	2007	2008	1H 2009
Volume of shipped goods (own production), rendered services and performed works (by own efforts):				
- production of mineral resources	6.0	12.8	13.5	13.8
- production of fuel and energy resources	3.9	11.8	13.2	14.3
- manufacturing sectors	8.2	8.4	8.5	9.3
- generation and distribution of electric energy, gas and water	10.7	11.4	13.0	10.5
Construction work scope (by own resources)	4.4	4.0	3.6	3.3
Passenger traffic (transportation companies) *	68.5	65.9	63.9**	64.9
Commercial shipments of goods made by transportation companies (without pipelines)	67.2	72.9	71.1**	72.4
Commercial traffic of transportation comp(without pipelines)	93.9	94.6	94.3**	92.6
Services of communications***	9.8	9.8	9.9	11.6
Internal R&D costs	70.4	72.4	72.6	75.4
Volume of paid services rendered to the community	17.2	16.4	16.3	16.1
Investments to main capital from all funding sources ****	18.1/14.4	19.5/15.0	21.5/15.9	18.1/13.6
Net proceeds from sales of goods, products, services and works (less VAT, excises and other similar payments)	10.2	10.2	9.8	10.1
Average headcount	26.0	24.9	24.0	24.2

\* – without city passenger transportation (electricity) organizations;

\*\* – data for January – September 2008;

\*\*\* – Net proceeds from sales of goods, products, works and services (less VAT. Excises and other similar mandatory payments);

\*\*\*\* in numerator: less small businesses

*Source:* Development of the public sector of economy in the Russian Federation in 2005, M, Rosstat, 2006, p. 8, 85, 92–93, 94, 103, 137, 139, 146–147, 167; Development of the public sector of economy in the Russian Federation in 2006, M, Rosstat, 2007, p. 8, 82, 89–90, 91, 100, 134, 136, 143–144, 164; Development of the public sector of economy in the Russian Federation in 2007, M, Rosstat, 2008, p. 9, 42, 90–91, 92, 103, 134, 136, 143–144, 164; Development of the public sector of economy in the Russian Federation in 2008, M, Rosstat, 2009, p. 13, 43, 45–46, 47, 53, 61–63, 67–68, 88; Development of the public sector of economy in the Russian Federation in 1H of 2009, M, Rosstat, 2009, p. 13, 42, 44–45, 46, 49, 52–54, 58–59, 79.

As seen in *Table 6*, the share of the public sector in 2008 and in the 1H of 2009 was insignificant for the bigger number of the indicators (the similar trend was observed in all 2000's) not exceeding 10%-15%. The share of the public sector was a little greater for investments (15–20%, without small businesses) and employment (24–25%), while the traffic (over 60–90% depending on the indicator) and internal R&D costs (over 70%) are obvious exclusions.

However, the official statistics agencies reported a considerable increase of the weight of the entire public sector in 2008 – 2009 vs 2006-2007 in production of mineral resources (pri-

<sup>1</sup> M&A market review in 2008, Ernst I Yong, 2009, p. 17.

marily, fuel and energy), in manufacturing, communications, R&D costs and investments into main capital<sup>1</sup>. As a result, the 1H 2009 share of the public sector in the production of fuel and energy resources which was obviously lower than the public sector input into the production of mineral resources on the whole, surpassed this indicator.

Going into a more detailed review of the situation, we can say that according to the 2008 year and 1H 2009 results, the public sector domineered on a few positions (cargo and passenger traffic by rail, forest restoration, caustic ash). In almost all other cases the unit weight of the public sector was less than 20% except production of sodium chlorite, ethyl alcohol from food stuffs, railway packers for broad gage lines, certain types of machine building products (cargo cars, tractor grain drills, radio receiving sets), all types of paid services, where the public sector share did not exceed 50%.

It should be noticed that the Rosstat data based on the definition of the public sector as stated in Resolution of the RF Government of January 4, 1999 No 1 (the current version of this document adopted by Resolution of the RF Government of December 30, 2002 No 393) do not reflect the real unit weight of the public sector in the Russian economy<sup>2</sup>.

#### 5.1.4. The effect of the federal government property policy on the budget revenues in 2000 – 2009

The crisis that hit the Russian economy in autumn 2008, naturally led to reduction of budget revenues on almost all budget items in 2009. The revenues received by the budget as a result of the implementation of the government property policy were no exception.

Let us remind that all federal budget revenues generated by the property owned by the state can be divided into two groups depending on their nature and the source. One group comprises revenues generated by the use of the government-owned property (renewable sources). The other group comprises revenues generated by non-recurrent/one-off sources that can not be renewed because the government having sold the property transferred the property rights to some legal entities and physical persons including by way of privatization (non-renewable sources).

Below (*Table 7 and 8*) we show data on revenues that are (with minor exceptions) contained in the Laws on the execution of the federal budget for 2000-2008 pertinent to the use of the state-owned property and property sales (tangible objects only)<sup>3</sup>.

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<sup>1</sup> The 1H 2009 results did not confirm this trend for the last indicator.

<sup>2</sup> See for detail: Russian economy in 2007. Trends and prospects (Ed. 29), M, IEPP, March 2008, p. 485-490. An additional factor that negatively affects validity of data in the formal statistical reports is establishment of several state corporations that are given assets.

<sup>3</sup> Have not been considered the revenues of the federal budget received as payments for the use of natural resources (including water, biological resources, revenues from the use of the forest fund and subsoil), reimbursement of agricultural losses resulted from withdrawal of agricultural lands, financial transactions losses (revenues from investment of budget funds (revenues from the federal budget balance and their investment, since 2006 – also revenues from managing funds of the federal Stabilization Fund (in 2009 the Reserve Fund and National Wealth Fund), revenues from investment of funds accumulated during auctions of stock owned by the Russian Federation); interest received on budget credits granted inside the country from the federal budget funds; interest on state loans (funds received from foreign governments and foreign legal entities in the form of interest paid on loans granted by the Russian Federation; funds received from enterprises and organizations in the form of interest and guarantees payments on loans received by the Russian Federation from the governments of foreign countries and international finance agencies); revenues from paid services or compensation of the government costs; remittance of profits to the RF Central Bank; certain payments from federal and municipal enterprises and organizations (patent and registration fees for official registration of software programs, data-

*Table 7*

**Federal budget revenues generated by the use of the state-owned property  
(renewable sources) in 2000 – 2009, in mln rubles**

Year	Total	Stock dividend (2000–2009) and revenues from other forms of equity participation (2005–2009)	Land lease pay- ments for state- owned land	Revenues from leas- ing of state-owned property	Revenues from remitted profit that remains after FGUPs have paid taxes and other man- datory payments	Revenues from Vietsovetro JV business
2000	23244.5	5676.5	–	588.7	–	11687.3 <sup>1</sup>
2001	29241.9	6478.0	3916.7 <sup>2</sup>	5015.7 <sup>3</sup>	209.6 <sup>4</sup>	13621.9
2002	36362.4	10402.3	3588.1	8073.2	910.0	13388.8
2003	41261.1	12395.8		10276.8 <sup>5</sup>	2387.6	16200.9
2004	50249.9	17228.2	908.1 <sup>6</sup>	12374.5 <sup>7</sup>	2539.6	17199.5
2005	56103.2	19291.9	1769.2 <sup>8</sup>	14521.2 <sup>8**</sup>	2445.9	18075.0
2006	69173.4	25181.8	3508.0 <sup>8</sup>	16809.9 <sup>9</sup>	2556.0	21117.7
2007	80331.85	43542.7	4841.4 <sup>8</sup>	18195.2 <sup>9</sup>	3231.7	10520.85
2008	76266.7	53155.9	6042.8	114587.7 <sup>9</sup>	2480.3	–
2009	31849.3	10114.2	647.5	113507.3	1757.3	–

<sup>1</sup> – according to the Ministry of State Property of the Russian Federation, in the 2000 Law on the execution of the federal budget there was no separate item, the total amount of payments of government enterprises (RUR9,887.1 mln) was shown (with no break down);

<sup>2</sup> – the rental amount for (i) lands in agricultural use and (ii) city and settlements lands;

<sup>3</sup> – total revenues from renting property assigned to (i) research institutions (ii) educational institutions, (iii) health institutions, (iiii) state museums, state institutions of culture and arts, (iiiii) archives, (iiiii) RF Ministry of Defense, (iiiii) organizations of the RF Ministry of Railways, (iiiii) organizations of scientific services for Academies of Sciences with a government status and (iiiii) other revenues from renting of state-owned property;

<sup>4</sup> – according to the Ministry of State Property of the Russian Federation, in the 2001 Law on the execution of the federal budget there was no separate item, the amount coincided with the amount of other revenues in payments of federal and municipal organizations;

<sup>5</sup> – total revenues from renting of state-owned property (land rents are not shown separately);

<sup>6</sup> – rent amount for (i) lands of cities and settlements and (ii) lands in federal ownership after state ownership on land was delineated;

<sup>7</sup> – total revenues from renting property assigned to (i) research institutions, (ii) educational institutions, (iii) health institutions, (iiii) state museums, state institutions of culture and arts, (iiiii) state archives, (iiiii) postal offices of the federal postal communications of the RF Ministry on Communications and Information Support, (iiiii) organizations of scientific services for Academies of Sciences with a government status and (iiiii) other revenues from renting of state-owned property;

<sup>8</sup> – rent payments after the federal ownership to land was delineated and proceeds from sale of the right to conclude rent contracts for lands in federal ownership (for 2008-2009 – except land sites of federal autonomous institutions);

bases and topologies of integral microchips and other revenues which before 2004 had been a part of the payments by the state-owned enterprises (except revenues from Vietsovetro JV activity since 2001 and remittance of part of FGUPs' profits since 2002)); revenues from PSA implementation; revenues from disposal and management of confiscated and other property converted into government revenue (including property converted into government property received by way of inheritance or gift, or treasures); proceeds from lotteries, other revenues from the use of property and rights in federal ownership (revenues from disposal of rights to intellectual property results (R&D and technological works) of military, special and dual purpose; revenues from maintenance and use of highway property and other proceeds from the use of property in federal ownership); also from the allowed activities of organizations to be accounted in the federal budget; proceeds from sales of government reserves of previous metals and stones.

<sup>9</sup> – revenues from renting of property in operating management of federal government authorities and institutions established by these authorities and in FGUPs' management: transferred to operating management to the following institutions with a government status: (i) research institutions, (ii) organizations of scientific services for Academy of Sciences and sector Academies of Sciences, (iii) educational institutions, (iiii) health institutions, (iiiii) federal postal offices of the Federal Communications Agency, (iiiii) government institutions of culture and arts, (iiiii) state archives (iiiii) other revenues from renting of property in operating management of federal government authorities and institutions established by these authorities and in FGUPs' management<sup>1</sup> (for 2006–2009 without revenues from the allowed types of activity and federal property use located outside the Russian Federation gained abroad which had not been separated in previous years <sup>2</sup>).

*Source:* Laws on the execution of the federal budget for 2000 – 2008; Report on the execution of the federal budget as of January 1, 2010, [www.roskazna.ru](http://www.roskazna.ru); estimates made by the authors.

As for the analysis of preliminary results of the budget effect of the government property policy in 2009 regarding renewable sources, first of all a considerable drop of revenues should be noted that is a direct consequence of the economic performance results (dividends and remittance of a part of profits of unitary enterprises).

The dividends on federal stock fell sharply, by 5.3 times vs 2008 being compared to the 2002 level (slightly more than RUR10 bln) <sup>3</sup>, not mentioning the benchmarks outlined in 2008<sup>4</sup>.

In this connection the Federal Property Management Agency was active in recovering debts from joint-stock companies which shares are owned by the Russian Federation and the companies that evaded from their obligations to transfer dividends to the federal budget or failed to transfer dividends in full volume for 2006 – 2008<sup>5</sup>.

As of summer 2009, the Agency issued 20 claims against major debtors which total debt to the government was about RUR60 mln. Some of the debtors wishing to avoid court proceedings that would enforce them to pay outstanding dividends and interest on those dividends repaid their debts at once or expressed their intent in doing so. As for other debtors, the Agency lawyers prepared statements of claim for court prosecution. The aggregate debt amount (several hundreds million of rubles) does not make us believe that the general situation with dividends payment to the federal budget can change for the better even if such debts are retired quickly and in full amount.

Certain parts of FGUPs profits demonstrated lower sensitivity to the crisis. They reduced roughly by 30%, and their absolute value (RUR1.75 bln) exceeded the 2002 indicator by almost two times though was lower than the transfers to the budget in all subsequent years.

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<sup>1</sup> In 2008-2009 FGUPs as a source of revenues from renting of property in economic control were not mentioned while renting of property in operating management of federal authorities and institutions established by these authorities excludes the property of federal autonomous institutions..

<sup>2</sup> According to the RF Ministry of State Property, the revenues from the use of federal property being abroad (in addition to revenues due to the interest of the Russian participant of JV Vietsovpetro) amounted to RUR315 mln in 1999 and RUR440 mln in 2000. Further on FGUP "Predpriyatie po upravleniyu sobstvennostiyu za rubezhom (Company for managing property abroad) came to play a major role in the organization of commercial use of the federal property abroad.

<sup>3</sup> It should be noticed that in 2002 in addition to dividends on the shares of Russian joint-stock companies inside Russia the federal budget received about RUR13.4 bln as revenues on the stake of the Russian participant in JV Vietsovpetro. However, after completion of the actions for development of JSC Zarubezhneft which charter capital in 2007 in addition to stock of two joint-stock companies (research institutes) received a share (50%) of the Russian participant of JV Vietsovpetro., the federal budget ceased to receive revenues from this source which was not mentioned in the revenue structure from the renewable sources in 2008-2009.

<sup>4</sup> See Russian economy in 2009. Trends and prospects. (Ed. 31) M. IEPP.

<sup>5</sup> [www.rosim.ru](http://www.rosim.ru), 24.08.2009.

Against this background the situation with rent revenues looked quite favorable where the government received rent (for the use of real estate and land plots) not being involved in the organization of business processes of renting companies and building the relations with them on the contract basis concluded, as a rule, for a specific period of time at the earlier agreed rates. Rentals from the federal property (RUR13.5 bln) reduced slightly, by 7.4%, being pushed back to the level of 2003-2004. At the same time land rent proceeds did not shrink but rather increased by 7% in 2009 reaching their absolute maximum value since 2000's.

Thus a certain reconfiguration of the federal budget revenue structure from the renewable sources occurred. The revenues from leasing of federal property became the most significant item (42.4% vs 19.1% in 2008). Dividends regardless of their sharp decline preserved their important place (31.8%) though in 2007 – 2008 they made half of all the revenues from the reviewed sources. Specific weight of revenues from land rent grew considerably (20.3% against 5–8% of all revenues from the renewable sources in 2006 – 2008) while the profit input transferred by FGUPs (5.5%) reached its highest value in 2003 (5.8%) for the period starting 2000.

In analyzing the revenues of the federal budget from privatization and sales of state property (*Table 8*) it should be noticed that from 1999 proceeds from sales of the major part of such assets (shares, and in 2003 – 2007 - land plots<sup>1</sup>) have been looked at as sources of funding of the budget deficit.

*Table 8*

**Federal budget revenues from privatization and sales of property  
(non-renewable sources) in 2000 – 2009, in mln rubles**

Year	Total	Sale of stock in federal ownership (2000–2009 ) And other forms of equity participation (2005–2009 )#	Sale of land plots	Sale of various property
2000	27167.8	26983.5	–	184.3 <sup>1</sup>
2001	10307.9	9583.9	119.6 <sup>2</sup>	217.5+ 386.5+0.4 (intangibles) <sup>3</sup>
2002	10448.9	8255.9 <sup>4</sup>	1967.0 <sup>5</sup>	226.0 <sup>6</sup>
2003	94077.6	89758.6	3992.3 <sup>7</sup>	316.2+10.5 <sup>8</sup>
2004	70548.1	65726.9	3259.3 <sup>9</sup>	197.3+1364.6+0.04 (intangibles) <sup>10</sup>
2005	41254.2	34987.6	5285.7 <sup>11</sup>	980.9 <sup>12</sup>
2006	24726.4	17567.9	5874.2 <sup>11</sup>	1284.3 <sup>13</sup>
2007	25429.4	19274.3	959.6 <sup>14</sup>	5195.5 <sup>15</sup>
2008	12395.0	6665.2+29.6	1202.0 <sup>16</sup>	4498.2+0.025 (intangibles) <sup>17</sup>
2009	4544.1	1952.9	1152.5 <sup>16</sup>	1438.7 <sup>17</sup>

# –refers to internal financing sources to cover deficit of the federal budget, the amount of RUR29.6 mln for 2008 (Report on the execution of the federal budget as of January 1, 2009) refers to the federal budget revenues, but it is missing in the Law on the execution of the federal budget for 2008;

<sup>1</sup> – revenues from privatization of state-owned organizations included in the sources of internal financing of the federal budget deficit;

<sup>2</sup> – revenues from sales of lands and rent rights to lands in federal ownership (the land sites under privatized enterprises are shown separately) included in the federal budget revenues;

<sup>3</sup> – aggregate revenues from (1) sales of property in federal ownership included in the sources of internal financing of the federal budget deficit; (2) revenues from (i) apartment sales, (ii) sales of state production and non-production funds, transportation vehicles, other equipment and material values, also (3) revenues from sales of intangibles included in the federal budget revenues; ;

<sup>4</sup> – with RUR6 mln generated from sales of stock owned by the RF subjects;

<sup>1</sup> In 2003-2004 with account of sales of rent rights.

<sup>5</sup> – proceeds from sales of land and intangible assets which have not been shown separately; included in the federal budget revenues;

<sup>6</sup> – proceeds from state-owned property sales (including RUR1.5 mln from sales of property owned by the RF subjects) included in the sources of internal financing of the federal budget deficit;

<sup>7</sup> – includes proceeds from: (1) sales of land plots under real estate facilities that have been in federal ownership before their disposal; to be credited to the federal budget; (2) sales of other land plots and sale of rights to conclude rent contracts thereto; (3) sales of land plots after the land property rights have been delineated; also sale of rights to conclude rent contracts thereto; to be credited to the federal budget and treated as sources of internal financing of the federal budget deficit;

<sup>8</sup> – sum of (1) proceeds from federally owned property sales that are referred to the sources of internal financing of the federal budget deficit, and (2) proceeds from sales of intangible assets referred to federal budget revenues;

<sup>9</sup> – includes proceeds from: (1) sales of land plots under real estate facilities that have been in federal ownership before their disposal; to be credited to the federal budget, (2) sales of other land plots and sale of rights to conclude rent contracts thereto; (3) sales of land plots after the land property rights have been delineated; also sale of rights to conclude rent contracts thereto; to be credited to the federal budget and treated as sources of internal financing of the federal budget deficit;

<sup>10</sup> – sum of (1) proceeds from federally owned property sales that are referred to the sources of internal financing of the federal budget deficit, (2) revenues from (i) apartment sales, (ii) sales of equipment, transportation vehicles and other tangible property to be credited to the federal budget; (iii) sales of ships utilization products; (iiii) sales of GUPs' property, property of institutions and military property; (iiiii) sales of products of utilization of weapons, military equipment and ammunition; (3) proceeds from sales of intangibles to be included in the federal budget revenues;

<sup>11</sup> – includes proceeds from: (1) sales of land plots under real estate facilities that have been in federal ownership before their disposal; to be credited to the federal budget (2) sales of land plots after the land property rights have been delineated to be credited to the federal budget, (3) sales of other land plots owned by the government before the federal ownership on land have been delineated and not designated for housing construction (the last statement refers to 2006 only), the proceeds are included in the sources of financing of the federal budget deficit;

<sup>12</sup> – proceeds from sales of tangibles and intangibles (less federal budget funds from disposal of confiscated and other property converted to the state income) include proceeds (i) from apartment sales, (ii) sales of FGUPS' property, (iii) sales of property in operational management of federal agencies; (iiii) sales of military property, (iiiii) sales of utilization products of weapons, military equipment and ammunition; (iiiii) sales of other property in federal ownership; (iiiii) sales of intangibles, referred to federal budget revenues;

<sup>13</sup> – proceeds from sales of tangible and intangible assets (less revenues in the form of profitable products of the state under PSA) and federal budget funds from disposal and sale of confiscated, heirless and other property converted to the state income, include revenues from (i) apartment sales, (ii) FGUPS' property sales; (iii) sales of property in operational management of federal institutions; (iiii) sales of military property, (iiiii) sales of utilization products of weapons, military equipment and ammunition; (iiiii) sales of other federally owned property, included in the federal budget revenues;

<sup>14</sup> – proceeds from sales of land plots in federal ownership after the land property rights have been delineated, included in the sources of financing of the federal budget deficit;

<sup>15</sup> – proceeds from sales of tangible and intangible assets (less revenues in the form of profitable products of the state under PSA) and federal budget funds from disposal and sale of confiscated, heirless and other property converted to the state income, proceeds from sales of sequestered lumber include revenues from (i) apartment sales (ii) FGUPS' property sales; (iii) sales of property in operational management of federal institutions; (iiii) sales of released movable and immovable military and other property of the federal executive authorities with the military service and the service equated thereto; (iiiii) sales of products of military designation available at the federal executive authorities within the framework of military and technical cooperation; (iiiii) proceeds from sales of other federally owned property, included in the federal budget revenues;

<sup>16</sup> – proceeds from sales of lands in federal ownership (except lands of federal autonomous institutions) to be included in the federal budget revenues;

<sup>17</sup> – proceeds from sales of tangible and intangible assets (less revenues in the form of profitable products of the state under PSA) and federal budget funds from disposal and sale of confiscated, heirless and other property converted to the state income, proceeds from sales of sequestered lumber. Proceeds from sales of special feed-stock and fissionable materials include proceeds from: (i) apartment sales, (ii) sales of property in operational management of federal institutions (except autonomous)<sup>1</sup>, (iii) sales of released movable and immovable military and other property of the federal executive authorities with the military service and the service equated thereto, (iiii) sales of utilization products of weapons, military equipment and ammunition; (iiiii) sales of products of military designation available at the federal executive authorities within the framework of military and technical cooperation (2008 only), (iiiii) sales of utilization products of weapons and military equipment under the federal target program “Industrial utilization of weapons and military equipment (2005-2010);», (iiiii) proceeds from sales of other federally owned property and proceeds from sales of intangible assets included in the federal budget revenues;

*Source:* Laws on the execution of the federal budget for 2000 – 2008; Report on the execution of the federal budget as of January 1, 2010; www.roskazna.ru; estimates of the authors.

In 2009 the federal budget revenues of property nature generated from non-renewable sources continued falling down sharply following the trend of the previous year.

Proceeds from stock sales fell almost by 3.5 times, from sales of various types of property – by more than 3 times. While the proceeds from the latter source appeared to be comparable in absolute values (over RUR1.4 bln) with those in 2004 and 2006 and exceeded the 2005 level by 1.5 times, the proceeds from stock sales (leas RUR2 bln) reached its absolute minimal value for the entire period of 2000'es. Unlike 2008, when the proceeds from land sales grew by almost 1/4, in 2009 they dropped though insignificantly (by 4%) reaching RUR1.15 bln. However this source (land sale proceeds) remained less valuable (in terms of weight) (about ¼ of all revenues from non-renewable sources, approximately at the level of 2006) vs the proceeds from stock sale (43%) and sale of various types of property (31.7%). The proceeds from stock sales made less than a half of all such revenues for the first time in the period of 2000'es; the unit weight of the proceeds from sales of other property also shrank vs 2008.

The year of 2009 demonstrated a more than double fall of the overall volume of federal budget revenues from privatization (sales) and use of the state-owned property (*Table 9*). Their absolute values (RUR 36.4 bln) vs 2008 reduced by more than 2 times and proved to be minimal for the entire period of 2000'es. Still we can state that this value has exceeded the target figure voiced out at the working meeting of the RF Government Chairman with Yu. A. Petrov, Head of Federal Property Management Agency held in the mid of July 2009 where the latter expressed his assurance in that the Agency would remit to the budget about RUR20 bln in 2009<sup>2</sup>.

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<sup>1</sup> Also less proceeds from sales of FGUPs' property.

<sup>2</sup> www.rosim.ru, 16.07.2009. It should be noted, however, that the Federal Property Management Agency administers not all the revenues connected with the use of the state-owned property and its privatization.



Table 9

**Structure of the federal budget revenues of property nature generated from various sources in 2000–2009**

Year	Aggregate revenue from privatization (sales) and use of state-owned property		Revenue from privatization (non-renewable sources)		Revenue from the use of state-owned property (renewable sources)	
	RUR, mln.	% to total	RUR, mln.	% to total	RUR, mln.	% to total
2000	5041.3	100.0	27167.8	53.9	23244.5	46.1
2001	39549.8	100.0	10307.9	26.1	29241.9	73.9
2002	46811.3	100.0	10448.9	22.3	36362.4	77.7
2003	135338.7	100.00	94077.6	69.5	41261.1	30.5
2004	120798.0	100.0	70548.1	58.4	50249.9	41.6
2005	97357.4	100.0	41254.2	42.4	56103.2	57.6
2006	93899.8	100.0	24726.4	26.3	69173.4	73.7
2007	105761.25	100.0	25429.4	24.0	80331.85	76.0
2008	88661.7	100.0	12395.0	14.0	76266.7	86.0
2009	36393.4	100.0	4544.1	12.5	31849.3	87.5

Source: Laws on the execution of the federal budget for 2000 – 2008; Report on the execution of the federal budget as of January 1, 2010; www.roskazna.ru; estimates of the authors.

In 2009 the trend of increasing weight of the renewable sources in the structure of aggregate revenues from privatization (sales) and use of the state-owned property had further developed. The share of revenues from the use of the state-owned property was 87.5%, being the highest in the 2000'ses. The share of revenues from privatization and sales of property was minimal – 12.5%.

If in 2008 the revenues from the use of the state-owned property played a buffer role, not going lower than the 2006 level, in 2009 they exceeded the similar figures for 2000-2001 only when the actions were performed under the Concept of Management of State-Owned Property and Privatization in the Russian Federation in 1999, while the revenues from privatization and sales of various types of property proved to be minimal for the entire period of the 2000'ses.

#### 5.1.5. Changes in the legislative and normative framework regulating the public sector

The year of 2009 was marked by introduction of a number of important innovations in the legislative and normative framework regulating activities of the unitary enterprises and economic entities where the government has its stake (participates). Indeed, these innovations are going to influence seriously the property policy of the federal government in the near future.

Of priority is Regulation of the RF Government of December 31, 2009 No 1188.

This Regulation demands from the executive federal authorities except President's Administrative Department, to present, within three months and according to the established procedure, draft acts for specifying the lists of federal government unitary enterprises (FGUPs) in their jurisdiction.

The Federal Property Management Agency is instructed, by July 1, 2010, to carry out actions in reference to FGUPs not included in the mentioned lists for their restructuring, liquidation or inclusion into a forecast plan (program) of privatization and to exercise ownership rights in relation thereto until such actions are completed.

The said Regulation made a number of amendments in and additions to the legislative and normative acts regulating functions of the unitary enterprises in federal ownership, the most significant changes being as follows:

Amendments in Regulation of the RF Government of December 3, 2004 No 739 “On the authorities of the federal executive authorities in exercising the ownership rights to the federal government unitary enterprise” expanded the range of authorities of the federal executive authorities in relation to enterprises in their jurisdiction that are included in the Forecast plan (program) of privatization of the federal property.

Earlier these authorities were exercised only in relation to enterprises to be converted into joint-stock companies with the contribution of shares into the charter capital of other joint-stock companies or keeping them in federal ownership.

Besides, the range of authorities now includes rendering support in preparation of documents by the enterprises required for taking decisions about the terms of privatization and the submission of these documents to the Federal Property Management Agency that has been granted the right to:

- request documents from the enterprises which the enterprises are obliged to keep according to the 2002 Law on Unitary Enterprises; while in relation to enterprises included in the Forecast plan (program) of privatization of federal property – request also documents required for taking decisions on the privatization terms and also to set the dates for their submission;
- launch claims to courts on invalidation of transactions performed by enterprises in violation of the established procedure;
- audit, within the framework of their authorities, the use of federal property being in economic management of the enterprises, decide on and carry out documentary due diligence and other audits, including inspections, and make decisions on auditing enterprises including those in the Forecast plan (program) of privatization of federal property to see whether federal property is used efficiently and kept safe.

The list of grounds to terminate an employment contract with a Leader of a federal unitary enterprise under the RF Government Resolution No 234 of March 16, 2000, was supplemented with such grounds as a failure to present or a failure to present on time, a failure to present valid (correct) and/or complete data (information) as necessary to the Federal Property Management Agency and/or a respective executive federal authority under which jurisdiction the given enterprise falls.

The Federal Property Management Agency was also granted the right to include their representatives with the decisive votes in the commissions in organizing a competition to fill the vacancy of the enterprise director and in certifying director’s competences.

The Regulation on the management of federally owned shares of open joint-stock companies and the use of a special right of the Russian Federation (“golden share”) to participate in the management of open joint-stock companies approved by the RF Government Resolution of December 3, 2008 No 738 was changed as follows:

Earlier the Federal Property Management Agency exercised the right of the federal government as a shareholder in different ways based on the classification of joint-stock companies with the federal government interest in their capital (three categories):

- joint-stock companies included in a specialized list<sup>1</sup> as agreed with the federal ministry or federal authorities of executive power vested with the authorities of management of

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<sup>1</sup> A group of companies of importance in relation to which the position of the federal government as a shareholder on a number of significant issues is defined by resolution of the federal government, Russian Government Chairman or his/her Deputy upon the Chairman’s assignment. Initially this List was approved by the RF Government in 2003, however it has been changed since then many times.

state property under the guidance of the President of Russia or the Government of the Russian Federation;

- joint-stock companies included in the list of strategic companies approved by the President of Russia (hereinafter the Strategic List)<sup>1</sup>, except joint-stock companies that are included in a specialized list – based on proposals of a federal agency in the jurisdiction of the federal ministry concerned or the respective federal body;
- other joint-stock companies - independently, while where a federal agency or a federal body as a shareholder presents proposals according to the established procedure – with account of those proposals.

RF Government Resolution of December 1, 2009 No 978, cancelled the category of strategic joint-stock companies keeping only the category of joint-stock companies in the specialized list; it was stated that in other joint-stock companies the Federal Property Management Agency exercises the shareholder's rights based on the proposals of the federal agency in jurisdiction of the federal ministry or the relevant federal body.

It was stated additionally that if a joint-stock company not included in the specialized list does not submit any proposals (also on candidates proposed for inclusion in the list of candidates for electing board of directors), the Federal Property Management Agency shall develop independently proposals on the federal government position as a shareholder.

The general change of the legislative and normative framework regulating activities of the unitary enterprises and economic entities where the federal government is involved, may be described as having a growing number of exclusions.

Thus certain government acts established that the above mentioned Regulation on the management of federally owned shares of open joint-stock companies and the use of a special right of the Russian Federation ("golden share") to participate in the management of open joint-stock companies shall not apply to management of federally owned shares of OJSC State Transportation Leasing Company, shares of joint-stock companies to be transferred to GK Rostechologies as an asset contribution of the Russian Federal Government before such shares are transferred. A number of authorities of the Federal Property Management Agency have been passed over to Administrative Board of the President of the Russian Federation and the Federal Agency of Marine and River Transport in relation to unitary enterprises in their jurisdiction, while late 2008 these authorities were transferred to the RF Ministry of Defense.

#### 5.1.6. Possible impact of the financial crisis on the property relations and prospects of their development

The anti-crisis actions of the RF Federal Government with a domineering trend of limiting direct involvement of the government in capital in principle set the context for this or other privatization scenario.

The development of a future privatization agenda and its possible format, however, meets with certain difficulties.

Firstly, the bulk of the state-owned property was represented by either low-liquidity assets (that required sizable investments or were insufficient in terms of giving control as in case of

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As for joint-stock companies included in this specialized list, if a federal ministry has federal agencies under its control, proposals submitted to the Federal Property Management Agency must reflect consolidated positions of the federal ministry and its federal agencies on each issue.

<sup>1</sup>Decree of President of Russia of August 4, 2004 No 1009.

minority shares) or very attractive assets (e.g. control or blocking stakes in national monopolies) which sale was quite possible but at the adequate market price if certain conditions allowed for this. It is quite probable that the list of problematic assets owned by the state will be expanded as the crisis continues.

Secondly, the financial crisis that brought about the collapse of the stock market, devaluation of assets and withdrawal from the market of many potential investors who experienced serious problems in their native countries still acts as a natural limiting factor of privatization.

In such situation prospects of significant growth of budget receipts from privatization are quite low moreover with account of lacking assets in the fuel and power complex. We may hope receiving large amounts of revenues only when the Russian economy begins showing signs of going out of the crisis while in the countries with more developed economies the crisis will be close to its end, and as a result of this a flow of capital and investments would be observed to the emerging markets including Russia.

Therefore no inclusion of major assets such as Sberbank, VTB, RZhd, Aeroflot, Shermetievo airport in the privatization program is planned for the near future. As for VTB, it is enough saying that in the mid-term there is a probability of selling its minority block of shares while presently the government interest in the VTB capital reaches 85.5%.

Thirdly, the orientation on the budget revenues as the only criterion of conducting the privatization policy, specifically in the context of crisis, contradicts the tasks of the so-called structural privatization primarily in attracting investments for production upgrade.

The Ministry for Economic Development jointly with the Federal Property Management Agency is drafting amendments for the Law on privatization that would allow conducting auctions with investment terms. In a number of cases, e.g. where state-owned stakes in infrastructure facilities are sold the auction terms may include the requirement to preserve the business profile<sup>1</sup>.

In this connection it would be worth reminding the low efficiency of the investment bids in the 90's. The volume of investments received from the sales at the investment auctions (with account of delivery of obligations of the previous years) in 1997 made 1.3% only of the total investments in the capital assets (in 1994–1996 less than 1%). Alongside with this quite a large number of investors participating in the investment bids demonstrated obvious examples of unfair behavior disrupting their commitments. As a result, the investment bids were cancelled (Second Law on privatization of 1997) and replaced for commercial bids with investment and/or social terms<sup>2</sup> where the property rights were granted to the auction winner only after certain commitments had been delivered. The current 2001 Law on privatization provides for bids as an independent method of privatization, however the exhaustive list of its possible terms<sup>3</sup> does not contain the terms of attracting investments for restructuring of a company. De-facto an auction with social terms may be deemed.

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<sup>1</sup> Interview with the Head of the Federal Property Management Agency E. L. Adashkin, RIA Novosti, www.rosim.ru, 25.11.2009.

<sup>2</sup> The commercial bid as an independent method of privatization was actively applied in 1992-1997 mainly for privatization of small businesses when the buyer of an enterprise undertook certain obligations, preserving the business profile, among them. After Law on privatization was enforced in 1997, the investment and the commercial bids merged actually into one method.

<sup>3</sup> The bid terms may be like follows: (1) keeping a certain number of jobs (2) retraining and raising qualification of the employees; (3) restriction on changes of the business profile of the unitary enterprise or designation of

Speaking about possible return to privatization practices with investment obligations and their future, we can assume that this aspect is similar to the issue of reasonable fine tuning of the tax system towards encouragement of certain types of activity (e.g. innovations). In other words, whether the government administration is sufficiently able to control the use of certain legal norms/provisions for compliance with their target purpose.

Fourthly, the critical condition of many private companies that rushed to get support from the government threw light on the fact that had not been obvious until recently that the private business is not always a synonym of an efficient and responsible owner of the assets. Comparison of efficiency of state-owned and private companies in terms of their resistance to crisis and needs in the government support requires additional examination in the context of present-day realities.

Fifthly, a partial shift of the “gravity center” from the government authorities to various integrated entities with government involvement in making decisions on privatization (one of such examples is Rosneftgaz that secures its indirect control over Rosneft and Gazpromneft) when these entities become owners of a large number of assets due to various reasons (assets are received from the government in the process of establishment and M&A) makes the position of the management of such entities very weighty.

Where such entities initiate sales of their assets, the state is obliged to receive certain reimbursement at least for the assets that had been contributed to those entities earlier for free. It refers primarily to state corporations established in 2007 – 2008 that proved to be outside the scope of true corporatization, and to the recipients of state support programs during the crisis. In some cases the government may put up with ignoring budget-related problems in the course of “big privatization” by integrated entities; but then the obligatory set of behavioral requirements to such business entities must include the absence of outstanding debts, refusal from participation in mergers and acquisitions for the definite period of time, active investments with account of priorities of the federal government anti-crisis program.

Otherwise there may be a return to the earlier privatization stages in Russia with fast and uncontrolled enrichment of the management in cases where a “shell” of a holding head company became a subject of corporate governance or privatization deprived of its valuable subsidiaries with their expensive production or financial assets.

In the sixth place, one should understand that stimulation of the privatization process as such is not a sufficient condition for changing the corporate control market situation. Much depends on the regulation of participation of companies with the government stake in mergers and acquisitions. The focus here should be placed on restricting the acquisition of non-core assets, better selection of decisions that require the agreement of the state both as the owner and the market regulator.

Thus the degree of real submission to the state control of the management of those companies in which the state participates, the degree of manageability, loyalty and the vision of the place and roles of particular assets through the lenses of long-term development of various integrated entities including state corporations moves to the forefront. This makes the task of improving corporate and strategic governance in the companies with the government involvement more urgent and up-to-date.

In this context rolling out the practice of attracting professional directors<sup>1</sup> to the management bodies of such companies could play a certain role.

The Federal Property Management Agency jointly with the RF Ministry for Economic Development began doing some work in execution of the assignments of the President of Russia set as a follow-up of his meeting with representatives of the Russian Union of Industrialists and Entrepreneurs held in April 2008.

For this purpose general provisions and normative acts regulating both the process of attraction of independent managers to the board of directors of joint-stock companies with the stake of the Russian Federation in their charter capitals and the issues of their activities<sup>2</sup> were developed; changes were made in the RF Government Regulation of December 3, 2004 No 738 “On the management of federally owned shares of open joint-stock companies and the use of a special right of the Russian Federation (“golden share”) to participate in the management of open joint-stock companies” regarding election of independent directors to the management bodies of those joint-stock companies which shares are owned by the Russian Federation. Early 2009, the Federal Property Management Agency by its order established a Commission for selection of independent directors, representatives of the interests of the Russian Federation and the auditors for electing them to the management bodies of joint-stock companies and approved the respective Regulation<sup>3</sup>.

The RF Government performed certain actions to secure the conclusion of contracts with the members of the board of directors who are professional directors; also joint-stock companies with the state involvement and professional directors on their boards of directors have been monitored with the subsequent evaluation of the implementation efficiency of this institution.

At the first stage of work in this direction, professional directors were selected in nine joint-stock companies that are in the specialized list approved by the RF Government Resolution of January 23, 2003 No 91-r, which 100 % shares belong to the Russian Federation

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<sup>1</sup> Following the established tradition of corporate governance of joint-stock companies with the state participation, board of directors members elected by votes according to shares owned by the federal government as a shareholder can be grouped as follows: (1) government officials who represent the interests of the federal government are obliged to vote according to the owner’s instructions; (2) representatives of the government interests who are proxies are obliged to vote according to the owner’s instructions on the limited range of 5 issues while on other issues – at their own discretion (this mechanism of securing the government interests emerged in 1996 but has not been widely applied since then); (3) independent directors who vote being guided by their personal professional experience and opinion and meet the established selection criteria. According to the Federal Property Management Agency, the persons in the second and third groups may be called professional directors.

<sup>2</sup> Among others, were defined:

- criteria of professionalism and independence of BoD members applied to individuals proposed by the federal government for their selection and further engagement as independent directors in joint-stock companies;
- the list of joint-stock companies which BoDs should have professional directors;
- the number of independent directors and professional proxies determined in relation to the size of the RF government stake;
- the selection procedure of professional directors and the principle of creating a list of candidates for election into open JSC management bodies as independent directors and professional directors-proxies;
- criteria of referring a board director to independent directors and the development of the respective requirements to the candidates.

<sup>3</sup> Does not apply to JSC that are included in the specialized list in relation to which the position of the state as a shareholder on a number of important issues is defined by the decision of the RF Government, the RF Government Chairman or the RF Government Chairman Deputy in the name of the Chairman. Initially approved by the RF Government.

(OJSC Agency for Mortgage and Housing Crediting, OSC Joint-Stock Company for Oil Transportation Transneft, OJSC Zarubezhneft, OJSC Corporation Roskhimzaschita, OJSC International Airport Sheremetievo, OJSC Russian Railways, OJSC Rosselkhozbank, OJSC SG-Trans and OJSC Modern Commercial Fleet).

At the second stage of the implementation of the objective to increase the number of professional directors on the boards (Supervisory councils) of the joint-stock companies which shares are owned by the Russian Federation, extraordinary general meetings of shareholders were held, and new management bodies were elected with participation of professional directors in another seven companies: OJSC Aeroflot – Russian Airlines, OJSC Russian Fuel Company Rostoprom, OJSC FSK Unified Energy Network, OJSC Rosagroleasing, OJSC RusHYDRO, OJSC Holding MRSK and OJSC RAO Energy Networks of the East<sup>1</sup>.

According to the Federal Property Management Agency, by autumn 2009 the BoDs (Supervisory councils) of 253 joint-stock companies had 563 professional directors while at the end of 2008 their number was about 50<sup>2</sup>. Thus we can state that early 2009 this institution was implemented in 7.6% of the companies with the federal government stake of their total number. This institution has been most widely applied in the electric energy and communications sectors.

Besides, the Federal Property Management Agency also applied the practice of engaging managing companies that acted as sole executive bodies of the joint-stock companies, but this practice has been even less popular than the institution of professional directors (as of the end of 2009 only six managing companies had been involved in management of the joint-stock companies with the government stake).

A most important area of activities of professional directors to improve performance and efficiency of the joint-stock companies with the government interest should be their work on three specialized Committees at the management bodies of these companies (Strategic Planning Committee, Audit Committee and HR and Remuneration Committee); it is proposed to elect as Chairmen of these Committees those board members who are not government officials (but independent directors or professional proxies).

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<sup>1</sup> Federal Agency for Federal Property Management. Progress report for 2008, M., 2009.

<sup>2</sup> T. Zykova. To replace civil servants// Russian Gazette, September 16, 2009. Federal Agency for Federal Property Management. Progress report for 2008, M., 2009.