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Mixed Ownership in Corporative Sector: Evolution, Management, Regulation

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The main objective of this publication is to analyze the system of governance of companies with mixed ownership, reveal issues and contradictions arising as a result of this sector reform, evaluation of their place and prospects in the light of Russia's economy modernization. The authors analyze the dynamics and structure of economic entities with the state capital participation. They evaluate the normative and legal basis that regulate their activity, analyze the influence of the governments on economic entities of this type being their joint owners, provide policy proposals regarding public ownership policy with respect to improving the system of governance of such companies including potential privatization. Review of law enforcement in the sphere of mixed ownership (ch. 4.2, 4.3) was done by E. Apevalova. Review of the Canadian experience in this sphere (ch. 5) was prepared by Harry Swain.

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Introduction

The issue of state participation in the capital and activity of economic societies – or, in other words, the issue of forming companies with mixed capital in the corporate sector under conditions of transition from centralized economy to a market one, cannot be placed, either in terms of theory or in actual practice, within the category of issues that were actively discussed in the 1990s, when the themes of market transformation in post-socialist countries had come to occupy a prominent place in the studies of a wide circle of economists. This situation can be rather easily explained by the fact that the standard set of problems, which was the object of academic discussions and practical decisions of that time, included the issues of anti-inflation policy and financial stabilization, price and commodity markets liberalization, general principles of property reform and privatization of state property, attraction of foreign investments and the integration of the national economy into the global one. Apparently, the problem of acknowledging the place that should belong to the state sector during the period of market reforms, and the need to understand which of its forms should be conducive to the development of the economy as a whole were not viewed as a high-priority and important issue.

The development of an economy in transition is based on the interaction of economic subjects of various organizational-legal forms. Large-scale institutional changes centered on the reforming of ownership result in the reduction of the State's stake in the economy and in the concentration of economic activity in the private sector. Wedged between these two sectors are the enterprises of the mixed form of ownership, that is, those enterprises where some part of capital belongs to the State, and the rest of it – to other juridical and physical persons.

That the State did preserve significant control (including property control) over many spheres of the economy in the process of radical market reforms was, in a sense, predetermined by both objective and subjective initial circumstances.

In the former category of circumstances we may place the scale characterizing the object of potential privatization, which is incomparable with that in eastern European countries (a giant number of enterprises and

total lack of any legally existing private sector in all the spheres of the economy) and the specific structure of industry (a large share of the military-industrial complex and of the branches associated with it; a high power intensity of production, which explains the State's regulatory interest in the sectors whose economic activity has been largely determining the inflation background of the economy as a whole; the special role, in the budget, of the payments and contributions coming from the fuel and energy complex; the excessive concentration of production and the resulting monopolization of commodity markets; etc.).

The latter group of circumstances is associated with the opposition to the privatization process by the central bureaucracy, which still retains some of its former influence, and by a part of the directors' "corps". In the course of time, the state of ownership relations has also been increasingly influenced (because of the sheer size of the country and the large specificity of its territories) by the authorities in Russian regions. The enterprises with mixed capital offered an apparent and the most readily accessible base for strengthening this influence.

Global economic practice of the past two decades (including market reforms in the countries with economies in transition) has offered some examples of how the State was temporarily decelerating the process of privatization because of its desire, quite understandable from the point of view of common sense, to find appropriate investors for enterprises, as required by the programs of the structural transformation of the economy as a whole and of its individual branches in particular, or how the State suspended the already agreed upon sale of the blocks of shares in certain enterprises in expectation of their quotations to go up on the stock market.

In Russian reality of the 1990s (characterized by a weak State, by the existence of informal relations between some of its representatives and businesses, which resulted in an unjustified preferential treatment of certain structures over the rest of them, and by elements of corruption and criminality) this policy of state control agencies (which, in principle, can be possible and rather reasonable under certain conditions), got entwined with an acute conflict of interests between various bureaucratic structures within the system of state power, businesses, and the top managers of

those enterprises that became the main target of property reform in Russia during its first phase.

The emergence, alongside other corporate governance models, of the mixed private – public control model became one of the typical phenomena observed in the majority of countries with transition economies in the 1990s. However, it seems that only in Russia the issue relating to the functioning of this particular type of enterprises have come to play a very important, if not decisive, role from the point of view of the country's further development at a stage when the goal of rekindling economic growth became a priority.

Of course, many aspects of the functioning of these economic subjects have been already studied earlier, both in the context of the general problems associated with the reforming of the public sector in Russia's economy in transition and the management of state property, and within the framework of certain applied issues (comparative efficiency, management rotation, etc.). In the first category, the fundamental studies by V.I. Koshkin (1997, 2002), V.N. Shupyro (1997), V.V. Bandurin (1999), and those ed. by R.M. Nureev¹ stand apart as the most prominent ones. Special focus in this connection should be placed on the students' manual published by the G.V. Plekhanov Russian Academy of Economics, which

¹ *Upravlenie gosudarstvennoi sobstvennost'iu. [Management of state property.]* Ed. by V.I. Koshkin, V.N. Shupyro. – M.: Infra-M, 1997; *Pravovoe obespechenie ekonomicheskikh reform [Legal backing for economic reforms.]* / Ex. Ed. Ya. I. Kuz'minov, V. D. Mazaev. *Predpriiatiia. [Enterprises].* M.: SU-HSE, 1999; Bandurin V.V., Kuznetsov V.Yu. *Upravlenie federal'noi sobstvennost'iu v usloviakh perekhodnoi ekonomiki. [Management of federal property in conditions of a transition economy.]* M.: "Nauka i Ekonomika", 1999; *Upravlenie gosudarstvennoi sobstvennost'iu. [Management of state property.]* Ed. by Dr. Ec. Sci. V.I. Koshkin, An expanded and revised edition. – M.: EKMOS, 2002; *Ostatocchnaia gosudarstvennaia sobstvennost' kak ekonomicheskii institut. Ostatocchnaia gosudarstvennaia sobstvennost': problemy effektivnogo upravleniia. [Residual state property as an economic institution. Residual state property: problems of efficient management.]* In: *Ekonomicheskie sub"ekty postsovetskoi Rossii (institutsional'nyi analiz). [Economic subjects of post-Soviet Russia (an institutional analysis).]* Ed. by Dr. Ec. Sci. R. M. Nureev. 2nd edition, expanded and revised. In 3 parts. Part 3. *Gosudarstvo v sovremennoi Rossii. [The State in contemporary Russia].* Series "Nauchnye doklady: nezavisimyi ekonomicheskii analiz". ["Scientific reports: independent economic analysis"], No 150 (3). M.: Moskovskii obshchestvennyi nauchnyi fond [Moscow Public Science Foundation], 2003.

addresses specifically the issue of state-owned shares². Within the second category, the studies by P.V. Kuznetsov and A.A. Muraviov can be placed³. Some of the aspects of the functioning of companies with mixed capital are discussed in a number of studies on corporate governance performed at leading research centers⁴.

The latest works that address companies with mixed capital are as follows: “Enterprises with State Participation: Institutional-Legal Aspects and Economic Efficiency”, published by the MPSF and the Association of Researchers of the Public Sector of the Economy” in 2004; the study by S.B. Avdasheva, T.G. Dolgopiatova, and X. Plines “Corporate Governance in Joint-Stock Companies with State Participation: Russian Problems in the Context of Global Experience”, published at the State University – Higher School of Economics in 2007. These studies successfully combine a generalized overview of the problem and with a thorough examination of its individual aspects.

At the same time, it remains necessary to assess how the process of improving the governance of economic societies with state participation in capital is going on, and what progress has been achieved in recent

² Galanov V.A., Grishina O.A., Shibaev S.R. *Upravlenie gosudarstvennoi sobstvennost'iu na aktsii [Management of state ownership of shares: A Textbook.]* / Ed. By Galanov V.A. – M.: Finansy i statistika, 2004.

³ P. V. Kuznetsov, A. A. Muraviov. *Gosudarstvennye kholdingi kak mechanism upravleniia predpriiatiiami gosudarstvennogo sektora. [State holdings as a mechanism for managing enterprises in the public sector.]* In: *Voprosy ekonomiki*, 2000, No. 9, pp. 34–47; Muraviov A. *Gosudarstvennye pakety aktsii v rossiiskiykh kompaniiakh. [State-owned blocks of shares in Russian companies.]* In: *Voprosy ekonomiki*, 2003, No. 5, pp. 101–120.

⁴ E. g. Radygin A., Entov R. *Institutsional'nye problemy razvitiia korporativnogo sektora: sobstvennost', kontrol', rynek tsennykh bumag. [Institutional problems of the corporate sector's development: property, control, securities market. M.: IET, Nauchnye trudy [Scientific Works] No. 12-r, 1999; Radygin A., Entov R. Korporativnoe upravleniie i zashchita prav sobstvennosti: empiricheskii analiz i aktual'nye napravleniia reform. [Corporate governance and protection of property rights: empirical analysis and important directions of reforms]. M.: IET, Nauchnye trudy No. 36-r, 2001; Radygin A., Entov R. Problemy korporativnogo upravleniia v Rossii i regionakh. [Corporate governance issues in Russia and the regions]. M. IET-CEPRA, 2002. In this context the numerous studies conducted by the State University – Higher School of Economics (GU-HSE) and the Bureau for Economic Analysis (BEA) should also be noted.*

years in this part of the public sector as regards the directions outlined in the late 1990s – early 2000s.

The major goal of the present study is to analyze the system of management applied to enterprises with the mixed form of ownership, to reveal the problems and contradictions emerging in the course of reforming this sector, to assess their importance, role and prospects in the context of resolving the tasks of modernizing Russia's economy.

In accordance with the specified goal, the following problems were being dealt with in the course of our work:

- the dynamic and structure of those joint-stock companies whose shares were in public (mostly federal) ownership were analyzed;
- the normative-legal basis regulating their activity at all levels of power was assessed;
- the attempts undertaken by the control bodies in order to improve the governance of the sector of enterprises with the mixed form of ownership were estimated; and
- proposals were made concerning the improvement of the system of management of such enterprises, including the possibility of their privatization.

Bearing in mind the specificity of the present study and its apparent orientation to analyzing the practice existing in Russia, it was mainly based on the normative-legal acts and the official data, publications and other materials issued by various departments (first of all, the RF Federal Agency for the Management of Federal Property and its predecessors⁵), as well as on publications in the periodical press. Besides, we applied the RF Rosstat's information.

⁵ Because of the lengthy time-span addressed in the work, the names of government agencies as they existed both before and after the major reorganization of the RF Government in March 2004 will be used hereinafter.

1. State Participation in the Russian Corporate Sector in Conditions of Economic Growth Revival in the 2000s

The new phase of reforming ownership relations in Russia was initiated by the Concept for the Management of State Property and Privatization in the Russian Federation (hereinafter – the Concept), approved by Decree of the RF Government, No. 1024, of 9 September 1999. It is quite symptomatic that, maybe for the first time since 1992, the problem of managing state property did receive priority over that of formally changing the form of ownership. A sharp decrease in the value of enterprises and their blocks of shares after the devaluation of the rouble made it logical for the federal center to refocus its actions, in 1998–2000, so as to increase the share of non-tax revenues in the budget by using state property, which automatically required that clarity and transparency be introduced in the relations between various levels of authority.

That document, as well as “The Main Directions of the Socio-Economic Policy of the Government of the Russian Federation for the Long-Term Perspective”, approved by Russia’s government in summer 2000, are based on the assumption that under present conditions the main directions of state policy in the sphere of state property management should be as follows:

- improving the efficiency of the management of state property that has remained in state ownership;
- privatization of a significant part of state property.

As a separate object of state property policy, alongside unitary enterprises and real estate, the 1999 Concept singles out economic societies with state participation⁶.

⁶ The goals of managing state-owned blocks of shares (or shares or stakes) and the methods for achieving them in accordance with the 1999 version of the Concept are given hereinafter in an abridged form, so as to reflect only the essence of this document. In full, the formulations of the Concept and an analysis of the extent of their implementation are presented in *Appendix*.

The major **goals** of managing state-owned blocks of shares (or stakes) were defined as follows: (1) increasing the non-tax revenues in the federal budget; (2) ensuring the performance of general state functions by economic societies; (3) improving the financial and economic indicators of their activity, stimulating the development of production and the attraction of investments; (4) optimizing the administrative costs; (5) carrying out institutional changes in the economy.

A necessary precondition for taking measures designed to achieve the afore-said goals is the availability of objective information for choosing appropriate instruments to be applied to each object. Therefore, it is totally justifiable that the initial measure should be the classification of economic partnerships and societies by quantitative and qualitative indicators (the degree of liquidity of shares, the branch a partnership or society belongs to, the character of the goals pursued by the State in their activity, the possibility of influencing their activity, which depends on the size of the State's stake, their financial state, the number of workers, and the size of their fixed assets).

The major **methods** recommended by the document **for achieving the goals** are based on the following control mechanisms.

1. In order to perform the general state functions when managing the state-owned shares:

- the coordination of the activity of ministries and departments in the process of managing the blocks of shares by a federal agency for state property management;
- the establishment of the procedure for the certification of specialists in the sphere of management of economic partnerships and societies;
- the appointment of representatives of the State, from the ranks of state employees, to the administrative bodies of economic societies, and the issue to them of written instructions for voting therein;
- full-time representation of RF interests in the administrative bodies of largest joint-stock companies, whose products (or services or work) are of strategic importance for the national security of the State – as a rule, by a state employee;

- the allocation of financial resources for the upkeep of the institution of state representatives – for example, at the expense of dividends on state-owned shares;
 - the acquisition of shares in joint-stock companies for the purpose of increasing state participation therein, if this is deemed to be necessary for performing general state tasks.
2. In order to increase the non-tax revenues of the budget:
- the transfer of shares into the ownership of RF subjects as a set-off of the federal center’s financial liabilities, on condition of the regions’ submitting the programs for developing their enterprises;
 - the acquisition of shares for forming them into blocks, the subsequent sale of which would guarantee maximum revenues for the budget;
 - the issue of derivative securities with the right to acquire shares, after the expiry of a specified period of time, with a simultaneous transfer of the said shares into the trust management of the buyer of the derivative securities;
 - the realization of shares, which is to be preceded by the pre-sale preparation and reorganization of the enterprises;
 - with regard to some of the economic societies – the withdrawing from them, after receiving the actual value of a share, calculated on the basis of an estimation of the net assets of each organization.
3. In order to stimulate the development of production and to improve the financial and economic indices of activity of economic societies:
- the use of state-owned shares as a security for investments or credits allocated for purposes of implementing target projects;
 - the use of shares in order to attract investments in vertically integrated structures (the shares included in the authorized capital of an integrated structure serve as security);
 - the attraction of an efficient owner, who would acquire shares in the process of privatization on condition of making investments in the enterprise;
 - to increase the investment attractiveness of enterprises in the eyes of domestic and foreign investors by reducing the State’s share in their charter capital.

4. In order to optimize administrative costs:
 - to reduce the number of blocks of shares in federal ownership to the level that would make it possible to exercise the State’s regulatory and control functions through selling shares; their consolidation in vertically integrated structures with homogeneous technologies or sales markets, for their transfer to the regional (or municipal) level;
 - to include, in the charter capital of a company formed on a principle of “portfolio funds”, the small blocks of shares with regard to which a decision to sell has been made, but the actual sale has not been materialized, and the blocks of shares the selling of which could not result in any considerable revenues for the budget. Such a company would obtain a certain degree of independence, provided that there exists a mechanism for exercising control over its activity (a supervisory board or a board of trustees);
 - to sell small non-liquid blocks of shares, at favorable prices, to their issuer and the workers.
5. In order to undertake institutional reforms of the economy:
 - to form vertically integrated structures;
 - to encourage the adoption of decisions concerning the reorganization or bankruptcy of enterprises with considerable arrears of payments due to the budget, on their owners’ initiative, in order to capitalize the arrears into liquid shares in the efficient companies newly founded as a result of the reorganization;
 - to restructure large enterprises, with separating out the property complex needed by the State for dealing with general public issues, so as to create, on its basis, a joint-stock company totally owned by the State, and to sell the rest of the property in order to develop new production or to diversify production;
 - to carry out the acquisition and the subsequent sale of shares by way of including land plots in the charter capital of joint-stock companies.

1.1. The Quantitative Characteristics of the Ownership-Related Presence of the State in Corporate Capital

1.1.1. The General Dynamic and Branch Peculiarities

Despite the abundance of estimations concerning the extent of the State's involvement in the property relations in the corporate sector, which emerged in the second half of the 1990s as a result of mass privatization, officially (on the level of a government document) such information appeared only as late as 1999, when the Concept for the Management of State Property and Privatization in the RF was adopted. It is in the text of this document that for the first time the data on the number of economic societies subdivided in accordance with the percentages of corresponding blocks of shares (or shares or stakes) in charter capital were presented. Later on, such data were frequently published by the federal agencies for property management. All of them are generalized below in *Table 1*. The classification of joint-stock societies by the criterion of the State's stake in their charter capital is as follows:

- up to 25% of shares is in state ownership (or a minority block of shares);
- between 25% and 50% of shares is in state ownership (or a blocking parcel of shares);
- between 50% and 100% of shares is in state ownership (or a controlling block of shares);
- 100% of shares is in state ownership (or a complete block of shares);
- with the use of the special right of “golden share”, when singling out the companies where only this instrument is applied (without a parallel presence of ordinary shares).

It should be noted that in the following text the case in point will be precisely those open-end joint-stock companies (OJSCs) the shares in which constitute the most significant part of the treasury's federal property, because it is they that form the absolute majority of all economic societies with state participation, while companies of other organizational-legal forms (CJSCs) represent a rare exception. Also not to be considered are those economic societies in which regions and municipalities

have a stake; the functioning of these entities should be the subject of special investigation.

Table 1

The Dynamic and Structure of Joint-Stock Companies with State Stakes in their Capital in 1999–2006 (including by Applying the Special Right of “Golden Share”), by Size of the State Stake

Date	total		up to 25%		between 25% and 50%		between 50% and 100%		100%		“golden share”	
	units	%	units	%	units	%	units	%	units	%	total	no shares
1999	3316/ 3896*	100	863	26.0	1601	48.3	470	14.2	382	11.5	580	**
1 January 2001	3524***	100	1746	49.55	1211	34.4	506	14.35	61	1.7	...	...
1 August 2001	3949 ****	100	1843	46.7	1393	35.3	625	15.8	88	2.2	542**	
1 January 2002	4407 *****	100	2270	51.5	1401	31.8	646	14.65	90	2.05	750**	
1 January 2003	4222	100	2152	51.0	1382	32.7	589	13.95	99	2.35	1076	118
1 June 2003	4205	100	2148	51.1	1339	31.8	600	14.3	118	2.8	...	...
1 October 2003	4035	100	2051	50.8	1308	32.4	552	13.7	124	3.1	640	148
1 January 2004	3704	100	1769	47.75	1235	33.35	540	14.6	160	4.3	591	251
1 June 2004	3905	100	1950	49.9	1183	30.3	499	12.8	273	7.0	...	...
1 March 2005	4075/ 3791#	100	1697	44.8	1154	30.4	487	12.85	453	11.95	...	284
1 June 2005	3783/ 3524##	100	1544	43.8	1093	31.0	474	13.5	413	11.7	...	259
1 June 2006	3724/ 3481###	100	1063	30.5	885	25.4	397	11.4	1136	32.6	...	243

* – in the 1999 Concept for the Management of State Property and Privatization 3,896 economic societies are mentioned (including 3,611 open-end joint-stock companies (OJSCs), 251 close-end joint-stock companies (CJSCs) and 34 limited partnerships (LPs) and limited liability companies (LLCs)), in whose capital the RF held a stake. 3316 units is an estimated value obtained by adding up the numbers of variously sized shares (stocks, stakes) mentioned in the Concept’s text;

** – total number of joint-stock companies (JSCs) to which the “golden share” special right is applied, without distinguishing those where the State at the same time holds no blocks of shares;

*** – JSCs, without 48 stakes and blocks of shares in foreign companies;

**** – data taken from the 2002 draft privatization program submitted by the RF Ministry of State Property to the Government; at the same time, according to the RF Ministry of State Property's Register, as of 1 September 2001, 4308 blocks of shares in JSCs were federal property;

***** – OJSCs, without shares in 75 CJSCs and stakes in charter capitals of LLCs transferred on the basis of the RF Government's Order of 2 April 2002, No. 454-r, "On termination of state participation in charter capitals of credit institutions", or received in the procedure of inheritance, gift, or on other grounds;

– 3791 units – the estimated number of JSC whose shares are property of the RF, without 284 JSCs where the "golden share" right is applied (without holding a block of shares). The percentage of JSCs with certain stakes in their capital, for the sake of compatibility with the data as of previous dates, has been calculated on the basis of this value. Reference: as of 1 January 2005, shares in 3767 JSCs were federal property, without the already mentioned 284 JSCs with "golden share" and shares in charter capitals of 24 LLCs transferred to the treasury by Order of the RF Government of 2 April 2002, No. 454-r, "On termination of state participation in charter capitals of credit institutions";

– 3524 units – the estimated number of JSCs whose shares are property of the RF, without 259 JSC where the "golden share" right is applied (without holding a block of shares). The percentage of JSC with certain stakes in their capital, for the sake of compatibility with the data as of previous dates, has been calculated on the basis of this value;

– 3481 units – the estimated number of JSCs whose shares are property of the RF, without 243 JSC where the "golden share" right is applied (without holding a block of shares). The percentage of JSC with certain stakes in their capital, for the sake of compatibility with the data as of previous dates, has been calculated on the basis of this value.

Source: the official website www.mgi.ru; Rossiiskaiia ekonomika v 2001 godu. Tendentsii i perspektivy. [The Russian economy in 2001. Trends and prospects.] (Issue 23). Vol 2. M., IET, March 2002, 62; Braverman A.A. O merakh po povysheniiu effektivnosti upravleniia federal'noi sobstvennost'iu i kriteriiaikh eio otsenki. [On measures designed to improve the efficiency of management of federal property and criteria for its assessment] // Vestnik Minimushchestva Rossii [Herald of the RF Ministry of State Property], 2003, No. 1, pp. 13–14; Predpriiatiia s gosudarstvennym uchastiiem. Institut-sional'no pravovye aspekty i ekonomicheskaiia effektivnost'. [Enterprises with state stakes. Institutional-legal aspects and economic efficiency]. Series "Nauchnye doklady: nezavisimyi ekonomicheskii analiz" [Scientific reports: independent economic analysis], No. 155. M.: Moscow Public Science Foundation; Association for Research on the Public Sector's Economy, 2004, p. 47; Federal Property Privatization Program for 2004. (Forecast Plan (Program) for Federal Property Privatization in 2004 and the main directions for federal property privatization until 2006) // Vestnik Minimushchestva Rossii [Herald of the RF Ministry of State Property], 2003, No. 3, p. 4–5. Key issues of improving the efficiency of federal property management and the main directions of the dividend policy of the Russian Federation // Vestnik Minimushchestva Rossii [Herald of the RF Ministry of State Property], 2003, No. 4, p. 8; Forecast Plan (Program) for Federal Property Privatization in 2005; Materials for the RF Government Meeting on 17 March 2005, "On measures

designed to improve the efficiency of management of federal property”; Forecast Plan (Program) for Federal Property Privatization in 2006 and the main directions of federal property privatization for 2006 - 2008; Forecast Plan (Program) for Federal Property Privatization in 2007 and the main directions of federal property privatization for 2007–2009; the authors’ estimation.

As follows from *Table 1*, by the changes in the number of such companies in 1999–2005, two periods can be distinguished: 1) 2000–2001, when the number of JSCs whose shares were federal property was growing, and 2) 2002–2004, when their number began to decline. In the year 2001 alone the number of such JSCs increased by a quarter (or by 883 units) and amounted to 4,407 units, which represented an absolute high for the whole period of study. In later years there emerged a trend toward a decline in the number of JSCs whose shares were federal property. During 2002 their number decreased by 4.2% (or by 185 units), during 2003 – by 12.3% (or by 518 units).

The changes in the total number of JSCs whose shares were federal property represent the sum of two vectors: on the one hand, it may grow due to the transformation of FSUEs into joint-stock companies or to some other actions resulting in the transfer into federal ownership of blocks of shares (stocks, stakes), while on the other, the sale of such blocks of shares in the course of privatization procedures decreases their number in the RF treasury.

However, in terms of actual practice the noticeable growth in the number of JSCs with a federal stake observed in 2000–2001 reflects, most probably, the successful inventory of federal property carried out after the adoption of the 1999 Concept, rather than any true growth in the number of the JSCs in question, because the number of FSUEs being transformed into joint-stock companies and the number of sold blocks of shares, as it will be shown later, began to markedly grow only in 2003–2004.

If we look at the structure of all the JSCs with federal stakes from the point of view of the extent to which these federal stakes can indeed provide the State as its owner with the adequate control over a company, the following can be noticed. The percentage of those JSCs, where stakes of more than 50% (including all 100%) was federal property, in 2001–2003 amounted to 16–17 %, having increased by early 2004 to approximately

19%. Simultaneously there occurred a slight decline in the percentage of stakes sized up to 25 % of charter capital and of blocking stakes (sized between 25% and 50%), which had been approximately one-half and one-third of all federal stakes, respectively.

Special note should be made of the shifts that took place in 2004–2006, when the federal stakes of all sizes except 100% were decreasing. As a result, as of 1 June 2006 the structure of all federal stakes was as follows: the stakes sized up to 25% of total capital constituted slightly over 30% of all JSCs with state stakes, the stakes of blocking sizes (between 25% and 50% of capital) – approximately one-quarter, in 44% of all companies the State could execute majority or full control, the percentage of those belonging to the latter category (with a state stake of 100%) was nearly three times higher than the share of those JSCs where the State, while being a majority stakeholder, owned less than 100% of shares.

If we compare, by the size of the state stake in a charter capital, the structure of federal blocks of shares as it had emerged by mid-2006 with the structure considered by the RF Ministry of State Property as the expected one after the implementation of the 2003 privatization program⁷, it will be observed that the planned threshold was reached with a two-year lag. Thus, it was planned that the percentage of minority blocks of shares should be decreased to 36% (the actual index –30.5%), and that of blocking stakes – to 22% (the actual index – 25.4%). The percentage of complete stakes was to become 30% (actually – 32.6%). Only the expected percentage of controlling blocks of shares (12%) was approximately the same as that existing in mid-2006 (11.4%). The obvious distortion toward the prevalence of blocks of shares that did not enable the State to hold the necessary degree of control over companies, which had been the legacy of the monetary privatization of the late 1990s, was successfully eliminated.

⁷ It was expected that a total of 3,613 blocks of shares would be federal property. In: Braverman A.A. O merakh po povysheniiu effektivnosti upravleniia federal'noi sobstvennost'iu i kriteriakh eio otsenki. [On measures designed to improve the efficiency of management of federal property and criteria for its assessment] // Vestnik Minimushchestva Rossii [Herald of the RF Ministry of State Property], 2003, No. 1, p. 29.

A less homogenous picture emerges if we compare the structures of the federal blocks of shares in June 2006 and 1999 (according to the Concept). The main trend was that of a considerable increase (by 2.8 times) in the percentage of those JSCs where the whole capital was owned by the State and in that of minority blocks of shares (by 4.5 p.p.), while the percentages of all other groups of stakes were decreasing. The most noticeable decline (by 1.9 times) was demonstrated by the percentage of blocking stakes (from 25% to 50%), while the percentage of stakes sized between 50% and 100% also increased, although by only approximately 3 p.p. In this connection, it should be borne in mind that the data for 1999 are probably incomplete.

Nevertheless, it can be stated that the number of registered federal stakes less than 25% in size as of 1 June 2006 (1063 units) was by 1.23 times higher than in 1999, having reached its historic high in early 2002 (2270 units), followed by a steady decline (except during the first half-year of 2004). The number of federal stakes sized between 25% and 50% in 2006 (885 units) was nearly by 45% lower than in 1999 (1601 units). At the same time in early 2002 (1401 units) it was higher than one year earlier (1211 units), after which a steady decline was seen. The number of federal stakes sized between 50% and 100% in 2006 (397 units) was by approximately 15% lower than in 1999 (470 units), although it was fluctuating rather noticeably during the period of analysis, amounting to 646 units in early 2002 and 600 units as of 1 June 2003, after which a steady period of decline followed. As for the number of JSCs with 100% federal stakes, in 2006 it was approximately three times as high as in 1999. Its historic low was registered as of the beginning of 2001 (61 units). Later on it grew steadily, making a leap between 1 June 2005 and 1 June 2006 by 2.8 times (or by 723 units).

The scope of application of the special “golden share” right reached its historic high in early 2003 when, in addition to those 958 JSCs where it was applied simultaneously with the existence of a federal stake, there were also 118 JSCs where the State was not a shareholder (for reference: in 1999 there were 580 JSCs where this instrument was applied, and in early 2002 – 750). In 2003–2004, as the process of federal stakes being sold out was gaining in strength, the total number of such JSCs was de-

creasing (591 units as of the beginning of 2004), but at the same time the number of those companies where the state's participation in terms of property was reduced only to the exercise of the special right: 284 units as of 1 March 2005 (historic high for the whole period of 1999–2006), which is by 2.4 times higher than in early 2003. The number of JSCs with the exercise of the special right only in % of the total number of JSCs with “golden share” also increased: as of the beginning of 2003 it was approximately 11%, while as of the beginning of 2004 – more than 42%. However, later on the absolute number of JSCs with the exercise of only the special right became lower: 243 units as of 1 June 2006 against 259 units one year earlier.

As was demonstrated in subsection 4.3, an important aspect of the State's participation in a share capital is the status of federal stakes in terms of their being at the disposal of different departments. The information concerning this issue, in contrast to the structure of the total body of state stakes, is rather limited (*Table 2*).

Table 2

The Structure of Joint-Stock Companies in whose Capital the State was a Participant as of the Beginning of 2002, Depending on Status Based on the State Stake's Size

Status	Total		up to 25%		between 25% and 50%		more than 50%	
	units	%	units	%	units	%	units	%
RFPF*	2,333	100	1491**	63.9	543	23.3	299	12.8
Other	2,074	100	779	37.55	858	41.4	437	21.05
Total	4,407	100	2270	51.5	1,401	31.8	736***	16.7

* – for reference: in 2001 the RFPF had at its disposal approximately 2,400 blocks of shares, of which 1/3 were stakes of no less than 10% of shares, another 1/3 – stakes between 10% and 25%, while all the other stakes were more than 25%, including those 55 companies where the RFPF was the owner of 100% of shares;

** – including 692 stakes sized between 10% and 25%, 301 stakes sized between 5% and 10%, and 498 stakes sized less than 5% ;

*** – including 90 complete (100%) blocks of shares.

Source: Gazetov A., Ditrikh E., Kotliarova E., Skripichnikov D. Doklad po korporativnomu upravleniiu gosudarstvennymi predpriiatiiami v Rossii. [A report on corporate governance of state enterprises in Russia // Russia's Round Table on Corporate Governance, 2–3 June 2005 (within the framework of the TACIS Program and the Global Forum on

Corporate Governance); Muraviov A. Gosudarstvennye pakety aktsii v rossiiskikh kompaniiakh: proiskhozhdenie, tipy i vliianie na resul'taty deiatel'nosti. Analiticheskii dok-lad. [State-owned blocks of shares in Russian companies: origins, types and influence on the results of activity. An analytical report]. M., RCER, 2003, p. 8; p. 33; the authors' estimations.

A comparison between the structure of blocks of shares being managed by the RFPPF with that of all the other types of stakes has yielded some quite obvious results. Among those held by the RFPPF's, minority stakes prevail (of up to 25%), constituting approximately 64% of all its stakes, while among all the other types of blocks of shares they constituted less than 38%. The biggest groups of stakes held by the RFPPF's were those sized between 10% and 25% (692 units), between 25% and 50% (543 units) and sized less than 5% (498 units). At the same time, in the structure of all the other types of blocks of shares, by contrast with those held by the RFPPF, the shares of controlling stakes (21% against 12.8%) and of blocking ones (41.4% against 23.3%) were more prominent. At the same time, the RFPPF was managing approximately 39% of all the blocking and 41% of all the controlling stakes. And we take into consideration the data on the number of complete stakes held by the RFPPF in 2001, it can be supposed that it had at its disposal more than 60% of all complete stakes (100% of shares), although this does not follow from the table directly.

It is not easy to analyze the changes in the structure, by branch of industry, of JSCs with federal stakes (including those to which the special "golden share" right is applied, without holding any shares). This is because, firstly, such information was for the first time released only as late as the beginning of 2002, and secondly, because the classification of the branches of the national economy is constantly being changed, they are being regrouped or redistributed into larger units, the result of which is that they are quite incomparable if taken at different dates. More or less compatible are the data relating to the period of 2002–2003 (*Table 3*).

Table 3

**The Dynamic and Structure, by Branch of Industry, of those
Joint-Stock Companies whose Shares are Federal Property,
or to which the Special “Golden Share” Right is Applied,
in 2002–2003**

Branch	as of 1 January 2002		as of 1 January 2003		as of 1 June 2003	
	units	%	units	%	Units	%
Industry, including	1837	41.8	...	...	1350	32.1
- machine-building and metal processing (without industrial medi- cal technologies)	778	17.7	719	16.6	225*	5.4
- food, flour and grains, mixed fodder industries	312**	7.1	288	6.6	43***	1.0
- timber, woodwork, pulp and paper industries	223	5.1	221	5.1	...	...
- fuel industry	131	3.0	130	3.0	...	...
- construction materials industry	100	2.3	102	2.4	21	0.5
- light industry	67	1.5	...	...	16	0.4
- chemical industry	66	1.5	...	...	19	0.4
- metallurgy	64	1.4	...	...	34	0.8
- medical industry	34	0.8	...	...	...	...
- electrical power engi- neering	26	0.6	...	...	...	...
- printing industry	24	0.5	...	...	...	...
- microbiological industry	12	0.3	...	...	...	...
- other branches	...	...	...	...	992	23.6
Construction	622	14.1	573	13.2	492	11.7
Transport and communica- tions	477	10.8	448	10.3	383	9.1
Agriculture and forestry	83	1.9	...	...	62	1.5
Nonproduction sphere****	1388	31.5	...	...	1918	45.6
- material and technical supply and sales	499	11.3	460	10.6	...	...

Branch	as of 1 January 2002		as of 1 January 2003		as of 1 June 2003	
	units	%	units	%	Units	%
- science and science services	410	9.3	398	9.2	...	...
- commerce and public catering	179	4.1	179	4.1	...	...
- geology and prospecting, geodesic and meteorological services	88	2.0	...	...	...	...
- housing and utilities	67	1.5	...	...	...	...
- finance, credit, insurance, annuities	40	0.9	185	4.3	...	...
- public health care, physical culture and social security	28	0.6	...	...	...	...
- administration	20	0.4	...	...	...	...
- culture and arts	6	0.1	...	...	...	...
- other branches of industry	51*****	1.2	637	14.7	-	-
Total	4407	100.0	4340	100.0	4205	100.0

* – machine-building;

** – data as of 1 January 2002: 214 units – food industry and 98 units – flour-and-grains and mixed fodder industries;

*** – food industry only;

**** – according to the All-Russian Classifier of Branches of the National Economy (ARCBNE), not all these branches belonged to the nonproduction sphere, but the use in the data published as of 1 June 2003 of the notion of the entity of all branches except industry, agriculture and forestry, construction, transport and communications, necessitates the application of this term also in respect of information published as of other dates;

***** – other types of activity in the sphere of material production.

Source: data from the official website www.mgi.ru; Braverman A.A. O merakh po povsheniiu effektivnosti upravleniia federal'noi sobstvennost'iu i kriteriakh eio otsenki. [On measures designed to improve the efficiency of management of federal property and criteria for its assessment] // Vestnik Minimushchestva Rossii [Herald of the RF Ministry of State Property], 2003, No. 1, pp. 14; Federal Property Privatization Program for 2004 (Forecast Plan (Program) for Federal Property Privatization in 2004 and the main directions of federal property privatization until 2006) // Vestnik Minimushchestva Rossii [Herald of the RF Ministry of State Property], 2003, No. 3, p. 5 Vestnik Minimushchestva Rossii [Herald of the RF Ministry of State Property], 2003, No. 4, p. 5.

As follows from *Table 3*, in the years 2002 and 2003, in the structure of JSCs with state participation in their capital there was a decline in the share of companies belonging to the sphere of material production. Thus, the share of JSC in industry decreased by almost 10 p.p. (from 41.8% as of early 2002 to 32.1% as of mid-2003). In construction, the share of JSCs with federal blocks of shares declined during this period from 14.1% to 11.7; in transport and communications – from 10.8% to 9.1%. As for the other branches summarized under the title “nonproduction sphere”, in the year 2002, the share of JSCs engaged in material and technical supply and sales dropped from 11.3% to 10.6%. So far as the absolute reduction in the numbers of JSCs with federal blocks of shares is concerned, during the period of time from 1 January 2002 to 1 June 2003 it was registered in construction (by 130 units), transport and communications (by 94 units), the construction materials industry (by 79 units), light industry (by 51 units), chemical industry (by 47 units), and metallurgy (by 30 units)⁸. Over the year 2002 the number of JSCs with federal blocks of shares declined by 39 units in material and technical supply and by 12 unit in science and science services.

While the share of the material production branches (industry, construction, transport and communications, agriculture and forestry) in the whole conglomerate of JSCs with state stakes in their capital was shrinking, that of the other branches designated as the nonproduction sphere was rising. While by the beginning of 2002 they accounted for 31.5% of all such JSCs, by mid-2003 their share increased to 45%. However, the absence of information does not allow us to more precisely, at the level of individual branches, determine the causes of this growth, although a comparison of the data as of early 2002 and for the year 2003 makes it possible to identify one such branch. Over the year 2002, the number of JSCs with state participation increased by 140 units in the finance, credit, insurance and pension provision branch. Accordingly, the share of this branch also rose – from less than 1% to 4.3%.

⁸ The data on the situation in machine building are incomparable, because the numbers of JSC with state participation in machine building and metalworking were given as one aggregate value.

Starting from mid-2003, the general quantitative statistics of the state sector have been published in the annual Forecast Plans (Programs) for Federal Property Privatization, which are approved by regulations of the RF Government. These documents contain the data on the numbers of unitary enterprises in federal ownership (FSUEs) and joint stock companies with RF stakes in their capital, whose classification by branch of industry or economy somewhat differs from that presented in *Tables 2* and *3* for early 2002 and for the year 2003.

Let us consider in more detail and branch by branch the dynamic of the numbers of joint-stock companies with shares in federal ownership for the past few years (*Table 4*).

Table 4

The Dynamic and Structure, by Branch of Industry, of those Joint-Stock Companies whose Shares are in Federal Ownership or in Respect to which the Special Right of “Golden Share” is Applied, in the Years 2003–2006

Branch	as of 1 June 2003		as of 1 June 2004		as of 1 June 2005		as of 1 June 2006 r.		% by 1 June 2003
	units	%	units	%	units	%	units	%	
Nonproduction sphere	1,918	45.6	1,781	45.6	685	18.1	356	9.6	18.6
Industry, including	1,350	32.1	1,253	32.1	2,078	54.9	1,772	47.6	131.3
- machine-building	225	5.4	209	5.4	187	4.95	663	17.8	294.7
- food industry	43	1.0	40	1.0	54	1.4	141	3.8	327.9
- metallurgy	34	0.8	32	0.8	28	0.75	101	2.7	297.1
- construction materials industry	21	0.5	20	0.5	19	0.5	53	1.4	252.4
- chemical industry	19	0.4	18	0.5	46	1.2	98	2.6	515.8
- light industry	16	0.4	15	0.4	9	0.2	27	0.7	168.8
- other branches of industry	992	23.6	919	23.5	1735	45.9	689	18.5	69.5
Construction	492	11.7	457	11.7	287	7.6	380	10.2	77.2
Transport and communications	383	9.1	356	9.1	459	12.1	396	10.6	103.4

Branch	as of 1 June 2003		as of 1 June 2004		as of 1 June 2005		as of 1 June 2006 r.		% by 1 June 2003
	units	%	units	%	units	%	units	%	
Agriculture	46	1.1	43	1.1	229	6.1	363	9.7	789.1
Forestry	16	0.4	15	0.4	45	1.2	99	2.7	618.8
Other branches of industry	–	–	–	–	–	–	358	9.6	...
Total	4205	100.0	3905	100.0	3783	100.0	3724	100.0	88.6

Source: Forecast Plan (Program) for Federal Property Privatization in 2004 and the main directions of federal property privatization until 2006; Forecast Plan (Program) for Federal Property Privatization in 2005; Forecast Plan (Program) for Federal Property Privatization in 2006 and the main directions of federal property privatization for 2006–2008; Forecast Plan (Program) for Federal Property Privatization in 2007 and the main directions of federal property privatization for 2007–2009; the authors' estimations.

As follows from *Table 4*, the number of joint-stock companies with shares in federal ownership dropped by 11.4% in the period between 1 June 2003 and 1 June 2006, including by 1.6% between 1 June 2005 and 1 June 2006. At the same time, during the period between 1 June 2005 and 1 June 2006 the decrease, in absolute terms, of the number of the aforesaid JSCs (59 units) was two times less than during the period between 1 June 2004 and 1 June 2005 (122 units) and more than five times less than between 1 June 2004 and 1 June 2003 (300 units).

The main change in the branch structure of JSCs with shares in federal ownership was the increase in the share of enterprises in industry (from 32.1% as of 1 June 2003 to 47.6% as of 1 June 2006), transport and communications (from 9.1% to 10.6%), agriculture (from 1.1% to 9.7%), and forestry (from 0.4% to 2.7%).

At the same time there was a decline in the percentage of JSCs belonging to the group of non-production branches (from 45.6% as of 1 June 2003 to 9.6% as of 1 June 2006) and the construction industry (from 11.7% to 10.2%). The number of those JSC whose shares were federal property went down, in three years, within the group of non-production branches by 5.4 times (or by 1,562 units), in construction – by less than one quarter (or by 112 units).

In this connection, it is necessary to emphasize that the growth in the percentage of industrial JSCs with a state-owned stake in their capital occurred across all the branches of industry, except in the specially separated out group of “other branches of industry”, which are not related directly to those listed in the table (metallurgy, machine-building, chemical industry, the construction materials industry, light industry, and the food industry). It is the percentages demonstrated by this group that decreased both in relative terms (from 23.6% to 18.5%), and in absolute terms (by 303 units, or by more than 30%).

In other branches the number of JSCs with federal blocks of shares as of 1 June 2006 grew substantially against the level as of 1 June 2003: in chemical industry (more than five-fold), in the food industry (approximately by 3.3 times), in machine-building and metallurgy (almost by 3 times), in the construction materials industry (approximately by 2.5 times), and in light industry (nearly by 1.7 times). The most noticeable growth in the absolute number of JSCs with a state stake in their capital was observed in machine-building (by 438 units), while in all the other branches listed above it did not exceed 100 units. Substantial growth was also seen in agriculture (by 317 units).

In 2006, within the structure of the by-branch distribution of JSCs with federal blocks of shares, as well as within that of FSUEs, a new category of “other branches of industry” was singled out. These branches were left outside the basic classification of branches of industry and accounted for 9.6% of such JSCs, resulting from which in the period between 1 June 2005 and 1 June 2006 the percentage of JSCs belonging to the group of non-production branches was nearly halved (decreasing from 18.1% as of 1 June 2005 to 9.6% as of 1 June 2006, or by 329 units). In this connection it can be noted that during the same period the by-branch structure of the JSCs whose shares were federal property the percentage of enterprises belonging to industry became somewhat lower (decreasing from 54.9% as of 1 June 2005 to 47.6% as of 1 June 2006)⁹, as did that of transport and communications enterprises (from 12.1% to 9.6%). The percentages of some other branches, on the contrary, increased. These are

⁹ Mainly because of the separation of a special group of “other branches of industry”.

construction (from 7.6% to 10.2%), agriculture (from 6.1% to 9.7%) and forestry (from 1.2% to 2.7%).

A reduction in the percentages of enterprises belonging to non-production branches occurred once again between 1 June 2005 and 1 June 2006. Between 1 June 2004 and 1 June 2005 this index had already demonstrated a decline from 45.6% to 18.1%. In absolute terms the number of JSCs with federal blocks of shares decreased by 2.6 times (or by 1,096 units). At the same time there was growth in the percentage of industrial enterprises – from 32.1% to 54.9%, mostly due to growing indices of “other branches of industry” (from 23.5% to 45.9%), which in absolute terms increased by 1.9 times (or by 816 units).

It can be supposed that the causes of such changes in the by-branch structure of those JSCs whose shares were federal property were not so much associated with the implementation of privatization procedures (sale of state-owned blocks of shares and transformation of unitary enterprises into joint-stock companies) as with changes in the classification of JSCs – their placement within a certain branch of industry or redistribution between branches.

Some data are also available concerning the by-branch distribution of JSCs with state participation in accordance with a classification which is quite different from those previously discussed. The information relating to the year 2005 (*Table 5*) is based on a classification including industry and construction (as one entity), the fuel and energy (FEC), the agroindustrial (AIC) and the military-industrial (MIC) complexes, transport and communications, financial and foreign trade organizations, science and the social sphere (as one entity), and land use. It is obvious that industrial enterprises may belong to the fuel and energy, the agroindustrial or the military-industrial complexes, and similarly the military-industrial complex may also encompass research organizations. Thus, the only comparable branch (according to the previous classification) is that of transport and communications¹⁰.

¹⁰ The number of JSCs with state participation by 2005 (496 units) rose on mid-2003 by almost 30%, having exceeded the value of this index registered as of the beginning of 2002 (by 19 units).

Table 5

The Structure in 2005, by Branch of Industry, of Joint-Stock Companies whose Shares are Federal Property, or those to which the Special “Golden Share” Right is Applied, Depending on the Size of Such Blocks of Shares

Branch	Number of joint-stock companies													
	total		up to 25 %		between 25 % – 1 share and 50 %		between 50 % – 1 share and 75 %		between 75 % – 1 share and 100 %		100 %		“golden share” (no block of shares)	
	units	%	units	%	units	%	units	%	units	%	units	%	units	%
Industry and construction	1675	100	805	48.1	429	25.6	138	8.2	33	2.0	131	7.8	139	8.3
Fuel and energy complex	826	100	235	28.5	440	53.3	49	5.9	21	2.5	48	5.8	33	4.0
Agroindustrial complex	538	100	211	39.2	117	21.75	117	21.75	9	1.7	76	14.1	8	1.5
Transport and communications	496	100	191	38.5	102	20.6	43	8.7	8	1.6	53	10.7	99	19.9
Financial and foreign trade organizations	227	100	193	85.0	16	7.0	5	2.2	4	1.8	9	4.0	-	-
Science and social sphere	212	100	57	26.0	42	19.8	42	19.8	4	1.9	62	29.2	5	2.4
Land utilization	58	100	-	-	-	-	-	-	-	-	58	100.0	-	-
Military – industrial complex	43	100	5	11.6	8	18.6	4	9.3	10	23.3	16	37.2	-	-
Total	4,075	100	1,697	41.6	1154	28.3	398	9.8	89	2.2	453	11.1	284	7.0

Source: Materials for the RF Government’s meeting on 17 March 2005 “On measures designed to improve the efficiency of federal property management”; the authors’ estimations.

In the new classification applied in 2005 the three main zones of the concentration of JSCs with state stakes are as follows (in the descending order): industry and construction (1,675 units or 41.1%), the fuel and energy complex (826 units or 20.3%) and the agroindustrial complex (538 units or 13.2%). Each of these groups is represented by more than 500 JSCs with state stakes. Their number is slightly less in transport and communications (496 units or 12.2%¹¹). These are followed by financial and foreign trade institutions (227 units or 5.5%), and by science and the social sphere (212 units or 5.2%). The least number of JSCs with state stakes were registered in the land utilization sector (58 units) and in the military-industrial complex (43 units), which together accounted for approximately 2.5%.

An important component of the by-branch distribution of JSCs with state stakes is the differentiation between branches based on the state stake's size. The highest percentage of those JSCs where the size of a state stake is less than 25% is registered among financial and foreign trade institutions (85.0%) and in industry and construction (48.1%), while in the group of JSCs with state participation taken as a whole they constitute 41.6%. In all the other branches this index amounts to less than 40%, although in the AIC and in transport and communications it was only slightly lower – 38–39%. The percentage of stakes of a blocking size (between 25% + 1 share and 50%) was the highest in the FEC (53.3%), while in the whole mass of stakes it was 28.3%. At the same time, in another three branches it was higher than 20%: in industry and construction (25.6%), in the AIC (21.7%), and in transport and communications (20.6%). An increased percentage of JSCs with state stakes sized between 50% + 1 share and 75% was seen in the AIC (21.7%) and in science and the social sphere (19.8%) (the average level being approximately 10%). The next group of JSCs by the size of a state stake (between 75% + 1 share and 100% – 1 share) constituted only 2.2% of the total number of JSCs with state stakes, the highest percentage of such JSCs being observed in the MIC (23.2%), while in all the other branches it was no more than 2.5%. The JSCs where the State owned 100% of shares constituted

¹¹ The share of transport and communications in the total group of JSCs with state participation increased by comparison with early 2002 (10.8%) and early 2003 (10.3%).

slightly more than 11% of all the JSCs with state participation. Their number was notably higher in the MIC (37.2%), in science and the social sphere (29.2%), in the AIC (14.1%). In another branch (transport and communications) the percentage of JSC whose total capital was federal property was somewhat below the average level (10.7%). High percentages of those JSCs where the special “golden share” right was applied were noted in transport and communications (19.9%) and in industry and construction (8.3%), while their average number in the group of JCSs with state stakes was 7%.

Thus it can be concluded that the RF in the capacity of a fully-fledged majority shareholder owning a total block of 50% + 1 share and more participated most often in the capital of joint-stock companies belonging to the MIC (approximately 70%) and science and the social sphere (more than 50%). Of course, in absolute terms the numbers of JSCs with federal stakes of this size were highest in other branches-industry and construction (302 units) and the AIC (202 units). As a blocking shareholder (owning between 25% + 1 share and 50%) the State participated most noticeably in JSCs belonging to the FEC (53.3 %). The highest number of JSCs with federal stakes of this size in absolute terms was also noted in the FEC (440 units) and in industry and construction (429 units).

1.1.2. Main Factors Determining the State's Presence in the Corporate Sector

As has been pointed out earlier, the number of federal blocks of shares was a value determined as a derivative of two trends: the transfer into federal ownership of certain blocks of shares as a result of a variety of acts (mainly the transformation of unitary enterprises into joint-stock companies), and their withdrawal from federal property as a result of sale.

It should be reminded that, in accordance with the RF Government's Decree of 6 December 1999, No. 1348, issued soon after the approval of the Concept for the Management of State Property and Privatization in the RF in 1999, the transformation into joint-stock companies (or corporatization) of unitary enterprises was pointed out as one of the directions for their reorganization, alongside the other directions (sale of their property complexes, transfer to the regions, and creation of treasury-owned enterprises by right of operative management).

In actual practice this process was very slow (*Table 6*). It is quite difficult to assess its rate and results, despite the seeming simplicity of such a task, because the planned targets, often changed toward increasing the number of enterprises to be privatized, were usually not met. Besides, there existed considerable discrepancies between the data published by the RF Ministry of State Property and those found in the reports of the RF Goskomstat (a certain compatibility between the two could only be observed in 2002). The explanation of this phenomenon has appeared only recently, when the RF Goskomstat clarified that its published data on the privatization of unitary enterprises did not incorporate the information concerning the property complexes owned by federal state unitary enterprises (FSUE), the privatization of which has been carried out by the RF Ministry of State Property Russia¹².

Table 6

Comparative Data on the Dynamic of Privatization of Federal State Unitary Enterprises in 2000–2005

Pe- riod	Number of privatized FSUEs (according to the RF Ministry of State Property)		Number of privatized enterprises (or objects) – formerly federal property (according to the RF Goskomstat	
	included in privati- zation program, units	actually privatized, units	total number, units	Creation of open- end joint-stock companies (OJSC), units
2000	...	2	170	36
2001	...	5	125	11
2002	152/576*	102	86	10
2003	435/825/911/ 970*	562/571**	188	161/159***
2004	1063/ 1374 /1096*	517/525****	121	121
2005	1453	741	129	112

* – the numerator represents the number of FSUEs included in the Forecast Plan (Program) for Privatization, after its adjustments made during a given year;

** – without those FSUEs whose property complexes became contributions to the charter capital of the OJSCs “RZhD”, in the denominator – based on later data;

*** – the numerator represents the total number of privatized property complexes formerly owned by unitary enterprises, of which in the denominator there is the number of

¹² Sotsial'no-ekonomicheskoe polozhenie Rossii [Russia's socio-economic situation]. January 2004. M., Goskomstat RF, p. 131.

unitary enterprises transformed into OJSCs; another two property complexes formerly owned by unitary enterprises were sold at an auction;

**** – the by-name list contains 525 units.

Source: data published at the official website www.mgi.ru; Svedeniia o khode privatizatsii gosudarstvennykh i munitsipal'nykh predpriatii (gosudarstvennogo i munitsipal'nogo imushchestva) v Rossiiskoi Federatsii za ianvar' – dekabr' 2000 g. [Information concerning the process of privatization of state and municipal enterprises (state and municipal property) in the Russian Federation in January – December 2000] (p. 64), 2001 (p. 63), 2002 (p. 63), 2003 (p. 198), 2004 (p. 205), 2005 (p. 185–186). M., Rosstat (Goskomstat of Russia); Materials for the RF Government's meeting on 17 March 2005 "On measures designed to improve the efficiency of federal property management"; Report of the Federal Agency for Federal Property Management (FAFPM) "O privatizatsii federal'nogo imushchestva v 2005 g." ["On federal property privatization in 2005"] M., 2006.

On the whole it can be stated that the rate of privatization of FSUEs after 2002 became much higher. While in 2000–2001 the total number of privatized unitary enterprises which were formerly federal property was negligent (less than 10 units), in 2002 it became as high as a hundred, and in the next two years (2003–2004) exceeded five hundred units. In 2005 all the preparatory measures were completed, and decisions were made concerning the terms of privatization of 741 unitary enterprises, which was by 30 % higher than the previous peak value achieved in 2003 (571 units). The growing volume of privatization, in 2003–2005, of unitary enterprises formerly in federal ownership has been confirmed by the Rosstat's information, although the latter figures are far from those published by the Rosimushchestvo (the RF Ministry of State Property).

However, despite the growth in the number of privatized FSUEs registered in recent years, this process is developing rather slowly, with marked deviations from forecasted indices. Thus, out of the 1,453 federal state unitary enterprises included in the Plan (Program) for Federal Property Privatization in 2005, the privatization procedures in respect of 711 enterprises have been suspended or discontinued altogether.

Among the causes behind the obstacles faced by unitary enterprises, the following factors can be pointed out: (1) financial and economic (negative balance – sheet value of the assets of enterprises to be privatized, their involvement in bankruptcy or liquidation procedures, lack of any real economic activity), (2) organizational and administrative (lack of approved decisions concerning the terms of privatization, or privatization

is impossible due to certain restrictions, etc., reorganization through merger of affiliated enterprises to their parent unitary enterprises, transfer of enterprises to regions, non-compliance of the heads of enterprises with lawful requirements concerning the preparation for privatization, including failure to submit information, delays in privatization procedures, etc., untimely transfer of documentation between different bodies of authority), and (3) normative-legal (lack of legal documents establishing the rights of enterprises or relating to the technical inventory of their objects of federal property, including plots of land, due to shortage of money needed for their formalization, or due to the refusal thereof of local authorities, or through the fault of the heads of enterprises; legal proceedings concerning issues of property ownership).

The regular consequence, in the majority of cases, of the absence of correctly registered rights of unitary enterprises to immovable property and plots of land, of technical inventory documentation, the formalization of which is the responsibility of an enterprise itself, or of faulty accounting and managerial records would be the need for proper formalization of rights, correction of financial reports, and in some instances – judicial proceedings in respect of disputed property. Therefore, the issue of privatization clearly goes beyond the purely technical procedures of transformation of an organization, this requiring additional financial expenditures¹³ and markedly delaying the process of privatization itself.

The overwhelming majority of FSUEs are privatized by being transformed into OJSCs, which means that at least in the short term there will emerge federal property in the form of a complete (100%) block of shares, later possibly to be sold in full or to be reduced to a block of shares of a controlling, blocking or minority size. It would be sufficient to say that among the 525 FSUEs privatized by the end of 2004 only 6 (or 1.1%) were not transformed into OJSCs (by sale of property complex). In 2005 the decisions concerning the privatization of 39 of 747 enterprises (or 5.2%) envisaged the sale of property complexes through open bidding.

¹³ For example, the State's duties relating to the registration of rights to property objects, the cost of technical inventory and land use documentation, the formalization of certificates issued by bureaus for technical inventory and cadastre plans of plots of land, etc.

In addition to the transformation of unitary enterprises into joint-stock companies, other sources of increasing the size of share capital owned by the State were as follows:

- greater participation in charter capital within the framework of corporate procedures and dividend policies (e. g., in the OJSC “Tekhnabeksport” – up to 100%, in the OJSC “Samara-neftegeofizika” and “Sibneftegeofizika” – up to the size of a controlling block of voting shares);
- exchange for investments of budget funds within the framework of federal target investment programs (e. g., a number of regional energy suppliers and electric power plants (“Astrakhanenergo”, “Vuliiskaiia GES-3”, “Sulakenergo”, “Kharanorskaia GRES”, “Yakutskenergo”, “Zavod trub bol’shogo diametra” [“Plant for Large-Diameter Pipes], etc.). A serious problem associated with the implementation of this scheme is that in many cases the State becomes only a minority shareholder, as it happened in the case of the power engineering objects mentioned here, where the RF’s participation was no more than 1% ¹⁴;
- exchange for the contribution to charter capital of plots of land occupied by privatized enterprises (for example, the M. I. Kalinin machine-building plant in Ekaterinburg, where plots of land became the RF’s property contribution in lieu of an additional placement of shares in 2004) or of rights to intellectual property owned by the State (for example, the OJSC “Tupolev” in 1999, where the RF’s stake, in accordance with the government’s decision, was to amount to 50% + 1 share, with taking into account the fixed assets and the assets owned by the JSC “ANTK imeni A. N. Tupoleva” and “Aviastar”);
 - by way of returning into federal ownership those shares that previously had been:

¹⁴ Tikhonov A. V. Departament toplivno-energeticheskogo kompleksa (po materialam otchiota na zasedanii kollegii Minimushchestva Rossii 21 maia 2003 g. [Department for the fuel and energy complex (based on the materials of the report to the collegial meeting of the RF Ministry of State Property)]. In: Vestnik Minimushchestva Rossii [Herald of the RF Ministry of State Property], 2003, No. 2, p. 37.

- transferred into use or ownership in violation of existing legislation (the most vivid examples observed in recent years are 5% shares in the CJSC AK “ALROSA” and 40 % shares in the OJSC “Irkutskenergo”);
- sold in violation of existing legislation; the most obvious examples of stakes being returned to the State are the situations when new owners have failed to fulfill their investment obligations and / or other obligations undertaken when shares were bought at a tender; out of the 1,084 blocks of shares sold in 1992–1997, 328 (or more than 30%) were returned to the State through a court of justice, mainly because of the buyer’s failure to fulfill related obligations¹⁵;
- in this connection, special place belongs to Item 79 of the 2002 federal budget, under which it was assigned to the RF Government, in order to take out of pledge the shares in the CISC “Novoship”¹⁶ and the OJSC “Severo – Zapadnoe parokhodstvo” [“Northwest Steamship-Line”], that it should ensure the fulfillment of obligations under the loan agreements concluded in accordance with Edict of the President of the Russian Federation of 31 August 1995, No. 889, “On the procedure for putting in pledge, in 1995, of shares in federal ownership”, by introducing changes in those agreements concerning their redemption at the expense of the 2002 federal budget, with the simultaneous termination of pledge agreements in respect of the shares in the aforesaid joint-stock companies;
- in the procedure of restructuring the payables and tax arrears of individual enterprises due to the federal budget and the RF Government (for example, the outstanding debt of the OJSC “KAMAZ” against its obligation of a timely return into the state material reserves of borrowed material values in the amount of 370.2 million roubles was restructured by transferring into federal ownership the bonds convertible into ordinary registered shares of the aforesaid joint-stock com-

¹⁵ Rossiiskaiia ekonomika v 1999 godu. Tendentsii i perspektivy. [The Russian economy in 2001. Trends and prospects.] (Issue 21). Vol 2., M., IET, April 2000 pp. 341–342.

¹⁶ In 2001 the RFPF, at the request of the RF Clearing House, prepared materials concerning the feasibility of mutual setting off of the outstanding debt of the CISC “Novoship” to the federal budget.

pany, at their face value, with subsequent increase of the state stake in the charter capital);

- in the procedure of redeeming interstate debt, one example of which is the agreement, signed in November 2002, concerning the transfer to Russia, by way of settling her debt to Armenia, the shares in 5 enterprises (Razdanskaia GRES, CJSC “MARS”, research institutes for management systems automation, mathematical machines and studies of materials), under which before May 2003 these shares were to be transferred to the RF Ministry of State Property in exchange for \$ 93.76 million in cash, or nearly 97 % of Armenia’s major debt to Russia)¹⁷;
- during the implementation of measures designed to restructure individual branches and sectors (for example, in electric power engineering and in the banking sphere, which will be discussed later in the appropriate section).

However, in the majority of these examples the case in point was not the acquisition of new blocks of shares but the enlargement of the already existing ones.

An alternative option for the disposal of federal blocks of shares in recent years has been their sale (*Table 7*).

As follows from these data, the dynamic of sales of federal blocks of shares displayed no consistent trend. Thus, in 2002 their sales were lower than in 2001 (approximately by 10%)¹⁸, in 2004 were lower than in 2003 (by 5.4%)¹⁹, and in 2005 were lower than in 2004 (approximately by 8%)²⁰. At the same time, the dramatic leap (by 5.65 times) in the sale of

¹⁷ Korop E. Kas’ianov privez armianskiie aktsii [Kasianov has brought Armenian shares] // Izvestiia [News] Izvestiia [News], 6 November 2002, p. 2.

¹⁸ Judging by the total number of privatized blocks of shares (including those blocks of shares that had been sold in the previous calendar year but the results of sale were filed in the next year). However, if only those blocks of shares that were actually sold during a calendar year are taken into account, in 2002 the number of those sold was slightly higher than in 2001 (90 units against 81 units).

¹⁹ In the results of 2004 those 31 blocks of shares are included the sale of which took place in 2004, while the results were filed in 2005.

²⁰ Without those blocks of shares that had been sold in the previous calendar year but the results of their sale were filed in the next year.

federal blocks of shares in 2003 by comparison with that in 2002 cannot be overlooked. It is in 2003 that the highest number of blocks of shares was sold in the last 5 years (630 units).

Table 7

**The Dynamic of Privatization of Blocks of Shares in JSCs
with Federal Stakes in 2001–2005**

Pe- riod	Blocks of shares to be privatized		Num- ber of sales an- nounc ed	Results of sales		Dead- line for filing results – next year	Results of sales de- clared in pre- vious year	Num- ber of privat- ized blocks of shares, total
	Initial number	Final number		sold	left unsold			
2001	...	226	209	81	15*	113	44	125
2002	426	992	370	90**	94***	186	22	112
2003	628/ 1443/ 1978#	1978	...	...	...	...	...	630
2004	629/ 732/ 1702#	1461****	1109	565	376	168	...	596*****
2005	1496 (including shares in 15 LLCs)	1243 ****	927	521	133	273	31	521

– following / is the number of blocks of shares to be privatized in accordance with intermediate decisions made by bodies of executive authority in the period between the initial and final versions of the Forecast Plan (Program) for Privatization, which was periodically supplemented by the list of those JSCs whose privatization had been planned but for various reasons had not been completed in the previous year (e. g., in 2004 the number of such JSCs increased by 966 units);

* – all because of absence of any applications;

** – including 5 blocks of shares sold in part;

*** – including 92 blocks of shares because of absence of any applications and 2 blocks of shares because of refusal of the winner in bidding;

**** – the number of JSCs in federal ownership whose blocks of shares could be actually privatized, that is, the number of all those initially included in the Forecast Plan (Program) for Privatization less the number of the JSCs undergoing bankruptcy or liquidation procedures, or carrying out no economic activity, or included in the List of Strategic Enterprises

and Joint-Stock Companies, or placed as the RF's contribution in the charter capitals of integrated structures, or in whose documentation certain discrepancies had been found, or who had failed altogether to submit any documentation, or in respect to which no decision concerning the terms of their privatization had been made due to the imperfect procedure for calculating the normative price of federal property to be privatized;

***** – including those 31 blocks of shares whose sale was announced in 2004 but its results were filed in 2005.

Source: data from the official website www.mgi.ru; Medvedev Yu. M. Itogi deiatel'nosti Minimushchestva Rossii i ego territorial'nykh organov za 2002 god i zadachi na 2003 god. [Results of the activity of the Ministry of State Property of Russia and of its territorial agencies in the year 2002 and the tasks for the year 2003] // Vestnik Minimushchestva Rossii [Herald of the RF Ministry of State Property], 2003, No 1, p. 35–37; Materials for the RF Government's meeting on 17 March 2005 "On measures designed to improve the efficiency of federal property management"; Report of the Federal Agency for Federal Property Management (FAFPM) "O privatizatsii federal'nogo imushchestva v 2005 g." ["On federal property privatization in 2005"] M., 2006.

From the point of view of organizing the sale process, of great importance is the percentage of those blocks of shares in respect of which bidding had actually taken place within the overall number of stakes to be sold. The most favorable results in this respect were observed in 2001, when a total of 17 blocks of shares (or 7.5% of the total number of those to be sold) were not offered for sale. In 2002 the number of such blocks of shares was already 622 (or 62.7%), in 2004 – 352 (or 24.1%), in 2005 – 316 (25.4%). This makes it possible to conclude that the rise in the volume of sales of federal blocks of shares produced certain malfunction in the administrative regulation of this process by the government and the property management agencies, which was further aggravated by frequent adjustments of the volumes of sales, largely of a subjective character. This was done, in particular, by automatically including in the Forecast Plan (Program) for Privatization for a given year those blocks of shares that could not be sold earlier. In fact, the blocks of shares offered for sale for the first time in each current year constitute only a part of the whole bulk of potentially saleable stakes. Thus, in 2005 it became possible to privatize the shares in 1,243 joint-stock companies, of which only the shares in 470 companies (or 37.8%) were offered for sale for the first time.

The evidently unreasonable character of such adjustments is confirmed by the fact that the real number of sold blocks of shares during a

calendar year was always lower than the initial projections made by the RF Ministry of State Property. Thus, in 2002 90 blocks of shares were sold, which constituted 21.1% of the initial planned value, or 9.1% of the adjusted value. For the year 2004 these indices were 89.8% and 38.7%, respectively (even with due regard for the downward adjustment by subtracting the number of those JSCs whose shares could not be actually privatized), for 2005 – 34.8% and 41.9%, respectively. Somewhat better are the results of 2003, when the actual number of sold blocks of shares was equal to that initially planned, being at the same time less than one-third of the adjusted value.

The attractiveness of the blocks of shares offered for sale, quite obviously, left much to be desired. If in 2001 a total of 15 blocks of shares (or 15.6% of those offered for sale, for which the timeline for drawing up the results of sales did not go beyond a calendar year), in 2002 these values were 94 blocks of shares (or 51.1%), in 2004 – 376 blocks of shares (or 40%), and in 2005 – 133 (or 20.3%). And the prolongation of the period for drawing up the results of sales until the next year is by no means a guarantee of a higher rate of realization. Thus, out of the 113 blocks of shares offered for sale in 2001 with the deadline for drawing up the results established in the next year, in 2002 the results were drawn up for 22 blocks of shares, and out of the 168 blocks of shares offered for sale in 2004 with the deadline for drawing up the results established in the next year, in 2005 the results were drawn up for 31 blocks of shares. In fact, less than 1/5 of all blocks of shares were sold, of which the timeline for the drawing up of the results was beyond the limits of a calendar year. As shown by the actual practice of 2002, the main bulk of blocks of shares fails to be realized because of absence of applications, the instances of a winner in bidding refusing to finalize the deal being quite rare.

The complexity in administering the process of selling blocks of shares is associated with the fact that the actual decisions concerning the terms of privatization could not be finalized in respect of all of them during one calendar year. Thus, in 2002, out of the 992 blocks of shares earmarked for privatization (according to a final plan) the decisions concerning the terms of privatization were actually made in respect of only 676. The reasons for this vary very widely (*Table 8*).

Table 8

**The Reasons for Failures to Make Decisions Concerning
the Privatization of Stakes in those JSCs whose Shares
are Federal Property, in 2002–2005**

Period	undergoing bankruptcy procedure	liquidation	no economic activity	difficulties in obtaining accounting documentation needed for calculating standard price	incompatibility of number of shares in federal ownership with that indicated in privatization program	failure to submit documents needed for making decision concerning terms of privatization	inadequate procedure for calculating standard price	placed on List of strategic enterprises and JSCs	placed as contribution in charter capital of integrated structure
2002		18		177*					
2004		42**			3	2		92	108***
2005	43	5	13			5	35****		145*****

* – mostly those JSCs where the State owns a negligible stake, including approximately 80 units involved in competitive production;

** – the aggregate number of JSCs which carry out no economic activity, undergo a bankruptcy procedure, or have been liquidated;

*** – among those integrated structures into whose charter capitals stake shares were to be placed there were 31 strategic JSC;

**** – relates to federal property in the form of shares of credit institutions and organizations applying a simplified taxation system, as well as shares in charter capitals of LLC;

***** – including stakes in 77 JSCs earmarked for placement into the charter capital of the “Russian Fuel Company” (CJSC “Postoprom”), the creation of which in 2005 was recognized as not feasible.

Source: data from the official website www.mgi.ru; Medvedev Yu. M. Itogi deiatel'nosti Minimushchestva Rossii i ego territorial'nykh organov za 2002 god I zadachi na 2003 god. [Results of the activity of the Ministry of State Property of Russia and of its territorial agencies in the year 2002 and the tasks for the year 2003] // Vestnik Minimushchestva Rossii [Herald of the RF Ministry of State Property], 2003, No. 1, p. 36; Materials for the RF Government's meeting on 17 March 2005 “On measures designed to improve the efficiency of federal property management”; Report of the Federal Agency for Federal Property Management (FAFPM) “O privatizatsii federal'nogo imushchestva v 2005 g.” [“On federal property privatization in 2005”]. M., 2006; the authors' estimations.

If in 2002 the main reason for a failure to make a decision concerning the terms of privatizing shares in economic societies were difficulties associated with obtaining accounting documentation needed for calculating

their standard price, in 2004–2005 it was already their placement in the form of the RF's contribution in the charter capitals of integrated structures and their entry in the List of strategic enterprises and joint-stock companies. The shares of a rather big group of JSCs could not be sold due to their involvement in bankruptcy procedures, their liquidation, or absence of any real economic activity. The other reasons for the failure of shares to be sold were the incompatibility of the number of shares in federal ownership with that indicated in the Forecast Plan (Program), failure to submit, in the established procedure, the documents needed for making the decision concerning the terms of privatization, and the inadequacy of the procedure for calculating the standard price for a number of categories of federal property to be privatized.

In 2005 the factors that had been seriously aggravating the administering of the process of selling federal property were augmented by a conflict between the RF Ministry of State Property and the Russian Federal Property Fund (RFPF), which will be mentioned later.

Among the first 470 blocks of shares in joint-stock companies included in the Forecast Plan (Program) for Federal Property Privatization in 2005, which could be privatized, the decision of the RF Ministry of State Property concerning the terms of privatization was not made only in respect of 5 joint-stock companies – because of their failure to submit the necessary documents²¹. At the same time, the RFPF did not publish the information concerning the sale of shares in 183 joint-stock companies, which were for the first time included in the privatization program. Thus, out of the 470 JSCs whose shares were for the first time offered for sale, the shares in 188 companies (or 40%) during 2005 were never offered for sale.

1.1.3. The Main Characteristics of the Privatization of Federal Blocks of Shares

An important role in the process of the realization of federal blocks of shares belonged to their relative size (in % of charter capital). See below

²¹ The RF Ministry of State Property in 2005 made decisions concerning the privatization of shares in 1,238 JSCs.

the generalized data concerning the distribution of the sold blocks of shares, depending on their size (*Table 9*).

Table 9

**The Dynamic and Structure of Sold Federal Blocks of shares,
Depending on their Size, in 2001–2005**

Period	total		up to 25%		Between 25 % – 1 share and 50 %		Between 50% – 1 share and 100 % – 1 share		100 %	
	units	%	units	%	units	%	units	%	units	%
2001	125*	100	78	62,4	45	36,0	2	1,6	...**	...
2002	112*	100	51	45,5	56	50,0	5	4,5	...**	...
2004	565	100	406	71,85	119	21,05	34	6,0	6	1,1
2005	521	100	360	69,1	81	15,5	29	5,6	51	9,8

* – with regard to the results of sales announced one year earlier, when their results had been drawn up only during a given year;

** – the information concerning the sold blocks of shares amounting to 100% was not singled out, they were registered in the category of those amounting to 50% and above.

Source: data from the official website www.mgi.ru; Medvedev Yu.M. Itogi deiatel'nosti Minimushchestva Rossii i ego territorial'nykh organov za 2002 god I zadachi na 2003 god. [Results of the activity of the Ministry of State Property of Russia and of its territorial agencies in the year 2002 and the tasks for the year 2003] // Vestnik Minimushchestva Rossii [Herald of the RF Ministry of State Property], 2003, No. 1, p. 36; Materials for the RF Government's meeting on 17 March 2005 "On measures designed to improve the efficiency of federal property management"; Report of the Federal Agency for Federal Property Management (FAFPM) "O privatizatsii federal'nogo imushchestva v 2005 g." ["On federal property privatization in 2005"]. M., 2006; the authors' estimations.

The main trend in the shifts occurring within the structure of the federal blocks of shares sold in recent years was represented by an increasing percentage (alongside their number in absolute terms) of minority stakes (from 45.5% in 2002 to almost 72% in 2004) and stakes of a controlling size (from 1.6% to 6%) – due to a declining percentage of blocking stakes, which in 2004 was as low as 21% – against 36% in 2001 and 50% – in 2002. In 2004, by comparison with 2001, the number of sold majority stakes in absolute terms increased by 17 times, that of minority stakes – by 5.2 times, and that of blocking stakes – by only 2.6

times. In 2005 this trend was augmented by a new phenomenon: there occurred a reduction in the sold blocks of shares both in absolute terms (the most noticeable decline being demonstrated by minority stakes) and in relative terms (in this respect, blocking stakes were the leader) across all the categories, except that of complete stakes (i. e., equal to 100%). By comparison with 2004, the number of sold complete blocks of shares increased by 8.5 times, becoming equal to 9.8% (against 1.1% a year earlier). As a result, complete stakes were in the third place within the structure of sold blocks of shares, which in 2004 belonged to controlling stakes.

Some marked differences were noted in the realization of blocks of shares of different sizes (*Table 10*).

An analysis of the ratios between the blocks of shares included in the privatization program, announced for bidding and actually sold during 2005 has shown that the greatest difficulties in the administering of sales were associated with blocking and controlling stakes, of which only slightly more than a half of the blocks of corresponding sizes among those included in the privatization program were announced for bidding. On the contrary, almost 79% of complete (100% in size) blocks of shares were announced for bidding, while the position of minority stakes was intermediate, nearly 2/3 of them having been also offered for sale.

Table 10

The Implementation of the Privatization Program for Federal Blocks of Shares in 2005, Depending on their Size

Size of blocks of shares, in % of charter capital	Included in privatization program	Announced for bidding		Sold		
		units	in % of those included in privatization program	units	in % of those announced for bidding	in % of those included in privatization program
up to 25 %	810	529	65.3	360	68.1	44.4
from 25 % + 1 share to 50 %	361	190	52.6	81	42.6	22.4

Size of blocks of shares, in % of charter capital	Included in privatization program	Announced for bidding		Sold		
		units	in % of those included in privatization program	units	in % of those announced for bidding	in % of those included in privatization program
from 50% + 1 share to 100 % – 1 share	169	85	50.3	29	34.1	17.2
100 %	156	123	78.8	51	41.5	32.7
Total	1496	927	62.0	521	56.2	34.8

Source: Report of the Federal Agency for Federal Property Management (FAFPM) “O privatizatsii federal’nogo imushchestva v 2005 g.” [“On federal property privatization in 2005”]. M., 2006; the authors’ estimations.

Besides, very interesting is the ratio between the blocks of shares that were announced for bidding and those actually sold. Contrary to the common opinion that minority stakes cannot, as a rule, be an attractive object for privatization, since the struggle for corporate control is over, and stable structures of capital have been formed, with the emergence of a private majority shareholder in most companies, it is minority stakes that were sold with the highest degree of success in 2005. More than 2/3 of stakes of this size among those announced for bidding were sold, by comparison with 34% of controlling stakes and 41–42 % of complete and blocking stakes. As a result, it is in the category of minority stakes that the best ratio was observed between those sold and those included in the privatization program (44.4%), while the worst ratio was demonstrated by controlling stakes (17.2%), being somewhat better in the categories of blocking (22.4%) and complete (32.7%) stakes.

An interesting picture emerges if one compares the structures of blocks of shares included in the privatization program (Forecast Plan), announced for bidding and actually sold, when distributed by their sizes (*Table 11*).

Table 11

**The Structure of Federal Blocks of Shares, Included
in the Privatization Program, Announced for Bidding
and Actually Sold, Depending on their Size, in 2005**

Category of blocks of shares	Up to 25 %		Between 25 % + 1 share and 50 %		Between 50 % + 1 share and 100 % – 1 share		100 %	
	units	%	units	%	units	%	Units	%
Included in privatization program	810	54.15	361	24.15	169	11.3	156	10.4
Announced for bidding	529	57.0	190	20.5	85	9.2	123	13.3
Sold	360	69.1	81	15.5	29	5.6	51	9.8

Source: Report of the Federal Agency for Federal Property Management (FAFPM) “O privatizatsii federal’nogo imushchestva v 2005 g.” [“On federal property privatization in 2005”]. M., 2006; the authors’ estimations.

The structure of blocks of shares announced for bidding was different from the forecasted one by a higher percentage of minority and complete blocks of shares, while the actual structure of the sold blocks of shares – by a lower percentage of blocking, controlling and complete ones, and at the same time the percentage of minority stakes was more than 69% against 54% in the forecasted structure and 57% in the structure of those announced for bidding.

Nevertheless, despite the noticeable growth in the sale of state-owned blocks of shares of a small size, there was no demand for many of the offered blocks of shares – due to the consolidation of share capital within the property of dominating non-state shareholders and the end of the struggle for corporate control, which was conducive to a declining interest of other potential buyers and the general level of competition. And the acquisition of a minority block of shares could not always ensure payback through the payment of dividends or growing market capitalization.

In recent years, great changes have been observed in the methods being applied for privatizing federal blocks of shares (*Table 12*).

Table 12

The Dynamic and Structure of Sold Federal Blocks of Shares, by Applied Methods of Privatization, in 2001–2005

Methods of selling federal blocks of shares														
Period	total		Open auction (for 2001 – auction in general)		Closed auc- tion		specialized auction		Through public offer- ing		Without announced price		By realizing priority shareholder right	
	units	%	units	%	units	%	units	%	units	%	units	%	units	%
2001*	125	100	107	85.6			12	9.6	-	-	-	-	-	-
2002	112	100	1	0.9	99	88.4	12	10.7	-	-	-	-	-	-
2004	565	100	19	3.4	264	46.7	18	3.2	212	37.5	39	6.9	13	2.3
2005	521	100	127	24.4	82	15.7	0	0	85	16.3	219	42.0	8	1.6

* – For the year 2001, information is available concerning the total number of blocks of shares sold at an auction (without its division into an open and closed one), – 107 units, and another 6 blocks of shares not indicated in the corresponding row were realized through a commercial tender with investment and (or) social terms.

Source: data from the official website www.mgi.ru; Medvedev Yu. M. Itogi deiyatel'nosti Minimushchestva Rossii i ego territorial'nykh organov za 2002 god I zadachi na 2003 god. [Results of the activity of the Ministry of State Property of Russia and of its territorial agencies in the year 2002 and the tasks for the year 2003] // Vestnik Minimushchestva Rossii [Herald of the RF Ministry of State Property], 2003, No. 1, p. 36; Materials for the RF Government's meeting on 17 March 2005 "On measures designed to improve the efficiency of federal property management"; Report of the Federal Agency for Federal Property Management (FAFPM) "O privatizatsii federal'nogo imushchestva v 2005 g." ["On federal property privatization in 2005"]. M., 2006; the authors's estimations.

While in 2001–2002 the main methods of selling federal blocks of shares were auction and specialized auction, which together accounted for 95–100 % of all sales, in 2004 this index was slightly above 53 %. Thus shift can be explained by the beginning of a relatively mass-scale application of the new methods of privatization put forth by the third law on privatization, which came into force from 27 April 2002. Thus, in 2004, 212 blocks of shares (37.5% of all the sales) were sold through public offering, and without announcing price – 39 blocks of shares (6.9%). As a result, these methods of privatization became the second and the third (by their significance) channels for the realization of blocks of shares.

In 2005 the percentage of the blocks of shares sold at auctions became even smaller, having amounted to approximately 40 %. No block of shares was realized at a specialized auction, although in 2001–2002 this method was applied to approximately 10% of all sold blocks of shares, in 2004 – 3.2% (18 units). The RF Ministry of State Property explains the termination of such a practice by its low efficiency, shown by the dispersion of the transferred stakes of a controlling and blocking sizes, lowered incomes, and incomplete realization of the blocks of shares offered for sale.

The considerable growth in the percentage of the blocks of shares sold at an open auction (24.4% in 2005 against 3.4% in 2004), alongside a nearly threefold decline in the percentage of blocks of shares realized at a closed auction (15.7% against 46.7%). In absolute terms, the number of blocks of shares realized at auctions with an open form of price bidding increased from 19 units in 2004 to 127 units in 2005 (in 2002 – 1 unit). The RF Ministry of State Property is quite justified in its opinion that expanding the practice of open auctions is conducive to higher transparency of the privatization process, and so this practice is being consistently pursued. Out of the 470 decisions adopted by the RF Ministry of State Property concerning the terms of the privatization of shares offered for sale for the first time in 2005, in 85% of cases these decisions established, as the method of privatization, an open auction, whereas one-third of the 82 blocks of shares sold at closed auctions were sold on the basis of decisions made prior to the onset of administrative reform in 2004, when the RF Ministry of State Property had been still in existence.

However, the greatest number of blocks of shares (219 units, or 42%) in 2005 were sold without the announcement of their price. Public offering amounted to 16.3 % (or 85 units). The active application, in 2005, of the methods of public offering and of sale without the announcement of price was aimed at selling a considerable bulk of blocks of shares that had not been sold in previous years. Based on the results of the consideration, by the RF Ministry of State Property, of the aforesaid proposals put forth by the RFPPF with regard to the alteration of the method for privatizing the shares in 703 joint-stock companies, the sale of which could not be achieved earlier, it was decided that in respect of their main bulk these particular methods of privatization should be applied, namely public of-

fering (shares in 325 JSCs, of which those of 41 JSCs – for the second time) and sale without the announcement of price (shares in 243 JSCs).

It should be reminded that such methods of sale imply that the price of an object to be sold (a block of shares) may be lowered if an auction has not taken place, and they are designed for the sale of property with low liquidity, mostly represented by minority blocks of shares. However, they serve this function only to a certain extent. Thus, in 2004, out of the 461 blocks of shares offered for realization through public offering, in respect of which during a calendar year the results of sale were drawn up (without taking into account another 64, for which the timeline for drawing up the results of sale was established for 2005), 212 were actually sold. The percentage of realization in the event of sale without the announcement of price is much higher: 39 of 40 (within the framework of 9 sales, whose results were to be drawn up in the next year).

In instances when an auction for the bidding of shares was recognized as not having taken place, and there was only one potential buyer, the public offering of such shares resulted, as a rule, in bringing their price down to a level equal to 50% of the initial price set for the auction that had not taken place. With due regard for this circumstance, the RF Ministry of State Property in 2005 applied a new technology for an instant assessment of the “just” value of shares when making a decision concerning the feasibility of changing the method of privatization. In respect to the shares in 125 joint-stock companies, the RF Ministry of State Property decided in 2005 that a second sale at an auction should be undertaken. In fact, in 2004–2005, at second auctions, shares in 59 joint-stock companies were sold, which yielded revenues in the federal budget of approximately 1,454 million roubles, or by 750 million roubles more as compared with the amount of revenues expected from the sale of shares through public offering.

The sales of blocks of shares in the procedure of realizing the priority right of shareholders were only of a marginal character in the period of 2004–2005. By applying this method, 13 and 8 blocks of shares, respectively, were realized, which was higher than the number of blocks of shares sold in 2001 through a commercial tender with specified investment and (or) social terms. In the following years this method of sale was never applied.

Next we are going to analyze the structure of blocks of shares sold in the last two years from the point of view of their size and the methods of sale applied (*Table 13*).

Table 13

**The Structure of Federal Blocks of Shares Sold in 2004–2005,
by Size of Charter Capital and Method of Sale**

Period	total		up to 25%		between 25% + 1 share and 50%		between 50% + 1 share and 100% – 1 share		100%	
	units	%	units	%	units	%	units	%	units	%
Total for 2004, including	565	100	406	71.85	119	21.05	34	6.0	6	1.1
through realizing priority right	13	100	13	100.0	–	–	–	–	–	–
at open auction	19	100	7	36.8	6	31.6	6	31.6	–	–
at closed auction	264	100	199	75.4	42	15.9	18	6.8	5	1.9
at specialized auction	18	100	3	16.7	11	61.1	3	16.7	1	5.5
through public offering	212	100	152	71.7	54	25.5	6	2.8	–	–
without announcing price	39	100	32	82.0	6	15.4	1	2.6	–	–
Total for 2005, including	521	100	360	69.1	81	15.5	29	5.6	51	9.8
through realizing priority right	8	100	7	87.5	1	12.5	–	–	–	–
at open auction	127	100	31	24.4	27	21.3	20	15.7	49	38.6
at closed auction	82	100	69	84.1	11	13.4	2	2.5	–	–
through public offering	85	100	61	71.8	19	22.35	3	3.5	2	2.35
without announcing price	219	100	192	87.7	23	10.5	4	1.8	–	–

Source: Materials for the RF Government’s meeting on 17 March 2005 “On measures designed to improve the efficiency of federal property management”; Report of the Federal Agency for Federal Property Management (FAFPM) “O privatizatsii federal’nogo

imushchestva v 2005 g.” [“On federal property privatization in 2005”]. M., 2006; the authors’ estimations.

As was pointed out earlier, minority blocks of shares (i. e., up to 25 % of a JSC’s capital) constituted approximately 72% of all the sold blocks of shares in 2004, and 69% – in 2005.

If the sale of blocks of shares is looked at separately, depending on the method applied, it can be noted that more than 70–80 % blocks of shares privatized in 2004–2005 at a closed auction, through public offering and without the announcement of price were of the same size; within the structure of sales, the share of minority stakes sold at a closed auction and without the announcement of price in 2005 increased, while that of those sold through public offering – remained at the level of 2004. The structure of the blocks of shares sold at an open auction in 2004 demonstrated a more even distribution (by the size of the stake being sold): 7 units – stakes amounting to up to 25% of capital, and 6 units each – of blocking and controlling sizes (between 50% of shares – 1 share and 100% shares – 1 share). In 2005, 38.6% of the blocks of shares sold at open auctions were complete stakes (100% of shares), 24.4% – of the minority type, 21.3% – of the blocking type, and 15.7% – of the controlling size. Within the framework of privatization through a specialized auction, in 2004 more than 61% of the sold blocks of shares were of the blocking size (amounting to between 25% shares – 1 share and 50%). When blocks of shares were sold by way of exercising the priority right of shareholders, all the 13 blocks of shares realized in 2004 and 7 of the 8 blocks of shares realized in 2005 were of a minority size.

As a result, if in 2004 the main methods of selling minority blocks of shares were sale through a closed auction (49%) and public offering (37.4%), in 2005 these already had given way to sale without the announcement of price (53.3%). Blocking stakes in 2004 were sold mostly through public offering (45.4%) and at a closed auction (35.3%), in 2005 – at a closed auction (one-third) and without the announcement of price (28.4%). A closed auction was in 2004 the main method of selling controlling and complete (100%) blocks of shares (52.9% and 83.3%, respectively). In 2005, an open auction became the main method, by applying

which 69% of controlling and 96% of complete blocks of shares were sold.

In this connection, quite natural would be the question as to what would be the effects associated with a specific method of selling shares from the point of view of the excess of the trading value over the initial bidding price, which, in the final analysis, is what actually determines the returns on sales for the budget (*Tables 14, 15, 16*).

Table 14

The Price Range for the Sale of Shares and Stakes in Economic Societies at Open and Closed Auctions in 2004–2005

Period	Equal to initial price		Higher than initial price by less than 5%		Higher than initial price by more than 5%, but less than by 20%		Higher than initial price by more than 20%, but less than twofold		Higher than initial price by more than twice	
	units	%	units	%	units	%	units	%	units	%
2004	10	3.5	130	45.9	43	15.2	52	18.4	48	17.0
2005	52	24.9	78	37.3	20	9.6	33	15.8	26	12.4

Source: Materials for the RF Government’s meeting on 17 March 2005 “On measures designed to improve the efficiency of federal property management”; Report of the Federal Agency for Federal Property Management (FAFPM) “O privatizatsii federal’nogo imushchestva v 2005 g.” [“On federal property privatization in 2005”]. M., 2006; the authors’ estimations.

As regards the sale of blocks of shares (or stakes in economic societies) in 2004 at open and closed auctions, their structure in terms of price was as follows: 17% (or 48 units) were sold at a price twice or more as high as the initial price; slightly less than a half of the total amount (or 140 units) were sold at a price no more than by 5% higher than the initial price (including 10 units at the initial price); the trading value of the remaining blocks of shares (slightly more than one-third of the total amount) was in the range of more than 5% of the initial price but less than twice as high. In 2005 there was a dramatic rise in both the number and the percentage of the blocks of shares sold at the initial price (up to nearly 25%, against only 3.5% in 2004). The percentages of blocks of

shares sold at other prices became smaller. Nevertheless, the highest number of blocks of shares was realized at a price less than by 5% higher than the initial price (37.3%), just as it happened in 2004 (45.9%).

Table 15

Price Ranges of Shares and Stakes in Economic Societies Sold through Public Offering in 2004–2005

Period	Higher than initial price at auction that was not actually held		Equal to initial price at auction that was not actually held		Amounts to between 75% and 99.9% of initial price at auction that was not actually held		Amounts to between 50.1% and 74.9% of initial price at auction that was not actually held		Equal to minimum possible (50% of initial price at auction that was not actually held)	
	units	%	units	%	units	%	units	%	units	%
2004	0*	–	37	17.5	13	6.1	31	14.6	131	61.8
2005	0*	–	11	12.95	6	7.05	16	18.8	52	61.2

* – the RFPF never traded through public offering any shares with an initial price higher than that set for an auction that had not taken place, although such an opportunity is envisaged in legislation.

Source: Materials for the RF Government’s meeting on 17 March 2005 “On measures designed to improve the efficiency of federal property management”; Report of the Federal Agency for Federal Property Management (FAFPM) “O privatizatsii federal’nogo imushchestva v 2005 g.” [“On federal property privatization in 2005”]. M., 2006; the authors’ estimations.

When shares were sold through public offering, in 2004 in 61.8% of cases (131 units) their price was equal to the minimum possible threshold, or a half of the initial price set for an auction that had not taken place; 17.5% of blocks of shares (37 units) were sold at the maximum possible bid price, equal to the initial price set for an auction that had not taken place²²; and in the remaining 20.7% of cases (43 units) the trading value was varying in the interval between the highest and the lowest. In 2005 the percentage of blocks of shares (or stakes in economic societies)

²² The RFPF never offered any shares at a price higher than the initial price set for an auction that had not taken place.

sold at a maximum possible price went down to 13%, alongside a growing percentage of the blocks of shares sold at a price equal to between one-half and three-fourths of the initial price set for an auction that had not taken place – from 14.6% in 2004 to 18.8% in 2005. The percentages of blocks of shares sold at a minimum price and the price equal to three-fourths of the initial price set for an auction that had not taken place remained approximately at the same level. The number of blocks of shares realized at a price lower than the standard price set for an auction that had not taken place decreased from 77 units in 2004 to 30 units in 2005, but their percentage of the total amount of sold blocks of shares demonstrated no changes, amounting to 35–36 %.

Table 16

Price Ranges of Shares and Stakes in Economic Societies Sold without the Announcement of their Price in 2005

Period	Higher than initial price at auction that was not actually held		lower than initial price at auction that was not actually held, but higher than maximum price of sale through public offering (50 % of initial price at auction)		Amounts to between 25% and 50% of initial price at auction that was not actually held		Amounts to between 5% and 25% of initial price at auction that was not actually held		Amounts to less than 5% of initial price at auction that was not actually held	
	units	%	units	%	units	%	Units	%	units	%
2005	6	2.7	17	7.8	39	17.8	119	54.3	38	17.4

Source: Report of the Federal Agency for Federal Property Management (FAFPM) “O privatizatsii federal’nogo imushchestva v 2005 g.” [“On federal property privatization in 2005”]. M., 2006; the authors’ estimations.

The main bulk of shares and stakes in economic societies in 2005 (54.3%) was sold at a price between 5% and 25% of the initial price set for an auction that had not taken place, while another 17–18 % – within the range of 25% to 50% of the initial price set for an auction that had not taken place and less than 5% of this index. There were some instances when during trading without the announcement of price it was established at a level higher than the initial price set for an auction that had not taken

place and the minimum price of public offering, but these were very rare: less than 3% and 8% of all sales, respectively. 162 blocks of shares (or 74% of the total amount sold) were realized at a price lower than the standard price set for an auction that had not taken place.

The size of the traded federal blocks of shares is not the only factor determining the interest of potential investors. A certain role in the formation of demand for traded securities belongs to the investment attractiveness of each individual branch of industry or individual enterprises (*Table 17*).

Table 17

**The by-branch Structure of the Forecast Plan (Program)
for Privatization, in Terms of the Number of Blocks of Shares
Earmarked for Sale in 2004 and the Number of those Actually
Sold (without those Blocks of Shares the Results for the Trading
of which were Drawn up in 2005)**

Branch	Included in Forecast Plan (Program) for privatization	Number of sold blocks of shares				
		Total	under 25%	From 25% – 50%	From 50% – 100% – 1 share to 100% – 1 share	100%
Motor transport	77	39/ 50.6*	34	4	1	–
Agroindustrial complex (AIC)	237	86/ 36.3*	57	18	10	1
Nuclear power engineering	24	8/ 33.3*	6	2	–	–
Foreign trade organizations	1	–	–	–	–	–
Water transport	45	6/ 13.3*	3	3	–	–
Air transport	22	4/ 18.2*	2	–	2	–
Geology and processing of precious metals and stones	38	24/ 63.2*	22	1	1	–
Railway transport	3	–	–	–	–	–
Publishers and printers	11	1/ 9.1*	–	–	–	1

Branch	Included in Forecast Plan (Program) for privatization	Number of sold blocks of shares				
		Total	under 25%	From 25% – 1 share to 50%	from 50% – 1 share to 100% – 1 share	100%
Credit institutions	144	32/ 22.2*	32	–	–	–
Light industry	26	6/ 23.1*	6	–	–	–
Timber industry complex (TIC)	60	20/ 33.3*	15	2	2	1
Machine-building	141	33/ 23.4*	26	4	2	1
Medical industry	4	–	–	–	–	–
Metallurgy	26	13/ 50.0*	10	3	–	–
Science	7	2/ 28.6*	1	1	–	–
Non-production sphere	124	37/ 29.8*	15	10	11	1
Oil and gas complex	108	37/ 34.3*	15	19	2	1
Military-industrial complex (MIC)	217	85/ 39.2*	71	12	2	–
Construction materials industry	4	–	–	–	–	–
Fishery	6	4/ 66.7*	3	1	–	–
Communications	11	3/ 27.3*	3	–	–	–
Insurance institutions	7	3/ 42.9*	–	3	–	–
Construction complex	104	25/ 24.0*	22	3	–	–
Fuel and energy complex (FEC)	73	5/ 6.8*	5	–	–	–
Coal mining industry	28	11/ 39.3*	3	8	–	–
Chemical industry and petrochemical industry	42	16/ 38.1*	13	1	2	–
Power-	96	36/ 37.5*	12	24	–	–

Branch	Included in Forecast Plan (Program) for privatization	Number of sold blocks of shares				
		Total	under 25%	From 25% – 1 share to 50%	from 50% – 1 share to 100% – 1 share	100%
engineering construction complex						
Road system	–	–	–	–	–	–
Other branches	26	29/ 111.5*	29	–	–	–
Total	1702	565/ 33.2*	405	119	35	6

* – in the denominator: % of the number of those included in the Forecast Plan (Program) for Privatization.

Source: Materials for the RF Government's meeting on 17 March 2005 "On measures designed to improve the efficiency of federal property management"; the authors' estimations.

On the whole, among the 565 blocks of shares realized in 2004 the highest numbers belonged to the AIC (86 units, or 15.2%), motor transport (39 units, or 6.9%), the non-production sphere and the oil and gas complex (37 units, or 6.5% each), the power-engineering construction complex (36 units, or 6.4%), machine-building (33 units, or 5.8%), and credit institutions (32 units, or 5.7%).

The comparison, by branch of industry, of the number of sold blocks of shares with the number of those included in the Forecast Plan (Program) for Federal Property Privatization in 2004, has demonstrated that in the majority of branches less than a half of all the blocks of shares earmarked for privatization were actually sold. The highest indices were observed in metallurgy (50%), motor transport (50.6%), geology and the processing of precious metals and stones (63.2%), fishery (66.7%), as well as in a group of other industries, where the number of the blocks of shares actually sold was even higher than that of those earmarked (29 against 26). In the AIC, nuclear power engineering, the timber industry complex, the oil and gas sector, the military-industrial, the power engineering construction complexes, coal mining, chemical and petrochemical industry, and insurance organizations between 30% and 50% of the blocks of shares earmarked for sale were actually sold. This index amounted to less than 30% in water and air transport, light industry, ma-

chine-building, science, the non-production sphere, communications, the construction and fuel and energy complexes, credit institutions, and publishers and printers. No blocks of shares were sold in foreign trade organizations, railway transport, the medical industry, the industry of construction materials and in the road system, although only in the last one among those listed here no sale of shares had been planned.

In the majority of branches, more than 2/3 of the sold blocks of shares were of a minority size, and in light industry, communications, the fuel and energy complex, credit institutions and the group of other branches all of the sold stakes belonged to this category. In water and air transport, a half of the sold blocks of shares were of a minority size, while the other half was constituted by those of blocking and controlling size, respectively. In the non-production sphere, 40.5% of the sold blocks of shares were blocking, 29.7% – controlling, and 27% – blocking. In the oil and gas sector and in the power engineering construction complex, as well as in coal mining, more than a half of such stakes were of a blocking size, while all of the sold stakes in insurance organizations were blocking.

Among all the sold minority stakes, the highest numbers (no less than 30 units) were seen in the MIC (17.5%), the AIC (14.1%), motor transport (8.4%), and in credit institutions (7.9%). The main bulk among the sold blocking stakes was constituted by shares in the JSCs belonging to the power engineering construction complex (20.2%), and the oil and gas (16%) and the agroindustrial (15.1%) complexes. Among all the sold controlling blocks of shares, the most prominent were observed in the non-production sphere (31.4%) and the AIC (28.6%). Out of the 6 sold complete blocks of shares (amounting to 100%), the agroindustrial, the timber industry and the oil and gas complexes, publishers and printers, machine-building, and non-production sphere accounted for 1 unit each.

In 2005, the by-branch aspect of the implementation of the Annual Forecast Plan (Program) for Privatization was as follows (*Table 18*).

Table 18

**The by-Branch Structure of the Forecast Plan (Program)
for Privatization, in Terms of the Number of Blocks of Shares
Earmarked for Sale in 2005 and the Number of those Actually Sold
(without those Blocks of Shares the Results for the Trading of which
were Drawn up in 2006)**

Branch	Included in Forecast Plan (Program) for Privatization	Number of sold blocks of shares				
		Total	under 25%	from 25% + 1 share to 50%	From 50% + 1 share to 100% – 1 share	100%
Motor transport	30	20/ 66.7*	16	2	–	2
Agroindustrial complex (AIC)	234	93/ 39.7*	54	21	12	6
Nuclear power engineering industry	17	4/ 23.5*	2	2	–	–
Foreign trade institutions	–	–	–	–	–	–
Water transport	27	6/ 22.2*	6	–	–	–
Air transport	16	3/ 18.8*	1	2	–	–
Geology and processing of precious metals and stones	23	14/ 60.9*	8	1	1	4
Road system	–	–	–	–	–	–
Railway transport	6	1/ 16.7*	1	–	–	–
Publishers and printers	25	8/ 32.0*	3	–	1	4
Credit institutions	143	53/ 37.1*	51	2	–	–
Light industry	25	9/ 36.0*	9	–	–	–
Timber industry complex (TIC)	44	15/ 34.1*	13	–	2	–

Branch	Included in Forecast Plan (Program) for Privatization	Number of sold blocks of shares				
		Total	under 25%	from 25% + 1 share to 50%	From 50% + 1 share to 100% – 1 share	100%
Machine-building	124	58/ 46.8*	48	8	1	1
Medical industry	4	2/ 50.0*	2	–	–	–
Metallurgy	20	10/ 50.0*	9	–	–	1
Science	7	3/ 42.9*	2	–	–	1
Non-production sphere	158	51/ 32.3*	15	4	5	27
Oil and gas complex	56	24/ 42.9*	13	11	–	–
Military-industrial complex (MIC)	195	54/ 27.7*	45	4	2	3
Construction materials industry	5	3/ 60.0*	2	1	–	–
Fishery	2	1/ 50.0*	1	–	–	–
Communications	10	5/ 50.0*	3	1	–	1
Insurance institutions	4	–	–	–	–	–
Construction complex	111	39/ 35.1*	32	7	–	–
Fuel and energy complex (FEC)	86	3/ 3.5*	–	3	–	–
Commerce	18	8/ 44.4*	2	3	3	–
Coal mining industry	16	3/ 18.8*	1	2	–	–
Chemical industry and petrochemical industry	28	13/ 46.4*	11	–	1	1
Power-engineering	45	15/ 33.3*	7	7	1	–

Branch	Included in Forecast Plan (Program) for Privatization	Number of sold blocks of shares				
		Total	under 25%	from 25% + 1 share to 50%	From 50% + 1 share to 100% – 1 share	100%
construction complex						
Other branches	17	3/ 17.6*	3	–	–	–
Total	1496	521/ 34.8*	360	81	29	51

* – in the denominator: % of the number of those included in the Forecast Plan (Program) for Privatization.

Source: Report of the Federal Agency for Federal Property Management (FAFPM) “O privatizatsii federal’nogo imushchestva v 2005 g.” [“On federal property privatization in 2005”]. M., 2006; the authors’ estimations.

The highest number of sales of blocks of shares in 2005 took place in the agroindustrial complex (17.8% of all sold blocks of shares), machine-building (11.1% of all sold blocks of shares), the military-industrial complex (10.4% of all sold blocks of shares), credit institutions (10.1% of all sold blocks of shares), and the construction complex (7.5% of all sold blocks of shares).

By comparing, across the branches, the numbers of sold blocks of shares with those of included in the Forecast Plan (Program) for Privatization in 2005, it can be concluded that, just as in the previous year, in the majority of branches less than a half of all the blocks of shares initially earmarked for privatization was actually sold. The highest indices of the Program’s implementation were observed in motor transport (66.7%), geology and the processing of precious metals and stones (60.9%), the construction materials industry (60%), medical industry, metallurgy, fishery, and communications (50%), where no less than a half of all the blocks of shares included in the program was actually sold. In the AIC, light industry, the TIC, machine-building, science, the non-production sphere, construction and the power-engineering construction complexes, commerce, the chemical and petrochemical industry, and among credit institutions, publishers and printers, between 30% and 50% of all the blocks of shares earmarked for sale were actually sold. In nu-

clear power engineering, water, air and railway transport, the MIC, the FEC, coal mining, and in the group of other branches this index amounted to no more than 30%. No shares in the companies belonging to the category of foreign trade organizations and the road system were sold, not having been included in the privatization program. No information is available concerning the sale of blocks of shares in the insurance organizations included in the privatization program.

In the majority of branches, more than a half of all sold blocks of shares were of a minority size, and in water and railway transport, in light and the medical industries, fishery and the group of other branches all of the sold stakes were of this size. In the FEC all the sold parcels of shares were of a blocking size. In air transport and in coal mining, 2/3 of all the sold blocks of shares were of a blocking size, and another 1/3 were of a minority size. In nuclear power engineering the sold blocks of shares were distributed evenly between the minority and blocking categories. In the power engineering construction complex a similar picture was observed, but there among the sold blocks of shares, in addition to the equal quantities of minority and blocking stakes (7 units each), there was one controlling stake. More heterogeneous was the composition of the sold blocks of shares in commerce (37.5% each of the stakes of controlling and blocking sizes, and another 1/4 of a minority size) and among publishers and printers (a half of all the sold blocks of shares were complete, 37.5% – minority, and one controlling stake, or a total of 1/4 across that branch). In the non-production sphere more than a half of all the sold blocks of shares (52.9%) were complete, 29.4% – minority, 9.8% – controlling, and 7.9% – blocking.

Among all the sold minority stakes, the highest numbers (no less than 30 units) were observed in the AIC (15%), credit institutions (14.2%), machine-building (13.3%) and the MIC (12.5%). The main bulk of all sold blocking stakes was constituted by shares in the companies belonging to the AIC (25.9%), the oil and gas complex (13.6%), and machine-building (9.9%). Among the sold controlling blocks of shares the leaders were registered in the AIC (41.4%) and the non-production sphere (17.2%). Out of all the sold complete (100%) blocks of shares, the high-

est number was observed in the non-production sphere (52.9%) and the AIC (11.8%).

Of some interest is the comparison between the content of the 2004 and 2005 Forecast Plans (Programs) for Federal Property Privatization and the extent to which they were actually implemented in terms of different blocks of shares and stakes in economic societies, by branch (*Table 19*).

Table 19

Comparative Dynamic of the by-Branch Structure of Forecast Plans (Programs) for Privatization and the Sales Actually Carried out in 2004 and 2005

Branch	Included in Forecast Plan (Program) for Privatization		Number of sold blocks of shares									
			Total		under 25%		from 25% + 1 share to 50%		From 50% + 1 share to 100% - 1 share		100%	
					2004	2005	2004	2005	2004	2005		
Motor transport	77	30	39	20	34	16	4	2	1	-	-	2
Agroindustrial complex (AIC)	237	234	86	93	57	54	18	21	10	12	1	6
Nuclear power engineering industry	24	17	8	4	6	2	2	2	-	-	-	-
Foreign trade institutions	1	-	-	-	-	-	-	-	-	-	-	-
Water transport	45	27	6	6	3	6	3	-	-	-	-	-
Air transport	22	16	4	3	2	1	-	2	2	-	-	-
Geology and processing of precious metals and stones	38	23	24	14	22	8	1	1	1	1	-	4
Road system	-	-	-	-	-	-	-	-	-	-	-	-
Railway transport	3	6	-	1	-	1	-	-	-	-	-	-
Publishers and printers	11	25	1	8	-	3	-	-	-	1	1	4
Credit institutions	144	143	32	53	32	51	-	2	-	-	-	-
Light industry	26	25	6	9	6	9	-	-	-	-	-	-
Timber industry complex (TIC)	60	44	20	15	15	13	2	-	2	2	1	-
Machine-building	141	124	33	58	26	48	4	8	2	1	1	1
Medical industry	4	4	-	2	-	2	-	-	-	-	-	-
Metallurgy	26	20	13	10	10	9	3	-	-	-	-	1

Branch	Included in Forecast Plan (Program) for Privatization		Number of sold blocks of shares									
			Total		under 25%		from 25% + 1 share to 50%		From 50% + 1 share to 100% - 1 share		100%	
					2004	2005	2004	2005	2004	2005		
2004	2005	2004	2005	2004	2005	2004	2005	2004	2005	2004	2005	
Science	7	7	2	3	1	2	1	-	-	-	-	1
Non-production sphere	124	158	37	51	15	15	10	4	11	5	1	27
Oil and gas complex	108	56	37	24	15	13	19	11	2	-	1	-
Military-industrial complex (MIC)	217	195	85	54	71	45	12	4	2	2	-	3
Industry of construction materials	4	5	-	3	-	2	-	1	-	-	-	-
Fishery	6	2	4	1	3	1	1	-	-	-	-	-
Communications	11	10	3	5	3	3	-	1	-	-	-	1
Insurance institutions	7	4	3	-	-	-	3	-	-	-	-	-
Construction complex	104	111	25	39	22	32	3	7	-	-	-	-
Fuel and energy complex (FEC)	73	86	5	3	5	-	-	3	-	-	-	-
Commerce	-	18	-	8	-	2	-	3	-	3	-	-
Coal mining industry	28	16	11	3	3	1	8	2	-	-	-	-
Chemical industry and petrochemical industry	42	28	16	13	13	11	1	-	2	1	-	1
Power engineering construction complex	96	45	36	15	12	7	24	7	-	1	-	-
Other branches	26	17	29	3	29	3	-	-	-	-	-	-
Total	1702	1496	565	521	405	360	119	81	35	29	6	51

Source: Materials for the RF Government's meeting on 17 March 2005 "On measures designed to improve the efficiency of federal property management"; Report of the Federal Agency for Federal Property Management (FAFPM) "O privatizatsii federal'nogo imushchestva v 2005 g." ["On federal property privatization in 2005"]. M., 2006.

A comparison made between the Forecast Plan (Program) for Federal Property Privatization in 2005 and a similar document adopted for the year 2004 has shown that in the majority of branches the number of blocks of shares earmarked for sale was declining in absolute terms. Exceptions were represented by railway transport, publishers and printers, the non-production sphere, the industry of construction materials, the

construction complex, and the FEC, where the planned number of the blocks of shares to be sold was higher than in 2004. In medical industry and in science it was to remain at the previous year's level. The list of branches across which the blocks of shares to be privatized are classified was augmented by commerce.

Regarding a comparison between the actually sold blocks of shares, it can be noted that their number in 2005 rose on 2004 in several branches, i.e., in machine-building (by 25 units), among credit institutions (by 21 units), in the non-production sphere and in the construction complex (by 14 units), in the AIC, among publishers and printers, in light industry, science, and communications (less than by 10 units). In 2005 there were also some sales of blocks of shares in companies belonging to the spheres of railway transport, medical industry, the industry of construction materials, and commerce, which did not happen in 2004.

In the other branches (except water transport) the number of sold blocks of shares was decreasing by comparison with 2004, the most noticeable decline occurring in the MIC (by 31 units), in the group of other branches (by 26 units), in the power engineering construction complex (by 21 units) and in the oil and gas complex (by 13 units), in motor transport (by 19 units), and in geology and the processing of precious metals and stones (by 10 units). In water transport the number of sold blocks of shares remained at the same level as in 2004.

If the by-branch dynamic of sold blocks of shares is analyzed by the size of a stake being sold, the following facts can be noted.

In the category of minority blocks of shares in 2005, the number of those sold in water transport, among credit institutions, in light industry, in machine-building, in science, and in the construction complex rose on 2004. There were cases when the stakes of this size were sold in railway transport, among publishers and printers, in the medical industry, in the industry of construction materials, and in commerce, while none were observed in 2004. In communications and the non-production sphere their number remained at the same level. In the category of blocking stakes, the number of those sold increased in the AIC, machine-building, and the construction complex; for the first time the sold stakes of this size appeared in air transport, in the industry of construction materials, in

communications, the FEC and commerce. In nuclear power engineering, geology and the processing of precious metals and stones the number of sold stakes of a blocking size remained at the level of 2004. In the category of controlling stakes, the growth in the number of sold stakes can be noted only in the AIC; there emerged some instances of sale of such stakes among publishers and printers, in commerce and in the power engineering construction complex. In geology and the processing of precious metals and stones, the TIC and the MIC the number of sold blocks of shares of this size was at the same level as in 2004. In the category of complete stakes (100%), one can note growth in the realization of blocks of shares in the non-production sphere, in the AIC, among publishers and printers, as well as the emergence of such blocks of shares sold in motor transport, geology and the processing of precious metals and stones, in metallurgy, in science, in communications, in the MIC, and in the chemical and petrochemical industries. In machine - building the number of sold blocks of shares remained at the level of 2004. In all the other branches, not mentioned in connection with the sale of stakes of a certain size, the number of sold blocks of shares in 2005 decreased by comparison with 2004 (and sometimes no instances of the stakes of that size were registered altogether).

Below we present the results of our analysis of the compatibility between the by-branch structure of the Forecast Plans (Programs) for Federal Property Privatization adopted for 2004 and for 2005 and the structure of the actual sales of blocks of shares, as well as changes in the degree of the implementation of both programs (*Table 20*).

First of all, it is necessary to note that in 2004 within the actual structure of sales, by comparison with forecasted values, greater prominence was gained by motor transport, the AIC, geology and the processing of precious metals and stones, metallurgy, the MIC, fishery, coal mining, the chemical and petrochemical industry, the power engineering construction complex, and especially by the group of other branches, whose share became higher than the forecasted index by more than 3.4 times, because in that group the number of actually sold blocks of shares exceeded the forecasted value (the only instance of such an excess registered during the period of 2004–2005). The percentages within the actual structure of

sales in nuclear power engineering, the TIC, communications and insurance organizations were very nearly the same as forecasted. The percentages demonstrated by all the other branches were lower than the forecasted values, and among foreign trade organizations, in railway transport, in medical industry, or in the industry of construction materials no sales of blocks of shares were registered at all, despite the presence of these branches in the Forecast Plan.

Table 20

**The by-Branch Structure of the Forecast Plans (Programs)
for Privatization in 2004 and 2005 and the Degrees
of their Implementation**

Branch of industry	Share of branch in Forecast Plan (Program) Privatization, in %		Share of branch in actual structure of sales, in %		Degree of implementation of Forecast Plan (Program) for Privatization *, in %	
	2004	2005	2004	2005	2004	2005
Motor transport	4.5	2.0	6.9	3.8	50.6	66.7
Agroindustrial complex (AIC)	13.9	15.6	15.2	17.8	36.3	39.7
Nuclear power engineering industry	1.4	1.1	1.4	0.8	33.3	23.5
Foreign trade institutions	0.0	–	–	–	–	–
Water transport	2.6	1.8	1.1	1.1	13.3	22.2
Air transport	1.3	1.1	0.7	0.6	18.2	18.8
Geology and processing of precious metals and stones	2.2	1.5	4.25	2.7	63.2	60.9
Road system	–	–	–	–	–	–
Railway transport	0.2	0.4	–	0.2	–	16.7
Publishers and printers	0.6	1.7	0.2	1.5	9.1	32.0
Credit institutions	8.5	9.6	5.7	10.2	22.2	37.1
Light industry	1.5	1.7	1.05	1.7	23.1	36.0
Timber industry complex (TIC)	3.5	2.95	3.5	2.9	33.3	34.1
Machine-building	8.3	8.3	5.85	11.1	23.4	46.8
Medical industry	0.2	0.3	–	0.4	–	50.0
Metallurgy	1.5	1.3	2.3	1.9	50.0	50.0

Branch of industry	Share of branch in Forecast Plan (Program) Privatization, in %		Share of branch in actual structure of sales, in %		Degree of implementation of Forecast Plan (Program) for Privatization *, in %	
	2004	2005	2004	2005	2004	2005
Science	0.4	0.5	0.35	0.6	28.6	42.9
Non-production sphere	7.3	10.6	6.55	9.8	29.8	32.3
Oil and gas complex	6.3	3.75	6.55	4.6	34.3	42.9
Military-industrial complex (MIC)	12.7	13.0	15.05	10.4	39.2	27.7
Construction materials industry	0.2	0.3	–	0.6	–	60.0
Fishery	0.3	0.1	0.7	0.2	66.7	50.0
Communications	0.6	0.7	0.5	0.9	27.3	50.0
Insurance institutions	0.4	0.3	0.5	–	42.9	–
Construction complex	6.1	7.4	4.4	7.5	24.0	35.1
Fuel and energy complex (FEC)	4.3	5.7	0.9	0.6	6.8	3.5
Commerce	–	1.2	–	1.5	–	44.4
Coal mining industry	1.6	1.1	1.95	0.6	39.3	18.8
Chemical industry and petrochemical industry	2.5	1.9	2.85	2.5	38.1	46.4
Power engineering construction complex	5.6	3.0	6.4	2.9	37.5	33.3
Other branches	1.5	1.1	5.15	0.6	111.5	17.6
Total	100.0	100.0	100.0	100.0	33.2	34.8

* – in relation to the number of blocks of shares included in the Forecast Plan (Program) for Privatization, and not those that could be actually sold (with due regard for the adjustments resulting from failures, for a variety of reasons, to make appropriate decisions regarding the shares in some JSC concerning the terms of their privatization).

Source: Materials for the RF Government's meeting on 17 March 2005 "On measures designed to improve the efficiency of federal property management"; Report of the Federal Agency for Federal Property Management (FAFPM) "O privatizatsii federal'nogo imushchestva v 2005 g." ["On federal property privatization in 2005"]. M., 2006; the authors' estimations.

On the whole, the discrepancies between the actual structures of sales of blocks of shares and the forecasted ones were not so great. The highest percentage was demonstrated by the AIC (15.2% against the forecasted 13.9%) and the MIC (15.1% against 12.7%), by motor transport (6.9% against 5.4%), by the non-production sphere (6.6% against 7.3%), by the oil and gas complex (6.6% against 6.3%) and by the power engineering construction complex (6.4% against 5.6%). At the same time, significantly lower by comparison with the forecast were the percentages demonstrated by credit institutions (5.7% against the forecasted 8.5%), by machine-building (5.9% against 8.3%) and by the construction complex (4.4% against 6.1%). In fact, as significant deviations from the forecasted structure can be regarded the higher percentages shown by the AIC and the MIC, followed by motor transport instead of (formerly) credit institutions which, together with machine-building, contrary to forecasts, were not among the top five branches accounting for the highest contributions to the structure of sold blocks of shares.

In the Forecast Plan (Program) for Federal Property Privatization in 2005, by comparison with the same document adopted for the year 2004, it was envisaged that the structure of the blocks of shares being sold should contain higher percentages of those sold in the AIC, railway transport, publishers and printers, credit institutions, light industry, the non-production sphere, the MIC, the construction complex, and the FEC; and one new branch (commerce) was added. The percentages demonstrated by machine-building, medical industry, science, the industry of construction materials, communications, and insurance organizations remained at the previous year's level, and those of all the other branches decreased.

In 2005 the actual structure of sales of blocks of shares, by comparison with the forecasted values, contained higher percentages of demonstrated by motor transport, the AIC, geology and the processing of precious metals and stones, credit institutions, machine - building, metallurgy, the oil and gas complex, the industry of construction materials, communications, commerce, and the chemical and petrochemical industry. The percentages in the TIC, light and the medical industries, science, fishery, construction and the power engineering construction complex were at the forecasted level, and in all the other branches – lower than forecasted, while among

insurance organizations no blocks of shares were sold, despite having been included in the Forecast Plan.

As a result, in 2005 the actual structure of sales of blocks of shares, by comparison with 2004, higher percentages were demonstrated by the AIC, publishers and printers, credit institutions, light industry, machine-building, science, the non-production sphere, communications, and the construction complex. The most impressive growth in percentage points was demonstrated by machine-building (by 5.2 p.p.), credit institutions (by 4.5 p. p.), the non-production sphere and the construction complex (by 3.3 p.p.). The percentages shown by water and air transport remained the same as in 2004, while those shown by all the other branches declined. The most noticeable decline occurred in the group of other branches (by 4.6 p.p.), the MIC (by 4.5 p.p.), the power engineering construction complex (by 3.5 p.p.) and motor transport (by 3.1 p.p.).

Within the by-branch structure of the blocks of shares sold in 2005 the highest percentages were demonstrated by the AIC (17.8% against the forecasted 15.6%), by machine-building (11.1% against 8.3%), by the MIC (10.4% against 13%), by credit institutions (10.2% against 9.6%), by the non-production sphere (9.8% against 10.6%). The actual structure of sales, by the relative contributions of individual branches, was closer to the forecasted one than a year earlier. Machine-building and credit institutions now occupied a more prominent position, which was approximately as forecasted. As in 2004, the highest percentage of sold blocks of shares, by comparison with the forecasted values, was observed in the AIC, and those somewhat lower than the forecasted values – in the MIC and the non-production sphere.

If one compares the relative degrees, by branch, to which the Forecast Plans (Programs) for Federal Property Privatization in 2004 and in 2005 were implemented with regard to the categories of blocks of shares and the stakes in economic societies, it will be noticed that these indices increased in the majority of branches, except in nuclear power engineering, fishery, geology and the processing of precious metals and stones, metallurgy, the MIC, the FEC, coal mining, the power engineering construction complex, and the group of other branches.

In terms of comparative attractiveness, in 2004–2005 all the branches could be divided into several groups:

- those branches where during these two years a higher percentage of blocks of shares was sold than on the average among all the blocks of shares, while the realization coefficient in 2005 rose on 2004 or remained stable (motor transport, the AIC, geology and the processing of precious metals and stones, metallurgy, the oil and gas complex, fishery, the chemical industry and the petrochemical industry)²³;
- those branches where in 2005 the percentage of sold blocks of shares rose above the average level, while having been below that level in 2004 (credit institutions, light industry, machine-building, science, communications, the construction complex);
- those branches where in 2005 the percentage of sold blocks of shares went down below the average level, while not having been below the average in 2004 (nuclear power engineering and coal mining, the MIC, the power engineering construction complex, and the group of other branches);
- those branches where during these two years a lower percentage of blocks of shares was sold than on the average among all the blocks of shares (water and air transport, publishers and printers, the non-production sphere, and the FEC)²⁴.

The timber industry complex (TIC) in 2004–2005 by the percentage of sold blocks of shares was at the average level, while no comparison was possible for a number of branches (railway transport, medical industry, the industry of construction materials, commerce), because the sale of blocks of shares there happened only in 2005, and among insurance organizations – only in 2004.

In this connection it is necessary to remember that the indices demonstrating the degree of implementation of the Forecast Plan (Program) for Federal Property Privatization in terms of realization of federal blocks of shares reflect not only – and not so much – the attractiveness for private

²³ In this connection, the declining rate of realization of blocks of shares in 2005, by comparison with 2004, in geology and the processing of precious metals and stones, and in fishery should be noted, as well as the stability of this index in 2004–2005 in metallurgy.

²⁴ One should also note the growing rate of realization of blocks of shares in 2005, by comparison with 2004, in water transport, among publishers and printers, and in the non-production sphere. The last two branches, by the value of this index, in 2005 came close to the average level established for all blocks of shares.

businesses of federal shares in a JSC belonging to a certain branch, but rather the complexity of administering the sale process itself. It should be reminded that in 2004–2005 the shares in approximately 240–250 JSCs (each year), initially included in the annual Forecast Plans (Programs) for Privatization, could not in reality be sold, because they were on the List of strategic enterprises and joint-stock companies, or had been placed as the RF's contribution into the charter capitals of integrated structures, or were carrying out no economic operations, or were involved in bankruptcy or liquidation procedures, or there were some discrepancies in their documentation, or no proper documentation had been submitted, etc. Blocks of shares in another 300 JSCs (each year) were not offered for sale for other reasons, although there were none of the aforesaid impediments to privatization.

1.2. The Development of the Normative-Legal Base and the Actual Practice of Mixed Property Management in the Corporate Sector in the 2000

The period following the adoption of the Concept was highlighted by the approval of a number of very important documents aiming at the practical implementation of a new set of instruments for regulating the relations between the State and the economic societies with state stakes in their capital. There were two main directions for such activity 1) regulation of the activity of the State's representatives in economic societies; 2) the formation of a normative field for the activity of economic societies proper.

1.2.1. The Development of the Normative-Legal Base in the Sphere of Managing Shares in Federal Ownership in the Period prior to the Approval of the Third Law on Privatization (1999–2001)

The first and long-awaited steps in this direction were Decrees of the RF Government No. 1116 of 4 October 1999 and No 195 of 7 March 2000.

In accordance with the first of the aforesaid documents, adopted within the framework of the Concept's implementation, new model forms were introduced for reporting to be submitted by the RF's representatives

in an OJSC (twice in a year)²⁵. These reports should contain standardized information concerning an enterprise's profits and losses, dividends, its payables and receivables, rate of return (including the indices of liquidity, financial stability, business activity, the value of shares and net assets, and in kind settlements); the targeted use of profit, by area of activity; the presence of the indicia of bankruptcy; and account of the participation in the meetings of shareholders and the board of directors. Besides, an annual report on the OJSCs' financial and economic activity was to be submitted to the superior state administration bodies concerning issues like the distribution of share capital, various aspects of its activity, remuneration of the personnel, including the director general's salary, and the interaction with commercial structures and foreign investors.

The second document approved the Provision on the procedure for the appointment and activity of the representatives of the Russian Federation in the administrative bodies and audit boards of open-end joint-stock companies created as part of the process of privatization, whose shares are federal property, as well as those in respect of which the decision was made to apply the special right of the Russian Federation's participation in their management ("golden share"). It contains the classification of state representatives in an OJSC (these can be civil servants, members of the staff of the Russian Federal Property Fund (RFPF) or of its territorial agencies, and other citizens acting on the basis of contracts concerning the representation of the interests of the State), their duties and terms for the termination of their powers. For the first time the procedure for the interaction between the representatives of the State and the RF Ministry of State Property and branch administrative agencies was subject to detailed regulation, depending on the size of a state stake, with the determination of the timelines for notification, the submitting of proposals, coordination, issue of written directives, and the submitting of reports concerning the participation in the activity of an enterprise's administrative bodies. It was also determined that only civil servants could be represen-

²⁵ By way of implementing this Decree, by Order of the RF Ministry of State Property Management of 11 November 1999, No. 1506-r, the methodological guidelines were approved for the procedure of filling-in the reporting forms for representatives of the Russian Federation in the administrative bodies of open-end joint-stock companies.

tatives of the State in the administrative bodies and audit boards of the joint-stock companies in respect of which it was decided that the special right should be applied (“golden share”), while certain decisions concerning personnel matters in respect of 167 OJSCs (a group of biggest and the most important enterprises) were the exclusive prerogative of the RF Government. These included the 32 companies where a certain block of shares was held by the RFPPF, and in 3 it was the sole possessor of the state stake²⁶.

Another direction for improving the system for managing state stakes (or shares, or contributions) in economic societies was the creation of an appropriate mechanism for ensuring proper control over the activity of such companies. It is evident that the first step on the way toward creating such a mechanism should be the collection of information concerning their activity and its analysis. Therefore, a very important measure was the creation of the Register of indices of the economic performance of OJSCs with state participation in their capital, based on branch and territorial databases and envisaged by Decree of the RF Government of 11 January 2000, No. 23²⁷. Beside the approval of the procedure for reports to be submitted by the state representatives in OJSCs, this has opened up opportunities for the implementation of a wide range of administrative decisions made by the State regarding those joint-stock companies where it participates in capital; the most natural decision would be to receive dividends, which, in their turn, are generated by the profits resulting from the achievement of a certain performance level in a company’s current economic activity. Quite logically, the next milestone in implementing the Concept for the Management of State Property and Privatization became Decree of the RF Government of 3 February 2000, No. 104. This document envisaged that, for OJSC with a federal stake of more than 50%, similarly to federal state unitary enterprises (FSUE), the indices of

²⁶ Muraviov A. Gosudarstvennye pakety aktsii v rossiiskikh kompaniiakh: proiskhozhdenie, tipy i vliianie na resul'taty deiatel'nosti. Analiticheskii doklad. [State-owned blocks of shares in Russian companies: origins, types and influence on the results of activity. An analytical report.]. M., RCER, 2003, p. 23.

²⁷ By order of the RF Ministry for Property Relations, the Methodological recommendations for the organization and conduct of an analysis of the performance of those FSUEs and CJSCs whose shares are federal property, of 10 July 2000, No. 183-r, were approved.

economic performance should be approved on an annual basis, with appropriate control over the compliance with these indices and the use of property; and the size of dividends should be determined, to be recommended for voting by the RF representatives in the administrative bodies of those enterprises.

By way of executing this RF Government's decree, on 18 September 2001 a joint order of the RF Ministry of Economic Development and Trade, the RF Ministry of State Property and the RF Ministry for Taxes and Levies, whereby the list and procedure for determining the economic performance indices for unitary enterprises and open-end joint-stock companies with federal stakes was approved (registered by the RF Ministry of Justice on 19 November 2001, No. 3043). There existed, in fact, practically no difference between the indices to be established and controlled for FSUEs and for the JSCs with federal blocks of shares. These indices are as follows: 1) proceeds (net) from sales of goods, products, work, services (less the value added tax, excises and other mandatory payments); 2) net profit; 3) the part of net profit earmarked for the payment of dividends on the state block of shares (or the part of profit of unitary enterprises transferable to the federal budget); 4) net assets. Thus it became possible for the RF Ministry of State Property to begin the actual work of compiling the register of economic performance indices for unitary enterprises and open-end joint-stock companies with federal stakes in their capital.

By order of the RF Ministry of State Property of 16 November 2000, No. 1024-r, it was envisaged that the written directives for the State's representatives in joint-stock companies should, as a mandatory provision, address the voting, by their administrative bodies, on the issue of transfer of the responsibilities of keeping the registers of shareholders in the enterprises with state stakes to the empowered registrars at the Ministry. Shortly before the approval of the Concept for the Management of State Property and Privatization, by order issued by the RF Ministry of State Property as of 7 September 1999, No. 1249-r, the provision concerning tenders, by the results of which the selection of appropriate companies to act as empowered registrars was to be done, and the model agreement concerning the granting of such a status were approved.

And finally, by Order of the RF Ministry of State Property of 26 November 2001, No. 260, “On the Rules of Procedure for the exercise of the shareholder rights of the Russian Federation”, the procedure for implementing the basic measures designed to ensure the exercise of the Russian Federation’s shareholder rights was approved, which for the first time determined the step-by-step actions of the Ministry’s specialists while preparing and implementing the fundamental administrative decisions concerning OJSCs, including the procedure for preparing to shareholder meetings and ensuring the participation in these meetings of the State’s representatives, the procedure for forecasting the results of the companies’ operation and for the control over proper implementation of the decisions made by shareholder meetings, including those concerning the fulfillment of the annual assignment for the income from dividends.

In addition to general provisions and the schemes to be applied to all those joint-stock companies where the Russian Federation holds voting shares, the Rules of Procedure has 5 appendices, each of which contains different lists of joint-stock companies, with emphasized regulating norms (*Table 21*).

Table 21

The Structure and Content of the Appendices to the Rules of Procedure for the Exercise of the Shareholder Rights of the Russian Federation in 2001

Area of regulation	No. of Appendix	Regulating norms
Procedure for the placement, by the RF, of specific issues on the agendas of annual shareholder meetings, and for the appointment of candidates to companies’	1	1) The candidacies of directors general and members of audit boards must be coordinated with the RF Government only. 2) In the schedules for the dispatching to companies of letters concerning the issues to be placed on the agenda and the candidacies approved by Deputy Ministers, in addition to the dates on which the letters to companies should be dispatched, the dates on which proposals should be submitted to the RF Ministry of Property Relations (hereinafter – the Ministry) and to the RF Government must also be specified ²⁸ .

²⁸ Within the framework of a large-scale reorganization of the RF Government, in the spring of 2004 the functions of the RF Ministry for Federal property Management were transferred to the Federal Agency for Federal Property Management (FAFPM).”

Area of regulation	No. of Appendix	Regulating norms
administrative and controlling bodies (Article 2)	2	<p>1) The candidacies for the membership in the boards of directors must be coordinated with the RF Government only.</p> <p>2) In the schedules for the dispatching to companies of letters concerning the issues to be placed on the agenda and the candidacies approved by Deputy Ministers, in addition to the dates on which the letters to companies should be dispatched, the dates on which proposals should be submitted to the Ministry and the RF Government</p>
The procedure for the initiation, by the RF, of extraordinary shareholder meetings and the appointment of candidates from the RF to companies' administrative and controlling bodies (Article 4)	3	<p>1) The candidacies for the membership in the boards of directors must be coordinated both with the RF Government and the RF President's Administration.</p> <p>2) In the schedules for the dispatching to companies of letters concerning the issues to be placed on the agenda and the candidacies approved by Deputy Ministers, in addition to the dates on which the letters to companies should be dispatched, the dates on which the letters should be dispatched to the RF President's Administration and the RF Government.</p> <p>3) The letter to the RF Government must contain a copy of the coordination with the RF President's Administration of candidacies for the membership in the board of directors</p>
Procedure for ensuring participation representatives RF in shareholder meetings (Article 5)	1-3	<p>For the appointment of the candidacies of members in the board of directors, audit boards and directors general, the coordination with the RF Government and (or) the RF President's Administration is necessary (in addition to the opinions of the federal bodies of executive authority, to which the coordination and regulation in the corresponding branches is delegated (hereinafter – federal authorities), and of the bodies of executive authority of those RF subjects on whose territory the companies are located)</p>
Procedure for ensuring participation representatives RF in shareholder meetings (Article 5)	2	<p>The Ministry's power of attorney for voting at shareholder meetings is issued on the basis of separate decisions of the RF Government concerning the appointment of representatives. The drafts of such decisions are dispatched by the Ministry to the RF Government, as a rule, within five days from the moment of setting the date of a shareholder meeting, but no later than 10 days before the date of the meeting.</p> <p>The Ministry's power of attorney for voting at a shareholder meeting is issued on the day of the decision being made by the RF Government, on condition that it has been made less than 5 days before the date of the shareholder meeting</p>

Area of regulation	No. of Appendix	Regulating norms
The procedure for ensuring the participation of the RF in shareholder meetings in the form of absentee voting (Article 6)	3	<p>1) If the agenda of a shareholder meeting contains the issue concerning the election of a director general, simultaneously with the RF Government's draft directives, the Ministry's letter is dispatched to the RF President's Administration with proposals as to the procedure of voting on this issue, with the special mention of the fact that in this case the directives are to be approved by the RF Government.</p> <p>2) The Ministry's directives to the RF representatives concerning the issue of election of companies' directors general must be coordinated with the RF Government and the RF President's Administration. The draft directives are to be dispatched 15 days prior to the date of a meeting to the RF Government and the RF President's Administration. To the draft directives the candidate's personal data form is attached, and in the event of his or her secondary appointments – the information concerning his of her activity in the capacity of a company's director general during a previous period, a brief substantiation of the selection of that particular candidate, the date of a shareholder meeting, as well as the number of the voting shares in the company held by the RF.</p> <p>In instances when one week prior to the date of a shareholder meeting no document of coordination with the RF Government and (or) the RF President's Administration is received, the Ministry's directives concerning the election of a director general are issued on the day of arrival to the Ministry of the document of coordination with the RF Government and the RF President's Administration – separately from the Ministry's directives concerning other issues</p>
	4	The voting procedure is approved on the basis of the RF Government's directives.
	3	No absentee voting by the Ministry is allowed at extraordinary shareholder meetings convened on the Ministry's demand or directly by the Ministry, on condition that the selected form of conducting such a meeting envisages, alongside personal participation, also absentee voting
The procedure for annual forecasts of the results of a company's operation in the forthcoming year (Article 8)	5	<p>1) The economic performance indices submitted by federal authorities are submitted by the Ministry's branch structural subdivisions, within a three-day period, to its structural subdivision responsible for the monitoring of the financial status of enterprises and JSCs, which considers these indices with due regard for some specific materials*.</p> <p>2) In an event of disagreement with the federal authorities concerning the results of meetings, Deputy Ministers, in coordination with First Deputy Minister, adopt final decisions on eliminating thereof, on the basis of which they approve the economic performance indices for companies.</p> <p>3) The Ministry's structural subdivisions every year should ensure that before 1 April letters should be dispatched to companies with requests that a certain number of documents should be submitted before 1 June to the federal authorities and the Ministry **</p>
	5	1) Every year before 15 April, on the basis of the proposals submitted before 1 March by the federal authorities, a forecast of dividend pay-

Area of regulation	No. of Appendix	Regulating norms
proposals concerning dividend revenues, to be included in the RF draft budget for the next year (Article 9)		<p>ments in the next year is developed. The forecasted dividend indices are specified by federal authorities separately for each of the companies listed in Appendix 5.</p> <p>2) In an event of comments concerning the size of dividends to be paid by the individual companies listed in Appendix 5, the Ministry's branch structural subdivisions should make inquiries as to the point of view of the federal authorities. If fundamental disagreements are discovered, the responsible Deputy Ministers are notified within one day. Later on, the branch structural subdivisions should be guided by their instructions. In such cases, final decisions are made by the responsible Deputy Ministers in coordination with First Deputy Minister</p>
The procedure for preparing to the fulfillment of the assignment as to the revenues from dividends, as envisaged in the RF budget (Article 10)	5	<p>1) Every year before 1 December, on the basis of the proposals submitted before 1 November by the federal authorities, a forecast of dividend payments in the next year is made more precise. The forecasted dividend indices are specified separately for each of the companies listed in Appendix 5.</p> <p>2) On the basis of the considered proposals of the federal authorities, the Ministry's branch structural subdivisions compile adjusted forecasts of dividend payments for the next year and before 20 November submit them to the Ministry's structural subdivisions responsible for the monitoring of the financial status of enterprises and JSCs. The forecasted dividend indices are specified separately for each of the companies listed in Appendix 5</p>
The procedure for preparing to the fulfillment of the assignment as to the revenues from dividends, as envisaged in the RF budget for a current year (Article 11)	5	<p>1) Every year before 1 March, on the basis of the proposals submitted before 1 February by the federal authorities, Deputy Ministers approve, for each branch, plans – schedules for the receipts of dividends in a current year and dispatch them to federal authorities.</p> <p>2) In an event of comments arising in respect of the payment of dividends by individual companies listed in Appendix 5, the provisions to be applied in situations when comments arise as to the size of dividends to be paid by individual companies at the stage of preparing a forecast of annual dividend payments should be applied</p>

* – 1) forms 1–5, approved by order of the RF Ministry of Finance “On the forms of accounting reports of organizations” of 13 January 2000, No. 4n (for the last three years), with the decoding of individual accounts and rows (accounts 26, 58, 73, 84, 99; row 480), and in the presence of affiliated companies – also the group's annual consolidated balance sheets (for the last three years); 2) planned performance indices for a current year, including the size of net profit; 3) forecasts of financial-economic development for the next year (forecast of incomes from the main types of activity, forecast of expenditures, including the already assigned investment projects, with the estimation of their rate of return and period of recoupment, the description of sources of financing, and the expected annual net profit), with substantiating materials attached; 4) the medium-term goals of the management of blocks of shares in the companies (to be developed by the federal authorities and coordinated by the Ministry); 5) a forecast of Russia's national economy's social-economic development on the whole, and that of its corresponding branches, in the medium term.

** – 1) forms 1–5, approved by order of the RF Ministry of Finance “On the forms of accounting reports of organizations” of 13 January 2000, No. 4n (for the last three years), with the decoding of individual accounts and rows (accounts 26, 58, 73, 84, 99; row 480), and in the presence of affiliated companies – also the group’s annual consolidated balance sheets (for the last three years); 2) planned performance indices for a current year, including the size of net profit; 3) forecasts of financial-economic development for the next year (forecast of incomes from the main types of activity, forecast of expenditures, including the already assigned investment projects, with the estimation of their rate of return and period of recoupment, the description of sources of financing, and the expected annual net profit), with substantiating materials attached.

Source: Upravlenie gosudarstvennoi sobstvennost’iu. [Management of state property.] Ed. by Dr. Ec. Sci. V. I. Koshkin, An expanded and revised edition. – M.: EK MOS, 2002, p. 206–226.

Since these Appendices attached to the Rules of Procedure have not been published, an interesting question arises – to which no answer has been provided so far – as to how identical are the lists of OJSCs that they contain.

1.2.2. The Development of the Normative-Legal Base in the Sphere of Managing Shares, which are Federal Property, in the Period after the Adoption of the Third Law on Privatization (2002–2003)

Of paramount importance for the determination of the mechanisms for managing companies with state stakes in their capital was the coming into force of the new (the third since the onset of market-oriented reforms) law – Federal Law of 21 December 2001. “On privatization of state and municipal property” (No. 178 FZ).

The negotiated condition for the approval of this draft law by the RF Federal Assembly (FA) became the creation of a multi-tier decision-making system for dealing with the issues of privatization of objects belonging to various categories.

By Article 6 of this Law it is established that, for purposes of implementing a single state policy in the sphere of privatization, the RF Government should submit, for the approval by the RF President, proposals concerning the formation of the list of strategic enterprises and joint-stock companies which, in addition to those FSUEs that produce goods (or work, or services) of strategic importance for ensuring the defense capability and security of the State and protecting the morals, health,

rights and lawful interests of RF citizens (hereinafter – strategic enterprises), must also include those open-end joint-stock companies (OJSC) whose shares are federal property, and the State’s participation in their management protects its strategic interests, defense capability and security, and ensures the protection of the morals, health, rights and lawful interests of RF citizens (hereinafter – strategic joint-stock companies)²⁹.

Similarly, proposals should be submitted to the RF President concerning the introduction of changes into the list of strategic enterprises and strategic joint-stock companies for certain FSUEs to be taken off the list of strategic enterprises, including for their subsequent privatization (transformation into OJSCs), as well as the necessity for the RF to participate in the capital of OJSCs belonging to the category of strategic joint-stock companies and the degree of this participation, including for the subsequent privatization of shares in those joint-stock companies. After the RF President makes the decision concerning the diminishment of the State’s participation in the management of strategic joint-stock companies or concerning the exclusion of certain enterprises from the category of strategic enterprises, such objects may be included in the Forecast Plan (Program) for Federal Property Privatization. It was assigned to the RF Government to submit for the RF President’s approval, before 1 March 2002, the lists of strategic enterprises and strategic joint-stock companies.

Besides, it is necessary to note that the regulation of property relations in the sector of natural monopolies of national importance (the RJSC “UES of Russia”, the RJSC “Gazprom”, federal unitary enterprises in the railway transport sector) has been placed with parliament’s jurisdiction (a law should be passed for their privatization and the sale of shares therein to be effectuated) (Article 7). The decision-making concerning the priva-

²⁹ Previously, such enterprises were usually regarded as those included in one of the lists approved by Decree of the RF Government of 12 July 1996, No. 802, “On the list of enterprises and organization of the defense complex whose privatization is banned”, and of 17 July 1998, No. 784, “On the list of joint-stock companies producing products (goods, services) of strategic importance for the State’s national defense, whose blocks of shares consolidated in federal ownership cannot be subject to early sale” (in numerous later rewordings. However, no criteria for including (or taking off) enterprises in some or other list were offered.

tization of other objects of federal property, including blocks of shares, had been placed within the RF Government's jurisdiction, which must on its own, on an annual basis, approve the Forecast Plan (Program) for Property Privatization.

An important new point contained in the third law on privatization has become the equalization of preference shares of type B, held by property funds, with ordinary shares, thereby granting to the Russian Federation, RF subjects and municipal formations all the legislatively established rights of the holder of ordinary shares. The constituent documents of previously created open-end joint-stock companies, which contained the provision concerning the preference shares of B type, were to be brought in conformity with the norms established by the Law. Thus, the State (regions, municipalities) were granted additional opportunities for influencing those OJSCs where the former held a certain stake. Regretfully, however, it is impossible to perform a quantitative estimation of the addition of this category of blocks of voting shares.

The format of the special "golden share" right remained, on the whole, the same as established in the previous law adopted in 1997, with one exception, namely that the rights of state representatives (1) to receive from the holder of the register of securities issued by an open-end joint-stock company the information concerning the name (or designation) of the holders of that OJSC's securities registered in the aforesaid register of owners of securities, the number of those securities, their category (or type) and face value, and (2) to bring a suit in a court of justice against a member of the board of directors (or supervisory board) of an open-end joint-stock companies, its single executive body (director or director general), a member of a collegial executive body (board, directorate), or its managing organization (manager) for the compensation of losses in accordance with Item 2 of Article 71 of Federal Law "On joint-stock companies", were no longer mentioned in the law's text. There also appeared a direct reference to the right of the bodies of authority that had delegated a state representative to the administrative body of a OJSC to replace this representative by another person.

After the adoption of the new law on privatization, which came into force from 26 April 2002, additional innovations were also introduced into the process of managing state-owned blocks of shares.

By Decree of the Government RF of 23 January 2003, No. 44, the Provision on the procedure for managing federal property – the shares in open-end joint-stock companies, and the exercise of the Russian Federation’s special right to participate in the administration of open-end joint-stock companies (“golden share”) was approved³⁰.

In the text of this document two lists of joint-stock companies were mentioned. The first one was *a special list of individual joint-stock companies, to be approved by the RF Government*, for which the State’s position as a shareholder was to be determined by decision of the Government itself, by its Chairman or, on the Chairman’s assignation, by the Deputy Chairman of the RF Government in respect of the following issues:

- placing certain issues on the agenda of a general shareholder meeting and the appointment of candidates to be elected to the administrative bodies, the auditing commission the counting commission of a joint-stock company;
- putting forth the demand that an extraordinary general shareholder meeting be convened, and the convening of an extraordinary general shareholder meeting;
- voting on the issues placed on the agenda of a general shareholder meeting and the appointment of a representative for voting at a general shareholder meeting.

In addition to this list, the Decree mentions a *special list of joint-stock companies, to be approved by the RF Government, based on the estimation of the basic financial and economic indices of these joint-stock companies, including the volume of their proceeds, the value of fixed assets,*

³⁰ It replaced Decree of the Government of the Russian Federation of 7 March 2000, No. 19, “On the procedure for the appointment and the activity of representatives of the Russian Federation in the administrative bodies and auditing commissions of open-end joint-stock companies created during the process of privatization, whose shares are federal property, and in respect of which the decision was made that the special right of the Russian Federation’s participation in their management (“golden share”) should be applied.

*balance-sheet profit for a reporting period, their share on the market of commodities (or services) of strategic importance for ensuring the defense capability and security of the State, and other economic indices*³¹. It was envisaged that the RF Ministry of State Property, in coordination with the federal bodies of executive authority and the RFPPF, should submit to the RF Government RF proposals concerning the introduction of changes and amendments to this list.

On the same day, by Order of the RF Government of 23 January 2003, No. 91-р, two lists of OJSCs whose shares are federal property were determined, thereby making more precise the special list mentioned in Decree No. 44:

- those open-end joint-stock companies, in respect of which the stand-points of the Russian Federation as a shareholder were determined regarding the issues of appointing a representative for voting at a general shareholder meeting; placing issues on the agenda of a general shareholder meeting, appointing candidates to be elected to administrative bodies, an auditing commission and a counting commission; putting forth the demand that an extraordinary general shareholder meeting be convened; the convening of an extraordinary general shareholder meeting; voting on issues placed on the agenda of a general shareholder meeting; and the coordination of the directives issued for the representatives of the Russian Federation and the representatives of the interests of the Russian Federation in boards of directors (or in supervisory boards) were to be executed by the Government of the Russian Federation, the Chairman of the Government of the Russian Federation, or on the latter's assignation, by the Deputy Chairman of the Government of the Russian Federation (18 companies);
- those open-end joint-stock companies, in respect of which the stand-points of the Russian Federation as a shareholder were determined

³¹ In this connection it still remains unclear how exactly this list, in addition to all the others, mentioned in the RF Government's Decree of 23 January 2003 should be coordinated with the list of strategic joint-stock companies, which in accordance with the 2001 Law on Privatization was to be approved by the RF President, which happened only in August 2004.

regarding the issues of appointing candidates to be elected to administrative bodies, an auditing commission and a counting commission; voting at general shareholder meetings on issues relating to the formation of these bodies; and the coordination of the directives issued for the representatives of the Russian Federation and the representatives of the interests of the Russian Federation in boards of directors (or in supervisory boards) concerning the voting at the meetings of boards of directors (or supervisory boards) on issues relating to the formation of executive bodies and the election (or reelection) of the chairpersons of boards of directors (or supervisory boards) were to be executed by the Government of the Russian Federation, the Chairman of the Government of the Russian Federation, or on the latter's assignment, by Deputy Chairman of the Government of the Russian Federation (48 companies).

The personal candidacies of the State's representatives at the administrative bodies of major companies were approved by Orders of the RF Government of 29 January 2004, No. 126-r (43 companies) and of 30 January 2004, No. 127-r (21 companies). The RF Ministry of State Property's press service on 3 February 2004³² released the information concerning the appointment, by the State, of the candidates to the boards of directors (or supervisory boards) and auditing commissions of 43 Russian companies with state participation:

- the CJSC "ALROSA", the OJSC "IL'iushin Finans Co", the OJSC "KamAZ", the OJSC "Finansovaia lizingovaiia kompaniia" ["Financial Leasing Company"] (from the first list);
- the OJSC "Arsen'evskaia aviatsionnaia kompania "Progress" im. N. I. Sazykina" [N. I. Sazykin Arseniev Aviation Company "Progress"], the OJSC "Viatsko – Polianskii mashinostroitel'nyi zavod 'Molot'" [Viatka - Poliansk Machine – Building Plant 'Molot'], the OJSC "Kovrov elektromekhanicheskii zavod" [Kovrov Electrical Mechanical Plant], the OJSC "Krasnogorskii zavod im. S. A. Zvereva" [S. A. Zverev Krasnogorsk Plant], the OJSC "Mezhgosudarstvennaia aktsionernaia korporatsia 'Vympel'" [Interstate Joint-Stock Corpora-

³² www.rosim.ru.

tion ‘Vympel’”, the OJSC “Cheboksarskoe nauchno-proizvodstvennoe pribirostroitel’noe predpriiatie ‘ELARA’” [Cheboksary Research-and-Development Equipment-Building Enterprise ‘ELARA’], the OJSC “Pribaltiiskii sudostroitel’nyi zavod “Yantar’” [“Baltic Shipbuilding Plant “Yantar’”], the OJSC “Amurskii sudostroitel’nyi zavod’ [“Amur Shipbuilding Plant], the OJSC “Irkutskenergo”, the OJSC Nauchno – tekhnicheskaiia kompania “Rossiiskii mezhotraslevoi nauchno-tekhnicheskii kompleks “Nefteotdacha” [Scientific and Technological Company ‘Russian Interbranch Scientific and Technological Complex “Nefteotdacha”, the OJSC “Mezhgosudarstvennaia aviastroitel’naia kompania ‘Il’iushin’” [“Interstate Aircraft-Building Company ‘Il’iushin’”], the OJSC “Korporatsia ‘Aerokosmicheskoe oborudovanie’” [“Aerospace Equipment”], the OJSC Moskovskii vertoliotnyi zavod im. M. L. Milia” [“M. L. Mil’ Moscow Helicopter Plant”], the OJSC “Tupolev”, the OJSC “Aviadvigatel’” [“Aircraft Engine”], the OJSC “Ulan-Udenskii aviatsionnyi zavod” [“Ulan-Ude Aircraft Plant”], the OJSC “NPO Energomash imeni akademika V. P. Glushko” [Academician V. P. Glushko Scientific and Technological Amalgamation ‘Energomash’], the OJSC ‘Nauchno-proizvodstvennoe ob’edinenie “Saturn” [Research-and-Development ob’edinenie “Saturn”], the OJSC “Avto-dizel” (Yaroslavl Engine Plant), the OJSC “Moskvich”, the OJSC “Tverskoi vagonostroitel’nyi zavod” [Tver Carriage-Building Plant”], the OJSC “Motorostroitel’”(Samara), the OJSC “Khimprom” (Volograd), the OJSC “Kol’chuginskii zavod po obrabotke tsvetnykh metallov imeni S. Ordzhonikidze” [“S. Ordzhonikidze Kol’chuginskii Plant for Processing Non-Ferrous Metals”], the OJSC “Novorossiiskii kombinat khleboproduktov” [“Novorossiisk Baking Combine”], the OJSC “Novorossiiskoe morskoe parokhodstvo” [“Novorossiisk Sea Steamship-Line”] (Novoship), the OJSC “Murmanskoe morskoe parokhodstvo” [“Murmansk Sea Steamship-Line”], the OJSC “Yeniseiskoe rechnoe parokhodstv” [“Yenisei River Steamship-Line”], the OJSC “Sudokhodnaia kompania ‘Volzhskoe parokhodstvo’” [“Shipping Company “Volga Steamship-Line”] (Volga-Flot), the OJSC “Novorossiiskii morskoi torgovyi port” [“Novorossiisk Sea Trading

Port”], the OJSC “Murmanskii morskoi torgovyi port” [“Murmansk Sea Trading Port”], the OJSC “Tuapsinskii morskoi torgovyi port” [“Tuapse Sea Trading Port”], the OJSC “Aviakompania ‘Krasnoyarskie avialinii’” [“Krasnoyarsk Airlines”] (“Krasair”), the OJSC “Aviakompania ‘Domodedovskie avialinii’” [“Domodedovo Airlines”], the OJSC “Airport Kol’tsovo”, the OJSC “Rosagrolizing”, the OJSC “Rosgosstrakh”, the OJSC “Rossel’khozbank”, the OJSC Rossiiskii bank razvitiia’ [“Russian Bank for Development”] (from the second list).

In addition to the companies mentioned above, the first list also contained the airline “Aeroflot – Rossiiskie avialinii” [“Aeroflot – Russian Airlines”], the Agency for Mortgage Crediting, the Joint-Stock Company for Pipeline Transportation of Petroleum Products “Transnefteprodukt”, the Joint-Stock Company for the Transportation of Petroleum Products “Transneft”, Vneshtorgbank, “Gazprom”, Izhevsk Machine-Building Plant, the International Airport “Sheremetevo”, the oil company “Rosneft”, the S. P. Korolev Airspace Corporation “Energia”, the RJSC “UES of Russia”, Sviazinvest, “Modern Commercial Fleet” (“Sovkomflot”), and TVEL. To the second list also belonged “Aviatsionnaia kholdingovaia kompania “Sukhoi” [Aviation Holding Company “Sukhoi” (AHC) [Concern PVO “Almaz – Antei”], the Corporation “Takticheskoe raketnoe vooruzhenie” [“Tactical Missile Weapons”], “Rossiiskaia Elektronika” [“Russian Electronics”], “Lenzoloto”, “Tehksnabeksport”, “Cherepovetskii Azot” [“Cherepovets Nitrogen”], “Airport Vnukovo”, “Pervyi kanal” [“First Channel”].

Later on, the content of both these lists was repeatedly changed. First, in December 2003, “Airport Vnukovo” was taken off the second list of OJSCs³³. In January 2004, the first list of OJSCs was augmented by another 9 companies, and from the second list 8 companies were excluded, 6 out of these 8 OJSCs (“Tehksnabeksport”, “Aviatsionnaia kholdingovaia kompania “Sukhoi”, Concern PVO “Almaz – Antei”, the Corporation “Takticheskoe raketnoe vooruzhenie”, “Rossiiskaia Elektronika”,

³³ The State’s stake (more than 60% of capital) was transferred to the City of Moscow.

and “Pervyi kanal”)³⁴ later being added to the first list alongside the Russian Railways, the Corporation “Khimzachshita” and “Rosgazifikatsiia”.

By way of anticipating things, it should be noted that in September 2005 to the first list the OJSC “Rosneftegaz” was added, which had been created in order to carry out the transaction of increasing to a controlling size the federal stake in the OJSC “Gazprom”», and in 2006 – the OJSCs “Zarubezhnefl” and “Ob”edinennaia aviastroitel’naia korporatsiia” (OAK). Due to the creation of the latter and its inclusion into the first list, in April 2006 “IL’iushin Finans Co”, “Finansovaia lizingovaiia kompaniia” and the AHC “Sukhoi” were taken off that list. As a result, by early 2007 the first list consisted of 27 companies.

As for the second list, in 2005 the Scientific and Technological Company “Rossiiskii mezhotraslevoi nauchno-tekhnicheskii kompleks” [‘Russian Interbranch Scientific and Technological Complex “Nefteotdacha”], and in 2006, due to the creation of the OAK and the consolidation of the helicopter-building sector – “Mezhgosudarstvennaia aviastroitel’naia kompaniia ‘Il’iushin” [‘Interstate Aircraft-Building Company ‘Il’iushin”], the OJSC “Tupolev”, the OJSC Moskovskii vertoliotnyi zavod im. M. L. Milia” [“M. L. Mil’ Moscow Helicopter Plant”], and the OJSC “Ulan-Udenskii aviatsionnyi zavod” [“Ulan-Ude Aircraft Plant”] were taken off it. After the exclusion of a total of 14 aforesaid companies from the list, it was augmented by all the 4 companies (“SG – Trans”³⁵, “Vega” and “Elektromashina”³⁶, “Oboronprom”). Thus, by early 2007 the second list consisted of 38 companies.

1.2.3. The Practice of Corporate Governance in Companies with State Stakes in their Capital in the 2000s

The State’s opportunities as a shareholder, in terms of its participation in corporate governance, are generally determined by legislative norms and the size of its stake in a company’s capital.

³⁴ Only “Azot” in Cherepovets and “Lenzoloto” were finally excluded.

³⁵ The company’s sphere of activity is the transportation and sale of condensed gas.

³⁶ Integrated structures created in order to consolidate the enterprises belonging to defense industry.

As far as legislation is concerned, in accordance with the Russian Law “On joint-stock companies” the rights of and the opportunities for a shareholder depend on the size of that shareholder’s stake in charter capital.

Table 22

The Rights of Shareholders, Depending on their Shares in Paid-up Charter Capital

Participation “threshold”	Rights of shareholder
1 share	1) right of vote at a general shareholder meeting. 2) right to receive dividends on a given category of shares 3) right to receive part of property (or its adequate value) during a JSC’s liquidation. 4) right to demand buyout of shares on certain conditions. 5) right to appeal to a court of justice against decisions adopted by a general shareholder meeting. 6) right to get acquainted with the documents relating to the activity of a JSC, as envisaged in the law, with the exception of documents relating to accounting records and protocols of the meetings of the collegial executive body of a JSC. 7) right to obtain an extract from the register of a JSC. 8) right to obtain an extract from the list of persons granted the right to participate in a general shareholder meeting of a JSC
1%	1) right to get acquainted with the list of persons granted the right to participate in a general shareholder meeting of a JSC 2) right to appeal to a court of justice with a suit against a member of the board of directors, the single executive body, a member of the collegial executive body of a company, or to appeal to a managing organization or a manager concerning the compensation of losses inflicted by a JSC in instances envisaged by the law
2%	1) right to place issues on the agenda of an annual general shareholder meeting. 2) right to appoint a candidate to the board of directors, the auditing commission, the collegial executive body, or the counting commission of a JSC
10%	1) right to demand the convening of a general shareholder meeting of a JSC. 2) right to demand, at any time, of an audit of the financial-economic activity of a JSC.

Participation “threshold”	Rights of shareholder
25%+1 share	1) right to ban the decisions of a general shareholder meeting concerning the issues relating to the introduction of amendments to a company’s charter, or the approval of the charter in a revised version; the placement of shares (closed subscription; placement of ordinary shares through an open subscription, if more than 25 % of the previously placed ordinary shares is being placed; the placement, through an open subscription, of issued securities convertible into ordinary shares, amounting to more than 25 % of the previously placed ordinary shares); the reorganization and liquidation of a JSC; the appointment of a liquidation commission; the approval of liquidation balance sheets, the determination of the number, face value, category (or type) of declared shares and the rights granted by these shares; the acquisition by a company of placed shares in instances envisaged by the law; the approval of decisions concerning large-scale transactions (amounting to more than 50 % of the balance-sheet value of a company’s assets). 2) right to get acquainted with the documents relating to accounting records and the protocols of meetings of the collegial executive body of a JSC
30%+1 share	Right to conduct a general shareholder meeting convened for a second time (instead of the meeting that did not take place because of absence of quorum)
50%+1 share	1) right to conduct a a general shareholder meeting 2) right to make decisions at a general shareholder meeting (except on issues requiring a qualified majority)
75%+1 share	Full control over a JSC

As follows from *Table 22*, Russian legislation offers a rather substantial set of opportunities for shareholders to defend their interests in the course of executing corporate governance procedures. In this connection, it is noteworthy that small shareholders are also granted impressive opportunities, which, however, cannot always be realized in actual practice due to the existence of various obstacles.

From this point of view the State, in accordance with its status enjoying greater opportunities than those available to rank-and-file minority shareholders, is potentially capable of influencing the management of joint-stock company without necessarily being the holder of a controlling block of shares, although the stakes of this size usually were consolidated as state property in the course of privatization. If its representatives possess adequate will and motivation, the State can be capable of influencing the situation even when holding only residual blocks of shares, especially when capital is largely diffused among many shareholders. Special role in such a situation may be played by stakes of the size amounting to 25%

plus 1 share, which require the approval by a qualified majority (75%) of shareholders for certain decisions to be finalized, namely those concerning the issues of increasing charter capital, changing and amending a company's charter or approving a new version of its text, reorganizing and liquidating a company (including the appointment of a liquidation commission, and the approval of liquidation balance sheets), determining the format of declared shares, approving the acquisition by a company of shares being placed, and approving big transactions. Naturally, of great importance also are the presence or absence, within the structure of a company's capital, of other groups of shareholders beside the State, and the size of their blocks of shares.

While beginning the discussion of the issue of changing the size of the State's stake in charter capital, it should be borne in mind that the overall trend in the evolution of joint-stock property and the struggle for corporate control in the second half of the 1990s and early 2000s was that of growing capital concentration alongside the increasing shares held by various categories of external non-state owners (mainly Russian commercial non-financial enterprises and organizations). The principal donor responsible for such shifts in the structure of capital was the share belonging to rank-and-file employees and the State (including the local level).

As the residual - and sometimes specially consolidated blocks of shares - were gradually being sold, the type of an economic society with a state stake in its capital was becoming less widespread. According to the results of the sample surveys conducted by the Economic Conuncture Center (ECC) under the RF Government, in 2002 the State was shareholder in 24% of enterprises, whereas in 2000 - in 33%, holding a dominant stake in the capital of 7% and 9% enterprises, respectively³⁷. As demonstrated by the surveys of the SU - HSE, by the end of the year 2001 the bodies of state authority were represented in the capital of 19 % enterprises within a sample, against approximately 40% in 1995 and

³⁷ Dolgopiatova T.G. *Stanovlenie korporativnogo sektora i evolutsiia aktsionernoi sobstvennosti. [The corporate sector's consolidation and the evolution of joint-stock property]*. Preprint WP1/2003/03. Series WP1. *Institutsional'nye problemy rossiiskoi ekonomiki. [Institutional problems faced by the Russian economy]*. M., SU-HSE, 2003, pp. 21-22.

1998, no noticeable changes occurring during this latter 3-year period of the second half of the 1990s, when 94% of the enterprises, which in 1995 had state authorities among the participants in their capital, three years later once again specified this category of their shareholders. The overlap of the representation of federal and regional (or municipal) bodies of authority in the capacity of shareholders was negligent³⁸.

Later studies³⁹ demonstrated that companies with the participation of the State in their capital became no less common by comparison with 2001. During a survey covering 822 heads of JSCs in 8 branches of industry and in the communications sector (with the exception of postal services) conducted in the spring and summer of 2005 in 64 regions across Russia within the framework of a study addressing the issues of corporate governance and integration processes, implemented by the SU – HSE in cooperation with the Hitotsubashi University (Tokyo) in 2005–2007, it was demonstrated that, in a sample oriented to big companies with more than 100 employees, over 11% of JSCs had federal-level shareholders, and 7.6% – regional or municipal. In the sample produced by a survey covering 1002 enterprises in industry (only big and medium-size enterprise of the processing industries, without biggest companies with the number of employees over 10,000), conducted in the autumn of 2005 and the winter of 2006 within the framework of a joint project of the SU – HSE and the World Bank aimed at studying the competitive capacity of Russian businesses, there were approximately 10 % of JSCs (of the total number of respondents) with federal participation in their capital, and 8 % – with regional or local.

³⁸ Dolgopiatova T. G. *Otnosheniia sobstvennosti i modeli korporativnogo kontroliia v rossiiskoi promyshlennosti (po materialam empiricheskikh issledovanii)*. [Property relations and corporate control models in Russian industry (based on the materials of empirical studies)]. M., SU-HSE, 2000, p. 13.

³⁹ S. B. Avdasheva, T. G. Dolgopiatova, and X. Plines, “Korporativnoe upravleniie v AO s gosudarstvennym uchastiiem: rossiiskie problemy v kontekste mirovogo opyta”. [Corporate Governance in Joint-Stock Companies with State Participation: Russian Problems in the Context of Global Experience]. Preprint WP1/2007/01. Series WP1. Institutstional’nye problemy rossiiskoi ekonomiki. [Institutional problems faced by the Russian economy]. M., SU-HSE, 2007.

Nearly all the empirical studies (*Table 23*) have demonstrated that, on the whole, the State's participation in share capital, depending on the size of its stake, is of a minority character, this stake having been diminishing at least until 2002.

Table 23

**The Share of Bodies of Authority in the Structure of Share Capital,
as Shown by the Results of Empirical Studies, in %**

Source and period of data collection	Sample size, units	Bodies of authority (total number)	Federal bodies	Bodies of authority of RF subjects	Bodies of local self-government
<i>RF Goskomstat</i>					
1999*		18.5	10.4	7.3	0.8
2000*		12.6	6.7	5.0	0.9
2001*		13.5	6.6	5.1	1.8
2002*		17.7	9.9	6.8	1.0
1999**	790	9.5	4.7	3.4	1.4
2000 **		9.0	4.3	3.3	1.4
2001 **		7.8	3.2	3.3	2.5
2002 **		6.9	3.4	2.5	1.0
1999 **	290	11.1	6.4	3.4	1.3
2002 **		9.6	4.5	3.9	1.2
<i>SU-HSE (independent studies within the framework of individual projects)</i>					
end of 1995	277	9.7	5.1		4.6***
end of 1998	318/260****	8.4	4.6		3.8***
end of 2001	350/243****	8.7	3.3	3.5	1.9
spring-summer of 2005.	822	7.4	5.3		2.1***
<i>BEA</i>					
early 2000	437/350****	5.7	3.1		2.6***
<i>REB</i>					
early 2001	Regular surveys /150****	7.9	...	...	...

Source and period of data collection	Sample size, units	Bodies of authority (total number)	Federal bodies	Bodies of authority of RF subjects	Bodies of local self-government
<i>ISELS</i>					
early 2002	regular surveys	21+7*****	...	...	...
<i>IET</i>					
early 2003	283/255****	9,9	...	...	...

* – according to the results of annual total structural surveys conducted by the RF Goskomstat among 27,000 big and medium-sized industrial enterprises in the form of JSCs, LLCs, LPs (without small-sized businesses); this index reflects the structure of capital of bigger companies;

** – the results of estimations made by the authors of the book *Strukturnye izmeneniia v rossiiskoi promyshlennosti* [Structural changes in Russian industry], based on the results of a structural survey by the RF Goskomstat (with the number of JSCs in a sample specified);

*** – aggregate share held by the authorities of RF subjects and local self-government;

**** – in the denominator – the number of enterprises that provided answers to the question concerning the groups of shareholders;

***** – the sample contains only defense enterprises; 7% is the participation of other types of state enterprises.

Source: Dolgopiatova T. G. Otnosheniia sobstvennosti i modeli korporativnogo kontroliia v rossiiskoi promyshlennosti (po materialam empiricheskikh issledovani). [Property relations and corporate control models in Russian industry (based on the materials of empirical studies). M., SU-HSE, 2000, p. 42; Dolgopiatova T. G. Stanovleniie korporativnogo sektora i evolutsiia aktsionernoi sobstvennosti. {The corporate sector's consolidation and the evolution of joint-stock property}. Preprint WP1/2003/03. Series WP1. Institut-sional'nye problemy rossiiskoi ekonomiki. [Institutional problems faced by the Russian economy]. M., SU-HSE, 2003, pp. 19–23; Strukturnye izmeneniia v rossiiskoi promyshlennosti. [Structural changes in Russian industry]. M., SU-HSE, 2004, pp. 223–225; Ekonomika perekhodnogo perioda. [The economy in transition]. Ocherki ekonomicheskoi politiki postkommunisticheskoi Rossii 1998–2002. [Essays on the economic policy of postcommunist Russia in 1998–2002] M., IET, 2003, p. 364; S. B. Avdasheva, T. G. Dolgopiatova, and X. Plines, “Korporativnoe upravleniie v AO s gosudarstvennym uchastiiem: rossiiskie problemy v kontekste mirovogo opyta”. [Corporate Governance in Joint-Stock Companies with State Participation: Russian Problems in the Context of Global Experience]. Preprint WP1/2007/01. Series WP1. Institut-sional'nye problemy rossiiskoi ekonomiki. [Institutional Problems faced by the Russian economy]. M., SU-HSE, 2007, p. 36–37.

On the average, the share held by bodies of authority in share capital was slightly less than that held by the main categories of shareholders, with the exception of credit and financial institutions, not-for-profit organizations, and in the majority of cases – foreign investors, although the share of the latter was quite comparable to that of regional and local bodies of authority. Thus, among the 19 enterprises (13 OJSCs and 6 CJSCs) belonging to 6 branches of the processing industry and located in 5 regions (including Moscow), whose directors in the autumn of 1999 gave in-depth focused interviews within the framework of a project of the Bureau for Economic Analysis (BEA), only 3 had a state stake, while in the capital of the fourth one, another state enterprise (Metropoliten – the underground traffic system) was participant, simultaneously being the former's customer. The state stake was sufficiently big (44%) only in one enterprise, in order to ensure state corporate control through appointing an appropriate person to the post of its director. This was a big machine-building company which, while being involved in development works in the field of aircraft building, was preparing for becoming a part of an integrated structure with the participation of the State⁴⁰. And among 37 enterprises belonging to 4 branches and interviewed in 2003, the State was a dominant shareholder only in one machine-building enterprise⁴¹.

As shown by the data in *Table 23*, the following ratio between the sizes of shares belonging to different levels of public authority are typical. The average size of the share held by federal bodies of authority, is, as a rule, larger than that held by regional authorities, which, in its turn, is bigger than that held by bodies of local self-government, although there also exist some exceptions. Quite interesting is the question as to which level of public authority is more rapidly diminishing its stake in share capital.

⁴⁰ Dolgopiatova T. G. *Otnosheniia sobstvennosti i modeli korporativnogo kontroliia v rossiiskoi promyshlennosti (po materialam empiricheskikh issledovanii)*. [*Property relations and corporate control models in Russian industry (based on the materials of empirical studies)*]. M., SU-HSE, 2000, p. 45–49.

⁴¹ *Strukturnye izmeneniia v rossiiskoi promyshlennosti*. [Structural changes in Russian industry]. M., SU-HSE, 2004, pp. 226–231.

Thus, according to the overall indices generated by the RF Goskomstat, the stake held by federal bodies of authority decreased between 1999 and 2002 to the same degree as that of regional bodies (by 0.5 p.p.), while the stake held by bodies of local self-government increased by 0.2 p.p. However, such shifts are backed by the multidirectional trends characterizing this particular timespan. The share of federal bodies of authority, having reached its historic low in 2001 (6.6%), in the next year increased by 1.5 times – nearly to 10%, which produced the final result – rather similar to the initial value registered in 1999 (10.4%). The share of regional authorities was changing in accordance with a similar pattern. After the historic low of 2001 (approximately 5%) it grew to 6.8% in 2002 (against 7.3% in 1999). At the same time, the share of municipal authorities increased twofold by 2001 by comparison with 1999 – to 1.8%, while in the next year it went down to 1%.

According to the estimations published in *Strukturnye izmeneniia v rossiiskoi promyshlennosti [Structural changes in Russian industry]* and based on the results of a structural survey conducted by the RF Goskomstat in the period between 1999 and 2002, the stakes held by federal bodies of authority diminished more noticeably than those held by regional and municipal bodies, and in the sample of 290 JSCs the stakes held by regional bodies even increased – from 3.4% to 3.9%. The increasing share of regional and municipal bodies is also confirmed by the results of surveys conducted by SU-HSE, demonstrating that in 2001 the aggregate share of the local level of public authority (5.4%) was found to be higher than in 1998 (3.8%), while the share of federal bodies of authority decreased from 4.6% to 3.3%. In this connection it should be stressed that between 1995 and 1998 the stakes held by all levels of authority were decreasing (by 0.5 p.p. at the federal level, and by 0.8 p.p. – at the local level).

In principle, these data conform with the results obtained during the 2000 survey conducted by the BEA and demonstrating that regions and municipalities in the second half of 1990s were much more slowly withdrawing and were less inclined to reduce their presence in the capital of privatized enterprises than did the federal center (*Table 24*).

Table 24

**Reduction, at Different Levels of Authority, of the State's Stake
in the Capital of Industrial Enterprises in the Period
from the Moment of Privatization until the End of 1999, in p.p.**

Level of authority	Total	Only for JSCs with state stakes in capital
Federal bodies	– 4.4	– 30
Regional и municipal bodies	– 2.1	– 10

Source: Rossiiskaia promyshlennost': institutsional'noe razvitie. [Russian industry : institutional development.] Issue 1 / Ed. by T. G. Dolgopiatova, M., GU-HSE, 2002, p. 20, 26.

The results of the BEA's studies have shown that within 5–8 years, by early 2000, the shrinkage of the stakes held at the federal level of authority was twice as great as that at the local level, these stakes being understood as the aggregate regional and municipal shares, without any further specification of the latter (by 4.4 p.p. and 2.1 p.p.). Even more striking will be the differences in the privatization policies of different levels of authority when only those enterprises where these levels had a stake in capital are taken into consideration. In this case, the gap between the shrinkage indices is sometimes threefold – in favor of the federal authorities. Similar results were obtained by D. Earl and D. Brown during surveys conducted in 1999–2000 by the Stockholm School of Economics jointly with the RECEP⁴²: the share of federal bodies of authority decreased by 6.3 p.p. against the reduction by 3.3 p.p. in the share of local authorities in the period from mid-1994 to the end of 1998.

While there existed a general trend toward the shrinkage of the state stake (including that of municipalities) in share capital – at least until 2001–2002, if the whole body of the sample of enterprises is considered, somewhat different is the situation regarding the state representation within the group of only those enterprises where the bodies of authority of all levels were shareholders (*Table 25*).

⁴² The sample is based on the RLMS' sample, 430–480 respondents (Privatization and restructuring in Russia: evidence from panel data on industrial enterprises/ Report at the RES's Annual Conference in 2001).

Table 25

**The Stake of Bodies of Authority in the Structure of Share Capital
of those JSCs where they are Represented among
the Shareholders, in %**

Period	Federal bodies		Bodies of authority of RF subjects		Bodies of local self-government	
	stake, in %	number of JSC, units	stake, in %	number of JSC, units	stake, in %	number of JSC, units
end of 1995**	24.0	59	23.2*	55*	...	...
end of 1998**	23.1	56	21.7*	57*	...	...
As of 1 January 2000***	23.1		24.7*		...	...
end of 2001	35.9	22	52.9	16	36.6	13
1999****	37.7	48	41.8	23	38.0	10
2002****	36.0	37	45.6	25	33.7	10

* – aggregate index of the participation in capital of regional and municipal authorities;

** – based on the SU-HSE's survey of 1999;

*** – based on the BEA's survey of 2000;

**** – as estimated by the authors of the book *Strukturnye izmeneniia v rossiiskoi promyshlennosti* [Structural changes in Russian industry], based on the results of a structural survey by the RF Goskomstat (a sample of 290 JSCs).

Source: Dolgopiatova T. G. Otnosheniia sobstvennosti i modeli korporativnogo kontroliia v rossiiskoi promyshlennosti (po materialam empiricheskikh issledovani). [Property relations and corporate control models in Russian industry (based on the materials of empirical studies). M., SU-HSE, 2000, p. 43; Rossiiskaia promyshlennost': institutsional'noe razvitiie. [Russian industry : institutional development.] Issue 1 / Ed. by T. G. Dolgopiatova, M., GU-HSE, 2002, p. 26; Dolgopiatova T. G. Stanovleniie korporativnogo sektora i evolutsiia aktsionernoi sobstvennosti. [The corporate sector's consolidation and the evolution of joint-stock property]. Preprint WP1/2003/03. Series WP1. Institutsional'nye problemy rossiiskoi ekonomiki. [Institutional problems faced by the Russian economy]. M., SU-HSE, 2003, p. 20; Strukturnye izmeneniia v rossiiskoi promyshlennosti. [Structural changes in Russian industry]. M., SU-HSE, 2004, p. 225.

While the enterprises with state stakes were becoming less common, and the size of this stake in the structure of share capital was diminishing, on the whole it can be established that in the group of enterprises with state stakes in their capital the size of that stake was growing. According to the data for 1995 and for 1998, the average size of the blocks of shares

held by federal and local bodies of authority was under 25% – that is, less than the blocking size, having somewhat decreased in three years (by 1–1.5 p.p.). And by the end of 2001 the share of federal bodies (35.9%) had become almost by 1.5 times higher than by the end of 1998 (23.1%). No such comparison between the stakes held by regional and municipal bodies of authority is possible. Nevertheless, the fact of the stake of regional bodies becoming nearly as high as 53% is quite significant by itself. This index is higher than that of commercial organizations (except credit and financial institutions) and of the employees in the groups of enterprises where this category of shareholders is present in capital. As for the stake of municipal bodies, it was somewhat higher than that of federal bodies of authority.

Slightly different, but also rather close results were obtained by the authors of *Strukturnye izmeneniia v rossiiskoi promyshlennosti. [Structural changes in Russian industry.]*, whose estimations were based on the data yielded by the structural surveys of the RF Goskomstat in the period between 1999 and 2002 (a sample of 290 JSCs). The size of the stakes held by federal and municipal bodies in charter capital of JSCs in 2002 (33–36 %) was comparable to the aforesaid results relating to the end of 2001. Somewhat lower, although at the same time the biggest by comparison with those of the other levels of public authority was the stake held by regional bodies (less than 46%). One more distinctive feature was the share of municipal bodies (33.7%) being less than that of federal bodies of authority (36%). In face of a rather substantial reduction of the share of municipal bodies in the period between 1999 and 2002 (by 4.3 p.p.), the share of regional bodies demonstrated noticeable growth (by 3.8 p.p.). The share of federal bodies of authority during the same period diminished (by 1.7 p.p.), but to a lesser degree than that of municipal bodies.

These data are quite compatible with those presented in the table concerning the State's participation in capital across the whole sample, from which it follows that, while the share of federal bodies of authority between 1998 and 2001 continued to decline, the average aggregate share of regional and municipal bodies increased from 3.8% to 5.4%, becoming higher than the value of the same index in 1995. At the same time, it is necessary to note that the stakes in capital held by other types of state

enterprises (holdings, banks) are not cited separately. However, according to the surveys conducted by the Institute for Socio-Economic and Legal Sciences (ISELS) among the enterprise in the military sector only, in the six years between 1996 and 2002 the average stake held by other state enterprises increased by 6 p.p., while the direct participation of the State only by 1 p.p.

The structure of share capital of a company is reflected in the structure of its board of directors as a major administrative body. In order to estimate the changes in the representation of bodies of authority in boards of directors between 1998 and 2002, we are going to look at the results of empirical studies conducted by the SU – HSE, the somewhat different versions of which are cited in a variety of publications (*Table 26*).

Table 26

**The Share of Bodies of Authority in the Aggregate Composition
of a Board of Directors, in % of the Total Number
of the Board’s Members**

Period	Dolgopiatova T., Kuznetsov B. Faktory adaptatsii promyshlennykh predpriatii [Factors determining the adaptation of industrial enterprises] Doklad na IV Mezhdunarodnoi nauchnoi konferentsii GU-VShE “Modernizatsiia ekonomiki Rossii: sotsial’nyi kontekst” [Modernization of Russia’s economy: the social context], 2–4 April 2003		Strukturnye izmeneniia v rossiiskoi promyshlennosti [Structural changes in Russian industry]	
	Number of JSCs for which answers are obtained	% of total number of members in board of directors	Number of JSCs for which answers are obtained	% of total number of members in board of directors
As of end of 1998	273	5.2	278	5.1
As of beginning of 2002	289*	6.4*	294	6.7

* – 2001.

Alongside the diminishing sizes of the boards of directors (to less than 7 persons)⁴³ and the gradually diminishing insider representation, the most rapid growth was demonstrated by the representation of bodies of authority, which can be regarded as the consequence of the strengthening state control after 1999. Nevertheless, in purely quantitative terms the growth in the representation of bodies of authority was negligible, being both in 1998 and 2001–2002 less than that of the majority of other groups of shareholders (except for not-for-profit organizations and independent directors).

Although the role of bodies of authority in the structure of control has become more prominent, they remain, as before, the “discriminated” party when exercising their ownership rights through the universal internal mechanisms of corporate control.

Nevertheless, regional and local bodies of authority remain influential participants in corporate governance (or stakeholders), while federal bodies of authority – are the least important among all the participants in corporate governance. They, as well as banks not belonging to a holding, are in the same category as the other groups of participants, the interaction with which requires the least coordination of key decisions.

According to the survey covering 822 JSCs, with interviews of their directors taking place in the spring and summer of 2005, this situation was typical for nearly all the companies, except the biggest holdings with the number of employees in excess of 10,000, where the federal authorities, by the scope of their influence (35.1% of such JSCs coordinate their key decisions with them), have priority over the banks (25.4%), suppliers and consumers (27.2%) not belonging to a holding, being, nevertheless, behind regional authorities (51.3%). Approximately the same gap in the levels of influence between federal and regional authorities can be observed also in the holdings with the number of employees between 3,000 and 10,000 (16.1% against 23.5%). In the holdings with the number of employees below 3,000 and in autonomous enterprises the gap between federal and regional authorities is increasing: in the first of these groups the stakes of companies coordinating their decisions with federal and re-

⁴³ According to the results of empirical studies conducted in the late 1990s, an average board of directors consisted of 8 persons.

gional authorities amounted to 12.1% and 29%, respectively, for autonomous enterprises – to 9.6% and 22%, respectively. Thus, it can be stated that the influence of federal authorities directly correlates with the size of an enterprise, achieving its peak in very big holdings. The influence of regional authorities is also highest in the biggest holdings, but there is no direct relation to the size of an enterprise: the share of JSCs coordinating their decisions with them among the holdings with the number of employees between 3,000 and 10,000 (23.5%) is less than among the holdings with the number of employees below 3,000 (29%), being only slightly different from the same index for autonomous enterprises (22.7%). By the scale of their influence regional authorities are ahead not only of federal authorities, but also many other participants in corporate governance. Thus, in autonomous enterprises and holdings with the number of employees in excess of 10,000, regional authorities are second only to work collective; in holdings with the number of employees below 3,000 and between 3,000 and 10,000 – to work collective and the participants in a holding (the gap between the latter and regional authorities by the scale of influence is less than 1 p.p.)⁴⁴.

According to the afore-listed normative-legal acts, the general scheme of the State exercising its shareholder rights and powers in companies with the State's stake in capital, which has been in place in its present form since the late 1990s, should be as follows:

- the positions of state representatives in companies with the State's stake should be determined on the basis of coordinating the positions of branch ministries (or departments), and the RF Ministry of State Property (in certain instances, the RFPF), to be followed by the issuance of corresponding directives;

⁴⁴ Integratsionnye protsessy, korporativnoe upravleniie i menedzhment v rossiiskikh kompaniakh. [Integration processes, corporate governance and management in Russia companies] Series "Nauchnye doklady: nezavisimyi ekonomicheskii analiz. [Scientific reports: an independent economic analysis], No. 180. M., Moscow Public Science Foundation; ANO "Proekty dlia budushchego: nauchnye i obrazovatel'nye tekhnologii", 2006, p. 131.

- proposals regarding state representation in the boards of directors and auditing commissions should be annually dispatched to those economic societies in which the State is a shareholder (or participant);
- via its representatives, the State takes part in the process of decision-making (introduction, initiation of issues by the managerial bodies of such companies with regard to the major issues of their activity, including (1) the determination of the priority directions thereof, (2) the approval of annual and accounting reports, (3) the distribution of profit and the declaration (or payment) of dividends, and (4) the formation of the executive bodies of companies and the early discontinuation of their activity;
- the reports of the State's representatives provide the basis for a systemic monitoring of the financial and economic activity of such companies, for control over them and the supervision of the activity of state representatives.

In practice, the majority of branch ministries (departments) mismanaged their participation in the preparation of the directives to the State's representatives by violating the timelines for submitting the proposals on voting to the RF Ministry of State Property, which forced the latter, in order to eliminate the disagreements, to submit the draft directives on all issues to the RF Government, which increased the load on its apparatus and delayed the adoption of managerial decisions. The haste in the preparation of the directives results in the worsening of the quality of managerial decisions and makes it impossible to properly consider the specificity of individual companies.

Apart from this, it is possible to point to a number of other drawbacks in the activity of the institution of state representatives. The series of studies carried out by the Russian Institute of Directors in the period of time between July 2003 and March 2004⁴⁵ with regard to companies with the State's stake in their capital have revealed the insufficient transpar-

⁴⁵ Gosudarstvo – effektivnyi sobstvennik ? [Is the State an efficient owner ? // Rynok tsennykh bumag [Securities Market], 2004, No. 16 (271), p. 52–55; V interesakh gosudarstva. [In the interests of the State] // Zhurnal dlia aktsionerov [The Journal for shareholders], 2004, No. 11–12, p. 9–18.

ency of the system of managing the state stakes, which manifests itself as follows:

- there is no coherent system of principles on the basis of which state representatives can be appointed to companies with the State's stake in their capital;
- the research has not revealed any publicly available confirmations of the existence, in the federal agencies of authority, of a system of reporting for the work of state representatives in these very agencies, of estimating the results of their work, of taking into account the achieved results when nominating state representative for a new term in office, and of analyzing the reports submitted by state representatives with regard to the results of the financial and economic activity of those companies where they represent state interests;
- there is no system of incentives for the employees of bodies of authority who act as state representatives in economic societies – they receive no remunerations or inducements for their work and are not subjected to sanctions in an event of having failed to perform their duties properly. Frequent are the situations when they are overburdened with work, when one official is forced to simultaneously represent state interests in several companies alongside performing important work at his own department;
- there is but a weak interaction between the various departments and the judicial bodies as regards the issues of introducing the norms of corporate governance and improving the efficiency of law enforcement;
- the employees of bodies of authority who act as state representatives are insufficiently informed on legal innovations in the sphere of corporate governance. As a result, their activity in the part of improving the practice of corporate governance in companies with the State's stake in their capital is clearly inadequate. The research has found no evidence of the existence of reports concerning the implementation, by the persons who represent state interests in the boards of directors (or supervisory boards) of the OJSCs whose shares are in federal ownership or a Directive addressed to them with regard to the issues of realizing (or applying) the provisions of the Corporate Governance

Code (the Directive was jointly elaborated by the RF Ministry of State Property and the Federal Securities Commission (FSC) and was approved on 17 July 2002). According to this document, representatives of state interests are obliged to initiate the introduction, in the charters of companies and the other inter-firm documents, of amendments aimed at implementing the provisions of the said Code.

Nevertheless, the quantitative increase of the corps of state representatives and the adoption of a number of normative-legal acts regulating their activity have caused a certain activization of state representatives' efforts, who have become more insistent when certain decisions of the administrative bodies of companies with the State's stake in their capital are being substantiated. As is pointed out in one of the recent studies focused on the problems of corporate governance in the companies with the State's stake in capital, it is in the companies with the State's stake in their capital that formally demonstrate the best practice of corporate governance (*Avdasheva, Dolgopiatova, Plines, 2007*).

Thus, a comparative analysis of the performance of the boards of directors in 2001-04 indicates that the proportion of companies where a considerable or complete renewal of the composition of the boards of directors has taken place is larger among companies with the State's stake in their capital than in companies without state participation, and on the contrary, the proportion of companies where the former composition of the boards of directors has remained unchanged is smaller. In more than half of the companies with the State's stake in their capital, the boards of directors meet once a month or more frequently, while among those without the State's stake such results are demonstrated by less than 40% of companies. In this respect, there are practically no profound differences between companies with federal blocks of shares and companies where blocks of shares are owned by regional and municipal authorities.

The presence of the State as a shareholder in the 1990s was conducive to the accelerated rotation of the corps of directors. Thus, the average number of years in the office of a director amounted to approximately 5 years in joint-stock companies with a region's participation, and to more than 6 years in companies with federal participation, and to more than 8.5 years when the bodies of authority were not among the shareholders

(sample). If among the latter joint-stock companies 38% of the directors who had kept this job before the onset of mass privatization remained in office, among companies with state participation, such persons managed to “survive” only in 16% of cases. The bodies of authority with stakes in companies did impede the entrenchment of old directors under conditions of a wide proliferation of the model of combined ownership and management in the corporate sector of Russia. According to the later data (the sample included 822 joint-stock companies whose directors were interviewed in the summer and spring of 2005), the intensity of replacement of directors in the private and public sectors in 2001–04 was quite comparable, while among the companies with state stakes in their capital the percentage of those where the chairman of the board of directors had been replaced was higher (52% against 46% in private companies).

As regards the combination of the functions of manager and shareholder in companies of various types, it can be pointed out that the smallest share of the companies where neither the director nor managers are shareholders is detected among companies with federal stakes (20%), while among companies with regional participation this share is compatible with that of private companies (28–29%). Also the smallest among companies with federal stakes is the share of those where the director and managers are shareholders (approximately 1/3), while among private companies the proportion of such companies is almost 50%. Companies where regional bodies of authority hold a stake in capital are intermediate between these two groups. At the same time, in more than 47% of companies with a federal block of shares, the director is a small shareholder, against 20% among private companies and 28% among companies where regional bodies of authority hold a stake in capital.

Companies with state stakes are more active in the sphere of dividend policy. Among these, by the results of three financial years (2001–04), dividends were disbursed at least once by 61% of companies, and were disbursed on a regular basis in more than 46% of them. In companies without state stakes, the percentage of the above proportions were one third and 22% respectively. The main factor determining the probability of the dividends being disbursed was the size of a state stake. Among companies, where a controlling block of shares was in state ownership,

69% of companies disbursed dividends at least once, and 57% did so on a regular basis, whereas among companies with a state stake of between 10% and 25%, the percentage was 46% and 5% respectively (according to a sample of 822 joint-stock companies where controlling blocks of shares were in state ownership)⁴⁶.

Thus, companies with state stakes turn out to be rather attractive by a number of aspects of corporate governance. However, a more intensive rotation of managers including the board of directors, as well as a greater activity of the latter can well be a consequence of a more complicated financial-economic situation, and of lower indices of efficiency by comparison with private companies, which requires an adequate response on the part of the owner. At the same time, the very fact that such a response does exist deserves a positive appraisal, though requiring some clarification in the light of the estimates regarding the share of companies with state stakes, which have transferred monies to the federal budget (p. 1.4).

At the same time, it should not be forgotten that the problem of the boards of directors' efficiency is twofold. On the one hand, in conditions of a limited (with few exceptions) liquidity of the market, this body rapidly acquires special importance in the system of representation of shareholders' interests and managers monitoring. On the other hand, in many companies, the role of the board of directors remains to be rather formal and incomparable with that of top executive managers; according to the afore-mentioned study, this is especially true in regard of companies with federal blocks of shares. Thus, almost one half of such companies noted a strong influence of a collegiate executive body against less than ¼ among companies with regional authorities' stakes and 15% among private companies. As regards companies with federal blocks of shares, the average numerical composition of an executive body was larger than in private companies, while the scope of its rotation in the

⁴⁶ S. B. Avdasheva, T. G. Dolgopiatova, and X. Plines, "Korporativnoe upravleniie v AO s gosudarstvennym uchastiiem: rossiiskie problemy v kontekste mirovogo opyta". [*Corporate Governance in Joint-Stock Companies with State Stakes: Russian Problems in the Context of Global Experience*]. Preprint WP1/2007/01. Series WP1. InstitutSIONal'nye problemy rossiiskoi ekonomiki. [Institutional Problems faced by the Russian economy]. M., SU-HSE, 2007.

years 2001–04 was approximately similar to that demonstrated by the latter.

Bearing in mind their role in Russian economy, the practice of corporate governance in the largest Russian companies with state stakes is of special importance. The composition of their share capital considerably differs from the structure of property in the companies which usually become the objects of various surveys in the course of empirical studies and were repeatedly mentioned above. These differences consist in a much higher share of the State and state holding companies, a significantly smaller share of the personnel (including managers), and a relatively higher share of non-residents which in many respects determines a greater liquidity of these companies' stock.

Shareholders' meetings in the largest companies with state stakes have become noticeable events in economic life which attract growing attention of the media and society as a whole. After 2000, radical changes in the composition of the management of many such companies did take place. Among state representatives in their administrative bodies we now see some topmost officials from the Presidential administration who, together with government officials have become heads of the boards of directors of such companies as "Gazprom", "Rosneft", "Transneftprodukt", "Rossiiskie Zheleznye Dorogi" [Russian Railroads], Kontsern PVO "Almaz-Antei" [Anti-Aircraft Defense Concern "Almaz – Antei"], "Takticheskoe Raketnoe Vooruzhenie" [Tactical Missile Systems], and "Pervyi kanal" [First Channel], a phenomenon totally unknown in the 1990s.

The stand taken by state representatives in the course of shareholders' meetings in a number of large national companies (OJSC «Gazprom», RJSC "UES of Russia", "Transneft", "Sviaz'invest", "Aeroflot", "Sbergatel'nyi Bank RF" [RF Savings Bank], etc) has become determining when making the crucial decisions regarding their further development. These decisions turned out to be major events in the business life of the country. Thus, in 2002, the state representatives in the administrative bodies of joint-stock companies ensured the adoption, at the annual shareholders' meetings, of the new versions of the joint-stock companies'

charters composed in accordance with Federal Law, of 26 December 1995, No. 208-FZ “On Joint-Stock Companies”.

However, these developments had little to do with improving the practice of corporate governance, because of having been mainly concentrated on the issue of dividend payments. Just a few facts from Russian practice in the years 2003–04 would suffice to show that the stand taken by state representatives in the administrative bodies of large companies was rather remote from the recommendations of the Code of Corporate Behavior⁴⁷:

- OJSC “Gazprom» and the RJSC “UES of Russia”: in spring 2003, the state representatives in the boards of directors, in accordance with the negative resolution issued by the RF Ministry of Economic Development and Trade, voted against the proposals of minority shareholders to create committees within the respective boards of directors;
- the OJSC «Gazprom»: by the results of the 2003 general meeting of shareholders not a single outside director was elected to the board of directors;
- OJSC “Rosneft”: failure to disclose all the aspects of the spring 2003 transaction aimed at acquiring control over the company “Severnaia nef” [Northern Oil] by buying out its shares from private shareholders;
- OJSC “Bashneft”: some of minority shareholders were prevented from taking part in a general meeting of shareholders;
- OJSC “AvtoVAZ”: the refusal of the state representatives to nominate, by means of the state-owned block of shares, their representatives to the board of directors in early 2004 was one of the reasons for the two thirds of the block of shares put up for auction having remained unsold; the sold shares were realized at a price significantly lower than the market quotations of the company’s shares, and the chances for selling the rest of the shares declined because the State had lost the capability to independently nominate, by means of its block of shares, candidates for the inclusion in the board of directors;
- OJSC “KAMAZ”: in accordance with the received directives, the state representatives in the board of directors have ensured the adop-

⁴⁷ V interesakh gosudarstva. [In the interests of the State] // Zhurnal dlia aktsionerov [The Journal for Shareholders], 2004, No. 11–12, p. 12.

tion of the decision that the dividends should be disbursed in an amount exceeding the company's net profit.

Another example of the problems regarding the quality of corporate governance and the violation of shareholders' rights is the activity of the oil company "Rosneft" aimed at consolidating its assets. In 2002, "Rosneft", like many private oil companies, published its financial reporting for the years 2000–01 in accordance with US GAAP standards. Nevertheless, from the point of view of the property relations developing in the holding company, "Rosneft" lagged behind its competitors. The latter completed the processes of consolidating their affiliates and switched over to the single share in the late 1990s – early 2000s, when "Rosneft" was only beginning to consolidate its assets. In this connection, one of the problems is the structure of ownership in its affiliated companies – the company owns 51% of voting shares but only 38% of charter capital (in an event of not paying the dividends on preference shares "Rosneft" would, therefore, lose control, as it already happened in 1997). The apparent final goal of "Rosneft" was the establishment of qualified control over its affiliated enterprises, to be followed by switching over to the single share. This control was all the more important for the company in the light of the 2002 conflicts with minority shareholders regarding transfer pricing in the holding company.

In spring 2002, the general public became aware of the conflict between "Rosneft" and the shareholders of the OJSC "Rosneft – Krasnodarneftegaz". The holding company's loss of control over its affiliate in 1997 caused by an additional issue of shares which reduced its stake from 51% of voting shares, as it had been established in 1994 at the time of privatization, to 38% resulted in the fact that between 1998 and 2000 "Rosneft-Krasnodarneftegaz" pursued an independent policy in the sphere of making strategic decisions. From the end of 1999, "Rosneft" began to buy in shares in order to obtain real control over this company and was able to get 5 out of 9 seats on the board of directors by the results of the April 2001 meeting of shareholders in the aftermath of the acquisition of 12.9% of shares. One year on, the minority shareholders accused "Rosneft" of withdrawing the assets and using transfer pricing. As a result, in March 2002, a number of courts in Krasnodar Krai rendered the

rulings which prohibited “Rosneft” to dispose its shares, to conduct any operations concerning its client account in the register of shareholders of “Rosneft – Krasnodarneftegaz”, to call general meetings of shareholders of the affiliated company, to ship its crude oil, and to handle transactions with its real assets⁴⁸. The opponent of “Rosneft” was the company “Sovlink” representing the interests of 4 offshore companies which owned, among themselves, 45.01% of shares in “Rosneft – Krasnodarneftegaz”, while “Rosneft” itself owned 50.6% of voting shares, and the stake held in charter capital by the friendly structures amounted to 13%. In May 2002, “Sovlink” initiated a take-over bid with regard to this stake, but the bid price (110 million USD) failed to satisfy “Rosneft”. Meanwhile, the public prosecutor’s office began to receive complaints from “Krasnodarneftegaz”’s employees that in 1999-2000 they were being forced to sell their shares under the threat of dismissal⁴⁹.

This conflict was developing against the background of the audits carried out, in 2000–02, by the Audit Chamber with regard to the activity of “Rosneft” and its affiliated enterprises. As a result of these audits, in 2003, the Public Prosecutor’s Office of Krasnodar Krai initiated criminal proceedings against the management of the OJSC “Rosneft – Krasnodarneftegaz” and of the LLC “Yugneftegaz” in connection with abuse of authority, misappropriation, and embezzlement. The amount of losses incurred by the State amounted to more than 200 million roubles. In Stavropol Krai, criminal proceedings were then initiated against the management of the OJSC “Rosneft – Stavropolneftegaz” in connection with tax evasion or non-payment of insurance contributions to off-budget funds⁵⁰.

The overview of the corporate governance practice of Russian companies with state stakes in their capital in the first half of the 2000s will be incomplete without touching upon the availability of financial provision and manpower coverage which enabled the State to participate in this process, as a shareholder, because it was in this part that the 1999 Con-

⁴⁸ Izmailovich K. Aдекватnyi otvet minoritarnykh aktsionerov. [An adequate response from minority shareholders.] // Izvestiia [News], 28 March 2002, p. 5.

⁴⁹ Ignatova M. Bolevoi priiom. [A painful trick.] // Izvestiia [News], 28 June 2002, p. 5.

⁵⁰ Ot slov – k delu. [From words to deeds] // Finansovyi kñontrol’ [Financial Control], March 2004, No. 3 (28), p. 145–146.

cept for the Management of State Property and Privatization envisaged certain innovations.

When the notions of this documents were introduced into practice, certain progress was achieved in the part of the allocation of financial resources designed to back the activities dealing with the management of shares in OJSCs. From the year 2002 onwards, in the laws on the federal budget, the expenditures related to the above activities are placed under a separate heading. *Table 27* contains the data on the planned expenditures entered under this sub-head, and on the actual expenditures made by the federal body for the management of federal property.

Table 27

The Dynamics of the Expenditures Dealing with the Activities Relating to the Management of Federal Shares in OJSCs, Charged to the RF Ministry of State Property (from 2004 – the Federal Agency for Federal Property Management) in 2002–07

Period	under laws on federal budget			under laws on implementation of federal budget			
	thousands of roubles.	% of previous year	% of total expenditure	thousands of roubles	% of planned amount	% of previous year	% of total expenditure
2002	63000.0	-	1.6	61913.4	98.3	-	0.12
2003	146848.0*	233.1	2.16	127500.3**	86.8	205.9	1.9
2004	104800.0	71.4	2.58	52995.8***	50.6	41.6	0.6
2005	121586.0	116.0	1.44	...	...	...	...
2006	128134.3	105.4	0.7	...	...	...	...
2007	134140.0	104.7	4.52	...	...	...	...

* – in 2003, apart from the expenditures dealing with the activities relating to the management of federal shares in OJSCs, which were envisaged for the RF Ministry of State Property, there were similar expenditures envisaged for the RF Ministry of Power Engineering (735 thousand roubles) and the Russian Agency for Shipbuilding (417 thousand roubles) which constituted a tiny share (less than 0.1%) of total expenditure envisaged for the given departments;

** – in 2003, apart from the expenditures dealing with the activities relating the management of federal shares in OJSCs, which have been made by the RF Ministry of State Property, there were similar expenditures which have been made by the RF Ministry of Power Engineering (249.5 thousand rouble, or 33.9% of the planned amount), by the Russian Agency for Shipbuilding (172.2 thousand roubles, or 41.3% of the planned amount), and by the Russian Agency for Conventional Weapons (90.0 thousand roubles, not envis-

aged by the federal budget) which constituted a tiny share (less than 0.1%) of the total expenditures made by the given departments;

*** – in connection with the implementation, in 2004, of administrative reform, the expenditures dealing with the activities relating to the management of federal shares in OJSCs, were made, at the beginning of that year, by the RF Ministry of State Property and then by the Federal Agency for Federal Property Management (FAFPM) (7081.2 thousand roubles, or 0.1% of the total expenditures).

Source: the Laws on the Federal Budget for 2002–2007, the Laws on the Implementation of the Federal Budget for 2002–2004.

For the first time, the expenditures dealing with the activities relating to the management of federal shares in OJSCs were entered under a separate heading in the federal budget for the year 2002 (63 million roubles). In the following year they grew by more than 2.3 times, but in 2004 they dropped by almost 29%. In 2005-07, there was a gradual growth of allocations entered under this heading, although their amount planned even for 2007 (134.14 million roubles) is smaller than that planned for 2003 (146.85 million roubles). At the same time it should be noted that in the plans for 2007 these expenditures, as a percentage of the RF Ministry of State Property's total expenditure (4.5%), are the highest by comparison with the same indices of the previous years when their dynamics did not have the character of a clearly expressed trend and did not exceed 2.1 and 2.6% in 2003 and 2004 respectively.

So far as the actual expenditures under this heading are concerned, they were much smaller than those envisaged by the laws on the implementation of the federal budget for the years 2002–04; moreover, the ratio between these two values was on a constant decrease, and in 2004 amounted to little more than one half of those planned. In 2003, actual expenditures more than doubled by comparison with 2002, but in 2004 they decreased by more than 58% to less than 53 million roubles against 61.9 million roubles in 2002. The maximum share of the expenditures dealing with the activities relating to the management of federal property in the form of shares in OJSCs, ever envisaged in the expenditure estimates of the RF Ministry of State Property dates back to the year 2003 (1.9%).

All the expenditures dealing with the activities relating to the management of federal shares in OJSCs were charged to the RF Ministry of

State Property (the Federal Agency for Federal Property Management). The only exception was the 2003 federal budget where, apart from the RF Ministry of State Property, such expenditures were envisaged for the RF Ministry of Power Engineering and the Russian Agency for Shipbuilding. All these expenditures amounted to only 0.8% of total expenditure on the management of federal shares. In fact, they were made by the above mentioned bodies and the Russian Agency for Conventional Weapons; taken together, they accounted for 0.4% of all expenditures entered under this heading.

In conclusion of the analysis of the expenditures dealing with the activities relating to federal property in the form of shares in OJSCs it should be pointed out that all the examination performed is of purely preliminary nature because of the lack of data on the implementation of the federal budgets for 2005–07, and the absence of any concretization of the notion itself which should have been accompanied by subdividing this item of expenditure into more specific budget sub-items. Nevertheless, it could already be noted that placement of the expenditures on the management of federal shares in OJSCs under a separate heading only roughly corresponds to the approaches put forth by the 1999 Concept for the Management of State Property and Privatization in the RF, because the case in point of this document was the allocation of financial resources to the maintenance of the institution of state representatives at the expense of the dividends on shares in federal ownership (no less than 10% with the subsequent readdressing of one half of this amount to branch administrative bodies).

As we are coming now to the issues of manpower coverage it is necessary to say that in practice, despite all the innovations envisaged in the 1999 Concept, the main instrument for managing state property in the corporate sector remains the institution of state-interests representatives in joint-stock companies, although its format has undergone some changes.

In response to the requirements of the Law on Privatization and owing to the fact that the State began to pay more attention to the functioning of economic societies with state stakes in their capital, the number of state representatives in economic societies has considerably increased. By

comparison with 1999, it has grown by more than one and a half times, which has made it possible to considerably alleviate the strains within the management of state-owned assets in the corporate sector, whereas the most typical feature of the 1990s was a situation when one official was obliged to represent the State in several companies simultaneously.

According to the 1999 Concept for the Management of State Property and Privatization in the RF, the number of representatives appointed by the RF was around 2000, 92% of whom were employees of the federal executive bodies and their territorial agencies, and 8% - employees of the RF Ministry of State Property, the RF Ministry for Anti-Monopoly Policy, the RF Ministry of Finance, and the RFPPF. In 2000, the number of RF representatives-officials soared to 2855, 1178 (or 41.3%) of whom were federal public officials, and 1677 (or 58.7%) – public officials of RF subjects. Concurrently, certain progress was also achieved with regard to the attraction of managers from the private sector, which had been an extremely rare phenomenon in the 1990s. The above-mentioned 1999 Concept pointed to the fact that at that time the institution of state representatives was 99% public servants, and the attraction of professional managers to managing state-owned blocks of shares was an exceptional and sporadic event, whereas in 2000, the number of persons from their ranks who were contracted to represent RF interests on the boards of directors rose to 362.

Thus, by comparison with the data presented in the 1999 Concept, in 2000 the total number of RF representatives increased by more than 1200 and reached 3217⁵¹. The rise in the number of public servants (more than by 40) could be put at 870–880, while the number of contracted representatives grew manifold and reached approximately 28% of the total number of state representatives. Nevertheless, despite the indisputable progress in this respect, their share in the corps of representatives amounted to only 11.3%.

⁵¹ Gazetov A., Ditrikh E., Kotliarova E., Skripichnikov D. Doklad po korporativnomu upravleniiu gosudarstvennymi predpriiatiiami v Rossii [A report on corporate governance of state enterprises in Russia] // Russia's Round Table Meeting on Corporate Governance, 2–3 June 2005 (within the framework of the TACIS Program and Global Forum on Corporate Governance).

The fact that the attraction of hired managers to the management of state-owned blocks of shares was significantly intensified in the early 2000, was also noted by the heads of the federal bodies of authority. Thus, according to Vice-Chairman of the RFPF V. Fatikov⁵², during the first period after the issuance of Decree of the RF Government No. 625, of 21 May 1996, which authorized the attraction of entrepreneurs to the management of federal blocks of shares, instances of the appointment of outside managers could be characterized as exceptional. Later on, as positive experience was accumulated, this practice came into a more frequent use. In 2001, as many as 42 outside managers were appointed, and immediately afterwards, in early 2002, the Fund put forward more than 80 candidacies for such posts, and announced a contest.

However, it is apparent that the role of the RFPF itself remained rather passive. It was V. Fatikov's acknowledgement that the Fund resorted to the quest for new managers only in the situations when the "prostrated" state of an enterprise was absolutely clear, and everybody understood that it could not be improved, bearing in mind the complete indifference of the officials representing the State in its administrative bodies. In general, the initiative of putting forward a candidacy for the job of outside director usually belonged to other minority shareholders and regional authorities.

The above situation is exemplified by the case of the OJSC "Usol'ekhimprom" [Usol'e Chemical Plant] (Irkutsk Oblast). In 1997, this enterprise was on the brink of bankruptcy and had a large indebtedness, in the structure of which the heaviest debts were those to the energy suppliers ("Irkutskenergo"). In order to cope with this state of affairs, the RFPF passed the decision that the interests relating to the state-owned residual block of shares (15%) be represented, on a contractual basis, by the three managers, recommended by the Oblast administration, who represented the Eastern-Siberian Financial and Industrial Group which had an approximately similar stake in the company. By a joint effort, the failed general director was replaced by a more qualified manager with a degree in crisis management. The finance flows were established from

⁵² Fatikov V. Chasto dlia prodazhi nam peredaiut aksii polubankrotov. [Often they transfer to us for sale the shares in half-bankrupt companies] // Finansovye Izvestiia [Financial News], 5 February 2002, p. 1.

scratch, and all delivery contracts were renewed. Under the new managers, settlement of transactions became 90-percent monetary while in the past the share of barter was very high (90%); also, it took them only half a year to make the enterprise capable of timely effecting current payments and of beginning to repay the outstanding debts. As a result, the capitalization of the company increased twofold, while the value of one share grew from 7 copecks to 2 roubles 40 copecks.

As the Vice-Chairman of the RFPF has put it, it is advantageous for the State when management is transferred to outside managers because, although being obliged to coordinate with the Fund all the key issues (major transactions, the appointment of heads to the enterprise's administrative bodies, the introduction of changes into constituent documents, etc.), they are still capable to more efficiently resolve the current issues dealing with the board of director's activities with respect to the preparation and effectuation of investments as well as to the mapping out and analysis of business-plans in accordance with the specificity of a given branch. The submission of the plan for an enterprise to get over the crisis should be preceded by its being approved by the RFPF. The proposed business-plan would be the criterion on the basis of which an outside manager would be contracted to represent state interests in the managerial bodies of the enterprise. This contract should strictly specify the responsibilities of the parties including the duty of the manager to coordinate the key issues (including the movement of assets) with the RFPF as well as his subsidiary liability for harm to the JSC.

For all this, it should be noted that it is with the minority blocks of shares that the RFPF deals with, and that its managerial efforts with regard to corresponding enterprises should better be considered as a pre-sale preparation aimed at getting the maximum possible sum of money at the moment of realization. At the same time, the Federal Agency for Federal Property Management (FAFPM) (formerly the RF Ministry of State Property) is involved in the process by more weighty blocks of shares not necessarily intended for sale, at least in a short-term perspective.

After 2000, the general dynamics of the conclusion of contracts for representation of state interests in the managerial bodies of economic societies is as follows (*Table 28*).

As transpires from *Table 28*, it was in the years 2001 and 2003 that contracts for RF interests representation were concluded most intensively, while the period 2002–2003 can be characterized as a lull. In 2004 the number of concluded contracts rose by more than 11 times on 2003, while that of state representatives – by 6.7 times.

Table 28

The Dynamics of the Conclusion of Contracts for Representation of State Interests, 2001–2004

Period	The number of contracts	The number of representatives
2001	103	...
2002	23	11
2003	19	10
2004	210	67

Source: Gazetov A., Ditrikh E., Kotliarova A., Skripichnikov D. Report on the corporate governance of state-owned enterprises in Russia // Russia’s Round Table Meeting on Corporate Governance, 2–3 June 2005 (in the framework of the TACIS / Global Corporate Governance Forum program).

For all the intensification of the activity of the institution of state representatives in the administrative bodies of economic societies, such issues as the motivation of their activity, the principles of preparing decisions, the assessment of the results of work, and the conferment of required transparency on the whole process remain unresolved.

So far as the other versions of state-owned property management in the corporate sector are concerned, it could be said that since the year 2000, in conditions of the general drive towards overcoming the State’s weakness of the 1990s, as declared by the topmost national leadership, it was absolutely logical that the practice of transferring state-owned blocks of shares into trust management has become even more rare than in the 1990s when it was hardly noticeable. It should be mentioned in this respect that from the year 2000 onwards, official statistical reports contain no information on transferring the blocks of shares in enterprises being

privatized into trust management and to holding companies. Judging from the publications in the mass media, the most significant, if not singular, instance of the trust management mechanism being used was the transfer of the state-held block of shares in “Voronezh Aviazavod” [Voronezh Aircraft Plant] (OJSC “VASO” into trust management to “Natsional’nyi Rezervnyi Bank” (NRB) [National Reserve Bank, NRB].

Much more widespread were the arrangements dealing with the integration of state-owned enterprises and companies with mixed capital into holding structures.

1.3. The Impact of the Ownership-Related Presence of the State on the Conduct of Structural Policy and on the Optimization of the State’s Participation in the Economy

By the moment of the resumption of economic growth in Russia in the year 1999, the State’s presence in the corporate sector, while being huge from the point of view of quantitative indicators, had been considerably scattered in the form of many thousands of isolated and poorly managed, if managed at all, enterprises and blocks of shares in the joint-stock companies recently established virtually in all branches of the economy. The integrated structures with state participation created during the initial stage of privatization on the State’s initiative, operated mainly in the fuel and energy complex. They also represented the natural-monopolistic types of activity.

For purposes of increasing the efficiency and improving the management of its assets, the State launched a number of projects designed to integrate them into holding companies in such branches as nuclear power engineering, the defense and alcohol industries, railway transport, the air and sea transport infrastructure, and the mail services. In parallel with this, the State began to restructure the natural monopolies.

The first example of such post-1999 developments was the creation, on 22 May 2000, of the FSUE “Rosspirtprom” [Russian Alcohol Industry] (designed to centralize the management of state assets in the alcohol industry). As of autumn 2000, the holding company included, as its affiliates, 18 SUEs (mainly regional SUEs designed to control the

activity of distilleries in a region); it also held blocks of shares in a large number of enterprises of the alcohol branch. The process of state property consolidation in this branch went on, and by the beginning of 2003 the holding company comprised more than 100 enterprises (including the state stakes in 102 JSCs of the alcohol industry which had been transferred into operative management, without the right of alienation, to “Rosspirtprom”; the latter exercised its shareholder rights in the name of the RF).

In the framework of implementing Edict of the RF President, of 4 April 2001, No. 390, the open-end joint-stock company [Rossiiskii Kinoprokat” [Russian Film Distribution and Exhibition] was created. It was based on 18 federal state-owned enterprises engaged in the exhibition and distribution of films (including the FSUE “Opytno-eksperimental’nyi zavod (tsentr teatral’nogo svetotekhnicheskogo oborudovaniia)” [Pilot-Production Plant (center of theater lighting equipment)]. By early 2005, 7 enterprises, 3 of which were in the stage of being integrated into the OJSC “Rossiiskii Kinoprokat”, had been joint-stockicized.

Measures designed to ensure the transfer, by state-owned enterprises, of their shares (or stakes) in charter capital to the RF treasury were implemented relatively energetically and effectively⁵³. By July 2002, it had been established, by the results of inventory, that 548 FSUEs hold 642 blocks of shares in banks. By November 2002, the collected data indicated that 551 unitary enterprises were holders of 730 blocks of shares in credit institutions. On the whole, by January 2003 the Ministry of State Property had information on 574 federal state unitary enterprises (including treasury ones) and establishments which held 772 blocks of shares in 156 credit institutions. As of 23 October 2002, the Russian Federation in the person of the RF Ministry of State Property exercised shareholder rights with regard to shares in 139 credit institutions whose shares had

⁵³ In accordance with Regulation of the Government of the Russian Federation of 2 April 2002 No. 454-r, the federal bodies of executive authorities, entrusted with the task of coordinating and regulating the operation in the corresponding branches, were asked to ensure, in collaboration with the RF Ministry of State Property, the transfer by their subordinated federal state enterprises of the shares and stakes in the charter capital of credit institutions to the RF treasury, and to complete this transfer no later than by 1 July 2002.

been transferred to 359 enterprises, as confirmed by 424 extracts from the register of shareholders.

In the framework of implementing the afore-said directive, it was planned to privatize these blocks of shares, the realization of which was expected to yield more than 2.5 billion roubles. Thus, it was planned to privatize, in 2003, approximately 160 blocks of shares in banks, transferred to the federal treasury. In 2004, 32 blocks of shares in credit institutions were sold (against 144 included in the annual Forecast Plan (Program) for Federal Property Privatization). Naturally, the case in point is not exclusively the blocks of shares in credit institutions transferred by enterprises in recent years but also those blocks of shares that have been in federal ownership from the very beginning. However, it should be borne in mind that all those shares were in medium-size and small banks, whereas, by that time, federal ownership had already been extended to several relatively large banking structures including “Vneshtorgbank” (transferred to government control by the RF Central Bank⁵⁴) which became, from 2003 onward, one of the largest payers of dividends to the federal budget, and the newly established Rossel’khozbank [Russian Agricultural Bank] and the Russian Bank for Development.

In the sphere of telecommunications, structural reforming was completed in the holding “Siaz’invest” with its nearly 80 subsidiary companies having been merged into 7 regional JSCs (“Tsentrtel’kom”, “Severo-Zapadnyi Telekom”, “Volga Telekom”, “Iuzhnaia Telekommunikatsionnaia Kompaniia”, “Uralsviaz’inform”, “Sibir’telekom”, “Dal’sviaz”). In each of these 7 joint-stock companies as well as in “Rostelekom”⁵⁵, the holding company’s stake amounts to 51%. In 2004-05, there was an active debate regarding the possible versions of privatizing the state stake in it (50% + 1 share is owned by the FAFPM, and 25% – 1 share – by the RFPF). However, privatization was postponed, because of the objections of power agencies, pending the

⁵⁴ The RF CB remains Sberbank’s biggest shareholder.

⁵⁵ In addition to controlling blocks of shares in these companies, “Sviazinvest” also owns a blocking stake in the MGTS, as well as some blocks of shares in “Tsentral’nyi telegraf” [“Central Telegraph”] and “Giprosviaz”.

adoption of the law on the protection of the interests of special consumers of communication services.

In accordance with Decree of the RF Government of 18 May 2001, No. 384, “On the Program of Structural Reform in the Railway Sector”⁵⁶ and a number of federal laws, primarily Law “On Railway Transport in the Russian Federation”, No. 17-FZ, of 10 January 2003, and Law “On the Specificity of the Management and Disposal of Railway Transport Property”, No. 29-FZ, the economic and managerial functions of the RF Ministry of Ways of Communications were divided. By Decree of the RF Government of 18 September 2003, No. 585, the largest in the country OJSC “Rossiiskie Zheleznye Dorogi” (RZhD) [Russian Railways] (with a charter capital of 1535.7 billion roubles, or 53.8884 billion USD), with a state stake of 100%, was created on the basis of enterprises and organizations of the federal railway transport system in order to carry out both the monopolistic (maintenance and upkeep of the infrastructure) and potentially competitive (cargo and passenger carriage, repair of the rolling stock, etc.) types of activities. The other economic subjects were also authorized to effect carriage, but only on condition that a contract for the use of the infrastructure be concluded with the OJSC “RZhD” and a corresponding license be issued by the latter.

At present, the company is in the process of spinning off subsidiaries, with the basic principles for the organization of their activity being determined and new control models being introduced. Next in line is the issue of creating a federal passenger company to be engaged in long-distance passenger carriage. It was planned that a Federal Passenger Directorate should be created in 2000 to form the basis for establishing a separate joint-stock company (the OJSC “FPK”) by way of spinning it off from the OJSC “RZhD”. The new company should have included 16 regional directorates concerned with passenger carriage, and been in charge of 46 railway car shops, 323 railway terminals, 25.5 thousand passenger cars, and other assets. It was planned that, on the whole, approximately 100-billion-roubles worth of property should be transferred to the charter

⁵⁶ The RF Government’s Decree No. 811, adopted in December 2004, introduced some changes in the Program for Structural Reform of Railway Transport.

capital of the company. The logical question then arose of what would be the source of funds for covering the losses to be incurred by railway transport in the event of railway carriage being spun off to form a separate company (in essence, the case in point was the volume of subsidies from various budgets, primarily the federal one) and of what would be the status of this company. As regards the status, the choice was between making the new company a subsidiary of the OJSC “RZhD” and preserving the situation of the State having a 100-percent stake (with a possible participation of the regions). Yet another issue of the discussion was the question of whether the cargo carriers should be spun off from the parent company and what would be their optimal number from the point of view of organizing a competitive environment in the railway transport sector.

In late 2005, the news spread that part of the state-held block of shares in the OJSC “RZhD” as well as the shares in its subsidiaries operating in the market segment open to competition, might be offered for sale by the end of the third stage of reforming the railway transport sector (2006–08).

The beginning of restructuring the RJSC “UES of Russia” was a significant event in the post-2000 economic development of the country. On 11 July 2001, the Russian government approved the Major Directions of Reforming the Power-Engineering Complex of the Russian Federation, and on 3 August authorized the Plan of Measures for the first Stage of Reforming the RF Power-Engineering Complex. For the purpose of implementing this plan and in order to ensure the uniformity of technological management and the integrity of the dispatcher vertical, the OJSC “Federal’naia Setevaia Kompaniia (FSK) EES” [Federal Power Mains Company (FGC) of the UES] and “Sistemnyi Operator (SO-TsDU) EES” [Systems Operator (SO-CDC) of the UES] were founded. For the purpose of organizing trade on the wholesale market of energy and of ensuring that the supplied energy and the services provided to market participants be paid for, “Administrator Torgovoi Sistemy” [Commercial System Administrator], a non-for-profit partnership formed by the major participants of the electrical energy market, was created with direct participation of the State’s representatives. The final outlook and the legal framework of reforming the power engineering sector were determined in the parcel

of five fundamental federal laws adopted in 2003, with Law “On Power Engineering” No. 35-FZ, of 26 March 2003, being its core.

In 2004-6, in the framework of implementing the adopted decisions, the regional power-generating and distributing companies within the holding company were being actively reorganized either by spinning them off or by creating the new juridical persons designed to engage in specific types of activity, first of all, wholesale (WGC) and territorial (TGC) companies, servicing structures, etc.

Such reorganization is well exemplified by the case of OJSC “Mosenergo”⁵⁷. In accordance with the project of reforming, coordinated with the RF government and approved by the boards of directors of the RJSC “UES of Russia” and the OJSC “Mosenergo”, the general meeting of shareholders, of 28 June 2004, was to spin off, from the company, 13 new companies: 3 distributing power mains companies (“Moskovskaia Gorodskaiia Elektrosetevaia Kompaniia”, “Moskovskaia Oblastnaia Elektrosetevaia Kompaniia”, “Moskovskaia Teplosetevaia Kompaniia”)[Moscow City Power Mains Company, Moscow Oblast Power Mains Company, and Moscow Heat-Supply Company], 1 power mains system company (to be later integrated with the “FSK”), 1 energy marketing company, 1 management company, 3 repair companies and 5 power generating companies (on the base of the Kashira, Riazan’, and Shatura State Raion Power Stations to be integrated into the wholesale generating companies OGK-1, OGK-5, and OGK-6⁵⁸). This would leave “Mosenergo” proper with 17 power stations with a total capacity of more than 10 MW. It was also planned to sell 10 repair companies which were to be established, after the reorganization, as 100-percent affiliates of the OJSCs “Mosenergo” and “Moscovskaia Oblastnaia Elektrosetevaia Kompaniia”. Each

⁵⁷ Vasil’ev D. Iuridicheskie i ekonomicheskie aspekty transformatsii prav sobstvennosti v usloviakh reformy elektroenergetiki (na primere “Mosenergo”). [Legal and economic aspects of the transformation of property rights in conditions of reform in electric power engineering (as exemplified by “Mosenergo”). In: Sotsial’no – ekonomicheskaiia transformatsiia v stranakh SNG: dostizheniia i problemy. [Socioeconomic transformation in the CIS countries: achievements and problems] (Materials of an international conference). M., IET, 2004.

⁵⁸ On its spinning-off, Zagorsk GNPP after its separation will become a separate OGK-10.

of the spin-offs was to be created in the form of an open-end joint-stock company; each of the shareholders of “Mosenergo” was to receive the same number of shares in them as he had in the main one.

As the reorganization was preceded by the conclusion of the agreements on the OJSC “Mosenergo” with the governments of Moscow and Moscow Oblast, it meant that after the spinning-off of the new companies, the shareholders of the Moscow city and Moscow Oblast power mains companies and the Moscow heat-supply company could pass the decision to carry out additional issues of shares to be placed, by closed subscription, in favor of the city and oblast governments which would then increase their stake to the size of a controlling block of shares by way of contributing either the money or their own tangible assets relating to heat and power supply⁵⁹. Apart from this, the agreements envisaged a direct interest of the shareholders of the RJSC “UES of Russia” in the charter capital of “Mosenergo”, “Moskovskaia Oblastnaia Setevaia Kompaniia” and the three repair companies, as a result of which the block of shares in “Mosenergo” (51%) held by the national holding companies was to be distributed between the minority shareholders of the RJSC “UES of Russia” (25%) and the State (26%) thus making it possible to make the federal center a full-fledged blocking shareholder of “Mosenergo”.

In 2005, there was a slowdown in reforming the electric power industry, expressed by the failure to carry out the initially planned sales of the generating facilities which were to follow them having been spun-off, by type of functioning, from the regional energy companies, and also by the negative phenomena in the dispatcher and power-mains sectors which came to light during the late May 2005 energy crisis in Moscow and neighboring regions. Then, in the fall of that year, the plans for restructuring the RJSC “UES of Russia” were subjected to a certain adjustment. The adjusted plans included a new aspect dealing with the additional issues of shares having been carried out by a number of generating compa-

⁵⁹ The assets of this type owned by the city are accumulated by Moscow United Energy Company (CJSC “MOEK”), created in 2004 on the basis of three former SUEs (“Teploremnaladka”, “Mosteploremnaladka”, “Mosgorteplo”).

nies. The realization of this aspect was to follow in autumn 2006, when the management of the holding energy company announced the rather successful results of the first additional issue of shares, the placement of 14.4% of shares in “OGK-5” which made it possible to obtain 459 million USD for investment purposes. At the same time, the holding company has never discontinued the use of the other sources of investment: its own funds, the obtaining of credits, and the direct attraction of private capital, including by the results of selling the assets of its power generating companies⁶⁰.

As additional issuing of shares on the part of the newly established companies means a smoother and more moderate version of admitting private capital into the branch, the issue of the future distribution of the capital of the affiliated and controlled companies once these emissions are carried out, and the extent of participation in these companies of the RJSC “UES of Russia” and its shareholders, including the State, remains very important and debatable. It should be mentioned in this respect that according to the plans of restructuring the branch after the liquidation of the RJSC, the State intended to keep in its ownership 75% + 1 share in both “Federal Power System Company” and “Systems Operator”, as well as to preserve its controlling block of shares in the generating company created on the basis of hydroelectric assets. For the state stake in these companies to be increased to the desired size will require direct investment of budget means, or contribution of other assets.

By contrast with the electric power industry, developments in the gas industry were confined to the discussion aimed at finding the best ways to reform “Gazprom”. So far as the gas monopoly is concerned, judging from the statements made by a number of officials, the case in point is the carrying out of measures designed to reduce the costs, to increase the transparency and to achieve the financial recovery of the company. Thus, the RF President’s adviser I. Shuvalov stated that, by contrast with the electric power industry, no major reform was expected in the gas industry, and that the pipe-line system would remain within the company

⁶⁰ Thus, in October 2006, 12% of shares in “Peterburgskaia Generiruiushchaia Kompaniia” [Petersburg PowerGenerating Company], owned by “Lenenergo”, were sold.

which should be vested with the monopolistic right to handle export on condition that independent producers would have indiscriminate access to the pipelines. Currently, the issue of launching a pilot project designed to create a competitive gas market with a volume of approximately 5 billion cubic meters per year is being discussed⁶¹.

However, the restructuring of all natural monopolies is a special subject to be considered in its own right. At the same time, it should be emphasized that it is far from clear whether the privatization of the natural monopolies' assets is possible at all, and that the conditions for its implementation are equally disputable. This state of confusion has been best demonstrated by the case of "Sviaz'invest", whose position in the 1990s, when it was being transformed into a joint-stock company, was that of a virtual monopoly in the communication services as well, because, at that time, mobile communications were not widespread as yet. Although the issue of selling the state-owned block of shares had been repeatedly discussed, last year, the objections on the part of the power agencies resulted in its privatization having been postponed until after the adoption of the law on the protection of the interests of the special consumers of communication services and the development of corresponding practical mechanisms.

The processes of integration are especially important for the enterprises of the defense-industrial complex (DIC).

These processes were initiated as early as the second half of the 1990s. In accordance with the Federal Target Program for the Restructuring and Conversion of Defense Industry for 1998–2000, it was planned to create 82 integrated structures. By 2001, the branch had numbered 51 such structures, but in effect, only 35 of them had been operating, including 20 financial-industrial groups (FIG), 8 holding companies, and 7 concerns⁶². As is known, owing to the normative-legal base which existed in the 1990s, the officially registered FIGs were not characterized by a high

⁶¹ Shvedov I. "Trogat' ikh nado ochen' akkuratno". [They should be touched with utmost care"] // *Izvestiia* [News], 18 March 2005.

⁶² *Upravlenie gosudarstvennoi sobstvennost'iu*. [Management of state property] Ed. by Dr. Ec. Sci. V. I. Koshkin, An expanded and revised edition. – M.: EKMOS, 2002, p. 514.

degree of property integration and controllability on the part of the State; it was not uncommon that they were created with no proper economic justification whatever. Therefore it could be assumed that by the late 1990s, the predominance of FPGs among the integrated structures of defense industry no longer satisfied the increased requirements for economic efficiency proceeding from the 1999 Concept for the Management of State Property and Privatization in the RF.

An important role in the further development of holding structures within the DIC has been played by Edict of the RF President, of 23 October 2000, No. 713. It stipulates that, for the purpose of concentrating and rationalizing defense production, the inclusion of the blocks of shares in the JSCs created in the process of privatization, into the charter capital of the holding companies being created or functioning in this branch, should be authorized only on condition that no less than 51% of shares in this very holding companies are consolidated in federal ownership.

One year on, by Decree of the RF Government, of 11 October 2001, № 713, the federal target program “The Reforming and Development of the Defense-Industrial Complex” was confirmed. In the framework of this program, it is planned to create a number of integrated structures being one of the most efficient forms of managing state property in the DIC. Judging from the very name of the document, it is clear that the time bracket is set at five years. From the organizational-and-legal point of view, it is also important that the case in point should be the creation of structures designed to consolidate both the FSUEs and the state stakes in the OJSCs.

During the years 2001–2003, the following integrated structures were created or being created: “TVEL”, “Spetsstroimaterialiy” [Special Construction Materials] (nuclear-power-engineering industry), the AMPC “Sukhoi”, the RPC “MIG”, the OJSC “Aviastroitel’naia Kholdingovaia Kompaniia “Tupolev” “Aircraft-Construction Holding Company “Tupolev”, “Aviapribor-Kholding” [Aircraft Instrument Making Holding Company], “Korporatsiia “Aerokosmicheskoe Oborudovanie” [Corporation “Aerospace Equipment”], “Mezhgosudarstvennaia Aviastroitel’naia Kompaniia “Iliushin” [Interstate Aircraft-Construction Company “Iliushin”] (aircraft industry), “Vympel”, Antei” (radio industry), “Rossiis-

kaia Elektronika” [Russian Electronic Equipment] (electronic industry), “Korporatsiia “Kompomash” [Corporation “Kompomash”] (missile and aerospace equipment), and “Almaz-Antei” (production of anti-aircraft-defense weapons and equipment).

In 2004, work was underway to create the integrated structures of the DIC such as the OJSC “Roskhimzashchita” (protection from chemical weapons), “Kontsern “Granit-Elektron” [Concern “Granit-Elektron”], Kontsern “Morinformsistema Agat”] (Concern “Naval Data System Agat”), “Kontsern Morskoe Podvodnoe Oborudovanie” (Naval Submarine Weapons Concern), “Aviatsionnyi Kompleks im. Iliushina” [Iliushin Aircraft-Construction Concern], “Kontsern Vega” [Concern “Vega’], “Takticheskoe Raketnoe Vooruzhenie” [Tactical Missile Weapons], “Korporatsiia ‘NPO “Mashinostroenie” [Corporation “Research and Production Amalgamation “Machine-Building”, and “Elektromashina” [Electrical Motors].

In 2005, in pursuance of the edicts of the RF President and the RF government, all the FSUEs subject to inclusion into the charter capital of the OJSC “Contsern “Sozvezdie” [Concern “Sozvezdie”], the OJSC “Contsern Radiostroeniia “Vega’ [Radio-Equipment-Buiding concern “Vega”], the OJSC “Okeanpribor” [Ocean-Navigating Instruments], the OJSC “Morinformsistema-Agat”, and the OJSC “Granit-Elektron” were privatized. The formation of the OJSCs “Korporatsiia “Takticheskoe Raketnoe Vooruzhenie” and “Ob’edinennaia Promyshlennaia Korporatsiia “Oboronprom” [United Industrial Corporation “Defense Industry” was completed.

In the aircraft industry, after the lengthy discussions with regard to Edict of the RF President, No. 140, of 20 February 2006, the creation of “Ob’edinennaia Aviastroitel’naia Korporatsiia” (“OAK”) [United Aircraft Construction Corporation (UAC)] integrating the manufacturers of military and civil aircraft, finally began. The state stake in the corporation would amount to no less than 75%. In November, it was announced that the managerial bodies of the new company were starting their work. Like many other already existing state corporations of national importance, (“Gazprom”, “Rosneft”, “RZhd”, etc.), will be headed, at the level of the board of directors, by state officials of the highest rank (First Vice Prime

Minister S.B. Ivanov), with attraction, to current management, of the former managers of the companies being integrated into “OAK”. Thus, the former head and co-owner of the company “Irkut”, A. Fedorov, is appointed to the post of director of “OAK”.

Prior to its integration into “OAK”, “Irkut” (formerly “Irkutskoe Aviatsionnoe Proizvodstvennoe Ob”edinenie [Irkursk Aircraft-Production Corporation]) was the largest non-state company⁶³ of Russia’s defense industry, specializing, in recent years, in exporting, to Asian countries, the various types of “SU” aircraft; it has also established its control over “Taganrog Aviatsionnyi Nauchno-Technicheskii Kompleks im. G. Berieva” [G. Beriev Taganrog Research and Technical Complex] (“TANTK”) and “Opytnoye Konstruktorskoe Biuro im. A. Yakovlev” [A. Yakovlev Experimental Design Office] (“A. Yakovlev OKB”). In all likelihood, it is “Irkutsk” along with the aircraft-constructing corporation “Sukhoi”, where all the 100% of shares are in federal ownership, will become the most weighty assets of the “OAK”.

In the process of the assets being valued by “Deloitte & Touche CIS”, “Irkut” was valued at only 940 million USD, and the corporation “Sukhoi” – at 2.2 billion USD. This much more modest than expected valuation of “Irkut” means that the latter will be able to claim only 20% of shares in “OAK”, at the most. It is likely that in spring 2007, shareholders of “Irkutsk” will be asked to exchange their shares for the securities of the newly formed “OAK” or to redeem them at a fixed price. When determining the price of redemption, the main benchmark, in all likelihood, will be the value of “Irkut” as estimated by “Deloitte & Touche”. The appointment of A. Fedorov to the top managerial post in “OAK” is considered as a compromise necessary for including “Irkut” in “OAK”⁶⁴.

On the whole, in the course of integrating the assets of the aircraft industry, the additional financing of the branch in the amount of 36 billion

⁶³ The State does not directly participate in the share capital of “Irkut”; the state-owned company AkhK “Sukhoi” is a minority shareholder.

⁶⁴ Frumkin K. Chebol po-russki. [Chaebol Russian style.] // *Kompania*, No. 48–49 (444–445), 25 December 2006, p. 22–31.

roubles was carried out on the part of the State, because the then existing size of assets (60 billion roubles) had been considered inadequate. The published estimated value of the assets of “OAK” amounted to 96 billion USD.

The creation of “OAK” is planned to be completed in spring 2007. At the same time it should be noted that there exist no plans as to the inclusion in “OAK” of any partner enterprises engaged in the production of engines, instruments, etc. Therefore it is most probable that some specialized integrated structures will be created, as it has been done in the case of the OJSC “Kontsern Avionika” [Concern “Avionics”] (designing and production of airborne equipment for military and civil aviation, and of the land-based systems necessary for the functioning of the above complexes). In “Concern Avionika”, the controlling blocks of shares are consolidated in federal ownership on the basis of integration of corresponding enterprises specializing in the production of aero- and space electronic equipment with the research and production center “Teknokompleks” [Technological Complex] which had comprised, by mid-2002, 13 enterprises (for example, the JSC “Elektronnaia Kompaniia “Elkus” [Electronic Company “Elkus”] in St. Petersburg, and the SFUS “Kazanskoe Priborostroitel’noe Biuro” [Kazan Instrument-Making Design Office]⁶⁵.

At the same time, it should be emphasized that the process of creating integrated structures turns out to be a slow one. The only projects materialized and functioning in defense industry are the ACC “Sukhoi”, “Takticheskoe Raketnoe Vooruzhenie”, and “Almaz-Antei” (production of weapons and equipment for anti-aircraft defense), although initially it was planned to create 74 holding companies and concerns; in 2002 this figure was reduced to 42. The candidates for inclusion in the group of integrated structures are the holding companies “Splav-Sistemy Zalpovogo Ognia” [Water-Borne Multiple Rocket-Launching Systems], Dal’niaia Radiosviaz” [Long-Distance Radio Communication], “Rossiiskie Kosmicheskie Dvigateli” [Russian Space Engines], “Strelkovoe

⁶⁵ Khikmatov T. Poka – trinadsat’. [So far – thirteen.] // Izvestiia [News], 29 June 2002, p. 6.

Oruzhie i Patrony” [Firearms and Ammunition], and “Bronetankovaia Tekhnika” [Armored Combat Vehicles].

In late 2006-early 2007, the RF authorities approved a draft law which would make it possible to create a new big state-owned company based on the assets of the Russian nuclear industry civilian sector with 100% of shares therein belonging to the State. The united integrated company “Atomenergoprom” [Atomic Energy Industry] will be a large corporation of the full cycle which will include the extraction of uranium, the production of fuel for nuclear power stations, the generation of electricity, the construction of nuclear power stations in Russia and abroad, and nuclear machine-building. The first-priority candidate for inclusion in “Atomenergoprom” is “TVEL”, a one-hundred-percent state-owned company for the production of nuclear fuel, which comprises a number of specialized enterprises including “Mashinostroitel’nyi Zavod” [Machine-Building Plant] in the town of Elektrostal’ (Moscow Oblast), “Novosibirskii Zavod Khimicheskikh Kونسentratov” [Novosibirsk Chemical Concentrates Producing Plant], and “Priargunskoe Gorno-Khimicheskoe Ob’edinenie” [Argun Mining and Chemicals-Producing Corporation] (Chita Oblast). In the future, the new holding company may also incorporate the concern “Rosenergoatom” comprising all nuclear power stations of Russia, a number of specialized scientific research- and specialized design organizations, and, probably, the group of enterprises presently incorporated in “Ob’edinennye Mashinostroitel’nye Zavody” [United Machine-Building Plants].

The same tendency is reflected in the plans for creating, in the second half-year of 2007, of yet another state-owned corporation, “Bank Vneshneekonomicheskoi Deiatel’nosti i Razvitiia Rossiiskoi Federatsii” [Bank for Economic Activity and Development of the Russian Federation], with a charter capital of 70 billion roubles, on the basis of the reorganized “Vneshekonmbank” and the taken-over “Roseksimbank” and “Rossiiskii Bank Razvitiia” [Russia’ Bank for Development]. The main aim of the new bank will be to financially support infrastructure- and innovation projects not especially attractive to private business, by way of granting credits to juridical persons for a term in excess of 5–10 years. The bank will not work with the population. The bank will be managed

and supervised by the board of supervisors appointed by the government, without the RF CB's participation.

The present capabilities of the State as to the integration of companies with mixed capital are much smaller than in the period of 1992–4, when the State owned a large share of all property (the major one in some branches), and the share capital structure was in the stage of formation. At present, in many companies, the State is just a minority or blocking shareholder, which significantly limits its managerial capabilities. Thus, according to General Director of the above-mentioned Scientific and Production Center “Tekhnokompleks” G. Dzhandzhgava, the State did not hold a block of shares of a controlling size in any of the enterprises integrated in the company (probably, with the exception of the unitary enterprises). These blocks of shares varied between 15 and 49%. Therefore, control could be exercised only when the State and “Tekhnokompleks” itself join forces as shareholders⁶⁶.

In summer 2002, on the eve of JSC “Permskie Motory” being reorganized into “Federal’nyi Tsentri Dvigatellestroeniia” [Federal Engine Building Center], 37.2% of shares were held by the JSC “Permskii Motorny Zavod” [Perm Engine Works], 14.2% – by the State (managed by the RF Ministry of State Property), 5.9% – by “Moskovskii Federal’nyi Nauchno-Proizvodstvennyi Tsentri Imeni Khrunicheva” [Khrunichev Moscow Scientific and Production Center], 2.8% – by “Gazprom”, and the rest – by the minority shareholders, mostly former employees of the enterprise. For all this, “Permskie Motory” was, in effect, a managerial holding company not engaged in any production activity of its own, which held blocks of shares in the differently specialized enterprises spun off from it in the course of its restructuring. However, from the point of view of management, the holding company rather resembled a “soft” financial-production group of the mid-1990s, because the head company did not hold the controlling blocks of shares in its most successful enterprises (“Aviadvigatel” [Aircraft Engine], “Permskii Motorny Zavod” (“PMZ”), and “Proton-M”). In its turn, the controlling block of shares in

⁶⁶ Khikmatov T. Poka – trinadtsat’. [So far – thirteen.] // Izvestiia [News], 29 June 2002, p. 6.

“PMZ” was held by “Interros”, approximately 26% of shares – by the structures close to the JSC “Tekhnologii Motorov” [Motor Technologies], and 25% + 1 share – by the US company “Pratt & Whitney, one of the leaders of aircraft engine building.

It is typical that RF Deputy Minister of Property Relations N. Gusev has stated, at a meeting of shareholders, that neither the State nor the minority shareholders could decide anything, and that 95% of issues are resolved by General Director of “PMZ” Yu. Reshetnikov. In response, the latter accused the State of having abandoned the enterprise at the time of its privatization and of having been indifferent to its state until recently. As a result, by decision of the shareholders’ meeting, a new board of directors was elected, which then voted for the first vice-governor of Perm Oblast to become its head (an on example of regional authorities’ participation in managing economic societies without holding a stake in them), and confirmed the appointment of the new general director⁶⁷.

It is only in 4 out of those 9 OJSCs of the aircraft industry, whose federal blocks of shares were included, in 2006, in the charter capital of “OAK”, that the size of these stakes exceeds 51% (including the corporation “Sukhoi” where 100% of shares are in federal ownership), in 2 companies, the federal block of shares amounts to 38%, and in another 2 – to 25%. For all this, the non-government shareholders’ contribution could be made in the form of shares in 13 companies, including the five ones whose federal blocks of shares are being transferred into the charter capital of “OAK” as the State’s contribution.

Along with the objective difficulties dealing with the necessity to analyze the advisability and possibility of creating such structures, and with the restrictions resulting from the already implemented partial privatization, a major role is played by the problems of organizational character.

Thus, in 2005, shares in 68 joint-stock societies excluded from the privatization procedure in accordance with Decree of the RF Government, of 25 August 2004, № 1306-r, were subject to inclusion in the charter capital of integrated structures. In effect, this decision could not be

⁶⁷ Nikitin A. Vmesto deneg – plamennyi motor. {Instead of money – a flaming engine.} // Izvestia [News], 21 June 2002, p. 5.

materialized, because, so far as 62 companies were concerned, no decisions of either the RF President or the RF Government had been passed as to the creation of the integrated structures as such, and shares in another 6 joint-stock companies could not be privatized by this method in the prescribed time brackets for the absence, in the head structure, of a state-held block of shares, and because the State, as a shareholder, was incapable to determine the decisions of corresponding societies with regard to additional emission of shares. In effect, it has turned out that there were only 18 joint-stock companies whose shares were introduced in the charter capital of integrated structures.

The organizational difficulties emerging in the course of the creation of holding companies can be vividly exemplified by the non-implemented project concerning the establishment of a holding structure on the basis of the OJSC “Rossiiskaia Toplivnaia Kompaniia” (hereinafter the OJSC “Rostopprom”). There were some prerequisites for its having been created.

In 2002, by the results of an inspection initiated by “Gazprom”, the decision as to the early termination of the term of duty of the general director was passed. The decision was confirmed by the RF Presidential Administration and the RF Government. The RF Ministry of State Property positively estimated the activity of “Gazprom”, in the year 2003, as a sole executive body of the OJSCs “Neft” [Petroleum] and “Labinsknefteprodukt” [Labinsk Petroleum Products] (Krasnodar Krai), both of which were and still are 100% in federal ownership⁶⁸.

The project of creating the above mentioned integrated structure was coordinated with the RF Ministry of Power Engineering, the RF Ministry of Finance and the RF FAS, and then submitted, in the established procedure, to the RF Presidential Administration and the RF Government. Shares in the 77 open-end joint-stock companies of the fuel industry, created as a result of their transformation into federal state unitary enter-

⁶⁸ Kliuchevye problemy povysheniia effektivnosti upravleniia federal'noi sobstvennost'iu i osnovnye napravleniia dividendnoi politiki Rossiiskoi Federatsii. [Key problems involved in improving the efficiency of federal property management and the main directions of the Russian Federation's dividend policy.]. In: Vestnik Minimushchestva Rossii [Herald of the RF Ministry of State Property], 2003, No. 4, p. 15.

prises in 2002-2004, were planned to be included in the charter capital of “Rostopprom”, and therefore were excluded from the privatization procedure in February 2005. However, three months on, by order of the RF Government, the project of creating the integrated structure was returned for elaboration, because the RF Ministry of State Property had considered it unadvisable that the afore-said blocks of shares would be included in the charter capital of “the JSC “Rostopprom”. As a result, after a lengthy discussion under the aegis of the RF Ministry of Economic Development and Trade, the negative opinion as to the creation of an integrated structure on the basis of the “Rostopprom” did prevail, which led to the emergence of the plans for the subsequent privatization, in 2006, of shares in 77 joint-stock companies of the fuel industry.

Yet another example of the various problems emerging in the course of holding structures being created by the State is the 2006 project of creating a joint structure, “Natsional’naia Upravliaiushchaia Aeroportovaia Kompaniia” [National Managing Airport Company] on the basis of the OJSC “Mezhdunarodnyi Aerport Sheremetevo” [Sheremetevo International Airport] (with 100% of shares in federal ownership). “NUAK” could incorporate the largest Russian airports “Pulkovo” (St. Petersburg), “Tolmashiovo” (Novosibirsk), “Kol’tsovo” (Ekaterinburg), “Kurumoch” (Samara), and “Yemel’ianovo” (Krasnodar). However, chances for the practical realization of this project are rather slim.

Firstly, the creation of a new state-owned company for managing large airports could require a redistribution of competence, responsibility, and property between the state structures as two federal state unitary enterprises are already functioning in the sphere of airport activity. These enterprises are “Goskorporatsiis Grazhdanskikh Aeroportov (aerodroms)” [State Corporation of Civilian Airports (or Airfields)] and “Administratsiia Grazhdanskikh Aeroportov (Aerodromov)” [Civilian Airports (or Airfields) Administration] established , in 2001, on the basis of the exempted from privatization property of the airports “Bykovo”, “Vnukovo” and “Sheremetevo” (as regards such property, consolidation is not likely

to be confined to the property of the above Moscow airports, there are prospects for its being extended to other civilian airports as well)⁶⁹.

Secondly, one should bear in mind the ongoing discussion regarding the plans for privatizing a number of the most lucrative airports. Thus, one of the potential candidates for incorporation in the new state-owned company, Sochi Airport, has already been privatized after having been excluded from the list of strategic enterprises. In November 2006, 100% of shares in Sochi Airport were purchased for 5.503 billion roubles (the starting price was set at 3.504 billion roubles), at an auction, by the LLC “Strategiia Iug” [Strategy South]. The LLC “Strategiia Iug” is known as an affiliated structure of the company “Bazovyi Element” [Basic Element] which, via “Russko-Aziatskaia Investionnaia Kompaniia” [Russo-Oriental Investment Company], controls the holding company LLC “Aeroporty Iuga” [Airports of the South] already owning a significant number of specialized assets (“Avialinii Kubani” [Kuban Airports] and the OJSCs spun-off from it in the course of privatization – “Mezhdunarodnyi Aeroport Krasnodar” [International Airport “Krasnodar”], “Territorial’noe Agenstvo Vozdushnykh Soobshchenii “Kuban” [Territorial Agency of Air Communications “Kuban”, and “Iugstroj” [Southern Airport Construction Company]). Apart from this, “Aeroporty Iuga” controls the airport of Anapa⁷⁰ and is building a new airport at Gelendzhik.

The company “Bazovyi Element” is not alone in its interest in airport business. Thus, the company “Renova” holds approximately 45% of shares in “Aeroport “Kol’tsovo” [“Kol’tsovo” Airport] (Ekaterinburg) while “Moscovskoe Rechnoe Parokhodstvo” [Moscow Steam-Shipping Company] (“MRP”) owns, via “Evraziiskaia Aeroportovaia Kompaniia” [Eurasian Airport Company], 42% of shares in the OJSC “Aeroport Tolmachevo” (Novosibirsk) and 48% of shares in “Aviappredpriatie “Altai”

⁶⁹ It should be pointed out that runways, taxiways, dispatcher equipment and other property directly relating to air traffic cannot be privatized and remain state property, which requires that specialized state organization should manage it. In an event of privatization the new owners will acquire the rights to an airport building, and in some cases – also to the adjoining territory.

⁷⁰ Anapa Airport has been placed on the list of strategic joint-stock companies (the state stake in its charter capital amounts to 25.5 %).

[Aviation Enterprise “Altai”]. Like the airport of Anapa, the airports “Kol’tsovo” and “Tolmachevo” are on the list of strategic joint-stock companies, however, it should be pointed out that the State’ stake in the former (34.5% of shares) is exceeded by that of private shareholders, whereas the state stake in the latter (51% of shares) makes the State a full-fledged majority shareholder. As reported, the same interest is manifested with regard to Khabarovsk Airport by “Gruppa Al’ians” [Group “Alliance”] and is reflected in the project of integrating the airports “Yemel’ianovo” and “Cheremshanka” (Krasnoiar’sk Krai) into a single hub, a company where 45% of shares would be owned by private shareholders, and another 45% – by the State. The project was initiated by the holding company “AirUnion” created on the basis of the airline company “KrasAir”.

The issue of the airport “Pulkovo” (St. Petersburg) where 50% of shares are claimed by the city authorities, could be considered under the same angle. However, the decision on the size of the block of shares to be owned by the city and on the mode of paying for it is yet to be taken⁷¹.

According to existing estimates, the reason for the current growth in interest to investing in the large airports claiming the role of hubs⁷², is competition for the budget funds which would be allocated to modernize and to build these objects, first of all, in their airfield part (for example, “Kol’tsovo”, Sochi, and Gelendzhik)⁷³.

For all this, it should be borne in mind that a mere transfer of a state-owned block of shares to a holding company cannot resolve the issue of effectively managing this block of shares. Also, the case in point is the

⁷¹ Vremia stroit’ aeroporty. [It’s time to build airports] // SNIP. Stroitel’stvo. Nedvizhimost’. Investitsii. Proekty. [Construction. Real Estate. Investments. Projects.] No. 02 (02), December 2006, p. 18–22.

⁷² In international practice, a hub is an airport hosting a considerable number of international and domestic airlines, providing passengers with opportunities for a quick change from one flight to another and complying with modern standards for infrastructure and ground services.

⁷³ Khoziaeva vozduzhnykh vorot planiruiut potratit’ na ikh modernizatsiiu sotni millionov dollarov. [The owners of air gates are planning to spend hundreds of millions of dollars on their modernization] // SNIP. Stroitel’stvo. Nedvizhimost’. Investitsii. Proekty. [Construction. Real Estate. Investments. Projects.], No. 02 (02), December 2006, p. 24–27.

extent of influence that would be exerted by the State on the holding company's activity. However, one of the recent studies devoted to the problems of corporate governance⁷⁴ indicates that the role of the State as an initiator of creating holding companies is very limited; moreover it considerably differs from the function of a controller because of its strong branch specificity. Out of the JSCs integrated into holding companies on initiative of the federal or regional authorities, 37 (or more than 80%) remain under control of the State, while out of the 18 JSCs integrated into the holding on the basis of a joint initiative of the holding company's owners and the State, only 8 (or less than 45%) remain under its control. The role of the State as an initiator of creating holding companies significantly varied from branch to branch; moreover, to a certain extent it was determined by the general situation at the time when one or another holding company was being formed. The federal authorities initiated more than one half of all such structures created before 1992; however, less than 3% of the 190 enterprises integrated into holdings after 1992, indicated that they had been created on initiative of the federal or regional authorities. The federal authorities initiated the integration into holdings of almost one half of the fuel and energy complex's enterprises, which, for the most part, took place in the year 1992, and of 30% of enterprises in the sphere of communications. In the rest of the branches, instances of the bodies of authority being involved in creating holding companies and in making one or another enterprise to join them, were rare and sporadic.

On the whole, the research covered 64 of the JSJs integrated into the holding companies controlled by the State (more than 21% of the total amount of enterprises integrated into holding companies)⁷⁵. Of these companies, 28 (or 43.8%) belonged to the communications industry, 23

⁷⁴ Integratsionnye protsessy, korporativnoe upravleniie i menedzhment v rossiiskikh kompaniiakh. [Integration processes, corporate governance and management in Russia companies]. Series "Nauchnye doklady: nezavisimyi ekonomicheskii analiz. [Scientific reports: an independent economic analysis], No. 180. M., Moscow Public Science Foundation; ANO "Proekty dlia budushchego: nauchnye i obrazovatel'nye tekhnologii", 2006, pp. 125, 158.

⁷⁵ A total of 39.2% of all the sample's enterprises were part of a holding (in industry – 35.7%, and in communications – 77.5%).

(or 35%) – to the fuel and energy complex, 6 (or 9.4%) – to machine building and metal processing, 4 (or 6.3%) – to the food industry, 1 – to metallurgy, the chemical, petrochemical, and the production of building materials industries each. There were no such holding companies in the timber, timber-processing, cellulose-and-paper production industries and light industry. The holding companies accounted for 85.5% of the workforce of the communications industry, for 55.5% of that of the fuel and energy complex, for 7.6% of that of the chemical and petrochemical industries, for 6.8% of that engaged in machine building and metal processing, and for less than 5% of that of the production of building materials and food industries and of that engaged in metallurgy.

According to another study based on the analysis of the same sample⁷⁶, almost one half of the companies with state stakes are integrated into holding companies, although only 60% of the respondents have indicated that control exercised over these companies is that of the State. At the state stake's size of less than 10%, only one half of these companies ((from the number of those integrated into various holding companies) are members of holding companies, however just 60% of the respondents have stated that control over the activity of their holding companies is in the hands of the State. At the state stake's size of between 10 and 25%, the proportion of such companies is less than 20%, and when the size of the state stake is between 25 and 50%, their proportion is approximately 70%. If the State holds a controlling block of shares, the said proportion is 90%. These data could be interpreted as indirect evidence of the "hidden privatization" of a holding company.

As is justly noted by Migranov (Migranov, 2005), in this case, proceeds from privatization are equal zero, because property is gratuitously transferred to a juridical person which possesses the uncontested right to realize it. Therefore, the economic advisability of state property (in-

⁷⁶ S. B. Avdasheva, T. G. Dolgopiatova, and X. Plines, "*Korporativnoe upravleniie v AO s gosudarstvennym uchastiiem: rossiiskie problemy v kontekste mirovogo opyta*". [*Corporate Governance in Joint-Stock Companies with State Participation: Russian Problems in the Context of Global Experience*]. Preprint WP1/2007/01. Series WP1. InstitutSIONal'nye problemy rossiiskoi ekonomiki. [Institutional Problems faced by the Russian economy]. M., SU-HSE, 2007, p. 38.

cluding state-held blocks of shares (or shares or stakes)) being contributed to the charter capital of economic societies (or holding integrated structures) is rather questionable. The extent of the state authority bodies' influence on the decisions being passed by these economic societies (or integrated holding structures) in the course of corporate governance procedures could turn out to be insufficient to block the probable subsequent decisions of the administrative bodies of such companies aimed at alienating the formerly state-owned property which has become property of economic societies (or holding integrated structures), or to pressure them into passing realistic decisions on disbursement of dividends. And it should be remembered that all this would be taking place against the general background of the low effectiveness of financial and economic activity so typical of many economic societies with state stakes (including holding companies).

The poor showing of state holding companies in the 2000's is vividly illustrated by the case of the already mentioned FSUE "Rosspirtprom". The enterprises of the alcohol and liquors industry incorporated into this holding company did not manage to improve their situation: a lot of them were on the brink of bankruptcy, while some enterprises have intentionally been driven into financial crisis. "Rosspirtprom" concentrated its main efforts on increasing its sphere of influence, which resulted in a number of loud scandals. Thus, as many as 6 meetings of shareholders took place at Moscow "Kristal" alone. As of the end of 2001, the legal department of the holding company was simultaneously involved in 157 court proceedings⁷⁷.

The difficulty for "Rosspirtprom" to exert its managerial influence on the enterprises results from the fact that the State holds the controlling blocks of shares only in some of them. Most of such enterprises are alcohol distilleries. Thus, out of 60 enterprises of the alcohol branch whose stakes of shares have been purposefully consolidated in state ownership and have not been intended for early sale under Decree of the RF Government, No. 784, of 17 July 1998 (an overall majority of these enter-

⁷⁷ Smovzh M. "Rosspirtprom" vozglavil general. [A general has been appointed to head "Rosspirtprom"] // Izvestia [News], 30 July 2002, p. 2.

prises are alcohol distilleries), there are only 10 enterprises with a state stake of less than 51%. So far as the liquor plants and wineries are concerned, it was not infrequently that the state stake was less than one half of shares (we have already cited the example of the OJSC “VINAP” in the city of Novosibirsk); the situation was further aggravated when the powers for the management of a state-owned block of shares were split.

Moreover, the creation of “Rosspirtprom” was in direct contradiction with the interests of those regional administrations and local businesses with the links thereto, for whom control over the alcohol industry had become, in the 1990s, one of the major instruments of economic policy (including budget formation) and a means of rented behavior. As an example of local authorities’ response to the creation of “Rosspirtprom” one could cite the selling of the fixed assets (including the immovable property) of the OJSC “Omsklikervodka” [Omsk Liquors and Vodka] to a local unitary enterprise being part of Omsk Oblast property. The sale has practically completely devalued the controlling block of shares that was potentially due to the all-Russian holding company. Previously, the interests of the State in managing this block of shares were represented by the Oblast Property Fund and a number of departments of the Omsk Oblast administration.

The auditors of the Audit Chamber have come to the conclusion that the FSUE “Rosspirtprom” created in spring 2002 failed to efficiently manage the alcohol industry and to increase the receipts of the federal budget. Out of 154 million roubles of profits received by the FSUE in 2001, only 4.6 million (or 3%) was transferred to the budget. Dividends on the shares in wine- and vodka producing JSC, transferred into operative management to the holding company (17.5 million roubles) also did not reach the treasury. All the way long, “Rosspirtprom” was actively establishing new juridical persons so as to close on them all major flows of goods in the course of products realization. The former managers of the enterprise who had become owners of valuable vodka assets withdrew the trading house of “Rosspirtprom” from state ownership by selling 75% for 7.5 million roubles. By the same method, several more enterprises were also withdrawn from state ownership only to be integrated into the commercial structure “Grad”. Without the owner’s consent, the property

of an affiliated company of “Lipetsspirom” was sold for 56 million roubles, to be paid, by installments, until 2010.

In 2001, the OJSC “Simbirsk Spirt [Simbirsk Alcohol] integrating 7 alcohol distilleries and liquor plants in Ulianovsk Oblast was divided into “Simbirsk-Spirom” (2 liquor plants and “Ulianovskii Spirtzavod” [Ulianovsk Alcohol Distillery]) and Ulianovsk-Spirt” (4 village alcohol distilleries). The reorganization was initiated by a company close to the former management of the FSUE “Rosspirtrom” which managed 51% of the state-owned shares in the OJSC “Simbirsk-Spirt”. As a result, both newly established enterprises had to launch bankruptcy proceedings. According to the minority shareholders, they were organized owing to artificially increasing the accounts payable and to selling imported alcohol at a time when the stores were overstocked with local output. On the passing, by the Ulianovsk Oblast Court of Arbitration, the decision that “Simbirsk-Spirom” should be deemed to be bankrupt (May 2003), production was discontinued and property arrested. Having been valued at 140 million roubles, it was bought, in early 2004, for 160 million roubles by the Moscow firm “InDel” (only two bidders took part in the auction)⁷⁸.

In response to the negative results of the holding company’s functioning, the RF government had to intensify the regulation of its activity. By Order of the RF Government, of 29 October 2002, No. 1512-r, “On the Introduction of Alterations in the Charter of the FSUE “Rosspirtrom”, the holding company was deprived of the right to be independently credited, to include in the agenda of shareholders’ meetings the issues regarding the election of the boards of directors and the election of the executive bodies of the JSCs whose shares have been transferred into the charter capital of the FSUE, and to terminate the term of duty of the management of the affiliated enterprises. All these actions should, thereafter, be carried out only on permission of the RF Government which would recommend the shareholders’ meetings of the afore-said JSCs the size of the dividends, and would take the decisions concerning the introduction of any changes in their charters and charter capital. The appointment of the

⁷⁸ Pribyl’noe delo [Profitable business] // Priamye investitsii [Direct Investments], No. 2 (22), 2004, p. 58.

general directors of all the 18 affiliates, as well as of the deputy director general and the accountant general of the holding company itself should be coordinated with the RF Ministry of Agriculture. Previously, “Rosspirtprom” had a limited say only in the matters pertaining to additional share issuing or conversing shares into bonds⁷⁹.

The RF Government justified such actions, first of all, by the necessity to reduce the number of premeditated bankruptcies in the alcohol industry, and by the fact of the numerous financial violations which had been uncovered by the RF Audit Chamber and the new management of the holding company. These violations had resulted in the budgetary losses in the amount of almost 200 million roubles⁸⁰.

The former management of “Rosspirtprom” accused of withdrawing its assets and of redirecting the finance flows generated by the selling of output, to outside firms, was replaced in July 2002. However, the activity of the holding company remained low effective, as was testified by the fact that the share of marketed counterfeit products was still very high and that the RF Audit Chamber had to investigate the same problem once again.

At the 12 March 2004 meeting of the Collegium of the RF Audit Chamber (AC) it was noted that since 2001, “Rosspirtprom” had not been transferring, to the federal budget, dividends on the blocks of shares transferred into operative management thereto. The checking of the implementation of the AC Collegium’s decisions taken by the results of the 2002 control measure indicated that the RF Ministry of State Property, the RF Ministry of Agriculture, and “Rosspirtprom” had failed to eradicate the uncovered violations. The 36-million-roubles dividends on the blocks of shares transferred into operative management to “Rosspirtprom” had not been transferred in full to the budget. A number of JSCs whose blocks of shares had been transferred into its operative management exhibited a pronounced worsening of financial and economic indicators. One of the reasons for this was the sales policy pursued by the

⁷⁹ Smovzh M. Za butylku. [For a bottle]. // *Izvestiia* [News], 1 November 2002, p. 6.

⁸⁰ Smovzh M. “Rosspirtpromu” ne zaschitali. [No set-off for “Rosspirtprom”]. // *Izvestiia* [News], 30 November 2002, p. 5.

OJSCs “Moskovskii Zavod “Kristall” and “Samarskii Kombinat “Rodnik” [Samara Integrated Works “Rodnik”] resulting in the incomes having been redistributed in favor of the wholesaler and the retailer at the expense of the producer whose share of income in the retail price of output amounted to less than 3% against a 40-percent share of profits from sales. The Collegium of the AC took a decision to issue the order, to “Rossirtprom”, to the effect that the dividends on the blocks of shares be transferred to the budget; to submit corresponding recommendations to the RF Ministry of Economic Development and Trade, the RF Ministry of Agriculture, and “Rossirtprom”, to submit a corresponding memorandum to the RF Ministry of Economic Development and Trade, and to submit a report on the audit performed to both Chambers of the RF Federal Assembly⁸¹.

In 2006, on the entry into effect of the Law “On the State Regulation of the Selection of Alcohol- and Alcohol-Containing Products”, the alcohol products market plunged into a crisis caused by the interruptions in the work of some production lines owing to a shortage of excise stamps and the consequences of the introduction of the State Single Excise System. Once again the authorities began to ponder the issue of introducing state monopoly. In the event such plans come true, it would require the establishment of a state alcohol company [Gosudarstvennaia Alkogol’naia Kompaniia, GAK] to be engaged in the realization of alcohol products. In these conditions, the SUE “Possirtprom” took the decision to launch production of the so-called “people’s vodka”. Vodka under the “Rossirtprom” brand will be distributed throughout the country at a price no higher than 60 roubles for half a liter. The disbursing price will amount to 53 roubles, thus covering, according to representatives of the distillery, only the taxes and the production costs. However, the plans of “Rossirtprom” are even more ambitious. Its managers have decided to diversify the assortment of “people’s vodka” by such popular varieties as “Khlebnaia” [Grain], “Pshenichnaia” [Wheat], “Rzhanaia” [Rye],

⁸¹ Daidzhest zasedanii Kollegii Schetnoi Palaty RF [Digest of the Collegium of the RF Audit Chamber’s meetings] // Finansovyi kontrol’ [Financial Control], 2004, No. 4 (29), p. 91.

“Kedrovaia” [Cedar], and [Solodovaia” [Malt]. According to experts, launching the new varieties of vodka could well result in a redistribution of the market, because many producers are weakened by the consequences of the crisis⁸².

As of the end of 2006, the FSUE “Rosspirtprom” managed the blocks of shares in more than 200 enterprises engaged in distilling alcohol and producing alcoholic beverages (against 118 as of early 2003). The FSUE accounts for more one third of all legal producers of alcohol and spirituous liquors in the country and controls more than 45% of Russia’s alcohol production and 26% of its spirits-making products output. The annual turnover of the FSUE is estimated at more than 2 billion USD. For the purpose of comparison, it could be noted that by the results of 2001, 76 enterprises of “Rosspirtprom” accounted for approximately 40% of all national output of products of spirits-making, and for 40.8% of the aggregate amount of excises paid by all Russian distilleries to the budgets of all levels⁸³.

1.4. The Role of the State as a Shareholder from the Point of View of Profit-Making and Influencing the State of the Budgetary System

It can be said with confidence that the State’s being more energetic in its role of a shareholder in the post-2000 period has been a major success from the point of view of increasing budget receipts from dividends.

1.4.1. General Characteristics of Transfer of Dividends to the Federal Budget

Since the late-1990s the RF Government has begun to deem dividends on the state-owned stakes as a crucial renewable source of budget revenues. *Table 29* below provides the dynamic of main parameters that char-

⁸² *K chemu privediot vypusk “narodnoi vodki” ? [What will result from the production of “people’s vodka” ?],* www.rian.ru, 22 November 2006.

⁸³ Smovzh M. “Rosspirtprom” vozglavil general. [A general has been appointed as the head of “Rosspirtprom”] // *Izvestiia [News]*, 30 July 2002, p. 2.

acterize the growth in the respective transfers over the past decade and their significance for the federal budget.

Table 29

The Dynamic of Dividends Transfers of to the Federal Budget in 1995–2007

Year	The number of JSC that transferred dividends to budget, as units*	Amount of transfers		The rate of fulfillment of the budgetary assignment, as %	The proportion of dividends transferred to the budget, as %			
		As RUR m. **	As % to the prior year		in revenues fixed by the respective RF Public Property Management Agency (Goskomi-muschestvo (1995–1997), the RF Ministry for State Property (1997–2000), the RF Ministry of State Property (2000–2004), The RF Ministry of State Property (2004–2007))		In the federal budget revenues	
					In revenues from renewable sources of public property	In aggregate revenues of public nature	From the use of public property or related activity	In non-tax revenues
1995	...	115.0/ 92.8#	...	-	54.6	1.9	2.8	0.27
1996	35	118.9#	103.4	-	34.8	8.2	2.2	0.28
1997	157	270.7#	227.7	-	47.0	1.45	5.9	0.63
1998	280/200/ 273	574.6	212.3	-	31.5	3.3	12.2	1.32
1999	246/ 600	1304.3/ 848.1	227.0	87.0	/9.7***	/4.9***	17.6/ 11.5****	2.65/ 1.72****
2000	488/1050	5676.5/ 3675.1	435.2	112.1	/19.6***	/7.3***	18.0/ 11.6****	7.6/ 4.9****
2001	734/ 782	6478.0	176.3	323.9	22.2	16.5	11.4	5.6
2002	747/ 749	10402.3/ 10259.5	160.6	137.7	28.9/ 28.5***	20.5/ 20.1***	13.1/ 12.9****	6.8/ 6.7****
2003	597	12395.8/ 12395.2	119.2	109.0	30.4	9.1	11.0	7.0
2004	319	17228.2/ 17222.0	139.0	137.8	34.6	14.4	10.0	7.7
2005	...	18610.0	108.0	109.5	34.2	20.8	...	...
2006	...	23000.0	123.6	100.0	34.0	26.6	...	...
2007	...	...	...	24080.0##	...	...	...	...

* – data: on 1996 – from Rossiiskaiia ekonomika v 2002 godu. Tendentsii i perspektivy. [The Russian economy in 2002. Trends and prospects]. (Issue 24). (2003, p. 367); on 1997 and 1998–2002 (in numerator), 2003 – from «Predpriyatiya s gosudarstvennym

uchastiyem» (2004, p. 48); on 1998-2001 (in common denominator) – from *Rossiiskaiia ekonomika v 1999 godu. Tendentsii i perspektivy*. [*The Russian economy in 2001. Trends and prospects*]. (Issue 24). (2003, p. 367) and *Rossiiskaiia ekonomika v 2005 godu. Tendentsii i perspektivy*. [*The Russian economy in 2001. Trends and prospects*.] (Issue 27). (2006, pp. 415–416), the data on 1998 (273 units) – from *Klyucheveye problemy* (2003, p. 16); on 2002 (in common denominator) – from Medvedev (2003, p. 32); on 2004 – from the materials for the RF Government’s meeting on 17 March 2005 “On measures designed to improve the efficiency of federal property management”;

** – data: on 1995–1996 – data from the official website www.mgi.ru, on 1997–1998. – from Medvedev (2003), on 1999–2004 – from the acts on execution of the federal budget; the data referred to in the common denominator for 1995 – from: *Rossiiskaiia ekonomika v 2002 godu. Tendentsii i perspektivy*. [*The Russian economy in 2001. Trends and prospects*.] (Issue 24). (2003, p. 367), on 1999 and 2000 – from Medvedev (2003), on 1999, 2000, 2003 – from *Predpriyatiya s gosudarstvennym uchastiyem»* (2004, p. 48), on 1999, 2000, 2002 and 2004 – from the materials for the RF Government’s meeting on 17 March 2005 “On measures designed to improve the efficiency of federal property management”, (for reference);

*** – the proportions were computed on the basis of the data of the RF Ministry of State Property and Materials for the RF Government’s meeting on 17 March 2005 “On measures designed to improve the efficiency of federal property management”, which are located in the common denominator in the respective lines of the third column, for 2004 – the diff between the values in the numerator and common denominator is insignificant and it does not affect the designed values;

**** – the proportions were computed on the basis of the data located, accordingly, in the numerator and common denominator in the respective lines of the third column, respectively, for 2003, 2004 – the diff between the values in the numerator and common denominator is insignificant and it does not affect the designed values;

– data: for 1995–1997 – in the post-1998 denomination numeraire;

– an absolute value of dividends on state-owned shares, as planned in the budget (as RUR m.).

Source: www.mgi.ru; Medvedev Yu. M. *Itogi deiyatel’nosti Minimushchestva Rossii i ego territorial’nykh organov za 2002 god I zadachi na 2003 god*. [Results of the activity of the Ministry of State Property of Russia and of its territorial agencies in the year 2002 and the tasks for the year 2003] // *Vestnik Minimushchestva Rossii* [Herald of the RF Ministry of State Property], 2003, No. 1, p. 31–32; *Rossiiskaiia ekonomika v 2002 godu. Tendentsii i perspektivy*. [*The Russian economy in 2001. Trends and prospects*.] (Issue 24). M., IET, February 2003; *Klyucheveye problemy povysheniya effektivnosti upravleniya federalnoy sobstvennostyu i osnovnye napravleniya dividendnoy politiki Rossiyskoy Federatsii* // *Vestnik Minimushchestva Rossii* [Herald of the RF Ministry of State Property], 2003, No. 4, p. 12–20; *Predpriyatiya s gosudarstvennym uchastiyem. Institucionalo-pravovye aspekty i ekonomicheskaya effektivnost*. Series «Nauchnye doklady: nezavisimyy ekonomicheskyy analiz», No. 155. M.: Moskovsky publchny nauchny fond; Assotsiatsia issledovateley gosudarstvennoy sobstvennosti, 2004, p. 48; V. L. Nazarov. *Administrativnaya reforma i*

upravleniye gosudarstvennoy sobstvennostyu // Upravleniye sobstvennostyu, 2005, No. 1, p. 6; Materials for the RF Government's meeting on 17 March 2005 "On measures designed to improve the efficiency of federal property management"; Rossiiskaiia ekonomika v 2005 godu. Tendentsii i perspektivy. [The Russian economy in 2001. Trends and prospects]. (Issue 27). M., IET, March 2006, pp. 415–416; Rossiiskaiia ekonomika v 2006 godu. Tendentsii i perspektivy. [The Russian economy in 2001. Trends and prospects.] (Issue 28). M., IET, March 2007; V.L. Nazarov's interviews to INTERFAX agency of 23 January 2007 and "Boss" monthly, February 2007 r., www.rosim.ru; Rossiysky statistichesky ezhegodnik 2006: Stat. sb../ The Goskomstat of Russia. M., 2006, p. 615; the authors' estimations.

While in 1996 there were just 35 open-end joint-stock companies (OJSC) that paid dividends on the state-owned stakes, there were over 700 of them in 2001–2002. The figure became the peak value over the decade in question. Between 1995 and 1999 the volume of dividend transfers to the federal budget grew 11.3 times, while between 1999 and 2004 – 13.2 times (including over the comparable 4-year time interval between 1999 and 2003 – 9.5 times). Meanwhile, by contrast to the late 1990s, inflation rates were moderate in the past 5-6 years. The greatest growth rates in dividend transfers fell on 1997 and 1999 (roughly accounting for 2.3 times) and 2000 (over 4.3 times). Post-2000, the annual dynamic of growth in dividend payments demonstrated a gradual deceleration of its growth rates, except for 2004 (the increment accounted for over 39% that year) and 2006 (over 23%, albeit these are preliminary data).

The noted positive dynamic is undoubtedly associated with a growing proactive stance of the federal government and its agencies (the RF Ministry of State Property) in charge of property management in particular. However, it can be assumed that this notable advancement in terms of growth of dividend payments on federal stakes has been propelled both by a more intense work with the stock issuers and objective processes that took place in the national corporate sector in the early 2000s (suffice it to mention the corporate governance policy and the one focused on growth of capitalization pursued by a number of large corporations, pressure on the part of holding companies, and cuts of the tax rates on dividends). Meanwhile, one cannot help but take into account the fact that a more proactive stance of the government as a shareholder in this aspect helps improve standards of corporate governance, as recipients of divi-

dividend payments have become other categories of shareholders, while accents shifted from generating receipts from property in favor of legal sources, rather than withdrawal of financial flows via false firms. Since 2000 budgetary tasks on dividend transfers on the state-owned stock have been beaten regularly, though with a different degree of success, while in 1999 the same assignment was fulfilled just at 87%⁸⁴. The peak of over-fulfillment of the budgetary order fell on 2001 (over 3.2 times), while 2002 and 2003 were also notable in this respect, as the budgetary task was outstripped at some 38%.

The specific weight of dividends in the aggregate volume of property-based revenues administered by the federal property management agency grew over 10 times in the past decade and reached 20.8% in 2005 vis-à-vis 1.9% in 1995. At this point, it should be noted that there were repetitive fluctuations and changes in the vector of the trend. Thus, in 1996 the rate of the indicator was 8.2% and it plunged dramatically to under 1.5% a year later. In the next three years the proportion of dividends in the aggregate volume of revenues from privatization and the use of public property was gradually growing, but it was only in 2001 when it exceeded its 1996 level and reached 16.5%. The next year, the respective index overshot the 20% barrier, but in 2003 it fell down more than twice (roughly to 9%). Finally, in 2004–05 it began to grow once again and bounced back to its 2002 maximum. Underlying such fluctuations was, largely, a different significance of all the renewable revenues from the use of public property (including dividends), whose proportion was quite understandably growing in the years when there were no privatization deals and declining when such deals took place.

Considering the role dividends played in the structure of renewable revenues alone, one cannot help noting a steady positive growth in the specific weight of dividends over the whole period following the renewal of economic growth in 1999. In 2004–06, their proportion in all the renewable revenues was over 34% vs. 9.7% reported in 1999. Of course, from the purely formal perspective, one can note a coincidence between

⁸⁴ Until 1999 in the federal budget acts dividends on the state-owned shares were not singled out as a separate revenue item in the list of revenues from the use of the state-owned property that fell under non-tax budgetary revenues.

the 2004–06 results with those registered in 1996 and 1998. In 1997, dividends accounted for 47% of all the renewable assets, while in 1995 – 54.6%. But such record-breaking results of the late-1990s were determined by the narrow base that generated renewable revenues, and it *de-facto* also included revenues from the federal property lease (mostly real estate). A whole range of other sources began to generate revenues later, including proceeds from Vietsovpetro (since 1998), revenues from land leases and transfers of a part of profits by public unitary enterprises (since 2001). Furthermore, the rise of new sources of renewable revenues in 2001 did not form an obstacle to the continuing trend to growth in the proportion of dividends in their structure.

That is why one-third of renewable revenues secured by dividend transfers over recent years has appeared far more important a contribution than analogous (and even more voluminous) values of the late-1990s. The rise in the proportion of dividends in the aggregate volume of renewable revenues evidences greater growth rates of this kind of revenues compared with other kinds of revenues. This allows asserting a higher quality of the government's management of public shares vs. other assets. At this point, of course, it is the quality of assets and the magnitude of their use by the state for the sake of revenues that matter. Obviously, the PUE sector (compared with economic companies with the government stake in them) is dominated by far less profitable and liquid economic subjects. With intensification of the process of demarcation of the public property for land one should expect a greater role of the rental payments for public land.

The dynamic of the growing role of dividends in the federal budget revenues from the use of property owned by the state or from the related activities basically proves the conclusion of a greater role this particular source with regard to public finance. Between 1995 and 1996 dividends accounted for less than 3% of such revenues, in 1997 the respective index grew up to 6%, in 1998 – over 12%. The greatest proportion of dividends in the amount of the noted revenues was reported in 1999-2000 (17–18%). It consequently plunged to 10–13% reported between 2001–2004, however, at this point, it should be noted that the national statistics employs quite a peculiar category of revenues to the budgetary system from

the use of property or related activities. Such a category does not include revenues from property sales, which, along with sales of public reserves, since 1999 have fallen under the sources of financing of the nation's budget deficit. The proportion of dividends in the aggregate volume of nontax revenues to the federal budget displayed yet a greater growth, that is, 5.6–7.7% post-2000 vis-à-vis less than 0.3% in 1995–1996 and 1.3% in 1998.

Meanwhile, it should be remembered that dividends constitute just one of components of renewable revenues from the state property use, which form an element of all non-tax revenues that play a fairly limited role, so far as formation of the federal budget is concerned.

The objective assessment of the role dividends play for the federal budget requires comparison of their value with other comparable sources of property-based revenues. The latter group comprises profit of the Russian side in Vietsovpetro joint venture and PUEs' transfers of a fraction of their profits, among others. In both cases we speak of public revenues that result from operations performed by economic agents that function in a manner similar to that of economic companies with the state share and chiefly in the competitive environment on markets for goods and services. This situation differs notably from the one associated with generation of budget revenues from leasing various kinds of property (mostly real estate and land lots), with the state being a passive collector of rental payments, rather than a contributor to organization of its corporate tenants' business processes.

Table 30

Significance of Dividends vs. Other Sources of Renewable Revenues to the Federal Budget and Amount of Cash Flows in the Economy in 1995–2005

Year	RURm.	Transferred dividends relative to		
		Some renewable revenue sources of the federal budget		% of the funds forwarded on dividend payments and interest by main sectors of the economy *
		% to the share of profit of the Russian participant in Vietsovpetro	Transfers of a part of profit by OUE	
1995	115.0#	...	–	0.5
1996	118.9#	...	–	2.7
1997	270.7#	Revenues were not adminis-	–	4.8

Transferred dividends relative to				
Year	RURm.	Some renewable revenue sources of the federal budget		% of the funds forwarded on dividend payments and interest by main sectors of the economy *
		% to the share of profit of the Russian participant in Vietsovpetro	Transfers of a part of profit by OUE	
		tered by the RF Ministry of State Property		
1998	574.6	73.4	–	7.0
1999	1304.3/ 848.1**	/14.9***	–	6.2/4.0****
2000	5676.5/ 3675.1**	/31.4***	–	16.1/10.4****
2001	6478.0	47.6	30.9 times greater	7.6
2002	10402.3/ 10259.5* *	77.7/76.6***	11.4/11.2*** times greater	10.3/10.2****
2003	12395.8/ 12395.2* *	76.5	5.2 times greater	...
2004	17228.2/ 17222.0* *	100.2	6.8 times greater	...
2005	18610.0	106.4	7.8 times greater	...

* – industrial sector, agriculture, construction, transport, communication, trade and public catering, wholesale trade with production and technical goods, the sector for housing and public utilities and amenities;

** – in numerator – by the data from the acts on execution of the federal budget in 1999–2004, in common denominator – by the data of The RF Ministry of State Property and Materials for the RF Government’s meeting on 17 March 2005 “On measures designed to improve the efficiency of federal property management”;

*** – the proportions were computed on the basis of the data of the RF Ministry of State Property and Materials for the RF Government’s meeting on 17 March 2005 “On measures designed to improve the efficiency of federal property management”, which are located in the common denominator in the respective lines of the second column, on 2003 and 2004 – the diff between the values in the numerator and common denominator is insignificant and it does not affect the designed values;

**** – the proportions were computed proceeding from the data contained, accordingly, in the numerator (the data from the acts on execution of the federal budget) and common denominator (the data of The RF Ministry of State Property and Materials for the RF Government’s meeting on 17 March 2005 “On measures designed to improve the efficiency of federal property management”) of the respective lines of the second column, for 2003 and 2004 – the diff between the values in the numerator and common denominator is insignificant and it does not affect the designed values;

– data: for 1995–1997 – in the post-1998 denomination numeraire;

Source: the 1999–2004 acts on execution of the federal budget; Klyuchevye problemy povysheniya effektivnosti upravleniya federalnoy sobstvennostyu i osnovnye napravleniya divididendnoy politiki Rossiyskoy Federatsii // Vestnik Minimushchestva Rossii [Herald of the RF Ministry of State Property], 2003, No. 4, p. 5; www.rosim.ru; Materials for the RF Government’s meeting on 17 March 2005 “On measures designed to improve the efficiency of federal property management”; Finansy Rossii: Stat. sb./ The Goskomstat of Russia. M., 1998, p. 98–101; Finansy Rossii: Stat. sb./ The Goskomstat of Russia. M., 2000, p. 126–129; Finansy Rossii. 2002: Stat. sb./ The Goskomstat of Russia. M., 2003, p. 130–133; Rossiyskiy statisticheskiy ezhegodnik 2006: Stat. sb./ The Goskomstat of Russia. M., 2003, p. 578; Rossiiskaiia ekonomika v 2005 godu. Tendentsii i perspektivy. [The Russian economy in 2001. Trends and prospects] (Issue 27). M., IET, March 2006, pp. 415–416; the authors’ estimations.

According to *Table 30*, the volume of dividends from the state participation in corporate capital actually transferred to the federal budget between 1997 and 2003 was steadily inferior to budget revenues from operations of a sole joint venture, that is, Vietsovpetro. Thus, in 1998 the volume all dividends from the use of state property and related activities accounted for 73.4% of dividends from the company’s operations, while the 1999 index was below 15%. The gap had been reducing slowly but steadily from 1999 on, and in 2004–2005 the volume of dividends transferred to the federal budget finally exceeded the one formed by dividends paid by Vietsovpetro. Meanwhile, volumes of dividend transfers from the state participation in capital were far greater than the overall amount of the fractions of the PUEs’ profits transferred to the budget. While in 2001–03 the gap between revenues from the two sources was reducing, it began widening again between 2004–05 and accounted for 6.8–7.8 times vs. 5.2. times reported in 2003.

It is worth assessing the “weight” of dividends transferred to the federal budget from the perspective of the national economy on the whole. To do this, one can compare their amount with that of cash forwarded on dividend payments and interest by its main sectors.

The data of *Table 30* evidence that yet prior to the 1998 crisis, in the conditions of then ongoing slump and arrears crisis, there had been noted a gradual rise in the specific weight of dividends transferred to the federal budget in the total volume of cash which enterprises of main sectors of Russia’s economy allocated to pay dividends and interest. The value of this indicator grew from 0.5% in 1995 up to 7% in 1998. The next year,

battered by the crisis, it plunged to 4%. The 1998 value was surpassed in 2000-2002, with the value of the indicator in the latter period exceeding 10%. The analysis of its consequent dynamic appears complex, as it has appeared missing in recently published statistical reports.

It would be more correct, of course, to compare dividend transfers with the amount of cash channeled solely for the sake of dividend payments, exclusive of interest, but the Russian statistics provides the value of the indicator without making such a separation. That is why the only option left is to try to compare the data on dividend transfers to the federal budget with expert assessments of dividend payments across the economy as a whole.

The analysis of the aggregate growth in dividend payments by 95 companies (by the comparable array of enterprises) over 2001–02 showed that their value grew 2.63 times and made up RUR 8,2665m vs. 3,1413m reported in the prior year. Interestingly, the respective increment indicator would have been somewhat more moderate (at 71%), if we excluded abnormally great dividends paid by Sibneft (RUR 28,969m). As a reminder, 2002 became the first year that saw a dramatic rise in dividend payments by Russian corporations on the whole, which was not associated with depreciation of the national currency or a drastic change of the enterprises' financial performance (as it was noted in the wake of the 1998 crisis)⁸⁵. By comparing these indicators with the data on dividend transfers to the federal budget in the respective years, one can estimate their proportion to be 20.6% in 2001 and 12.6% in 2002. The contribution of companies with the state participation appears far more modest if one compares the volume of dividends transferred to the federal budget with the total value of cash allocated for dividend payments by all the issuing companies whose shares trade in the stock market (the USD-equivalent estimate by *Commerzant-Daily*, September 2004). In this particular case the propor-

⁸⁵ Danilov Yu.A. Osnovnye tendentsii dividendnoy politiki rossiyskikh predpriyatiy v 2002 godu, Doklad na seminare GU-VShE "Institutsionalnye problemy rossiyskoy ekonomiki", 2003.

tion of dividends transferred to the federal budget would be: in 2000 – some 13.5%, 2001 – 6.7%, 2002 – 7.4%, 2003 – 6.4%.⁸⁶

Finally, yet another illuminating comparison that illustrates the weight of dividends transferred to the federal budget can be the one between their forex-denominated equivalent and dividends payable by overseas corporations of similar status. The dividends transferred to the federal budget made up: in 2003 – USD 420.89 m, in 2004 – 620.64 m.⁸⁷ For reference, the 2001 dividends paid by public companies in New Zealand accounted for USD 506.3 m⁸⁸. Thus, it can be reckoned that given Russia's public sector being far greater in size, to say nothing of the size of Russia's economy, vis-à-vis New Zealand's it was only in 2004 that the volume of the respective indicator overran the volume of dividend payments by public companies of the small insular state⁸⁹.

1.4.2. Factors Affecting Dividend Transfers to the Federal Budget

The main factors that determine the direct value of dividend revenues to the budget are: (1) the potential dividend base (the value of net profit of JSCs with the state share in them) as a derivative from the overall financial and economic state of such companies and their quality of corporate government on the whole; (2) the amount of the stake belonging to the state; and (3) the level of manageability of such stakes on the part of the state (what can be provisionally labeled as the “dividend discipline”). Having no data on the aggregate size of the potential dividend base across all the JSCs with state participation, let us try to analyze the impact of the other two factors.

⁸⁶ The estimates do not pretend to be highly accurate, due to possible inaccuracies associated with the date of the use for their sake of the USD/RUR exchange rate.

⁸⁷ Gazetov A., Ditrich E., Kotlyarova A., Skripichnikov D. *Doklad po korporativnomu upravleniyu gosudarstvennymi predpriyatiyami v Rossii// Krugly stol Rossii po korporativnomu upravleniyu, 2–3 iyunya 2005 g.* (in the framework of the TACIS program and the Global Forum on Corporate Governance).

⁸⁸ *Enterprises with state participation* (2004, p.118).

⁸⁹ To ensure a complete accuracy of the comparisons, one can also account transfers of a part of the PUEs profits to the federal budget (USD 81.7m in 2003). Thus, it can be maintained that the aggregate volume of transfers by JSC and PUE categories (less revenues generated by Vietsovpetro's operations) in Russian budget (USD 501.96m) has caught up with that of New Zealand (506.3m) as early as in 2003.

The critical factor that determines the receipt by the federal budget of dividends is the size of stock packages owned by the state. This is illustrated below (*Table 31*).

Table 31

Structure of Dividends Transferred to the Federal Budget vs. the Proportion of Shares in Federal Property

The amount of the proportion of shares in the federal property	The number of OJSC, of S that transferred Dividends, as units		The sum of the transferred dividends, as RUR m				The specific weight of OJSC with a certain share of RF in the overall volume of transferred dividends, as %	
	2002	2003	total		by 1 OJSC on average		2002	2003
			2002	2003	2002	2003		
	100%	29	29	1826.6	2807.1	63.0	96.8	17.6	22.6
between 50% and 100%	203	147	3134.9	3945.7	15.4	26.8	30.1	31.8
between 25% and 50%	343	262	4330.6	4084.1	12.6	15.6	41.6	32.9
Under 25%	171	159	1110.2	1558.3	6.5	9.8	10.7	12.7
Total	747	597	10402.3	12395.2*	13.9	20.8	100.0	100.0

* – the amount of dividends transferred in 2003 as cited in *Predpriyatia s gosudarstvennym uchastiyem*, appears somewhat different from the value contained in the act on execution of the 2003 federal budget (RUR 12395.8 m).

Source: *Predpriyatia s gosudarstvennym uchastiyem*. *Institutsionalno-pravovye aspekty i ekonomicheskaya effektivnost*. Series “*Nauchnye doklady: nezavisimy ekonomicheskyy analiz*”, No. 155. M.: *Moscovsky publichny nauchny fond; Assotsiatsiya issledovately ekonomiki gosudarstvennogo sektora*, 2004, p. 50, the authors’ estimations.

As shown in *Table 31*, over 89% of all the dividend payment in 2002 and 87% of those in 2003 the federal government received from OJSCs wherein the state owned over 25% of stock. It was OJSCs with the size of the state-owned stake between 25 and 50% that proved to be the most profitable for the budget, with their proportion in the total amount of the respective budget revenues accounting for 41.6% in 2002 and some 1/3 in 2003. Given the contraction in the specific weight of such OJSCs, there occurred a notable (at 5 p.p.) growth in the specific weight of OJSCs with the 100% state-owned stake (from 17.6% up to 22.6%). Meanwhile, the

contribution of other categories of OJSCs with the RF's share in their capital posted a more moderate growth: thus, the specific weight of the OJSCs with the state-owned stake under 25% grew by 2 p.p. (from 10.7% up to 12.7%), while that of the OJSCs with the state-owned stake between 50% and 100% rose at 1.7 p.p. (from 30.1% up to 31.8%).

Speaking of growth in dividend payments in absolute (not adjusted to inflation) terms, it should be noted that with a general 19% rise in them across all the mass of OJSCs with the federal stakes, it was its poles that posted an advanced growth in terms of the payments in question: while OJSCs with the 100% state stake secured a 53% growth in their dividend payments, those with the state-owned minority blocks posted a 40% growth in dividend payments. Revenues from the OJSCs with the state-owned control bloc grew by 26%, while from the OJSCs with the blocking stock owned by the state fell by 5.7%. With the overall number of OJSCs that paid dividends in favor of the federal budget sliding by 1/5, the number of such OJSCs with the control and blocking stakes fell by more than 23% (56 units) and 27.5% (81 units), respectively. The reduction in the proportion of OJSCs that paid dividends in the group of the OJSCs with the government-owned minority stake was less dramatic and accounted for 7% (12 units), while the number of the OJSCs with the 100% state-owned stake that paid dividends to the federal budget remained unchanged (29 units).

The data on the amount of actually transferred dividends per 1 OJSC appear quite illustrative. They evidence that the amount of dividend payments grows along with the growth in the size of the federal package in a company. The average dividend payment per 1 OJSC with the 100% state control appeared 9.7–9.9 times greater than the respective index of the OJSCs with a minority state-owned stake, 3.6–4.1 times greater than that of the OJSCs with the state-owned control bloc and 5.0–6.2 times greater than that of the OJSCs with the state-owned blocking stake in them. It is also interesting that while in 2002 the gap in terms of amounts of payments per 1 OJSC between the companies with the state control bloc and those with the state-owned blocking stake was less than between the companies with the state blocking stakes and those with the state minority stakes, there was no visible difference between them in 2003.

The indicator of the dividend discipline as an expression of the quality of management of state-owned assets in the corporate sector should be considered a specific weight of JSCs from which the federal budget received dividends in the overall mass of all the companies with state-owned shares in them (*Table 32*).

Table 32

**Dividend Base and Dynamic of Dividend Transfers
to the Federal Budget in 1995–2004**

Pe- riod	The number of JSC that transferred dividends to the federal budget		The amount of dividend revenues	
	total, units.	% of the overall number of JSC with federal stakes	RUR m	Per 1 JSC with federal stakes
1996	35	...	118.9	3.40
1997	157	2.4	270.7	1.72
1998	280	5.8	574.6	2.05
1999	246	5.0/ 5.5/6.3*	848.1**	3.45
2000	488	12.5	3675.1**	7.53
2001	734	20.8	6478.0	8.83
2002	747	16.95	10402.3	13.93
2003	597	14.1	12395.2*	20.76
2004	319	8.6	17228.2	54.00

* – estimated proceeding from different data on the number of JSC with federal stakes between late-1998 and early-1999;

** – cited in *Predpriyatia s gosudarstvennym uchastiyem (2004)* amounts of dividends transferred in, 1999, 2000, 2003 differ from values stipulated in the acts on execution of the federal budget for the respective years.

Source: *Predpriyatia s gosudarstvennym uchastiyem. Institutsionalno-pravovye aspekty i ekonomicheskaya effektivnost. Series “Nauchnye doklady: nezavisimy ekonomichesky analiz”, No. 155. M.: Moscovsky publichny nauchny fond; Assotsiatsiya issledovately ekonomiki gosudarstvennogo sektora, 2004, p. 50; Materials for the RF Government’s meeting on 17 March 2005 “On measures designed to improve the efficiency of federal property management”;* the authors’ estimations.

The data above evidence that already in the late-1990s, despite a general weakening of the state machinery, there occurred a steady rise in the absolute number of JSCs that transferred dividends to the budget. Thus, in 1998, their number was 8-fold greater than in 1995, and it was only in 1999, as an effect of the 1998 crisis, that it dropped by 12% (to 246

units). Given the above, the number of such JSCs did not exceed 7–8% of the total number of JSCs with a state stake in their capital.

After the Concept of Management of State Property and Privatization in 1999 was approved, the federal authorities' efforts in the respective areas allowed some progress, particularly in terms of expansion of coverage of the corporate sector with measures that ensured dividend payments to the federal budget. In 2000, the number of JSC that paid dividends to the federal budget nearly doubled, and the next (2001) year saw a notable (over 1.5 times) growth of this indicator, too. It is indisputable that underlying the process was the renewal of economic growth in the country, however, one should not count out the government's efforts as well.

But after the peak values registered in 2000–2002 (over 700 JSCs) the number of JSCs that were paying dividends began to decline quite notably. In 2004, there were only 319 of them, which made up the smallest figure over the whole 5-year period (2000–04), thus just a bit over the worst value registered in the crisis 1998 (280 units). Nearly a double contraction in the number of JSCs that paid dividends to the federal budget in 2004 vs. 2003 (597 units) cannot be compared with the intensity of the analogous phenomenon of 1999. Such a situation cannot be considered normal in the conditions of continuation of economic growth. Quite symptomatic phenomenon became a shrinking coverage of the corporate sector with the state participation with measures that resulted in dividend payments to the budget. While in 2000 over 1/5 of such JSC paid dividends to the budget, in 2004 their proportion accounted for just 8.6%, which is less than the 2000 indicator (12.5%) and just slightly greater than the respective indicators of the late-1990s.

None the less, the increment in the absolute value of the indicator of dividend payments to the budget per 1 company that effected such a payment continued. It was especially notable (2.6 times) in 2004 vs. 2003, while in 2002–03 the value of the indicator was within the range between 50 and 60%. In the late-90s, it was 1998 and 1999 that saw a substantial increment in dividend payments to the budget (1.7 times and 2.2 times, respectively), but it was clearly driven by inflationary processes fueled by the financial crisis and its consequences. Plus, it was preceded by nearly a double fall in dividends per 1 company in 1997 vs.

1996. It was only in 1999 when the 1996 level, in absolute terms, was reached once again.

The above evidences a shift in the federal authorities' focus in their pursuance of the dividend policy in 2003–2004 onto a narrow group of companies that paid dividends, which allowed fulfillment of the budgetary order without employing serious efforts on tightening the “dividend discipline” and expansion of the coverage of the corporate sector with the respective measures, as it had occurred in the late-90s and in 2000–02.

With account of the above, there arises the question as to how the fall in the proportion of JSCs with the state stake in their capital that paid dividends to the budget is related to the size of the proportion.

Table 33

**The Degree of Coverage of OJSC Whose Shares
Are Owned by the State with Dividend Payments
to the Budget in 2002–2003**

Data and size of the shares owned by RF	The number of OJSC, whose shares are in the property of RF, total, units	The number of OJSC, that paid dividends	
		units	As % of the total number
As of 01.01. 2002:	4407	in 2002: 747	16.95
100%	90	29	32.2
between 50% and 100%	646	203	31.4
between 25% and 50%	1401	343	24.5
under 25%	2270	171	7.5
As of 01.01. 2003:	4222	in 2003: 597	14.1
100%	99	29	29.3
between 50% and 100%	589	147	24.95
between 25% and 50%	1382	262	18.95
under 25%	2152	159	7.4

Source: www.rosim.ru; Predpriyatiya s gosudarstvennym uchastiyem. Institutionalno-pravovye aspekty i ekonomicheskaya effektivnost. Series “Nauchnye doklady: nezavisimyy ekonomicheskyy analiz”, No. 155. M.: Moscovskyy publichny nauchny fond; Assot-siatsiya issledovately ekonomiki gosudarstvennogo sektora, 2004, p. 50; the authors' estimations.

As follows from *Table 33*, in 2003, the specific weight of the OJSCs from whom the federal budget received dividend payments accounted for 14.1% against nearly 17% reported in 2002. Like the indicator of payments per 1 OJSC, it was directly proportional to the state-owned stake in

such companies' capital. The greatest proportion of OJSCs that paid dividends was noted among 100% state-owned companies (29.3%), while the respective index for OJSCs with the state-owned control bloc was under ¼, for those with the state-owned blocking stake – under 19%, and for OJSCs with the state-owned minority stake – 7.4%.

It is worth noting that 2003 vs. 2002 saw a fall in the level of the “dividend discipline” practically across all the categories of OJSCs, except for those wherein the state was a minority shareholder. As concerns OJSCs with the state-owned control bloc that paid dividends, their proportion in the total number of companies of this particular category dropped by 5–6 p.p. (24.95% vs. 31.4% reported in the prior year). A similar phenomenon was noted with regard to OJSCs with the state-owned blocking stake (24.5% vs. 18.95% reported in the prior year), while in the group of OJSCs which are at 100% state-owned the fall was a bit lesser (29.3% vs. 32.2%). In 2003 vs. 2002, there widened a gap in terms of the proportion of OJSCs that paid dividends between OJSCs with blocking state-owned stakes and those with the state-owned minority blocs, as well as between OJSCs with 100% state-owned stakes and those with the government control stake, albeit in the latter case the gap was minimal under a relatively great degree of coverage with dividend payments (over 30%). The above data form yet another proof of the critical role played by the size of the state-owned stake, so far as dividend payments to the budget are concerned, and highlight a fairly poor performance of the state as an assets manager, even providing the state is a majority or even a sole shareholder in a company.

As shown above, it is civil service represented by various ministries and agencies' staff that exercise practical control over federal stakes. In this respect, it is interesting to examine the distribution of dividends paid by JSCs with a federal stake in terms of agencies that exercise control over them (*Table 34*).

The data above constitutes yet another adequate illustration of the extent to which Russia's economy appears dependent on the fuel and energy complex: as much as 73% of all dividends received in 2003 by all the federal stakes was secured by companies under the RF Ministry of Energy. As concerns other payers of dividends, it is worthwhile noting the

RF Ministry of Finance and the RF Ministry of Transportation whose JSCs secured over 15% and 3.8% of the total volume of received dividends, respectively. The specific weight of other ministries and agencies accounted for less than 1%. It was the Department of Property of the RF Ministry of State Property who should be given most of credit for such an impressive performance. The Department in question controlled 797 OJSCs and 1 closed-end joint stock company (CJSC) (“ALROSA”) and interacted with 7 bodies of the national executive power (the RF Ministry for Nuclear Energy, the RF Ministry for Natural Resources (geology), the RF Ministry of Finance (diamond complex and gold-mining industry), the RF Ministry of Energy, the Federal Energy Commission, the State Technical Supervisory Body, the State Nuclear Supervisory Board). In 2003, public companies under the RF Ministry of Property paid dividends worth a total RUR 9,603.597m (77.5% of all the dividend revenues to the federal budget), or at 1,103.597m (or 13%) more than the planned value⁹⁰.

Table 34

The Largest Payers of Dividends to the Federal Budget in 2003 in Terms of their Departmental Subordination

Agency	The number of subordinated JSC as of end-2003	Dividends paid in 2003, as RUR Thos.		Proportional weight of dividends received from OJSCs controlled by a given department in the total volume, as %
		total	Averaged per 1 OJSC	
Ministry of Energy of RF	706	9,046,596	12,813.9	73.0
Minfin RF	33	1,866,674	56,565.9	15.05
Ministry of Transportation of RF	417	468353	1,123.1	3.8
the RF Ministry of Agriculture	441	71,100	161.2	0.6
Ministry for Economic Development and Trade of RF	207	18,458	89.2	0.15
The RF Defense Ministry	33	13,500	409.1	0.1
Ministry of Railway Transportation of RF	17	988	58.1	0.0
Ministry of Health Care of RF	6	860	143.3	0.0

⁹⁰ Tikhonov A.V. Departament toplivno-energeticheskogo kompleksa (on materials of the report at the meeting of the RF Ministry of State Property of May 21, 2003. In: Vestnik Minimuschestva Rossii [Herald of the RF Ministry of State Property], 2003, No. 2, p.35

Agency	The number of subordinated JSC as of end-2003	Dividends paid in 2003, as RUR Thos.		Proportional weight of dividends received from OJSCs controlled by a given department in the total volume, as %
		total	Averaged per 1 OJSC	
Ministry of Natural Resources of RF	80	55	0.7	0.0
The RF Russian Land Cadastre Agency	15	0	0	-
Ministry of Education of RF	3	0	0	-
Ministry of Culture of RF	2	0	0	-
The RF Ministry of Interior	1	0	0	-
Ministry of Labor of RF	1	0	0	-
Ministry of Emergency Situations of RF	0	0	0	-
Ministry of Justice of RF	0	0	0	-
The Goskomstat RF	0	0	0	-
Other agencies	1,993	908,659	455.9	7.3
Total	3,955	12,395,243*	3,134.1	100.0

* – cited in *Predpriyatiya s gosudarstvennym uchastiyem* (2004) amounts of dividends transferred in 2003 differ from values stipulated in the acts on execution of the 2003 federal budget (12,395,832 RUR Thos.).

Source: *Predpriyatiya s gosudarstvennym uchastiyem. Institutsionalno-pravovye aspekty i ekonomicheskaya effektivnost.* Series “Nauchnye doklady: nezavisimy ekonomicheskyy analiz”, No. 155. M.: Moscovskyy publichnyy nauchnyy fond; Assotsiatsiya issledovately ekonomiki gosudarstvennogo sektora, 2004, p. 50; the authors’ estimations.

As concerns the value of the indicator of payments per 1 subordinated JSC, it was companies controlled by the RF Ministry of Finance that demonstrated the best performance (RUR 56.6m), thus being nearly 4.5 times ahead of companies controlled by the RF Ministry of Energy (12.8m). The third place was held by companies under the RF Ministry of Transportation (1.1m), or more than 11-fold inferior to the companies under the RF Ministry of Energy. Other JSCs under other ministries and energies lagged far behind the leading group with their, at least, RUR 0.5m in dividends paid to the federal budget. Finally, another three ministries and agencies paid more than RUR 100,000 in dividends to the federal budget, namely, the RF Ministry of Defense (409.1 Thos.), the RF Ministry of Agriculture (161.2 Thos.) and the RF Ministry of Health Care (143.3 Thos.). The leading positions held by JSCs under the RF Ministry

of Finance appear quite natural due to their profile (extraction, processing and sales of precious stones and metals). One cannot help paying attention to the fact that, while exceeding the number of JSCs under the RF Ministry of Transportation (441 vs. 417), those under the RF Ministry of Agriculture fell behind 6.5 times in terms of paid dividends and by payments per 1 JSC – 7 times. Yet a far wider gap (some 20-fold) is noted in terms of payments per 1 JSC between companies under the RF Ministry of Transportation and the RF Ministry of Railway Transportation. Let us note that in this particular case we consider comparable kinds of operations, which, by their profile, are quite distinct from kinds of operations of companies that report to the RF Ministry of Finance and the RF Ministry of Energy.

The Russian Federal Property Fund has also contributed to the pursuance of the dividend policy. According to the Fund⁹¹, in 2001, as many as 420 joint-stock companies ruled to pay dividends. The total amount of dividends on the state stakes controlled by the RFPF accounted for RUR 1, 281m, or 1.7 times more than in 1999, with the respective reports on dividends by the state-owned stakes being submitted monthly to the Accounting Chamber. More specifically, on the AC's request, it received materials on OJSCs "Sayanskkhimprom", "Eletctozavodholding", "Turbo-motorny zavod" (Ekaterinburg), "Nevsky zavod" (St. Petersburg), "Kombinat "Yuzhuralnickel" (Chelyabinsk oblast).

1.4.3. The Place and Role of Individual Companies as Payers of Dividends

As noted above, the federal authorities' dividend policy has recently demonstrated an implicit shift of the focus onto work with a narrow group of corporate dividend payers. That is why it is particularly interesting to examine data on the largest dividend payers to the federal budget on the microeconomic level (*Table 35*).

⁹¹ Fatikov V: Chasto dlya prodazhi nam peredayut doli polubankrotov//Finansovye Izvestia [News], 5 Feb 2002, p. 1

Table 35

**Dynamics of Dividend Transfers to the Federal Budget
on the Part of the Largest Payers in 2001–2004**

Company	The size of the state-owned stake, as %	2001, As RUR m.	2002		2003		2004		
			As RUR m.	As % to 2001 r.	As RUR m.	As % to 2002	As RUR m.	As % to 2003	As % to 2001
OJSC "Gasprom"	38.37	2,089.38	3,781.94	181.0	3,455.00/ 3,633.71*	91.3	5,930.8 2	171.65	283.85
OC "Rosneft"	100.0	800.0	1,100.0	137.5	1,344.00/ 1,500.00*	122.2	1,410.0 0	104.9	176.25
JSC "Transneft"	75.00	634.01	1,272.42	200.7	1,222.08/ 1,300.03*	96.0	2,377.0 9	194.5	374.9
OC "LUKOIL"	7.60	517.11	911.82	176.3	1,186.45/ 1,260.45*	130.1	1,461.0 7	123.1	282.5
Company of project privatization	100.0	0	303.52	+	303.52				
RAO "UES Russia"	52.55	160.0	883.78	552.4	801.10*	90.6	...	...	...
Oil and gas company "Slavneft"	74.95	605.79	605.79		100.0		Federal package sold in December 2002		
CJSC "ALROSA"	37.00	10.00	312.04	3120.4	247.51/ 259.00*	79.3	321.01	129.7	3210.1
TVEL	100.0	154.81	210.00	135.7	230.00*	109.5	250.00	108.7	161.5
"Aeroflot-Russian Airlines"	51.17	17.05	34.10	200.0	154.93/ 164.82*	454.3	229.72	148.3	1347.3
International Airport "Sheremetyevo"	100.00	50.00	100.00	200.0	100.0**	100.0**	100.0	100.0**	200.0
"Sovkomflot"	100.00	70.00	70.00	100.0	70.0**	100.0**	65.80	65.8**	94.0
"Irkutskenergo"	40.00	56.22	38.10	67.8	69.7**	182.9**	...	...	...
"Tekhnabexport"	100.00	16.71	28.20	168.8	65.0**	230.5**	109.64	168.8	656.1
Novorossiysk sea merchant port (NSMP)	20.00	54.97	54.97	100.0	54.33**	98.8**	...	...	...
Vneshtorgbank	99.95	...	...	...	1,505.56	...	1,510.0 9	100.3	...
JSC "Transneftepordukt"	100.00	...	...	...	188.00	...	94.00	50.0	...
Magnitogorsk Metallurgical Kombinat (MMK)	17.82	...	...	...	...	...	282.00	...	...
JS Holding Company "Sukhoi"	100.00	...	...	...	...	...	186.41	...	...
Transcreditbank	75.00	...	...	...	...	...	106.02	...	...
Total by 15 companies		5,236.05 #	9,709.67	185.4 #	10,597.88 **	109.1 **	14,433. 67	136.2 **	276.0
For reference: by all JSC that transferred dividends		6,478.0	10,402.3	160.6	12,395.2 ***	119.2	17,228.2	139.0	265.9

* – for reference: the common denominator contains data dividends by the 2002 results that were due to be transferred to the 2003 federal budget, for companies of the project

privatization, RJSC “I UESRussia” and TVEL the volume of transferred funds matched that of payments due;

** – for OJSCs “Sheremetyevo”, “Sovkomflot”, “Irkutskenergo”, “Tekhsnabexport”, NSMP, due to the absence of data on the actual amount of dividend transfers to the 2003 federal budget, the authors used the data on the 2003 dividends due, which were also employed in computations of the 2002 dividends due for the purpose of comparison with the respective 2002 and 2004 data, both by each company and by the group of the 15 largest payers;

*** – the data on the largest payers of dividends in 2003 cited from *Государственным участникам* (2004), which contains the amount of dividends transferred in 2003. The 2003 data appears somewhat different from the value stipulated in the act on execution of the 2003 federal budget (RUR 12,395.8m), however, the difference is not fundamental, as long as the subsequent conclusions and calculations are concerned;

– for 2001 – the data on just 14 companies (exclusive of OJSC “Company of Project Privatization») were employed both for the sake of computations and comparison with the 2002 data.

Source: Materials for the RF Government’s meeting on 27 November 2005 “On the process of implementing the decisions of the Government of the Russian Federation designed to improve the efficiency of federal property management and on the main directions of the dividends policy”; *Государственным участникам. Институционально-правовые аспекты и экономическая эффективность*. Series “Nauchnye doklady: nezavisimyy ekonomicheskyy analiz”, No. 155. M.: Moscowsky publichny nauchny fond; Assotsiatsiya issledovateley ekonomiki gosudarstvennogo sektora, 2004, p. 50; Materials for the RF Government’s meeting on 17 March 2005 “On measures designed to improve the efficiency of federal property management”; the authors’ estimations.

In 2003–04, there were 5 Russian companies whose dividend payments to the federal budget were in excess of RUR 1bn (RAO Gasprom, Transneft, Vneshtorgbank, Oil Company LUKOIL, and Oil Company Rosneft, while there was just 1 such company in 2001 (Gasprom, and 3 in 2002 – Gasprom, Transneft and Rosneft. The latter two companies, together with LUKOIL and Slavneft in 2001–02, RAO UES Russia (in 2002–03) and Privatization Project Company (2003) formed the group of companies whose dividend transfers to the federal budget made up between RUR 500m and 1bn.

Whilst considering the aggregate dynamics of transfer dividends to the federal budget in 2001–04, the indisputable leaders were ALROSA and Aeroflot-Russian Airlines whose 2004 dividend payments exceeded those made three years before 32.1 and 13.5 times, respectively. Such a phenomenal performance is explained, primarily, by an extremely low

benchmark of 2001. The next group, in terms of the dynamic of dividend transfers, is formed by Tekhsnabexport (the 6.6-times growth) and Transneft (3.7 times) – the growth rates of their respective indicators were also far ahead of other JSCs that paid dividends. Gasprom and LUKOIL's performance (the growth in transferred dividends 2.8 times) was just slightly greater than by all JSC and the 15 largest payers (roughly 2.6–2.8 times). The worst dynamic (*vis-à-vis* the general one) of dividend transfers in 2004 vs. 2001 was displayed by Sheremetyevo, Rosneft and TVEL (2 times) and less, while Sovkomflot even reported contraction in its dividend payments in absolute terms. Such comparisons cannot be made by a whole range of other companies, due to the absence of comparable data.

Whilst analyzing the annual dynamic of dividend transfers, one can note that in 2002 practically all the largest payers reported growth in their volume but Irkutskenergo (a drop at one-third), Slavneft, Sovkomflot and NMTP (remained unchanged). The leading group comprised ALROSA (31.2 times up) and RAO UES Russia (5.5. times up)⁹². Meanwhile, the increment in Rosneft and Tvel's dividend transfers (37.5% and 35.7%, respectively) proved to be lesser than that by the group of companies that paid dividends (58.4%).

In 2003, Gasprom, Transneft, RAO UES Russia and Alrosa decreased the volume of their dividend transfers to the federal budget, with ALROSA making that to the greatest extent (at over 20%). The increment rate of TVEL's dividend transfers (9.2%) was lower than that by all the companies that paid dividends (20.8%). LUKOIL and Rosneft in this respect found themselves in a slightly better situation, with their respective indicators accounting for 30.1% and 22.2%, accordingly, while Aeroflot-Russian Airlines, Tekhsnabexport and the Project Privatization Company formed a leading group with their respective indices making up 4.5 times, and 2.3 times, respectively.

The 2004 leaders became Transneft (with its 94.5% growth rate in dividend transfers to the federal budget), Gasprom (71.1%) and Tekhsna-

⁹² Exclusive of Project Privatization Company, which displayed an impressive absolute increment in the volume of transferred dividends vs. 2001, when it had not paid any.

bexport (nearly 69%). The noted values were notably in excess of growth rates across all the OJSC that paid dividends (39%). Aeroflot also became a model company that displayed growth rates in its dividend transfers at the level over the average one (48.3%), while dividend transfers by ALROSA and LUKOIL grew at less impressive rates (29.7% and 23.1%, respectively). The group of clear outsiders in this regard comprised TVEL, Rosneft and Vneshtorgbank that managed to boost up their dividend transfers at a rate under 10%, which, given inflation rates on the consumer market, to say nothing of the deflator of GDP, actually meant their fall. Given the price dynamics for oil and petroleum derivatives on the international and domestic markets, LUKOIL and Rosneft fell short of justifying everybody's expectations. Finally, two companies found their dividend transfers on the decline: Sovkomflot reduced them by one-third, while Transneft- as much as twice. By results of 2003 the latter channeled a meager 3% of its net profit on dividend payments, which can be explained by the company's independent implementation of large-scale infrastructural projects (construction of an oil products pipeline and an oil storage facility).

As concerns other particularities with respect to dividend transfers noted in the period between 2001 and 2004, one can note their unchanged volume on the part of Sheremetyevo (RUR 100m) and large payments effected by Slavneft in 2001–02 and MMK in 2004, i.e. on the eve of the sales of state-owned blocs of shares in the companies. One cannot help but get surprised at seeing that the 2004 list of the largest payers of dividends lack two nationwide natural monopolists – RAO UES Russia (which was the sixth biggest dividend payer just a year before that) and OJSC “Russian Railways” established in 2003.

An important aspect of the analysis of efficiency of management of the federal stakes is the comparison of dynamics of dividend transfers across corporate payers classified into groups by the size of dividend transfers.

Table 36

Comparative Dynamics of Dividend Transfers to the Federal Budget in 2001–2004 by Groups of Companies

Group of companies	2001,	2002		2003		2004		As % to 2001
	As RUR m.	As RUR m.	As % to 2001	As RUR m.	As % to 2002	As RUR m.	As % to 2003	
The largest payer "Gasprom"	2,089.38	3,784.94	181.2	3,455.0	91.3	5,930.82	171.65	283.85
Payers ranked 2 nd to 5th	2,556.91	4,168.02	163.0	5,258.08	126.15	6,758.25	128.5	264.3
5 largest payers	4,646.29	7,952.96	171.2	8,713.08	109.6	12,689.07	145.6	273.1
Payers ranked 6 th to 10th	496.0	1,531.35	308.7	2,171.93	141.8	1,269.14	58.4	255.9
10 largest payers	5,142.3	9,484.3	184.4	10,885.0	114.8	13,958.2	128.2	271.4
Other JSCs whose stock is owned by the state	1,335.7	918.0	68.7	1,510.2	164.5	3,270.0	216.5	244.8
For reference: all OJSCs that transferred dividends	6,478.0	10,402.3	160.6	12,395.2*	119.2	17,228.2	139.0	265.9

* – the data on the largest payers of dividends in 2003 cited from *Predpriyatia s gosudarstvennym uchastiyem* (2004), which contains the amount of dividends transferred in 2003. The 2003 data appear somewhat different from the value stipulated in the act on execution of the 2003 federal budget (RUR 12,395.8 m), however, the difference is not fundamental, as long as the subsequent conclusions and calculations are concerned.

Source: Materials for the RF Government's meeting on 27 November 2005 "On the process of implementing the decisions of the Government of the Russian Federation designed to improve the efficiency of federal property management and on the main directions of the dividends policy"; *Predpriyatia s gosudarstvennym uchastiyem. Institutsionalno-pravovye aspekty i ekonomicheskaya effektivnost. Series "Nauchnye doklady: nezavisimyy ekonomicheskyy analiz"*, No. 155. M.: Moscovskiy publichny nauchny fond; *Assotsiatsiya issledovately ekonomiki gosudarstvennogo sektora*, 2004, p. 50; Materials for the RF Government's meeting on 17 March 2005 "On measures designed to improve the efficiency of federal property management"; the authors' estimations.

As evidenced by the *Table 36* above, in all, over the period between 2001 and 2004 the volume of transferred dividends slightly grow by the groups comprising the 5 and 10 largest dividend payers (at over 70% vs. 66% by all JSCs that transferred dividends to the budget). By contrast, as concerns the group of companies that formed the second quinary and

those not included in the group of the top ten companies in terms of the volume of dividend payments, their respective increment rates proved to be somewhat lower (56 and 44.8%, respectively).

Meanwhile, the dynamic of dividend transfers could vary from year to year. Thus, in 2002, with an absolute fall in the volume of dividends transferred by the companies that were not included in the noted Top Ten, the first and second quinquaries displayed an advanced growth in their dividend payments (at 71.2% and more than thrice, respectively). Overall, the dividend transfers to the federal budget in 2002 grew by 60.6% vs. 2001. In 2003, on the contrary, it was the companies from the 2nd quinary and those that failed to get to the Top Ten that became locomotives of the increment (41.8% and 64.5% up, respectively), while transfers by the 5 and 10 largest payers grew at a rate lower than that of all the JSC that paid dividends (at 19.2%). In 2004, the advance growth rates were posted by companies that were not included in the Top Ten (2.17 times) and the 5 largest payers (at 45.6%). One cannot help but note a drastic fall (at 42%) in dividend transfers from companies that were not included in the 2002 Top Ten and the second quinary of companies in 2004 vs. 2001 and 2003, respectively.

The dynamic of dividend payments displayed by companies ranked the 2nd to the 5th in terms of value of the indicator. In 2004 vs. 2001 they were on the rise at a rate roughly equal to that of all the group of JSCs that paid dividends to the budget (2.64 times vs. 2.66 times). Their dynamic was a bit lower than Gasprom's (2.84 times), but greater than other companies' ones. In 2002 vs. 2001 the group in question increased their transfer payments at a rate lower than Gasprom's (63% vs. 81.2%) and the 2nd quinary of companies' (more than thrice), but greater than the whole group of JSCs that paid dividends (at 60.6%) In 2003, due to the fall in its dividend transfers in absolute terms vs. 2002, Gasprom naturally found itself lagging behind the companies ranked the 2nd to the 5th, which in terms of their increment rates of dividend transfers still lagged behind the second quinary of companies (at 41.8%) and, at the same time, was ahead of the whole group of JSCs that effected such transfers (at 19.2%). In 2004, on the contrary, the group concerned boosted up the increment of their dividend payments by 28.5%, albeit fell short of catch-

ing up with Gasprom's 71.1% increment and the group of all the JSCs that effected such transfers (39%), but ultimately found itself ahead of the second quinary of companies whose transfers fell in absolute terms.

Table 37

Comparative Dynamics of Dividend Transfers to the Federal Budget in 2001-2004 per 1 JSC by Groups of Companies

Group of companies	2001,	2002		2003		2004		
	As RUR m.	As RUR m.	As % to 2001	As RUR m.	As % to 2002	As RUR m.	As % to 2003	As % to 2001
The largest payer "Gasprom"	2,089.38	3,784.94	181.2	3,455.0	91.3	5,930.82	171.65	283.85
Payers ranked 2 nd to 5th	639.2	1,042.0	163.0	1,314.52	126.15	1,689.56	128.5	264.3
5 largest payers	929.26	1,590.6	171.2	1,742.6	109.6	2,537.81	145.6	273.1
Payers ranked 6 th to 10th	99.2	306.27	308.7	434.39	141.8	253.83	58.4	255.9
10 largest payers	514.23	948.4	184.4	1,088.5	114.8	1,395.82	128.2	271.4
Other JSCs whose stock is owned by the state	1.84	1.25	67.9	2.57	205.6	10.58	411.7	575.0
For reference: all OJSCs that transferred dividends	8.83	13.93	157.8	20.76	149.0	54.0	260.0	611.55

Source: Materials for the RF Government's meeting on 27 November 2005 "On the process of implementing the decisions of the Government of the Russian Federation designed to improve the efficiency of federal property management and on the main directions of the dividends policy"; Predpriyatia s gosudarstvennym uchastiyem. Institutsionalno-pravovye aspekty i ekonomicheskaya effektivnost. Series "Nauchnye doklady: nezavisimiy ekonomicheskyy analiz", No. 155. M.: Moscovskiy publichny nauchny fond; Assotsiatsiya issledovateley ekonomiki gosudarstvennogo sektora, 2004, p. 50; Materials for the RF Government's meeting on 17 March 2005 "On measures designed to improve the efficiency of federal property management"; the authors' estimations.

Given that overall the 2001–04 dynamics of dividend transfers to the federal budget per 1 company (*Table 37*) did not differ from the above, it is worth noting that companies beyond the Top Ten of the largest payers displayed greater increment rates in dividend transfers in 2003–04. As a result, the gap between the average dividend payments per company of this particular group and by the Top Ten of the largest payers narrowed from 279.5 times in 2001 to 131.9 times in 2004 (in 2002 it was 758.7; in

2003 – 423.5). Meanwhile, the differences between dividend transfers per 1 company between the group of the five largest payers and the ten largest payers, which were diminishing in 2002 (5.2) and 2003 (4.0), proved to be greater in 2004 vs. 2001 (10.0 against 9.4).

With all the importance of the dynamic of the volume of dividend transfers on state-owned stakes to the federal budget, in absolute terms it is the proportion held by a particular company in such transfers which matters far greater, so far as the government's interests are concerned (*Table 38*).

Table 38

Significance of the Largest Payers of Dividends for the Federal Budget in 2001–04

Company	The size of the federal stake, as %	2001		2002		2003		2004	
		position	Share in the overall volume of revenues	position	Share in the overall volume of revenues	position	Share in the overall volume of revenues	position	Share in the overall volume of revenues
OJSC "Gasprom"	38,37	1	32,25	1	36,4	1	27,9	1	34,4
OC "Rosneft"	100,0	2	12,3	3	10,6	3	10,8	5	8,2
JSC "Transneft"	75,00	3	9,8	2	12,2	4	9,85	2	13,8
OGC "Slavneft"	74,95	4	9,35	6	5,8	–	–	–	–
OC "LUKOIL"	7,60	5	8,0	4	8,8	5	9,6	4	8,5
RAO "UES Russia"	52,55	6	2,5	5	8,5	6	6,5	...	...
TVEL	100,00	7	2,4	9	2,0	9	1,85	8	1,45
"Sovkomflot"	100,00	8	1,1	11	0,7	13*	0,6*	15	0,4
"Irkutskenergo"	40,00	9	0,9	13	0,4	14*	0,6*	...	...
Novorossiysk Sea Merchant Port (NSMP)	20,00	10	0,85	12	0,5	16	0,4*	...	...
International airport "Sheremetyevo"	100,00	11	0,8	10	1,0	12*	0,8*	13	0,6
"Aeroflot-Russian Airlines"	51,17	12	0,3	14	0,3	11	1,25	9	1,3
"Techsnabexport"	100,00	13	0,25	15	0,3	15*	0,5*	11	0,6
CJSC "ALROSA"	37,00	14	0,15	7	3,0	8	2,0	6	1,9

Company	The size of the federal stake, as %	2001		2002		2003		2004	
		position	Share in the overall volume of revenues	position	Share in the overall volume of revenues	position	Share in the overall volume of revenues	position	Share in the overall volume of revenues
Project Privatization Company	100,0	–	–	8	2,9	7	5,7	...	...
Vneshtorgbank	99,95	...	...	...	...	2	12,1	3	8,8
JSC “Transneftproduct”	100,00	...	...	...	...	10	1,5	14	0,5
Magnitogorsk Metallurgical Plant (MMP)	17,82	...	...	...	...	...	...	7	1,6
JS Holding “Sukhoy”	100,00	...	...	...	...	...	...	10	1,1
Transcreditbank	75,00	...	...	...	...	...	...	12	0,6

* – for 2001 – data on companies that held 11th–14th positions and by the total of 14 companies, as OJSC “Project Privatization Company” did not transfer dividends;

** – by companies “Sheremetyevo”, “Sovkomflot”, “Irkutskenergo” and “Tekhsnabexport” we used the data on the 2002 accrual of dividends and not on the actual dividend transfers to the 2003 federal.

Source: Materials for the RF Government’s meeting on 27 November 2005 “On the process of implementing the decisions of the Government of the Russian Federation designed to improve the efficiency of federal property management and on the main directions of the dividends policy”; *Predpriyatiya s gosudarstvennym uchastiyem. InstitutSIONalno-pravovyye aspekty i ekonomicheskaya effektivnost. Seriya “Nauchnyye doklady: nezavisimyy ekonomicheskyy analiz”*, No. 155. M.: Moscovskyy publichnyy nauchnyy fond; *Assotsiatsiya issledovateley ekonomiki gosudarstvennogo sektora*, 2004, p. 50; Materials for the RF Government’s meeting on 17 March 2005 “On measures designed to improve the efficiency of federal property management”; the authors’ estimations.

The information above highlights on a specific role Gasprom plays in formation of budgetary revenues of this particular type. Between 2001 and 2004 the company was permanently holding the first position among JSCs that transferred dividends and secured over 30% of the respective payments (except for 2002). Being among the three leaders in this respect in 2001–03 with its share accounting for over 10% of all dividend transfers, Rosneft in 2004 slid to the 5th position, while Transneft repeated its success of 2002 and was the 2nd largest payer of dividends to the budget (13.8% against 12.2% in 2002) (for reference: in 2001 and 2003, the company held the 3rd and 4th positions, respectively). The 2004 leading group also included Vneshtorgbank (8.8%), which in 2003 held the 2nd

position (over 12%). In 2001–04, Lukoil steadily held the 4–5th positions in the group (8–9.6%).

In certain periods, yet another three companies occasionally would make quite a serious contribution to dividend transfers: thus, Slavneft's proportion in the 2001 volume of dividend transfers was over 9.3% (the 4th position) and in 2002 – 5.8% (the 6th position). However, the federal stake was sold in December 2002 and the budget lost this source of dividends. RAO UES Russia secured 8.5% of the total volume of dividends in 2002 (the 5th position) vs. 2.5% reported in 2001. In 2003, the proportion of the electricity holding fell to 6.5% (the 6th position), while in 2004 the company merely failed to join in the group of the 15 largest payers of dividends. The Project Privatization Company in 2003 contributed with 5.7% of all the dividends transferred to the federal budget. As concerns the others, their individual contributions did not exceed 3% over the period in question. That said, it is worth noting that TVEL and Sovkomflot's proportions fell, while those of Aeroflot, Tekhsnabexport and ALROSA were on the rise.

Overall, the structure of dividend transfers to the federal budget appears highly concentrated and directly related to the financial health of the national fuel and energy complex (*Table 39*).

Table 39

**Structure of Dividend Transfers to the Federal Budget in 2001–2004,
by Categories of Payers**

Proportion in the overall amount of dividend revenues, as %	2001	2002	2003	2004
The largest payer (OJSC "Gasprom")	32,25	36,4	27,9	34,4
Payers that held 2 nd –5 th positions	39,45	40,1	42,4	39,2
5 largest payers	71,7	76,5	70,3	73,6
Payers that held 6 th –10 th positions	7,7	14,7	17,5	7,4
10 largest payers	79,4	91,1	87,8	81,0
Payers that held 11 th –15 th positions	1,4*	2,2	3,7**	2,8
15 largest payers	80,8*	93,3	91,5**	83,8
Other OJSCs whose stakes are in the federal property	19,2	6,7	8,5	16,2
The number of OJSC, That transferred dividends	734	747	597	319

* – for 2001 – data on companies that held 11th – 14th positions and by the total of 14 companies, as OJSC "Project Privatization Company" did not transfer dividends;

** – by companies “Sheremetyevo”, “Sovkomflot”, “Irkutskenergo” and “Tekhsnabexport” we used the data on the 2002 accrual of dividends and not on the actual dividend transfers to the 2003 federal .

Source: Materials for the RF Government’s meeting on 27 November 2005 “On the process of implementing the decisions of the Government of the Russian Federation designed to improve the efficiency of federal property management and on the main directions of the dividends policy”; *Predpriyatiya s gosudarstvennym uchastiyem. InstitutSIONalno-pravovye aspekty i ekonomicheskaya effektivnost.* Series “Nauchnye doklady: nezavisimyy ekonomicheskyy analiz”, No. 155. M.: Moscovskyy publichnyy nauchnyy fond; *Assotsiatsiya issledovateley ekonomiki gosudarstvennogo sektora*, 2004, p. 50; Materials for the RF Government’s meeting on 17 March 2005 “On measures designed to improve the efficiency of federal property management”; the authors’ estimations.

The proportion of the five largest payers did not plunge below 70% during the whole period between 2001 and 2004, albeit it did not exhibit a clear trend to growth. In 2004, these companies together secured 73.6% of the total volume of dividends transferred to the federal budget, of which 34.4% fell on Gasprom. Of the remaining four largest taxpayers three ones were in some way or another associated with the oil sector (Transneft, LUKOIL, and Rosneft), while yet another one was represented by a bank (Vneshtorgbank). The 2004 specific weight of the 4 companies that held 2nd through 4th positions was practically the same as in 2001, though in 2002–03 it somewhat exceeded 40%.

The contribution made by the second quinary of companies in terms of the volume of dividend transfers more than doubled in 2003 (17.5%) against 2001 (7.7%), but fell dramatically to 7.4% in 2004. As a result, between 2002 and 2004 the proportion of the Top Ten’s contribution with their dividends to the federal budget was sliding gradually from 92.4% to 81.0%, which, anyway, was slightly in excess of the respective 2001 index (79.4%). The proportion of companies that occupied 11th through 15th positions, on the contrary, had been on the rise until 2003 and ultimately reached 3.7%, but fell down to 2.8% in 2004.

As a result, the aggregate contribution of the 15 largest dividend payers reached its peak in 2002 (93.3%), was steadily on the decline over the next three straight years and hit the level of 83.8% in 2004. Accordingly, the proportion of all other companies with the RF Government stakes was on the rise and accounted for 16.2 in 2004 vs. 6.7% in 2002. Some diffusion in the distribution of the volume of dividend transfers to the federal

budget might be considered an unequivocally positive phenomenon, non the less the 2004 proportion of companies not included in the group of the 15 largest payers was, anyway, smaller than the 2001 indicator, and yet another, far more negative, fact is that the number of JSCs that transferred dividends to the federal budget in 2003–04 was steadily on the decline.

As in the prior years, 2005 saw Gasprom keep its position of the largest dividend payer. On October 28, 2005, the company transferred to the Federal Treasury RUR 10, 037.600bn. in dividends, or 60.6% of all dividend transfers to the federal budget in 2004. In all, as of Nov. 5, 2005, the federal budget collected RUR 16,572 bn. in dividends (against the planned 24 bln.), which exceeded the 2004 index⁹³.

1.4.4. Problems of Shaping the Dividend Policy and Its Reserves

As a reminder, while participating in capital of numerous companies emerged in the course of privatization in the 1990s, the government at the time basically ignored its shareholder's right for receiving the respective proceeds. [This can be partly attributed to the companies' complex financial and economic position due to then ongoing transformational recession. Having no possibilities for securing their support in a due volume at the expense of budget funds, the state allowed them to channel dividends on its stakes on economic and social development of such companies.

It seems to us, it is the general impotence of the state machinery, along with the predominant idea of future sales of the state-owned blocs that played a far greater role in the state's ignorance of reserves which would otherwise replenish the revenue part of the budget at the expense of this particular kind of nontax revenues. It was only the imminent 1998 crisis that compelled the state to pay attention to the source in question.

The renewal of economic growth in the aftermath of the crisis and improvement of the companies' financial health in the conditions when the state began implementing the course towards budget surplus on the federal level quite logically propelled the Government's interest in dividends on state-owned stock as a revenue source. The 1999 Concept of Man-

⁹³ Gasprom perechislil v budget dividendy v razmere 350 mln. Doll//Neftegazovaya vertikal, 7.11. 2005; www.rosim.ru.

agement of State Property and Privatization accentuated increase in non-tax revenues to the federal budget as a priority task, which should have established prerequisites for the government's decision to lower taxation on the respective operational results. However, the concept of dividend policy appeared missing in the document, and it was not enumerated among measures on increase in nontax revenues.

It was only in 2003 that the RF Ministry of State Property got back to the issue and formulated the dividend policy fundamentals as follows⁹⁴:

- necessity for the perspective planning of profits of the OJSCs with the government share in their capital on the basis of an efficient use of their assets, optimization of costs, and account of sectoral peculiarities and the market situation;
- compulsory channeling of a fraction of profit on dividend payments;
- provision of balance between the use of net profit for the purpose of consumption (dividend payments) and savings (investing);
- provision of eagerness and responsibility of managers of corporations with the state share in their capital in ensuring the set objectives.

The implementation pattern of the aforementioned approaches provides for design and approval by boards of directors of operational plans for every next year and projections – for two years ahead (with indicators of receipts from produce sales; net profit; planned dividends), attraction of nonpartisan experts to identify an economically justified profit rate and distribution of profit across certain areas and avenues, provision of implementation of the government policy by representatives of the state in an OJSC where the state participates in the capital. The government has also developed a thesis that it is mandatory to ensure a due accounting in the course of pursuance of a dividend policy by specific corporations that operate in the conditions of tariff regulation of their produce (services), as well as with respect to natural monopolists whose investment and financial plans are subject to the RF Government's consideration.

⁹⁴ Materials for the RF Government's meeting on 27 November 2005 "On the process of implementing the decisions of the Government of the Russian Federation designed to improve the efficiency of federal property management and on the main directions of the dividends policy".

The model of the dividend policy, as suggested by the RF Ministry of Property and, consequently, by the RF Ministry for Economic Development and Trade⁹⁵ suggests the following algorithm of distribution of net profit the corporation has actually earned: after deducting the amount of compulsory contributions and payments, as per the law, and to funds established by the company itself (reserve, etc.) from the actually received profit, the rest of it is used, in a mandatory order, on dividend payments. Then the company's executive body considers and approves financing of investment projects out of net profit. At this point, the financing of investment is viewed as efficient, if it simultaneously match three requirements: (1) a complete consumption of depreciation deductions; (2) inappropriateness of an increase of borrowed capital in the event the rate of return on investment becomes smaller than interest payments; (3) the profitability rate of the project financed out of net profit (without attraction of borrowings) should be not lower than the level of return on capital.

The above dividend policy fundamentals are correct at the level of theses, however their comprehensive translation into *real politik* casts certain doubts.

It is fairly evident that it is implementation of a balanced approach to distribution of profit which appears the most problematic among other policy fundamentals. It is asserted in the document that profit can be spent on investment in the event the latter's return rate is not lower than the one on investment capital (as demanded by the shareholders, including the state), while an attraction of borrowed capital does not undermine the company's financial stability. Overall, the return rate on the company's own capital should exceed the costs of the borrowed one. To defend this approach, its proponents employ fairly broadly known provisions of the theory of corporate finance regarding shareholders bearing greater risks vis-à-vis corporate creditors, as for the former investment may turn out to be irreparable. Plus, the use of borrowing is conceived as a disciplinary mechanism for corporations and their managers, as there exist the respective liabilities, while at the initial stage creditors' requirements should contribute to a greater level of the financial and economic

⁹⁵ Materials for the RF Government's meeting on 17 March 2005 "On measures designed to improve the efficiency of federal property management".

justification for investment and form a serious filter for implementation of insufficiently efficient projects.

In 2003, the RF Ministry of State Property tested the declared investment policy fundamentals by using OJSC “Transneft” and CJSC “ALROSA” for its pilot projects. In order to identify the value of economically justified level of dividends, the Ministry staff employed two approaches:

- analysis of corporations’ financial and economic performance and identification of reserves for boosting up dividend payments; and
- calculation of an economically justified value of dividends proceeding from the economically justified amount of net profit as a product of the market value of a stake and the rate of market return by the invested capital.

In the framework of the first approach, the Ministry experts identified production costs and the structure of the use of net profit as sources of reserves of increase in dividends. They practically failed to provide a detailed explanation of the nature of such a reserve as production costs, except for a possible decrease of rental payments to the budget of the Republic of Sakha (Yakutia) for the lease of the property complex of the Production and Research Company “Yakutalmaz”⁹⁶. As concerns Transneft, basing on substantially lower transportation tariffs and a greater operational profitability vis-à-vis overseas companies, the experts recognized the company’s production costs as adequate.

Meanwhile, on the basis of the analysis of the gearing rate, the experts make a conclusion regarding growth in financing of the company from borrowed capital, which is less expensive, without losing its financial stability, and channeling available funds to dividend payments. Thus, the potential amount of dividend payments on the federal stock package in OJSC Transneft appeared 18-fold in excess of the actual one and 3-fold – by CJSC ALROSA.

The other approach considered the economically justified size of dividends as a derivative from the economically justified value of net profit,

⁹⁶ The amount of rental payments that account for a considerable part of the Republic’s budget appears the product of a political consensus, rather than an economic category.

which is calculated as a product of the market value of a respective equity multiplied by its market profitability rate.

In the case of OJSC Transneft, the market value of its equity was calculated by means of comparative method with the use of information on analogous companies⁹⁷, while the calculation of the market return rate on the company's own capital was based upon the interconnection between return rates on the equity and those on borrowed capital with reference to analogous companies⁹⁸. Proceeding from Transneft's credit rating awarded by the respective international agencies and the aforementioned gearing proportions, the experts have found that the market return rate on the company's equity accounted for 17.9% annualized⁹⁹. Multiplied by the value of the equity itself, it allowed computation of an economically justified amount of net profit, which proves to be nearly twice as high as the actual results the company reported in 2002. This further increases the potential amount of dividends. For ALROSA, the average value of return on invested capital made up 20.8%, which, if multiplied by the market value of invested capital¹⁰⁰, makes it possible to speak of a 1.9 times increase in the economically justified amount of net profit vs. the actual one.

A detailed familiarization with results of the testing of the Ministry's dividend policy fundamentals on companies with the government share in

⁹⁷ By analogous companies, with account of adjustment to the country-specific risks, the experts identified 5 multipliers (capitalization/gains; capitalization/length of pipelines; capitalization/net profit; capitalization/volume of transportation; capitalization/ balance-sheet value of invested capital) that mirror the relation of the companies' market value to the respective indicators.

⁹⁸ The indicator of return on borrowed capital was computed on the basis of the match between the company's credit standing and the costs of debt servicing. To this effect the experts exposed a correlation between the analogous companies credit standing rating and return on borrowed capital.

⁹⁹ The weight values of the analogous companies employed for the sake of computation of the average value of return on invested capital of CJSC Transneft were obtained on the basis of their ranking in terms of the length of pipelines, the degree of the state regulation of the companies' operations, and values of gains and net profit.

¹⁰⁰ The market value of ALROSA's own capital (by contrast to Transneft) rested upon the appraisal of its assets and liabilities provided in the financial accounting completed according to international standards.

their capital allows specification of doubts regarding their implementation in practice.

It is necessary, first of all, to highlight fairly serious discrepancies in assessments of the potential amount of dividends that arise under employment of the noted approaches. As well, one cannot help paying attention to which substantial role various expert estimations and those by rating agencies in particular play in estimations of the value of dividends. Another factor that compels one to critically assess the estimations is an analogue base selected for the purpose of the comparative approach, because the analogous companies are represented mostly by corporations that headquarter in developed market economies, with their long-standing high corporate governance standards and the state's involvement in entrepreneurship being an exception, rather than a rule. As well, the group of analogous companies may include, at least, corporations headquartered in the developing or developed countries with an extensive public sector, which can be, at least, partly compared with modern Russia's, but in neither case can such analogous companies originate from the transitional economies.

In more general terms, it is possible to point out at the following flows in the RF Ministry of State Property and the RF Ministry for Economic Development and Trade's approach to the dividend policy:

- resting upon theoretical provisions, the present approach *per se* allows a possibility for shareholders (including the state) to receive greater dividends largely at the expense of the substitution of investments from the corporations' own resources with borrowings. In Russia's country-specific realities, the companies with the state participation, as a rule, find their financial and economic health being worse than that of other corporations, which is pregnant with the rise in their debt burden, potential financial instability, up to the possibility to be deprived of a part of their assets, should their creditors raise claims, as it repetitiously happened in the past, for instance, in the 1990s;
- the potential opportunity to boost up dividend payments in the event the corporations increase borrowing is justified by their reserves of growth in borrowed capital due to the prevalence of their own capital.

At this point, however, it should be remembered that Russia has not yet completed the process of transition to the international financial accounting standards and it is not quite clear as to what is the general state of affairs in this respect, as long as companies with the state participation are concerned, and what will their corporate finance look like after the transition is over¹⁰¹;

- requirement to ensure return rates on the state-owned equity capital at the level comparable with that of fully private owned companies can conflict with the practice of tariff and other regulation of operations of numerous companies with the state participation and their need to solve specific objectives which the state was pursuing when it fixed the state-owned stock;
- due to the above, drawing an accurate comparison between companies with the state-owned share in their capital and other companies poses a complex challenge. Furthermore, in the conditions of the Russian transitional economy, the situation is complicated by great differences in the capitalization and profitability indicators, whose nature is driven by the dependence of the prior development (decisions made in the period of the planned economy and peculiarities of privatization), rather than by efficiency of the current economic activities, and in number of cases, picking an analogue is unlikely to be possible in principle, while employment of international comparisons imposes a number of constraints, as noted above;
- as shown by the analysis of the pilot projects, the solution of the task of maintaining a reasonable balance with regard to distribution of net profit between investment and dividend payments is considered separately from the analysis of the targeted nature of investment and the necessity to center it on the company's basic operational profile, which appears quite urgent in light of regulation of natural monopoli-

¹⁰¹ The quality of book-keeping and specificity of assets of numerous companies with the state share in their capital, which derives from their sectoral attribution (a number of industries, infrastructure, R&D) are such, that their actual valuation may be lower than figures given in the accounting forms; plus, in a number of cases, there might be no analogous objects that have a market valuation.

lists, MIC corporations, as well as some other corporations' operations;

- neglected remained positive and negative incentives for the corporations' management and representatives of the state, which should secure attainment of the dividend policy objectives;
- a very fair provision regarding the necessity of attraction to the analysis of operations of companies with the state participation in their capital of independent experts (auditors, appraisers) conflicts with the existing practice of the general audit, when such experts fail to assess observance with proprietors (shareholders, participants') interests, efficiency of individual operations and exercise of management of the company on the whole and limit themselves with expressing their opinion on the consistency of the financial (book-keeping) accounting and the respective procedures of its conduct with the RF law. As well, the experts limit themselves to the expression of their view of what they believe forms a pivotal element (for instance, value materiality of a given abuse)¹⁰².

Somewhat forestalling, let us note that the aforementioned approaches were implemented only after a long period of time, when the RF Government issued its Resolution of May 29, 2006, No. 774-p.

In the early 2000s, when the ministries just launched the work on designing approaches to the dividend policies, the RF Ministry of Property developed an important means that helped replenish the budget system with nontax revenues, that is, the so-called targeted initiative auditing of the financial and economic performance with elements of financial consulting of open joint-stock companies whose shares were owned by the federal government. Such auditing allowed a more objective evaluation of the financial and economic situation in a given company and decision making with regard to dividend payments.

In conjunction with this, it is necessary to remind that in addition to the initiative audit, the Department of Financial Control and Audit of the RF Ministry of State Property also conducted a compulsory audit of or-

¹⁰² Toropov S.V. Problemy kontrolya za effektivnostyu ispolzovania gosudarstvennoy sobstvennosti // Vestnik Minimuschestva Rossii [Herald of the RF Ministry of State Property], 2003, No. 2, p. 43–45.

ganizations with the state-owned share in their authorized (joint-stock) capital accounting for no less than 25%. The scope of employment of this particular kind of audit was far greater than that of the initiative audit – suffice it to note that the 2002 plan of the initiative audit provided for its conduct at 2,073 corporations, while the actual output was 57 ones. In 2003, likewise, the respective figures were 1,722 and 50 corporations. In 2003, with its Resolution of May 23, No. 2334-p, the RF Ministry of State Property approved the list of 49 OJSCs, which was further extended to include 63 units.

The first, and most significant, facts of additional accrual of dividends basing on results of the initiative auditing became making decisions on dividend payments by Rosneft and Slavneft in 2002¹⁰³. The analysis by the Accounting Chamber of RF showed that while in 2001 private oil companies spent between 14% and 23% of their net profit on dividend payments (exclusive of OJSC Sibneft and YUKOS), the largest corporations with the government participation allocated between 4% and 8% of their net profit on dividend payments¹⁰⁴.

As a result, Rosneft actually paid dividends worth a total of RUR 1,100m vs. the planned 880m. The noted amount was transferred to the federal budget in 2002. Meanwhile, an analogous measure by OJSC Slavneft, which implied an increase in its dividend payments from RUR 650m up to 800m was vain, and in 2002 the budget *de-facto* received RUR 605.8m, which was equal to the 2001 indicator¹⁰⁵.

As concerns the other 15 OJSCs, a direct economic effect that might have been ensured, provided one followed the auditors' advice made in the process of financial consulting and initiative audit, was an additional accrual of dividends (for 2001) worth a total of RUR 1,781.853m. In other words, the recommended 2002 volume of dividends by OJSCs ex-

¹⁰³ Basing on the materials of the All-Russia Convention of the Minimuschestvo of RF, Nov. 26–27, 2002, “On implementation of objectives in the sphere of property relations”.

¹⁰⁴ Ignatov V. *Mozhet li gosudarstvennaya sobstvennost obespechit sotsialnyu zaschitu grazhdan Rossii // Izvetsia [News]*, mar 18, 2002, p. 4.

¹⁰⁵ In “*Predpriyatiya s gosudarstvennym uchastiyem*” (2004, p. 57), the authors cite the data that Slavneft ultimately raised the preliminary amount of dividends from RUR 487m up to 605.8m, i.e. up to the value that had been transferred to the federal budget in 2002 and 2001).

ceeded the actual one 7.8 times. It goes without saying, the amount in full could not be collected to the budget, as the state, as a rule, owned just a fraction of the companies' stock. Thus, the state share in the charter capital of OJSC "Eysky Portovy Elevator" and "Bryanskholod" accounted for 51%, in OJSC "Aeroport Vnukovo" – 60.87%, in OJSC "Spetsstroy-materialy" – 60.93%, in OJSC "Rossiyskiye Loterei" – 100%.

The bulk of additional accrual fell on 3 companies: 50.6% of that – on OJSC "Pervy Kanal", 32.8% – on CJSC ALROSA, and 6.2% – on OJSC "Transnefteprodukt"¹⁰⁶. Contribution of any of the remaining 12 companies did not exceed RUR 100m. Of the 15 companies, it was just one corporation (OJSC "Galogen", the city of Perm) whose actual amount of dividends accounted for over a half of the recommended one (65.4%), while the other companies' recommended amount of dividends was more than twice as high as the actual one. The group of companies whose coefficient of excess of the recommended amount of dividends vis-a-vis the actual one comprised OJSC "Eysky Portovy Elevator" (Krasnodar krai) (35.6 times), "Surovikinsky Portovy Elevator" (Volgograd oblast) (16 times), while OJSC "Pervy Kanal", Transnefteprodukt, Vladivostok-Avia, Spetsstroyaterialy did not pay dividends at all, and the value of the excess by the rest of the companies accounted for between 2.3 and 5.1 times¹⁰⁷.

Let us note that in the course of initiative audit inspections and a comprehensive analysis of production, financial state and the management quality analysis conducted in 2003, the group of companies wherein auditors found reserves for an additional accrual of dividends on the state-owned stakes, once again, included Eysky Portovy Elevator which, by the 2003 results was recommended to increase the amount of dividends 18 times. As a follow-up to the 2002 initiative audit, in 2003 Bryanskholod, Rossiyskiye Loterei, Aeroport Vnukovo, Spetsstroyaterialy, Surovikin-

¹⁰⁶ Toropov S.V. Problemy kontrolya za effektivnostyu ispolzovania gosudarstvennoy sobstvennosti // Vestnik Minimuschestva Rossii [Herald of the RF Ministry of State Property], 2003, No. 2, p. 43–45.

¹⁰⁷ The group of other companies that became objects for the initiative audit but omitted in this paper included CJSC "VO "ZARUBEZHSTVETMET", "Kursky kombinat khleboproduktov", "VO "SOUYZPUSHNINA", "Kholod".

sky Portovy Elevator were blacklisted, because of exposure of facts of their executives refusing and blocking access to conduct of the inspections, as well as of facts of various abuses and siphoning off the companies' assets¹⁰⁸. At the time (in 2003) auditors exposed facts of refusal to grant access to documents and information and siphoning off assets at OJSC "Novorossiyskoye Morskoye Parokhodstvo" where an earlier conducted audit had exposed an unjustified lowering of net profit at RUR 1.5bn, because of which the federal budget failed to collect Rb. 150m in dividends. Interestingly, the independent auditor, CJSC KPMG, had earlier considered this fact to be insignificant¹⁰⁹.

Overall, the initiative auditing resulted in finding the dividend payments reserves worth a total of: for 2000 – over RUR 700m; for 2001 – over RUR 1bn; for 2004 – RUR 2.2bn (inclusive of additional accruals of contributions to the federal budget from FPUEs' net profit).

The practice of corporate governance in companies with the state-owned stake in their capital evidenced situations when problems of calculation of the amount of dividends due to the federal budget form a subject of disagreement not only between corporate executives and government representatives on a company's board, but interdepartmental disputes as well. This can be exemplified by OJSC Transneft, which, basing on its 2003 performance, at first was going to transfer to the federal budget RUR 1,300m in dividends, which was 6.4% up against the respective amount of the prior year, but 18% down vs. the amount due to owners of the privileged stock (RUR 1,584 m) that formed as much as one-fourth of the company's authorized capital¹¹⁰. Representatives of the RF Ministry of Industry and Energy and the Federal Service for Tariffs opposed the idea to increase the amount of dividends payable on the state-owned stake (75% of the company's authorized capital). Underlying their stance was the perception of possible unfavorable consequences for the company's

¹⁰⁸ "Predpriyatiya s gosudarstvennym uchastiyem" (2004, p. 57–74).

¹⁰⁹ Toropov S.V. Problemy kontrolya za effektivnostyu ispolzovania gosudarstvennoy sobstvennosti // Vestnik Minimuschestva Rossii [Herald of the RF Ministry of State Property], 2003, No. 2, p. 41.

¹¹⁰ The Charter of Transneft requires that as much as 10% of the company's unconsolidated net profit should be allocated on payments on privileged stock.

investment activity and rise in the oil pipeline transportation tariffs. Meanwhile, the RF Ministry of State Property believed it would be possible to raise the amount of dividends up to RUR 1,600m and the RF Ministry for Economic Development and Trade speculated they could be raised up to RUR 2,377m. The general shareholders' meeting (and, *de facto*, the sole shareholder represented by the Federal Agency for Federal Property Management) followed the Directive of the Chairman of the RF Government and approved the value suggested by MEDT¹¹¹.

The above amount, equivalent to USD 83.4m, was transferred to the federal budget in 2004. The owners of privileged shares collected the originally planned amount of dividends (equivalent to USD 55.6m), i.e. at one-third less than the federal budget did. At this point, it should be noted that this particular correlation was not always maintained – for instance, the 2002 actual dividends on the federal stake (worth a total USD 41.45 m in forex equivalent) accounted for less than a half of the total amount of dividend payments made by Transneft (USD 84.34 m in forex equivalent)¹¹². Overall, by results of 2003 dividend payments accounted for one-fourth of net profit.

Whilst concluding the analysis of the role of the state as a shareholder in the corporate sector from the perspective of potential revenues, one has to admit that there are huge reserves for the budget replenishment. Nearly as much as $\frac{3}{4}$ of all the revenues falls on just 5 companies. The volume of dividends transferred to the federal budget during all the period in question was less than the volume of revenues from privatization of public property. It was only in 2004 that the former exceeded the value of the profit that falls on the Russian participant in Vietsovetpetro, though it was steadily superior to every individual group of revenues from other sources (property and land lease, part of profits made by PUEs). Quite an alarming symptom in 2003–04 was the contraction in the number of

¹¹¹ Gazetov A., Ditrich E., Kotlyarova A., Skripichnikov D. Doklad po korporativnomu upravleniyu gosudarstvennymi predpriyatiyami v Rossii // Krugly stol Rossii po korporativnomu upravleniyu, 2–3 iyunya 2005 g. (in the framework of the TACIS program and the Global Forum on Corporate Governance.

¹¹² Payments on the company's privileged shares accounted: in 2001 – RUR 1,344 m (vs. 1,272.4 m transferred to the federal budget in 2002); by the 2002 results – RUR 1,400 m (vs. RUR 1,222.01m transferred to the federal budget in 2003).

OJSCs that transferred dividends to the federal budget. But such a contraction should not be perceived as a unambiguously negative phenomenon, as their shareholders could rule to channel net profit to finance investment, which in turn can have a positive impact on a given company's market capitalization. In this context suffice it to remind that Transneft, for instance, is implementing the project of building the Baltic Pipeline System, while OJSC "Transnefteprodukt" is building export-oriented pipeline for petroleum derivatives Kstovo-Yaroslavl-Kirishi-Primorks (*aka* "Sever" project) and an oil storage facility in Lenigrad oblast. At this point, the main challenge lies in efficiency of investment, its objectives and to what extent such activities are coordinated with the state as a shareholder.

1.5. Conclusions

The period after the adoption of the 1999 Concept of State Property Management and Privatization saw drastic changes that concerned economic companies with the state (the Russian Federation's) participation in their capital.

From the quantitative perspective, the sector has undergone no general contraction in its size. However, there occurred important shifts:

- the magnitude of the ongoing employment of such an instrument as the "golden share" right, as well as the frequency of its application to the corporate sector has diminished; the state has sharply contracted its participation in economic companies of the organizational and legal forms other than OJSC;
- the period between 2005 and 2006 saw a notable rise in the proportion of economic companies wherein the state owned more than 50% of capital. That took place thanks to growth in the proportion of companies whose 100% stock is owned by the state, due to the recent practice of transformation of public unitary enterprises into joint-stock companies;
- as a result, by mid-2006 the state has become an owner of more than 50% of capital in all the economic companies with its participation vs. 25% reported in 1999, which substantially extends its capacity to exercise a full-fledged majority control;

- against such a background there unfolds a negative phenomenon, namely, the continuous existence of the specific weight of economic companies with a minority state-owned stake against the contraction in the proportion of companies with a blocking stake, which diminishes the government's capacity both as a shareholder and a potential seller, because of a low liquidity of such minority stakes;
- the structure of the federal blocs of shares as of mid-2006 roughly coincides in terms of the state-owned share in companies' authorized capital with the structure the RF Ministry of State Property envisaged to unfold upon implementation of the 2003 privatization program.

The size of the state presence in Russia's corporate sector was determined by a whole series of factors that contributed both to its expansion and contraction.

The sources of the expansion of the size of the state-owned share in joint-stock capital were:

- transformation of federal public unitary enterprises (FPUEs) into joint-stock companies in the course of implementation of privatization programs;
- growth in the government's participation in companies' authorized capital in the framework of corporate procedures and a dividend policy;
- offset for the investing of budgetary funds in the frame of federal targeted investment programs;
- offsets for a contribution with land sites under privatized enterprises or with rights for intellectual property owned by the state to companies' authorized capital;
- return under the federal property of shares that were earlier assigned to corporations for their use, control, or which were sold to those with violations of the law;
- restructuring and repayment of accounts payable and tax arrears before the federal budget and the RF Government (including intergovernmental debts);
- implementation of measures on restructuring of individual sectors and industries.

The main factor was transformation of FPUEs into joint-stock companies. The pace of the transformation has recently accelerated notably and accounted for 500–700 units between 2003 and 2005 vs. roughly 100 units in 2002.

The contraction of the state presence in the corporate sector took place at the expense of sales of federal blocs of shares in the process of implementation of privatization programs. In this respect it should be noted that:

- in 2003–05 vs. 2001 the government has managed to notably increase sales of federal blocs of shares in the course of privatization. Notwithstanding this, the real number of blocs sold during a given calendar year was always less than originally projected, to say nothing of plans adjusted towards their increase;
- in 2003–05 vs. 2001, there was growth in the proportion of stakes sold by new means of privatization (public offering and sales without announcing the price); the proportion of minority, control and full blocs in the overall number of blocs sold was on the rise, while the proportion of blocking stakes was falling.

At the federal level, there took place a vigorous formation of the legal base that regulates operations of economic companies with the state-owned share and activities of the federal government's representatives in the respective executive bodies:

- new forms of reporting by the government representatives were approved (1999);
- the decision was made to create a Register of economic efficiency indicators of joint stock companies with the state participation in capital (2000); the list of such indicators was approved (2001); with regard to the companies in which the state-owned share exceeded 50%, such indicators have become subject to annual approval;
- the basic document that regulates activities of the state representatives in companies with mixed capital became the Statute on procedures of appointment of and activities by representatives of the Russian Federation in executive bodies and auditing committees of open-end joint-stock companies established in the process of privatization whose shares are in the federal property, as well as those with respect

to which the decision was made to use a special right for the RF's participation in their management (the "golden share right"), which was initially introduced in 2000 and consequently replaced by a new version in 2003;

- procedures of provision of main measures on realization of rights of the state as a shareholder, that for the first time ever set step-by-step actions of experts of the RF Ministry of State Property with regard to preparation and implementation of fundamental managerial decisions concerning joint-stock companies with the state-owned stakes were mirrored in the adopted Regulation on realization of the rights of the Russian Federation as a shareholder (2001);
- the third Act on privatization promulgated in 2001 granted the executive power with a broad freedom of action in the part of pursuance of a property policy; the Act limited only the freedom of action with regard to strategic enterprises and joint-stock companies that could be privatized only upon the respective decision of the RF President, as well as natural monopolists wherein modifications in the property structure required an adoption of the respective legal acts.

In practice, however, logical on the surface, the system of management of state-owned stakes suffered from numerous failures. Its trouble spot became a dual nature of the existing model, which implied that in the process of preparation of decisions the RF Ministry of State Property's efforts were to be complemented by those of sectoral management agencies. Most sectoral ministries (agencies) failed to ensure their due contribution to preparation of directives to the state representatives by failing to meet deadlines for the submission of suggestions with regard to voting to the RF Ministry of State Property. In order to eliminate discrepancies, the Ministry was consequently compelled to submit draft directives on all the issues to the RF Government, thus increasing the workload of its staff and causing delays in decision making. Hastiness in preparation of such directives entails a lower quality of managerial decisions and it does not allow one to duly account specificity of individual companies.

Another serious shortcoming is an unsatisfactory degree of transparency of the system of management of the state-owned stakes, which manifests itself in the following phenomena:

- the absence of a clear system of principles of appointment of state representatives to companies with a state-owned share in capital;
- the absence of an effective reporting system for state representatives to the respective agencies that have delegated them to a given company; the absence of the system of evaluation and account of their performance in the event their candidatures are recommended for a new term; the absence of evaluation of their reports on the financial and economic performance of companies wherein they operate in the state's behalf;
- the absence of a system of motivation (awards and penalties) for the staff of government agencies that exercise the role of a state representative in economic companies;
- a poor organization of interaction between different agencies and judicial bodies on matters of introduction of corporate governance standards and a greater efficiency of enforcement procedures;
- an insufficient brio with which the government agencies' staff that exercise the role of state representatives contributes to the improvement of the corporate governance practices in the respective companies (including realization of provisions of the Corporate Behavior Code).

Notwithstanding the above, the rise in the number of the corps of state representatives and enactment of a series of legal acts that regulate their activities helped regalanize the state representatives' efforts, and they began to display a greater persistency while justifying for these or those decisions made by executive bodies of companies with the state participation in their capital. There is certain evidence that, according to a series of formal signs (boards of directors' activity, executives rotation, dividend payments), economic companies with the state (including regional and local authorities) participation exhibit a better performance than purely private companies. Another question in this respect is as to how one should accurately interpret the respective data, as they such data do not always succeed in testifying to a favorable state of affairs in a given company, nor they can always highlight on its positive dynamics.

As in the late-1990s, some empiric research into the structure of joint-stock capital and corporate governance evidenced that the state generally

appeared a minority shareholder. That was mirrored by the structure of boards of directors, among others. Nonetheless, according to some research data, the proportion of representatives of government agencies of different levels in boards of directors posted some growth vis-à-vis the 90s. That occurred thanks to the regional and local administrations that were reported to have a greater coefficient of representation against the federal level. At this point, it is worthwhile noting that the period of 2002–2003 saw some signs of the fact that the state-owned share in the companies' capital structure discontinued to shrink and began to grow (different research quote the rise in the proportion of this or that level of government), which became especially notable, should one analyze the structure of capital of only those enterprises in which any level of government had some participation.

One should pay a particular attention to the largest, nationwide, companies with the state participation in their capital. The period post-2000 saw a serious renewal of the personal composition of their executive bodies – there appeared high-rank officials from the presidential Administration and the RF Government as state representatives, or even chairmen of their boards. Shareholders' meetings in such companies became notable events in the nation's economic life and attracted a great attention on the part of media and public at large, as the state representatives' stand became critical, so far as decision making on such companies' development is concerned. But this appears to a minimum degree associated with improvement of corporate governance in and enhancement of transparency of such companies, as the state representatives' activity mostly concerns the problem of dividend payments. Like in purely private corporations, the large companies with the state-owned shares often suffer from cases of abusing shareholders' rights, opportunism and direct abuses on the part of their management, which causes damage to the state itself.

Like in the 90s, the main instrument of control of the state-owned property in the corporate sector has remained the institution of state representatives, within which a relatively small niche was occupied by individuals that are not government agencies' staff and exercise the representation in the state's behalf on the contractual basis. The control over state-owned stakes by means of trust is still neglected, while creation of inte-

grated holding structures with inclusion in their authorized capital of state-owned blocs has become a normal practice. In the 2000s, it was the defense industry that formed the main field for creation of the integrated structures. In 2006–07, the RF Government launched the process of creation of such structures to embrace whole industries (the nuclear, aircraft- and ship-building industries), including the segment of civil production. It should be noted that the process implies inclusion of private assets as well. The recently launched restructuring of natural monopolists also implies the government's participation both as a shareholder in the respective companies and its subsequent contribution to the plans of recombination of the respective assets and exercise of property control in a new format.

While realizing its shareholder's right for collecting proceeds from participation in joint-stock companies, the state has managed to ensure a considerable increase in dividend-based revenues to the federal budget. In 2006, they grew more than 17-fold vs. 1999, which is quite in the mainstream of general trends of advancement of the national corporate sector. Dividends have begun to account for over one-third of all the renewable revenues registered by the federal property management agency.

It was the companies of the fuel and energy complex and JSCs in which the state owned a stake over 25% that played a pivotal role in provision of dividend payments to the budget. Interestingly, the research revealed a positive correlation between the size of the state-owned bloc and dividend payments per 1 company and the proportion of companies that paid dividends. The level of concentration of dividend revenues was very high – in the period of 2001–04 as many as 10 companies, of which the largest one was Gazprom, secured no less than 80% of dividend payments to the budget.

Despite all the recent positive shifts in the area of dividend payments to the budget, there exist huge reserves in this regard. This is proved by results of the initiative audit, as well as by estimations of the contribution to the revenue part of the budgetary system. In 2003–04, dividends provided the meager 10–11% of all the federal budget revenues and slightly over 7% of its nontax revenues. In the period of 2004–05 alone, the aggregate volume of dividends by stakes owned by the federal government

domestically has caught up with proceeds the country received from its participation in a single overseas joint-stock company (Vietsovpetro). The absolute number of joint-stock companies that transferred dividends to the federal budget and their proportion in the overall number of joint-stock companies with the state share in their capital has been declining since 2002. In the early 2000s, the state was just developing approaches to pursuance of its dividend policy with regard to companies in whose capital it participated, and it was only in 2006 that the state fixed the approaches at the level of a particular legal act.

2. Problems of State Participation in the Corporate Sector in the Conditions of a New Phase of Institutional Development (2004–2006)

Certain positive outcomes from implementation of the 1999 Concept of State Property Management and Privatization, as well as enactment of new acts on privatization in 2001 and on unitary enterprises in 2002 granted the executive power a greater freedom of action in the area of privatization and created grounds for discussions in 2002–2003 of new initiatives that concerned the public sector management¹¹³. According to the RF Ministry of State Property, the government policy in this area should focus on the following objectives: 1) classification of the federal property; 2) improvement of new mechanisms of management of the respective objects; 3) optimization of the structure of federal property.

Addressing the noted objectives proved to be closely related to problems of control over economic companies with the state-owned shares and their role in the national economy.

2.1. State participation in the corporate sector in the context of planned novelties

The federal bill “On the public and municipal property” the RF Ministry of State Property submitted to the RF Government on January 31, 2003¹¹⁴, suggests that, in addition to public enterprises and institutions and transfer of a corporation under concession, one of organizational and

¹¹³ Materials of the All-Russia Meeting of the Minimuschestva RF of Nov. 26–28 2002 “On implementation of objectives in the sphere of property relations; materials prepared by the RF Ministry of State Property for the RF Government’s meeting of Feb. 6, 2005 “On measures designed to improve the efficiency of the federal property management and criteria of its assessment”; materials for the RF Government’s meeting on Nov. 27, 2005 “On the process of implementation of decisions of the RF Government designed to improve the efficiency of the federal property management and on the main avenues of the dividend policy”.

¹¹⁴ Vestnik Minimuschestva Rossii [Herald of the RF ministry of State Property], 2003, No. 2.

legal forms of functioning of the public and municipal property should become the government's contribution to capital of an OJSC's 50-plus% of whose shares belongs to the RF, its Subjects and municipalities. Meanwhile, the property, which, in compliance with the federal law, is not subject to alienation from the public or municipal property (*aka* the property withdrawn from the civil turnover), may not be used for the purpose of contribution with it to an OJSC's capital.

The core of the bill is that, while the property necessary only for the exercise by government agencies of a certain level of their respective power can be assigned under the state and municipal ownership, at the same time, it allows the presence of strategic assets exclusively in the federal property, and the list of such property objects is approved by the RF President on the basis of the RF Government's submission. At this point, it should be noted that in contrast to unitary enterprises on the basis of economic control, which may have discontinued their existence by 2008–09, OJSCs with the state-owned share in their capital will continue to remain a main form of the government participation in Russia's economic life in the long run.

Basing on the declared fundamentals, the RF Ministry of State Property also designed proposals on the short-term privatization program. For the first time ever the program covers a three-year perspective, that is, the period of 2004–06, and sets an objective of offering to the private sector all the assets that do not exercise state-related functions, with the ultimate goal to complete the privatization process by 2008. The respective document (Forecast Plan (Program) for Federal Property Privatization in 2004 and the Main Directions of Federal Property Privatization until 2006) was approved by the RF Government with its Resolution No. 1165-p of August 15, 2003.

The document set the sequence of the government actions with regard to privatization of certain enterprises (objects), including large-scale sales of federal blocs:

In 2004, it was planned:

- to continue privatization of blocs in joint-stock companies of the machine-building, energy construction, chemicals and petrochemicals

- and nuclear industries, sea, automobile and air transport, communication, bread products suppliers, and those in the nonproduction sphere;
- to offer for privatization all the federal stakes in joint-stock companies that render geophysical services in the oil and gas complex, oil and gas construction, coal-mining, fuel, metallurgical, automobile-making, clock-making, food-processing and light industries, the word-working complex, cold store facilities, credit institutions, as well as joint-stock companies operating in the area of fishery (exclusive of those that were supposed to be included in the list of strategic joint-stock companies subject to the RF President's approval);
 - to put up for sale all the federal stakes whose size did not exceed 25% of a respective joint-stock company's capital, exclusive of blocs in joint-stock companies operating in the energy sector (until the completion of the RAO UES Russia's reorganization), gas utilities, and joint-stock companies subject to financing in the framework of the Federal Targeted Program, joint-stock companies that participated in the formation of an integrated structure, as well as blocs in the largest joint-stock companies the sale of which should be made proceeding from the needs for formation of the revenue part of the 2004 federal budget and the budgets of the following years;
 - in order to implement the federal targeted program "Reforming and Developing the Military Industrial Complex (2002–2006)", it was envisaged to transform a number of federal public unitary enterprises into joint-stock companies and contribute with the federal government-owned blocs of joint-stock companies to authorized capital of integrated structures established in the form of joint-stock companies.

In 2005:

- in the process of privatization one should put up for sale stakes in the joint-stock companies founded in 2003–04, in the course of transformation of federal public unitary enterprises into joint-stock companies, except for the joint-stock companies that would be included in the list of strategic joint-stock companies or those participated in the formation of integrated structures;

- it was envisaged to discontinue the Russian Federation's participation in joint-stock companies of the gas-related economy, energy-construction sector, fishery, construction complex, cinematography and film distribution, foreign trade organizations, as well as in machine-building joint-stock companies (except for the strategic joint-stock companies);
- one should have put up for sale all the federal stakes whose size did not exceed 50% of a given joint-stock company's authorized capital, except for the stakes in the largest joint-stock companies (the sales of which should be exercised basing on the needs for formation of the revenue part of the federal budget in a respective year), as well as joint-stock companies that would be enumerated in the list of strategic joint-stock companies or those that participated in the formation of an integrated structure.

In 2006:

- in the process of privatization one should put up for sale stakes in the joint-stock companies founded in 2004–05, in the course of transformation of federal public unitary enterprises into joint-stock companies, except for the joint-stock companies that would be included in the list of strategic joint-stock companies;
- it was planned to discontinue the Russian Federation's participation in joint-stock companies of civil aviation, health care, chemicals and petrochemicals, polygraphic industries, geology, fishery, poultry breeding, crop production, cattle breeding, forestry complex, medical industry, as well as to complete the transformation of federal public unitary enterprises into joint-stock companies in the nuclear industry;
- it was envisaged to complete privatization in the aviation industry; production of arms, means of communication, airspace equipment, ammunition, production of special chemicals; ship-building and electronic industry; radio industry by means of formation of integrated structures in the frame of the federal targeted program "Reforming and Developing the Military Industrial Complex (2002–2006)".

Thus, the main guides for implementation of the privatization programs in the corporate sector became selling in 2004 all the state-owned

blocs accounting for up to 25% of a given company's authorized capital, those accounting for up to 50% – in 2005, and the remaining ones, except for strategic corporations – in 2006. According to the RF Ministry of State Property, that very ambitious program required annual sales of state-owned blocs in some 4,000 joint-stock companies (including the reorganized FPUEs). By 2008, the government will ultimately have been left with no more than 2,000 PFUEs and 500 various stakes in hands. As demonstrated above, the degree of success of the program implementation has proved to be very low.

In the next three years the guides for privatization program have become less specific and contained some repetitious items.

The Forecast Plan (Program) for the Federal Property Privatization for 2005, which the RF Government approved with its Resolution No. 1124-p of August 26, 2004, ascertained that in 2005–07 the state should put up for sale its stakes in the joint-stock companies founded in the course of transformation of federal public unitary enterprises into joint-stock companies, except for joint-stock companies that would be enumerated in the list of strategic joint-stock companies or those participating in the formation of integrated structures.

The year of 2005 should have seen the following assets put up for sale:

- stakes accounting for up to 25% of authorized capital of the respective joint-stock companies, except for blocs in strategic joint-stock companies or those participating in the formation of integrated structures, as well as the stock whose sales would be exercised proceeding from needs for formation of the revenue part of the 2005 federal budget and through 2007, as per the perspective financial plan;
- stakes in joint-stock companies of the oil and gas complex, fuel industry, machine-building sector, energy construction complex, fishery, construction complex, metallurgical industry, chemicals, polygraphic industry, automobile, sea and air transportation, communication, nonproduction sphere, bread products supply, foreign trade enterprises, land development companies.

In 2006–07, the state should put up for privatization its stock in open-end joint-stock companies founded in the course of transformation of the said federal public unitary enterprises into joint-stock companies.

The Forecast Plan (Program) for the Federal Property Privatization for 2006 and main guidelines of the federal property privatization program for 2006–2008 which the RF Government approved with its Resolution No. 1306-p of August 25, 2005, maintained that in 2006–08 the government would put up for sale its stakes in joint-stock companies founded in the course of transformation of the said federal public unitary enterprises into joint-stock companies, except for the joint-stock companies that were subject to inclusion in the list of strategic joint-stock companies or those participating in the formation of integrated structures.

In 2006, the Government should have put up for privatization the following assets:

- stakes accounting for up to 50% of authorized capital of the respective joint-stock companies, except for blocs in strategic joint-stock companies or those participating in the formation of integrated structures, as well as stock whose sales would be exercised proceeding from needs for formation of the revenue part of the 2006 federal budget and through 2008, as per the perspective financial plan;
- stakes in joint-stock companies of the gas-related sector, energy construction complex, construction complex, cinematography and film distribution, civil aviation, health care, chemicals, petrochemicals and polygraphic industries, geology, fishery, poultry breeding, crop production, cattle breeding, forestry complex, medical industry, foreign trade organizations, as well as joint-stock machine-building companies (except for the joint-stock companies included in the list of strategic joint-stock companies).

In 2007–08, the government should put up for sale all the federal public unitary enterprises that do not provide for exercise of state functions of the Russian Federation, as well as stakes in open-end joint-stock companies founded in the course of transformation of the noted federal public unitary enterprises into joint-stock companies.

The Forecast Plan (Program) for the Federal Property Privatization for 2007 and the main federal property privatization guidelines for 2007–09

the RF Government has approved with its Resolution No. 1184-p of August 25, 2006, likewise provide for putting up for sale in 2007–09 stakes in joint-stock companies founded in the course of transformation of federal public unitary enterprises, except for joint-stock companies included in the list of strategic joint-stock companies or those participating in the formation of an integrated structure.

In 2007, the government should put up for privatization:

- stakes accounting for up to 50% of authorized capital of the respective joint-stock companies, except for blocs in strategic joint-stock companies or those participating in the formation of integrated structures, as well as stock whose sales would be exercised proceeding from needs for formation of the revenue part of the 2007 federal budget and through 2009, as per the perspective financial plan;
- stakes in companies of the fuel and energy complex, energy construction complex, construction complex, foreign trade organizations, civil aviation, health care, chemicals, petrochemicals and polygraphic industries, geology, fishery, poultry breeding, crop production, cattle breeding, forestry complex, medical industry, as well as joint-stock machine-building companies (except for the joint-stock companies included in the list of strategic joint-stock companies).

As concerns large federal property objects, in 2007 the Government is going to privatize belonging to the Federation stakes in open-end joint-stock companies “VO “Stankoimport”, “Moskovsky metrostroy”, “Aeroport Salekhard”, “Mezhdunarodny aeroport Ufa”.

The period between 2007 and 2009 should see continuation of the work on creation of integrated structures in the military-industrial complex, airspace, ship-building and nuclear industries.

In 2007–09, the government should put up for privatization all the federal public unitary enterprises that do not provide for exercise of state functions of the Russian Federation, as well as stakes in open-end joint-stock companies founded in the course of transformation of the noted federal public unitary enterprises into joint-stock companies.

2.2. Novelties in the legal regulation that concerns public property management in the corporate sector

In 2004–06, the government adopted new legal acts that currently regulate activities of economic companies with the state participation in their capital and public unitary enterprises.

One should first of all refer to presidential Decree of August 4, 2004, No. 1009 “On approval of the list of strategic enterprises and strategic joint-stock companies”. The list included 514 federal public unitary enterprises (FPUEs) and 549 open-end joint-stock companies in which the state had different stakes. It should be noted that from the perspective of the possibility for the state to exercise a controlling impact on the companies, the structure of the aforementioned group of OJSCs appeared more optimal than that of all the joint-stock companies with federal stakes. This can be explained by a smaller proportion of minority and blocking stakes in the former group. Notwithstanding this, the structure was yet far from optimal (*Table 40*).

Table 40

The 2004 Structure of Joint-Stock Companies with the State Participation and the Structure of the List of Strategic OJSC

Date	The number of joint-stock companies									
	total		Up to 25%		between 25% and 50%		between 50% and 100 %		100 %	
	units.	%	units.	%	units.	%	units.	%	units.	%
Total in federal property, as of June 1, 2004	3,905	100	1,950	49.9	1,183	30.3	499	12.8	273	7.0
Strategic OJSC (according to presidential Decree of August 4, 2004, N 1009)	549	100	4	0.7	376	68.5	105	19.1	64	11.7

Source: Forecast Plan (Program) for Federal Property Privatization in 2005, presidential Decree of August 4, 2004, No. 1009; the authors’ estimations.

It was just 30% of strategic OJSCs (169 units) in which the state-owned stake exceeded 50% of their authorized capital, including 11.7%

of companies (64 units) fully owned by the state¹¹⁵. In the other 380 OJSCs the size of the state-owned stake did not exceed 50% of authorized capital, including 4 enterprises in which the government share was less than a blocking stake¹¹⁶. In all fairness, in 118 companies (less than one-third of all the companies with the state-owned stake accounting for between 25% and 50%) the state-owned stake was between 37.5% and 50%, which under certain circumstances (for instance, providing one-fourth of the authorized capital is formed by privileged shares) could ensure majority control for the state. Once compared with the number of strategic OJSCs as per the presidential Decree with the overall number of companies whose shares are in the federal property (as of June 1, 2004), it can be argued that the former accounted for just 14% of all the JSCs with federal stakes. Yet more paradoxical is the fact that the proportion of strategic OJSCs was the greatest one in the group of companies in which the state owns between 25% and 50% of stock. By contrast, in the group of companies with the state-owned majority stakes the proportion of strategic JSCs accounts for just 21%, while in the group of JSCs whose stock is 100% state-owned the respective rate is 23.4%.

By contrast to government resolutions of 1995 and 1998 that identified lists of companies with the federal stakes that may not become subject to an early sale, the document in question does not contain a classification of OJSCs in sectoral terms. A mere familiarization with the list allows one to assert that, along with enterprises of the defense industry, machine building, fuel and energy complex, transport, research organizations, also enumerated there are enterprises whose strategic importance for the national economy is not explicit, such as, for instance, regional gas storage, transportation and distribution networks, local organizations dealing with fuel storage and supply, a number of construction and repair enterprises, and river ports¹¹⁷.

¹¹⁵ Including a number of integrated structures founded in the process of implementation of the MIC reorganization program and with account of 2 CJSCs with the state-owned stake varying between 98 and 100% (Bank vneshney torgovly and "Izmeritel", which allowed the owner not exercise procedures stipulated in the act on JSCs.

¹¹⁶ CJSCs "Iskra" (Ulyanovsk), "Permskoye motory", "Stavropolkraigas" and "Tverobl-gas".

¹¹⁷ Which does not exclude their great significance for the RF Subjects and municipalities.

The Decree reads that the RF Government can include in a privatization program enterprises and OJSCs enumerated in the noted lists upon the RF President makes a decision of their exclusion from the respective lists¹¹⁸. The Decree sets the sole method of privatization of strategic FPUEs, namely, their transformation into OJSCs 100% stock of which belongs to the federal government.

As a reminder, it was provisions of the federal Act of December 21, 2001 (No. 178-FZ) “On privatization of public and municipal property” that demanded for approval of such a list, while presidential Decree No. 1514 promulgated in parallel with the Act commissioned the RF Government to submit for President’s approval lists of strategic enterprises and strategic OJSCs until March 1, 2002. However, like many other problems, this particular one has not been solved on time, and it took over two years upon enactment of the noted Act to fix the problem.

The Decree also commissioned the RF Government to provide for the inclusion of the noted enterprises and OJSCs in the list of strategic enterprises and organizations, which was approved in January 2004 for the sake of an efficient enforcement of the bankruptcy law.

At this point, one should refer to yet another list of strategic enterprises and organizations approved by the RF Government with its Resolution of January 9, 2004, No. 22-p. The adoption of this particular document proceeds from Art. 190 of the federal Act “On insolvency (bankruptcy)”. In conjunction with this, it must be remembered that the whole p. 5 (Art. 190–196) of the third Act on bankruptcy is about regulation of bankruptcy of strategic enterprises and organizations¹¹⁹. The Act attributes to strategic structures those OJSCs whose stock is in the federal

¹¹⁸ The letter and spirit of the Decree may give a rise to a thought of a legal collision, for, proceeding from the new Act on privatization of 2001, shares of companies and enterprises operating in the spectrum of natural monopolists can be included in a privatization program only on the basis of a special act, as it happened, for instance, to blocks of shares of the respective enterprises upon adoption of acts on restructuring electricity sector and railway transport.

¹¹⁹ The noted articles contain legal norm that take the noted enterprises off the framework of standard procedures applied in the event an economic agent’s insolvency. The procedures increase requirements to participants in bankruptcy and allow the state to exercise a repetitious interference with the bankruptcy process.

property and which carry out production of produce (works, services) that have strategic importance for the provision of defense capacity and state security, protection of morale, health, rights and legal interests of citizens of RF. So far as such structures are concerned, the Act introduces the regime of use of special insolvency procedures, of which the most important one is the state's privileged right for acquisition of an indebted enterprise.

In the event such an enterprise (a strategic organization which by its legal form is not a FPUE, i.e. this mostly concerns OJSCs), which is designated for operations associated with execution of works on the state defense order, provision of the federal state needs in the area of maintenance of the RF's defense capacity and security, is to be sold at an auction, the Russian Federation has a right, within a month upon signing a protocol on the auction results, to conclude a purchase and sale contract that provides for the purchase of a given enterprises at a price set by results of the auction and stipulated in the respective protocol and subject to conditions set for holding the auction.

In the event during the noted term the RF fails to conclude the said contract, it should be concluded with a victor in the auction, as per the protocol on the auction results. The winner is bound to pay the sale price of the enterprise set at the auction within a term as per the announcement on conduct of the auction, which may not exceed 1 month upon the date of conclusion of the sale contract. Bankruptcy creditors and their affiliated entities may not participate in an auction.

The law demands that the Government should approve the list of strategic enterprises and organizations, providing its publication is mandatory. As of the moment of approval of the list, it contained 1,131 organizations, including 494 OJSCs, 8 CJSCs and 1 LLC. The document, however, fails to clearly set the role of the state in their capital, except for that of the unitary enterprises being in the federal property. Between 2004 and 2006 as many as 9 enterprises were excluded from the list (there were no economic companies and partnerships among them), while another 8 ones were included into that (OJSC "Kamaz", along with four enterprises separated from the composition of the company, according to their profiles, and 3 public enterprises). With its Resolution No. 592 of October 2,

2006, the RF Government approved Regulations of interaction between federal agencies of executive power in the process of preparation of proposals on formation of the list of strategic enterprises and organizations, subject to the RF Government's approval in compliance with the federal Act "On insolvency (bankruptcy)".

With enactment of the aforementioned lists the legal base of the state property policy with regard to economic companies with the state participation in their capital was quite logically renewed, which had long been demanded by provisions of the privatization and bankruptcy law. On the other hand, there occurred a rise in the number of various lists of economic companies with the state participation in their capital, which are subject to different legal norms and regulatory apparatus¹²⁰.

Meanwhile, the regulation of the composition of the sector of economic companies with the state participation in their capital has seen the completion of transition from the output-based approach (in the frame of which one identified the array of kinds of operations, enterprises involved in which could be incorporated with their control stakes being fixed in the state property or using the "golden share" right) towards lists of concrete enterprises, each being individually included in a respective list.

After the reorganization of the RF Government in spring 2004, the position the RF Ministry of Property Relations had been holding in the state administrative system was inherited by the Federal Agency for Federal Property Management (the RF Ministry of State Property). Overall, in the framework of administrative reform at the federal level there occurred transition towards a three-tier system of government, that is, Ministry – Agency – Service. The RF Ministry of State Property has now had to report to the RF Ministry for Economic Development and Trade. All that propelled a new round of law making in the area of public property management.

¹²⁰ As a reminder, the Regulation on realization of the rights of the RF as a stockholder approved by the RF Ministry of Property Relations with Order of Nov 26, 2001, No. 260, in addition to general provisions and arrangements applied to all joint-stock companies in which the RF holds voting shares, has 5 annexes, each containing different lists of joint-stock companies. As the noted annexes to the Regulation have not ever been published, an provocative and unanswered question is as to what is the degree to which the lists of CJSCs therein overlap.

With its Resolution of December 3, 2004, No. 738 the RF Government approved a new Statute on management of the federal stock of OJSCs and the use of a special right for the RF's participation in management of OJSCs (the "golden share right"). The document has replaced an analogous Statute approved by the previous Cabinet (Resolution of January 23, 2003, No. 44), albeit mostly replicating that. The main provisions of the document are as follows:

Rights of stockholders in OJSCs whose stock is owned by the federal government fall under the respective mandate of the RF Ministry of State Property that acts on behalf of the RF Government. It is this particular Ministry that exercises with respect to OJSCs, except for those whose voting stock is in the federal property¹²¹, the right to introduce issues in the agenda of a shareholders' meeting, slate to a company's executive bodies, demand an early meeting and call of an early general shareholders' meeting, appoint a representative (to issue a proxy vote) for him to vote at the general meeting, to develop the stand of the state as a shareholder with regard to the agenda of the general meeting.

The RF' stance on items of the agenda of the general shareholders' meeting is highlighted in directives the RF Ministry of State Property provides in writing to the representative as to how he should vote at the general meeting. In such cases, therefore, the representative acts on the basis of such directives and the noted proxy vote.

As concerns OJSCs that are enumerated in a special list subject to the RF Government's approval, except for those whose shares are in the federal property, the state's stand as a shareholder with regard to introducing items into the agenda of the general meeting, slating individuals to the company's executive bodies, the auditing committee and counting commission, laying a demand for holding an early general meeting, voting on items in the agenda of the general shareholders' meeting is determined by

¹²¹ In this case it is Roskomimuschestvo that exercises the powers of the general shareholder meeting, and the respective decision is made by its order. In this case, provisions concerning procedures and timelines of preparation, calling and conduct of a general meeting are not applied. In the event such a CJSC is enumerated in the special list subject to the RF Government's approval, the stand of the state as a shareholder is determined by the decision of the RF Government, its Chairman or a Deputy Chairman who acts on behalf of the Chairman.

the RF Government or its Chairman's (or Vice-Chairman, on behalf of the Chairman) decision.

The rights of the state as a shareholder are exercised by the RF Ministry of State Property. In doing this, the Ministry proceeds from the classification of all the OJSCs with the federal stake in their capital into three groups:

- in joint-stock companies enumerated in the special list, the ministry acts upon conciliation with a federal Ministry or a federal body of executive power duly authorized to manage state-owned property, which is administered by the RF President or the RF Government (hereinafter referred to as the Federal Body)¹²²;
- in joint-stock companies enumerated in the list of strategic companies approved by the RF President (hereinafter referred to as the Strategic List)¹²³, except for joint-stock companies enumerated in the special list – on the basis of proposals put forward by a federal agency reporting to a federal Ministry (hereinafter referred to as the Federal Agency) or by the Federal Body;
- in other joint-stock companies – at its own discretion, and in the event a Federal Agency or a Body puts forward, following the respective procedures, proposals on matters related to determining the shareholder's stand, it acts as a shareholder and with account of the noted proposals.

If federal ministries, agencies or other federal bodies have proposals on calling of an early shareholders' meeting, they should forward their proposals to the RF Ministry of State Property no later than in 20 days prior to the planned date. If the agenda of the meeting comprises issues on re-election of members of the board or the supervisory council of a JSC, the respective deadlines will make up 30 and 40 days, respectively.

The noted proposals should contain formulations of items subject to inclusion in the agenda of an early shareholders' meeting and formula-

¹²² As concerns joint-stock companies enumerated in the special list, in the event a given federal Ministry has subordinated federal agencies, proposals submitted to Rosimuschestvo on every item of the agenda should bear a consolidated stance of the said Ministry and agencies subordinated to it.

¹²³ Approved by presidential Decree of Aug 4, 2004, No. 1009.

tions of decisions on them, as well as proposals on the form in which the meeting should be conducted. Such proposals are submitted together with an explanatory note, which should contain a justification for the inclusion of a given item in the agenda and materials needed for decision making. In the event one introduces to the agenda of an early shareholders' meeting the item of changing the composition of the company's executive bodies, the auditing committee and counting commission, he should also provide information of candidates to be elected to the noted bodies and commissions of the joint-stock company (references produced by the HR department of the company the candidate currently works).

The procedure of preparation for the annual general shareholders' meeting suggests that the Federal Ministry (Body, Agency) forwards to the RF Ministry of Property its proposals on introducing items to its agenda and slated candidates for their election at the noted meeting to the company's executive bodies, the auditing committee and counting commission until December 1 of the year preceding the year in which such a meeting is to be held.

Such proposals should contain a stance that concerns voting on the proposed issues, formulations of decisions to be made, along with an explanatory note and necessary materials, as well as information of candidates for their election to executive bodies, the auditing committee and counting commission of the joint-stock company (references produced by the HR department of the company the candidate is currently employed with).

Upon receipt of the announcement of holding a general shareholders' meeting, the Federal Ministry (Body, Agency) forwards to the RF Ministry of State Property its proposals concerning voting on items enumerated in the meeting agenda and appointment of a representative to vote at the general meeting (this concerns joint-stock companies included in the special list) within 3 days, but no later than 15 days prior to the date when the meeting is to be held and within 20 days, if the agenda of the general shareholder meeting contains the issue of the company reorganization.

If the announcement on holding the general shareholder meeting has failed to reach the recipient in time, such proposals can be formulated on the basis of the meeting agenda approved by the board of directors.

The proposals are submitted along with an explanatory note, which contains a justification for the proposed decisions, and necessary materials.

Proposals can be developed and forwarded to the RF Ministry of State Property well in advance on the basis of minutes of the Board meeting at which the Board has set the agenda of the general shareholders' meeting.

The number of candidates suggested for the company's Board cooptation list the RF Ministry of State Property forwards to an OJSC should exceed by 3 the number of candidates which corresponds to the state share in the company's authorized capital. The number of candidates suggested for inclusion in the list for election to the Board, the auditing committee and counting commission of a JSC may not exceed the quantitative composition of the bodies in question set by the general stockholders' meeting.

As concerns JSCs that are not enumerated in the special or strategic lists, the Federal Agency (Body) enjoys the right for submitting its proposals to the RF Ministry of State Property (and those with regard to candidates proposed for inclusion in the list for election to the Board, among others) arranged in accordance with requirements of the said point.

The RF Ministry of State Property completes voting directives to the state representatives who are going to attend general meetings.

The Procedure of identification of the stand of the state as a shareholder in OJSCs enumerated in the special list (Art. 12–15 of the Statute) reads that slating proposals with regard to a joint-stock company's executive bodies, the auditing committee and counting commission, as well as introducing other items in the agenda of the general stockholders' meeting, except for issues stipulated in p.1 Art. 47 of the federal Act "On Joint-stock companies"¹²⁴, are to be submitted to the RF Government by the RF Ministry for Economic Development and Trade no later than December 1 of the year preceding the one during which the general stockholders' meeting is held (and in the event of an early meeting – no later

¹²⁴ Meaning the mandatory for this particular kind of meetings issues, including election of the board of directors (supervisory council) of the company, auditing committee (company's auditor), approval of the company's auditor, annual reports, annual accounting report.

than in 10 days prior to the deadline of their presentation to the joint-stock company), with the necessary materials attached to them, including:

- proposals received from the Federal Ministry (body);
- information of candidates for election to the OJSC's executive bodies, auditing committee and counting commission (references supplied by HR departments of the company the candidate works at the moment);
- information of the OJSC (the state share in its authorized capital, the composition of its executive bodies, auditing committee and counting commission, main financial and economic performance indicators, and other necessary data);
- notarized or verified by the RF MEDT copies of the company's statutory documents and accounting reports over the last year.

Proposals on the demand for calling of an early general stockholders' meeting is submitted to the RF Government by the RF MEDT no later than in 10 days prior to the envisaged date when such a demand is to be put forward, supplemented with necessary materials.

The RF MEDT likewise is bound to meet the same deadline, so far as its proposals on voting on items of the agenda of the general stockholders' meeting, and, again, it should submit to the RF Government materials the JSC has prepared for the meeting, as well as other necessary materials.

Proposals on items included in the agenda of a general stockholders' meeting of a joint-stock company enumerated in the special list, whose voting shares are in the federal property, are to be submitted by the RF MEDT to the RF Government no later than in 30 days prior to the date of conduct of the general stockholders' meeting, and in the event of conducting an early shareholder meeting, – no later than in 10 days prior to the intended date of making the respective decision.

Acting in behalf of the Russian Federation in an OJSC's Board of Directors are individuals elected to the Board in a due order from candidates slated by the state.

The procedures read that such representatives of interests of the state in the Board of Directors exercise voting on items of the agenda of the Board meeting on the basis of the RF Ministry of State Property's direc-

tives issued in writing. The Ministry is bound to issue directives on matters stipulated in sub-points 1 (identification of priority avenues of the company's operations), 2 (calling of the annual and early shareholder meetings, except for cases in which the term of the calling of an early meeting has been broken or one was refused to hold such a meeting), 3 (approval of the agenda of the general stockholders' meeting), 5 (increase of the company's authorized capital by means of placement of additional stock within the limits of the quantity and categories (types) of the authorized stock, if the company's Charter, in compliance with the law, reads that this matter falls under purview of the Board of Directors), 6 (placement by the company of bonds and other papers in the event provided for by the law), 7 (identification of the price (monetary appraisal) of the property, price of placement and redemption of issued papers in the events provided for by the law), 9 (establishment of the executive body of the company and an early termination of its powers, if the company's Charter reads that this falls under the competence of its Board of Directors), 11 (recommendations on the amount of dividend on its stock and procedures of its payment), and 15 (approval of large transactions) of p. 1 of Art. 65 of the federal Act "On joint-stock companies), as well as on the matter of election (re-election) of the Chairman of the Board¹²⁵. The RF Ministry of State Property has a right to issue directives on other matters to representatives of the state interests in the Board of Directors.

With account of the aforementioned classification of all the OJSCs with the federal share in their capital, one designs directives to representatives of the state interests in the Board of Directors:

- of joint-stock companies enumerated in the special list – upon reconciliation with the Federal Ministry (Body);
- of joint-stock companies enumerated in the strategic list – on the basis of proposals of the Federal Ministry (Body);

¹²⁵ As concerns representatives of the state interests in the Board of Directors of CJSCs enumerated in the special list, the matter stipulated in subpoint 2 p.1 Art. 65 of the federal Act "On joint-stock companies" is absent in the list of matters on which directives are issued.

- of other joint-stock companies – at his own discretion, and in the event the Federal Agency (Body) presents, in a due order, its proposals – with account of the noted proposals;
- as concerns joint-stock companies enumerated in the special list, in the event the Federal Ministry has subordinated federal agencies, proposals submitted to the RF Ministry of State Property should reflect a consolidated stand of the Federal Ministry and the Federal Agency subordinated to it.

The Federal Ministry (Body, Agency) forwards to the RF Ministry of State Property its proposals within 3 days upon the date of receipt of necessary materials, but no later than in 12 days prior to the date of the Board meeting. The proposals in question can be designed and forwarded to the RF Ministry of State Property well in advance on the basis of data received from representatives of the state interests in the Board of Directors. The Federal Agency (Body) has a right to forward to the RF Ministry of State Property its proposals on the agenda of meetings of other joint-stock companies' boards.

Directives to representatives of the state interests in boards of directors of joint-stock companies included in the special list on matters enumerated in subpoints 1,3,5,6,7,9,11,15 of p. 1 Art. 65 of the Act on joint-stock companies are subject to approval of the Chairman of the RF Government or his deputy acting in his behalf.

Draft directives to representatives of the state interests in boards of directors completed according to the present Statute are submitted by the RF Ministry for Economic Development and Trade to the RF Government no later than in 7 days prior to the date of the Board meeting.

Procedures of appointment and *modus operandi* of state representatives in a Board of Directors and the Auditing Committee of an OJSC on which the decision was made to use the special right for the RF's contribution to its management (the "golden share") suggests that such individuals are appointed by the RF Government upon recommendation of the RF Ministry for Economic Development and Trade upon reconciliation with the Federal Ministry (Body). Meanwhile, the latter's opinion should be cleared with the federal ministry to which it reports. State representatives in the board of directors and the auditing committee exercise

their respective powers guided by directives the Ministry of State Property gives them in writing.

A formalized apparatus of the state's participation in the corporate governance procedures in joint-stock companies in the new conditions has become a set of model documents the RF Ministry of State Property approved with its Order of July 26, 2005, No. 228, which came in effect since August 1, 2005. The list of the documents in question includes:

- a model form of directives to representatives of the RF's interests in the Board of Directors of an OJSC whose shares are in the federal property;
- a model form of directives to the state representative at the general stockholders' meeting of such an OJSC;
- a model form of the proxy vote to the state representative to act in behalf of the Russian Federation at the general stockholders' meeting of an OJSC whose shares are in the federal property;
- a model form of the ruling of the sole shareholder of an OJSC 100% of whose stock is in the federal property;
- a model form of the ruling of the sole shareholder of an OJSC 100% of whose stock is in the federal property on increase of its authorized capital by means of placement of additional stock;
- recommendations with regard to formation of the state's stance on the matter of approval of the annual report of an OJSC whose shares are in the federal property;
- recommendations with regard to formation of the state's stance on the matter of reconciliation of a transaction involving proprietary interest and a large-scale transaction by the OJSC whose stock is in the federal property;
- a form of the passport of the meeting of a executive body of the OJSC whose stock is in the federal property.

The expressions used in *the Model forms of directives* make it mandatory for the state representative to vote in a particular way ("for" or "against") with regard to the proposed draft ruling (optional: to ensure election of given individuals as directors to the Board (including the Chairman), the auditing committee or to withdraw the matter from discussion with a due reference to the reason of the move). As concerns other items of the agenda, the state representative is bound to vote, in

compliance with the effective law, in pursuance of interests of the state and the joint-stock company. In the event there arise any additional items not enumerated in the officially received by the RF Ministry of State Property agenda, the state representative is bound to blackball any decisions. The state representatives are bound to submit to the RF Ministry of State Property minutes of the Board of Directors' meeting within a fortnight upon the date when it has been held.

Directives are made in the form of a letter from a deputy head of the RF Ministry of State Property. They are registered following the Ministry's records management procedures and are supplemented with the passport of the meeting of an executive body of the OJSC whose stock is owned by the federal Government. The passport is made in the form set by the Ministry Head's order. The directives are also supplemented with an explanatory note signed by the head of a department of the RF Ministry of State Property. The note bears justification for the recommended draft decision on each item of the agenda and the respective stance of the sectoral federal body of the executive power (if in existence). It is not allowed to employ in directives a wording different from that set by the Model Forms.

The proxy vote for one to act in behalf of the state contains the number of the state-owned stock and its proportion in the authorized capital. The proxy vote is granted with no right to delegate it to another entity. The proxy vote is valid for no longer than 7 days from the date preceding the one when the general stockholders' meeting is conducted, and it is also valid in the event of holding, in compliance with the RF law, a repetitive general stockholders' meeting whose agenda remains unchanged.

The Model Form of decision of a sole stockholder in an OJSC, 100% of whose stock is in the federal property has its own peculiarities, as it is executed in the form of the order of the RF Ministry of State Property. The Model Form bears direct references to matters that should be granted approval in a mandatory order: 1) annual report; 2) annual accounting report, including report on profits and losses; 3) distribution of profit, including dividend payments; 4) election of the Board of Directors, including a government representative; 5) election of the auditing committee, including a government representative; 6) appointment of the Director General; 7) approval of the auditor.

To have the RF Ministry of State Property develop its stand on items on the agenda of the general stockholders' meeting of a joint-stock company, 100% of whose shares are in the federal property, one should submit to the Ministry the following materials: 1) copies of minutes of the Board's meetings which tackled matters of preparation for the general stockholders' meeting; 2) the company's annual report in the form as per recommendations set by the Ministry's order; 3) the bookkeeping balance sheet with all the annexes over the reported year authenticated by the company head and bearing a tax office's mark; 4) an auditor's conclusion by results of examination of the company's financial and economic performance over the respective year; 5) conclusion of the auditing committee on results of examination of the company's financial and economic performance over the respective year; 6) recommendations by the Board of Directors of the company on distribution of profit, particularly with regard to the amount of dividends on its shares and procedures of their payment by the company's performance over the financial year executed in the form of a protocol of the Board meeting; 7) data on the candidate(s) submitted to the company's executive bodies, its Board of Directors and the auditing committee; 8) protocol of the tender committee on selection of an auditor for the respective year; 9) other documents required for making decisions on certain matters in compliance with the effective law and the Order in question.

Whilst employing the Model Form of decision made by the sole stockholder in an OJSC, 100% of whose shares are in the federal property, to increase its authorized capital by placing additional stock, one is bound to refer to the number of shares up to which their number will be increased, the size of increase of the authorized capital, the placement costs of one nominal ordinary paperless stock of an additional issuance by face-value, dates of the beginning¹²⁶ and the end¹²⁷ of the stock place-

¹²⁶ The date of the beginning of placement of securities of a give issuance is the day following the date when the notification of the state registration of the issuance of securities was received.

¹²⁷ In the respective case, the Order can also read that "the date of the end of the placement of security a given issuance is the date of receipt of the proprietor right for the number of stock in figures (the number of stock in writing) of the stock of the organization's name in full whose stock is contributed with to payment of the authorized capital, but no

ment, which, under their placement by private offering, should be paid for in full. Modifications in the OJSC's Statute associated with changes in the number of its stock¹²⁸ are likewise subject to approval.

The decision of the sole stakeholder of an OJSC 100% of which belongs to the Russian Federation to increase its authorized capital by means of additional stock placement is also legalized by the respective order of the RF Ministry of State Property. To have the Ministry develop its stance on this particular item of the agenda of the general stockholders' meeting, one should submit: 1) a copy of the minutes of the meeting of the Board of Directors at which the Board considered the matter of increasing the company's authorized capital by means of additional stock placement; and 2) other documents required for decision making on individual matters in compliance with the effective law and according to the present Order.

In the event additional stock is paid for with non-monetary means (securities, in kind, property rights or any other rights whose value can be appraised using cash equivalent) the RF Ministry of State Property's Resolution should provide for a list of property that can serve to the noted effect. In this case, to have the Ministry formulate its stand, one should present a conclusion which is based upon findings of an evaluation of the report on appraisal of the respective property drafted by the Department of Property Accounting, Analysis, Appraisal of and Control over its Use under the RF Ministry of State Property. If needed, in a respective case, one also states that "the additionally placed stock can be paid for with property".

Recommendations for formation of the state's stand on the matter of approval of the report of an OJSC whose stock is in the federal property consist of the following sections: 1) general data on the company; 2) description of executive and control bodies of the OJSC (the general stockholders' meeting, Board of Directors, executive body, auditing commit-

later than in one year upon the date of the state registration of the additional securities issuance".

¹²⁸ In the event the company's Statute bears no reference to the required quantity, nominal value, categories (types) of stock the company has a right to place in addition to the already placed stock (authorized stock) and the rights granted by the stock.

tee); 3) the enterprise's position in the sector; 4) priority profile avenues; 5) report of the Board of Directors (Supervisory Council) on results of the enterprise's development by its priority profile avenues; 6) information of large-scale transactions and deals with interest concluded by the enterprise; 7) report on the dividend payment; 8) description of main factors of risks associated with the enterprise's operations; 9) prospects for the enterprise's development.

Recommendations for formation of the state's position on the matter of reconciliation of a transaction involving interest and a large deal by an OJSC whose stock is in the federal property state that to this effect the following materials should be analyzed: 1) verified in a due order copies of documents that prove the presence of parties' interest in execution of the transaction in compliance with the effective law (in the event of there is interest in completion of the deal); 2) certified in a due order copy of the accounting balance-sheet of the OJSC whose stock is in the federal property, as of the last date of reporting; 3) authenticated by the head of such an OJSC copy of the Statute of the respective joint-stock company; 4) prepared, in compliance with the RF law on appraising activities, report on the appraisal of the market value of the property with which one is going to make the future transaction, no later than in 3 months prior to its submission (if necessary); 5) conclusion by results of evaluation of the report on appraisal of the respective property prepared by the noted Department of Property Accounting, Analysis, Appraisal of and Control over its Use under the RF Ministry of State Property (if necessary); 6) draft contract on conclusion of the deal (except for cases when the contract is concluded at an auction held in the form of competition) and a detailed description of all the terms and conditions of the deal; 7) information of the forecast of the impact the deal should have on efficiency of the OJSC's operations in terms of its production and financial performance indicators; 8) opinion expressed in writing on appropriateness of conclusion of the deal prepared by a federal agency that exercise coordination and regulation of operations in the respective sector (sphere of management) (if any).

Passport of the meeting of the executive body of the OJSC whose stock is in the federal property should contain the following information:

1) the date when the meeting is held; 2) the number of stock in the federal property and their proportion in the authorized capital (with the number of the voting stock provided separately from other kinds of stock); 3) values of a number of economic performance indicators (gains, net profit, net assets) over the reported year and the prior financial one); 4) the suggested amount of dividends, particularly as a proportion from net profit (with separation of those falling on the federal stake); 5) composition of the Board of Directors (with separation of the actual and possible number of individuals that represent the state interests); 6) a part of documents at hand: the annual report, the one of the auditing committee, the auditor's conclusion, and the protocol by the tender committee on auditor selection.

Finally, the state resumed the problem of shaping a uniform dividend policy, as accentuated by the RF Government in its Order of May 29, 2006, No. 774-p. The Order directly commissions the federal agencies of executive power to guide themselves with the below provisions while shaping a stand of the Russian Federation as a shareholder in joint-stock companies whose stock are in the federal property with regard to dividend payments:

- identification of a fixed minimum proportion of the company's net profit forwarded on dividend payments;
- channeling the net profit not assigned for financing investment projects and for other purposes to dividend payments;
- investment projects should match return rates set by the company;
- employment of indicators of the aggregate (consolidated) reporting, while computing the amount of dividends in a joint-stock company that has daughter companies.

As concerns matters of distribution of net profit, while shaping the RF's stand as a shareholder, the federal agencies of executive power should proceed from the need for decision making on the basis of the analysis of:

- planned financial indicators of such a company, including profit, over a medium-term period (not less than 3 years);
- economic efficiency of the channeling of the company's net profit to finance investment projects and for other purposes;

- correlation between the proportion of net profit channeled for dividend payments and the ratio of the actual value of the company's profit to its planned value;
- amount of borrowed capital used to finance investment projects in the event depreciation resources appear scarce;
- correlation between the amount of rewards due to members of the company's executive bodies and attainment of its planned performance indicators.

The RF Ministry of Economic Development and Trade was assigned with a task to develop, within 3 months, with account of proposals of the federal agencies of the executive power concerned, and to seek approval of methodological recommendations on development of a stand of the RF as a shareholder in joint-stock companies with regard to dividend payments and, together with the federal agencies of executive power concerned to provide for the joint-stock companies' approval of the documents concerning dividend payments by December 1, 2006. The RF Ministry of State Property, as a principal agency responsible for implementation of the policy with regard to the federal blocs, together with the federal agencies of executive power concerned, was assigned with a task to ensure that the respective proposals would be included into agendas of meetings of the respective joint-stock companies' executive bodies.

While assessing the noted document, it is noteworthy that it is based chiefly on the aforementioned approach developed by the RF Ministry of State Property and the RF Ministry for Economic Development and Trade. The only novelty is a thesis of the necessity of the analysis, while making a decision on distribution of net profit, of the correlation between the amount of a reward due to members of the joint-stock company's executive bodies and attainment of the company's planned performance indicators. Accordingly, the reference to weak spots in the noted ministries' approach to the dividend policy retains its urgency. It can be assumed that the actual workability will largely depend on the substance of the methodological recommendations on identification of the RF's stand as a shareholder in the respective joint-stock companies with regard to dividend payments.

Important milestones that may have a substantial impact on advancement of the companies with the state share in their equity have become amendments to the RF Act “On privatization of the public and municipal property” of 2001. The most substantial amendments are:

In spring 2005 the Government lifted its ban on purchases of land lots occupied by all legal entities in which the government- and municipality-owned share exceeds 25%. This provision would enable a number of huge companies, including Gasprom, RAO “UES Russia”, Sberbank, among others, to buy land under their real estate objects. This should boost their investment attractiveness by means of growth in their capitalization and ability to borrow from overseas (mostly in the form of loans).

Yet more important novelty that concerns the public property management was formed become amendments to the effective 2001 Act on privatization. The amendments were introduced in July 2006 and their mission is to regulate procedures of an increase of the authorized capital of the OJSCs founded in the process of privatization, 25%-plus stock of which is in the state or municipal property.

The previous wording of the Act allowed an increase in the authorized capital of such companies by means of an additional stock issuance, only providing the state or municipal entity’s share remained unchanged. The RF MEDT believes in the conditions of economic growth such a restriction hampered attraction of investment by joint-stock companies with a state-owned share in their authorized capital, as in practice budgetary funds for those purposes were not allocated – at best, one could speak of contribution with some property as a form of payment for an additional stock issuance and for the sake of maintenance of the previous proportions in the distribution of the capital between different groups of stockholders.

The new variant of the Act on privatization (Art. 40) enumerates a whole series of government bodies (the RF President, the RF Government, a government body of the RF Subject, a local self-governance body), which enjoy the right for making a decision on the possibility to increase a company’s authorized capital along with a reduction in the share held by the state (municipal entity).

Now, given the stock held by the state (municipality) in an OJSC founded in the process of privatization, which at the moment of making the respective decision accounts for 25%-plus, but no more than 50% of votes at the general stockholders' meeting, an increase in the company's authorized capital by means of an additional stock issuance may be executed with a reduction in the state's (municipality's) share, providing there is a positive decision made by the RF Government, a body of the RF Subject's executive power or a local self-governance body and only providing the state (municipality) retains its share which should account at least for 25% plus 1 voting share. The same provision is applied to the OJSCs enumerated in the list of strategic JSCs, providing there is a positive decision by the RF President.

In the event the state (municipality) owns a stock in an OJSC established in the process of privatization, which account at the moment when the respective decision is made for over 50% of vote at the general stockholders' meeting, an increase in the company's authorized capital by means of an additional stock issuance can be exercised along with a reduction in the share held by the state (municipal entity), providing there is a positive decision by the RF Government, a body of the RF Subject's executive power or a local self-governance body and only providing the state (municipality) retains its share amounting for no less than 50% of vote plus 1 voting share. Like in the above case, should an OJSC be included in the list of strategic joint-stock companies, such a decision can be made exclusively by the RF President.

In a similar fashion, state bodies have been granted the right to identify the size of the state-owned shares in a company's authorized capital by means of open subscription and their listing exercised by a stock exchange, as well as by placing their stock outside Russia, including by means of placement, in compliance with an overseas law, of securities of foreign issuers that certify the rights for stock of open-end joint-stock companies (Art. 40.1):

- increase in the authorized capital of an OJSC enumerated in the list of strategic joint-stock companies and identification of the state-owned share in the company's authorized capital are made following the respective decision of the RF President;

- increase in the authorized capital of an OJSC founded in the process of privatization whose stock is in the federal or municipal property and account for more than 25% of vote at the general stockholders' meeting, and identification of the size of the state-owned share in the company's authorized capital are made as per the ruling by the RF Government, a body of the RF Subject's executive power or a local self-governance body.

On the surface this arrangement seems fairly flexible, as it gives joint-stock companies with state-owned stakes possibilities for attraction of investment combined with requirements to property control on the part of government agencies. However, it is only future practices which will show whether, and to what extent, this apparatus enjoys demand and will prove its viability.

The domestic record of previous attempts proves that whenever a problem with enforcement of the corporate law arises, the business community views a high stock concentration as the most acceptable guarantee against concomitant risks of investing in a given company. This makes an opportunity to attract new investors through an additional stock issuance fairly unlikely, as long as the government is a large stockholder, albeit so far as individual attractive companies that enjoy certain advantages or nonpareil resources are concerned, such a scenario may well be realized. As well, one should not forget risks associated with the state's involvement in economic activities. The group of such risks includes a low qualification of civil servants, their poor motivation, and possible rent-seeking behavior of theirs.

The respective pilot project was launched involving the Bank for Foreign Trade (*aka* VTB). Following the presidential Decree of late 2006, the Bank was allowed to execute procedures of increase of its authorized capital by means of an additional stock issuance and stage-by stage sales of its shares, while retaining the state-owned share not less than 50% of vote plus 1 voting share at the general stockholders' meeting. The respective modification concerning the size of the state-owned share was introduced to the list of strategic joint-stock companies.

2.3. Problems of Public Property Management in the Corporate Sector and the Administrative Reform

The period of 2004–2006 saw matters of management of economic companies with the state share in their capital interlaced into the context of the administrative reform and its consequences.

Firstly, the struggle around the List of strategic enterprises and joint-stock companies appeared particularly noteworthy. By early 2005 the RF Ministry for Economic Development and Trade had prepared and submitted to the RF Government a draft presidential Decree “On introducing amendments to the List of strategic enterprises and strategic joint stock-companies”.

The document suggested that 252 organizations, including 43 federal unitary enterprises and 209 OJSCs, should be excluded from the List. More specifically, it is provided for exclusion from the List of 8 blocs in joint-stock companies and 9 FPUEs that operate in the area of civil aviation, 23 OJSCs that are sea and river ports, 39 sea and river transportation companies, and 47 OJSCs whose profile is associated with gasification and the gas-related economy in the respective RF Subjects.

Thus, more than a half of the strategic joint-stock companies proposed for exclusion from the noted List fell under the transport and infrastructure sectors. The Ministry for Economic Development and Trade justified for such an approach with the need for attraction of extrabudgetary funds to kinds of operations the distinguishing features of which are a great capital coefficient and a long time of return on investment in the conditions when their need for investment exceeds the budget capacity of the state and internal sources of the respective enterprises, which intensifies disproportions between the growing demand for transportation services and possibilities for meeting that. In the same fashion and context the Ministry referred to contribution of the private capital into construction and operations of airports, ports that serviced river transport, and the presence of the private capital in the market for energy, and privatization of most companies that dealt with production of energy resources.

The Ministry argued that possible privatization outcomes would be a greater competitiveness of the infrastructural objects, lower transportation costs, acceleration of movement of passenger and cargo flows, greater

handling (transportation) capacities, the coming of new investors, a positive impact on the state of the competitive environment, and a greater quality of management of the respective objects. As an additional argument in favor of sales of the federal blocs of shares, the Ministry referred to a fall in their potential value in the event of an insufficient budgetary financing of the respective enterprises.

The draft Decree also suggested excluding from the list of strategic joint stock companies 73 ones, in which the Federation owned less than 51% of authorized capital. This proposal rested upon an analysis of the companies' operations which revealed that they failed to secure production necessary for provision of the nation's defense capacity and security, and protection of morale, health rights and legal interests of the citizens of RF. There are no legal acts in compliance with which there have been established requirements to production of the respective goods (works, services) exclusively by public organizations. For some JSCs production of strategic goods does not constitute an exclusive component in the overall volume of their output, with the private sector producing analogous goods (works, services). The RF MEDT believes that keeping such blocs in the federal property is inappropriate, and their size enables the state just to block decisions made by general stakeholders' meetings.

Plus, subject to exclusion became federal public unitary enterprises and open joint-stock companies whose inclusion in the 2004 and 2005 privatization programs was agreed upon with the federal bodies of executive power.

The document was prepared with account of proposals put forward by the federal bodies of executive power in charge for implementation of the government policy in the respective sectors. Once a disagreement arose, it was resolved in by means of reconciliation procedures with participation of the noted ministries and agencies.

Despite the due account of the sectoral specificity, the draft Decree developed by the RF MEDT underwent substantial modifications introduced by the RF Government staff. As a result, the number of enterprises and JSCs subject to exclusion from the noted List of strategic enterprises and JSCs was reduced. After that, submitted to the presidential Administration, the draft Decree contained a list of 8 federal public unitary en-

terprises and 179 open-end joint-stock companies. Hence, if compared with the original version, the number of OJSCs subject to exclusion from the group of strategic ones was cut roughly by 15%, while the number of FPUEs – more than 5-fold.

None the less, the Department for State and legal Affairs under the RF President rejected the draft Decree and returned it for further refining. In addition to technical comments, the Department experts expressed doubts as to the necessity to exclude from the noted list a great number of enterprises and JSCs without a detailed analysis of their role in provision of the nation's defense capacity and security. That necessitated holding a meeting to eliminate the discrepancies. The comments of the presidential staff were consequently taken into consideration. In light of the above, the RF MEDT acknowledged a proposal by the staff of the Security Council of RF concerning a subsequent development of a regulation on preparation of proposals on specification of the List of strategic enterprises and strategic JSCs, which would enable one to periodically update that, as required by the effective privatization law.

Between 2004 and 2006 as many as 31 FPUEs and 16 JSCs with the federal stakes were excluded from the list of strategic enterprises and joint-stock companies. The excluded enterprises mostly fall under the machine-building industry and the military- industrial complex and they were candidates for inclusion in the composition of integrated structures. Thus, in late-2004, as many as 4 OJSCs were excluded from the List, due to their inclusion in the Joint Industrial Corporation “Oboronprom¹²⁹”, while in early-2006 another 6 OJSCs and 2 PFUEs were likewise crossed out from the List, as they were included in the newly established Joint-Aircraft-Building Corporation. In 10 out of the 16 noted joint-stock companies the size of the federal stake varied from 25% to 50%, in another 6 ones it exceeded 50%, including 2 companies with the state owning the 100% stake in them. In addition, it should be noted that, excluded from the list of strategic enterprises and joint-stock companies in late-2004, Rosneft was replaced by Rosneftegas, due to implementation of a project on consolidation of the state control in Gasprom (see below for more de-

¹²⁹ The corporation deals with consolidation of assets of the domestic helicopter producers.

tails). So far as both companies are concerned, one speaks of the 100% state-owned stake.

Meanwhile, during the period in question new strategic enterprises and joint-stock companies joined the respective List, including 5 FPUEs: “Goznak” (with 8 profile unitary enterprises being transformed into its branches), 2 information agencies (ITAR-TASS and RIA “Novosti”), the TV technical center “Ostankino”, the departmental railroad security, Novorossyisk sea merchant port (with the state-owned stake accounting for 20%), and 3 integral structures being joint-stock companies (including the aforementioned Oboronprom¹³⁰). The federal government’s share in Oboronprom’s authorized capital is 51%, while that in “Sozvezdiye” and NORFEC – 100%.

As a result, by early-2007 the number of strategic enterprises had fallen from 514 to 488 units, while that of strategic joint-stock companies – from 549 to 537. It is quite notable that the reduction in the latter group was substantially smaller than in the former one¹³¹.

If judged by the state-owned share in their authorized capital, the structure of strategic joint-stock companies did not undergo any drastic changes against the original one of summer 2004 (see *Table 44*). The bulk of strategic JSCs was formed by those with the state-owned stake varying between 25% and 50% (366 units, or 68.2% of enterprises), the proportion of companies with the state-owned share ranging between 50% to 100% was 19% (102 units), and the rest (11.9%, or 64 units) mostly fell on the group of enterprises fully owned by the state, with companies in which state was a minority stockholder (under 25% of stock) accounting for less than 1% (5 units).

Secondly, the progress with privatization (including sales of the federal blocs) found itself seriously affected by a clash between the Russian Federal Property Fund (RFPPF) and the RF Ministry of State Property.

¹³⁰ While the state directly owns a control bloc in Oboronprom, its large stockholder also is Rosobornexport.

¹³¹ The list of strategic enterprises and joint-stock companies continued to undergo changes in 2007. Such changes were fueled by the further build-up of integrated structures, including the expansion of the Joint Aircraft-Building Corporation, with its introduction in the list, and establishment of a new “Joint Ship-Building Corporation” and its three daughter ship-building and repair centers.

With the launch of the administrative reform in spring 2004, the Ministry has been led by Mr. V. Nazarov. He started with an attempt to re-galvanize a long-standing idea of broadening the group of sellers of to-be privatized federal and referred to the need for acceleration of the process. But it was RFPPF whose mandate had for long comprised the function. The Ministry initiated amendments to the privatization law to deprive RFPPF of the exclusive seller's right. While drafting its new Statute, the Ministry specified its right to hold state-owned shares until the new owner took them over. The Ministry consequently initiated amendments to the RFPPF Statute, which were to deprive it of the right to own and control the privatized enterprises' assets, with a view to ultimately make RFPPF a structure funded from the budget, while today the organization's funding comes from commission fees from sales of privatized assets. That, perhaps, became one of the causes (others being purely interdepartmental tensions) underlying a serious conflict between the two agencies.

With reference to its Statute and earlier adopted regulation of its relationship with the RF Ministry of State Property, RFPPF demanded from the Ministry to pass stock subject to privatization under its control. However, by early summer 2005, the Fund failed to reassign to none of 34 victors in the auctions the enterprises they had bought, as the Fund failed to obtain their stock from the Ministry. Mr. Yu. Petrov, the Head of the Fund, expressed his intent to suspend further announcements of upcoming auctions, which would have meant a complete halt to the whole privatization process. In all, in 2005 the Fund failed to publish informational announcements on sales of stock in 183 joint-stock companies, which had been for the first time included in the privatization program¹³².

A temporary remedy became Order of June 7, 2005, No. 122 of the RF Ministry for Economic Development and Trade, which read that in compliance with certain procedures, the RF Ministry of State Property should register and reassign to the Russian Federal Property Fund originals of transfer orders on the transfer of privatized stock no later than within 3 working days upon receipt from RFPPF of copies of protocols on

¹³² О приватизации федерального имущества в 2005 году. Отчет федерального агентства по управлению федеральным имуществом. М., 2006.

auction results and sales contracts with regard to the stock the sales of which was recognized as valid. RFPPF in turn completes transfer orders on the transfer of the stock to buyers and exercises interaction with entities that keep stockholder registers. Meanwhile, the transfer orders on the transfer of stock in favor of the Fund are forwarded to registrars simultaneously with the transfer orders on the stock transfer to the buyers. This allowed one to minimize the time during which the stock are controlled by an entity that is not authorized to exercise the shareholder's rights on behalf of the Russian Federation (in reality, the stock pass via the seller's personal account by transit).

In late December 2005, with its Resolution N 782 the RF Government introduced modifications to the RFPPF Charter, of which the most significant one became restrictions on its independence. It was explicitly enunciated that the Fund was founded by the RF Government, the RF Ministry for Economic Development and Trade coordinated and controlled its operations, while the powers of the owner of the property that falls under operative administration of the Fund were exercised by the RF Ministry of State Property, following procedures and within the limits set by the federal law, presidential decrees and resolutions of the RF Government.

As concerns the exercise of the stockholder's powers on behalf of the Government, RFPPF is restricted only by sales of stock of economic companies owned by the federal Government that are included in the Forecast Federal Property Privatization Plan (Program). Accordingly, this provision was reflected in the Statute on management of the state-owned stock in open joint-stock companies and use of the special right for the RF's participation in management of joint-stock companies (the "golden share right").

RFPPF has retained the right to carry out commercial operations that conform to its profile, albeit the respective proceeds are to be accrued on its account with a territorial body of the Federal Treasury. The Fund can spend these funds according to the revenue and expenditure estimate approved according to procedures determined by the head manager of the federal budget funds and within the balance of the respective funds on its account. Earlier, the Fund enjoyed the right to place temporary free extrabudgetary funds on deposit accounts. The information on property the

Fund acquires at the expense of its proceeds from its entrepreneurial activities should be submitted to the RF MSP within a month after they were collected.

While in the past the main source of the Fund's funding was formed by resources it would receive for organization and conduct of privatization of the federal property at an amount and by categories of costs set by the RF Government, the new version simply refers to the federal budget funds, while the revenue and expenditure estimate of the Fund is to be submitted to the RF MEDT.

RFPF has also been deprived of such a source of financing as deductions from the value of sold property arrested according to the court's verdicts or acts of the bodies that had been granted the right to make decisions on exercising security on property, as well as funds received from sales of property confiscated by the inured court's (judge's) verdicts, or by decisions made by the customs bodies, that was duly recognized as having no proprietor, as well as withdrawn by the federal bodies of executive power according to their competence by standards and list of costs set by the RF Government.

Thus, it can be reckoned that the above conflict between RFPF and the Ministry of State Property was resolved mostly in the frame of proposals of the latter, as the said modifications have substantially restricted the Fund's independence.

Thirdly, the prospects for management of economic companies with the state participation in their capital should find themselves under a certain impact of the optimization of FPUEs and federal public institutions (FPIs). This work is conducted in the framework of the government Commission on administrative reform established by Resolution of July 31, 2003, N 451 of the RF Government.

In 2004, the Commission considered 25,473 organization of the budgetary network, including 6,498 FPUEs and 18,975 FUI. According to decisions included in the respective protocols, the Commission classified all the noted structures into five groups by which the following decisions are proposed.

The first group is formed by organizations due to remain in federal property. The group comprises public organizations related to provision

of the country's defense and security, exercise of the federal state functions, and protection of the national and cultural values of the RF. Their overall number should make up 10,538 (41% of the total number of organizations considered by the Commission), of which 1,019 are unitary enterprises (15.7%) and 9,519 institutions (50.2%). This group also comprises unitary enterprises that should be transformed into joint-stock companies the 100% stake of which should be state-owned.

The second group includes FPUEs, whose assets are subject to transfer under the ownership of the RF Subjects and municipal entities, as well as federal public institutions that are subject to transfer under control of bodies of the RF Subjects' executive power. The group includes a total of 3,970 organizations (16% of their total number considered by the Commission), of which 202 are unitary enterprises (3.1%) and 3,768 – institutions (19.8%).

The third group consists of organizations subject to privatization or liquidation as structures that have failed to meet the criteria sufficient for keeping them under the federal control. Their overall number is 6,119 (24% of the total number of structures considered by the Commission), of which unitary enterprises make up a total of 3,384 units (52.1%), while institutions account for 2,735 (14.4%).

The fourth group comprises enterprises and institutions due to an additional scrutiny after adoption of legal acts on social status on civil servants. These are individual public organizations delivering medical, sanatorium and rehabilitation, and transportation services to federal bodies of the executive power. Of the total number of organizations considered by the Commission, after adoption of the respective legal acts as many as 70 organizations (0.3% of the overall number of organizations considered by the Commissions, of which 37 unitary enterprises (0.6%) and 33 institutions (0.2%), require an additional consideration.

Finally, a separate group was formed by organizations whose status required further specification and/or conduct of reorganization or liquidation procedures and introduction of relevant modifications into the federal property register. Their number accounted for 4,776 (19% of the total number of structures considered by the Commission), of which unitary

enterprises accounted for 1,856 (28.5%) and institutions – for 2,920 (15.4%).

At the first glance, the completed work concerns matters of management of economic companies with the government participation only to the extent the Commission has identified slightly over 1,000 FPUEs due to be retained in the federal property (including enterprises subject to transformation into joint-stock companies with 100% of their stock to be owned by the Federation) and some 3,400 FPUEs subject to liquidation and privatization, with transformation into a joint stock company being one of the options under the latter variant.

Given the above, one should not forget that *circa* 1,900 FPUEs whose status requires further specification and/or conduct of reorganization or liquidation procedures and introduction of relevant modifications into the federal property register may join the above two groups of unitary enterprises some day in a not-so-distant future, while proportions of their respective breakdown into the two groups still remain vague. Meanwhile, a possible adoption of amendments to the law on privatization that would allow one to privatize public and municipal institutions may have yet a greater impact on the size of the sector of economic companies with the government participation. The respective bill extrapolates onto them the currently applied to unitary enterprises transformation into an open-joint-stock company.

Given that the Commission has managed to locate a minimum of 6,503 FPUEs that were recognized as being excessive, so far as functions of the federal bodies of executive power are concerned¹³³, it becomes possible now to assess the field for potential privatization. As a reminder, by the end of 2004 nearly 99% of all the privatized PFUEs were transformed into OJSCs; plus, the government has failed so far to expand its budgetary network optimization efforts onto some 23% of PFUEs and 48% of FPIs (basing on their total numbers as of March 1, 2005).

Another, and quite significant and independent, factor that determined a greater importance of matters associated with management of mixed property in the corporate sector became the continuation of the trend of

¹³³ In all fairness, 3,768 institutions of the noted amount are subject to transfer to the RF Subjects' bodies of executive power.

the 1990s towards enlargement of public enterprises. The process has been unfolding along with the growth in the public companies' role in a whole number of industries, which undoubtedly deserves a thorough consideration.

2.4. Expansion of the Public Sector and the Structural Policy Issues

While the period between 2000 and 2003 saw mostly the government try to optimize its presence in the economy, when it comes to property which had survived through the voucher (1992–1994) and monetary (1995–1998) privatization programs, the period between 2004–2006 was signified by a notable expansion of companies with the state participation in their capital and growth in their specific weight throughout the Russian economy as a whole.

By the moment of economic growth was renewed in the country (in 1999), formally, the state presence in the corporate sector had been quite extensive. But it existed in the form of many thousands of dispersed, poorly controlled or uncontrolled at all unitary enterprises and stock packages in joint-stock companies that were created shortly before 1999 practically in all the sectors of the economy. Integrated structures established by the government's initiative and with its participation at the initial stage of privatization operated largely in the fuel and energy sector, representing, at the same time, natural-monopolistic kinds of activities.

In this respect, the period of 2000–03 saw the government attempt to boost efficiency and improve manageability of their dispersed assets by means of their integration into holding structures in such sectors as the nuclear energy, railway transportation, defense and liquor industries, provision of functioning of the air and sea transportation, mail service. Growth in the state-owned share in individual companies' equity was nonpareil. In parallel with that, there started the process of restructuring of natural monopolists.

The distinguishing features of 2005–06 were as follows: (1) the government policy of integration of public assets into holding structure has become obscure; (2) the already existing holdings became far more proactive and began to expand and diversify their business by means of

mergers and takeovers; (3) the government became keen to raise its share in the authorized capital of various companies up to the value which would enable it to exercise a critical influence on the companies' operations. In practice all these avenues of the state participation in the economy in terms of property rights appeared closely interlaced and mutually complementing.

It was in 2004 that prerequisites for a new stage of evolution of property relations in the country matured, which manifested itself in an open conflict between the state and business. In this context, the purchase of Yuganskneftegas, Yukos's core oil-producing asset (the private oil giant had to sell it to pay its backtaxes¹³⁴) by the state-owned Rosneft became a particularly significant move.

In addition to the "YUKOS Case", the year of 2004 became notable thanks to the launch of a fairly ambitious project on the merger of Gasprom and Rosneft. Initially, the government favored the idea to swap Rosneft for a 10.74% stock of Gasprom owned at the time by its daughter companies¹³⁵ (as the state needed the package to consolidate a control stake of the gas holding in its property, which in turn would enable it to liberalize the market for the Gasprom stock without risk of losing its majority control over the company. To this effect, in compliance with presidential Decree of December 7, 2004, OJSC "Oil Company "Rosneft" was excluded from the list of strategic enterprises, due to the approval of the RF Government's proposal to contribute with its 100% state-owned stock package in the authorized capital of OJSC "Rosneftegas", which was included in the noted list of strategic enterprises. It was intended to create Rosneftegas as a temporary economic agent, under the aegis of which it could have been possible to complete the aforementioned swap. In the process of preparation for the move, Gasprom's top executives modified their stance on the issue, that is, they maintained that even the

¹³⁴ See I.Mezheraups, A. Radygin. Gibel "YUKOSa" i problemy zaschity prav sobstvennosti. Prodazha ZAO "Yuganskneftegas" nekotorye pravovye aspekty. In: Rossiyskaya ekonomika v 2004 godu. Tendentsii i perspektivy. [The Russian Economy in 2004. Trends and Outlooks.] (Issue 26). Vol. 2.M., IET, March 2006.

¹³⁵ Those were Gasprominvestholding, Gasprombank, Gasfond, Gaspromfinans and Gazprom Finance BV.

noted 100% stake in Rosneft would be not enough to allow the government to acquire the desired stake in Gasprom, and there was a need to complement the package with some other assets.

In 2005, the format of the deal changed. After a long tug of war between the both companies' executives, each group being back-upped by state representatives on their boards who were senior staff of the presidential Administration, it was decided that the source of payment for the 10.74% stake in Gasprom, which had been reassigned to Rosneftegas in June-July 2005, should become a loan Rosneftegas would have to seek from a consortium of Western banks under its non-control bloc, rather than Rosneft's assets. The USD 7.5 bn. loan was arranged by ABN AMRO, Dresdner Kleinwort Wasserstein, JP Morgan and Morgan Stanley. The source of the loan repayment may become proceeds from the sale of another non-control bloc of Rosneft. By late-2005 Rosneftegas had paid two first tranches for the Gasprom's stock (some USD 1.3 bn.), while yet greater amounts of payments are still to be made.

Such an arrangement would enable the state to establish its majority control over Gasprom, with Rosneft (with Yuganskneftegas as its integral part) retaining its autonomy from the gas giant and the Government supposedly still maintaining control over it. After Rosneft has placed its stock on the market and attracted monetary means sufficient to repay the above loan, Rosneftegas may be liquidated by late 2006 – early 2007. In that case, the Gasprom stock should be transferred to the balance sheet of the RF Ministry of State Property, i.e. they should become the government property¹³⁶.

An additional outcome would become planned by the government increase in its share in the capital of Rosgazifikatsia (which currently controls 0.89% of the Gasprom stock) from 72% practically to 100%, thanks to contributing to the company's authorized capital with minority blocs of public gas distribution companies. In the future, Rosgazifikatsia should be reorganized, with the Gasprom stock being singled out into a separate company. If successful, the state-owned stake in the newly established

¹³⁶ Interfax, 1 November 2005, www.rosim.ru.

company, which would control the Gasprom stake, should amount practically up to 100%, while that special company is to be liquidated¹³⁷.

An interim result of the above efforts to get the state-owned stake in Gasprom up to a control value became passed at the very end of the year amendments to the Act on gas supplies, which lifted the earlier effective restrictions for overseas owners (up to 20% of stock) and raised the minimal allowed aggregate proportion of the federal property and property of the JSCs wherein the state owns 50-plus% stock up to the threshold of 50% plus 1 share¹³⁸.

While the Gasprom executives viewed the would-be merger with Rosneft as its takeover, in reality the consequence of the failed deal became the acquisition by Gasprom (via one of its daughter companies) of the 72.66% stake in Sibneft worth a total of USD 13.1bn in October 2005. Prior to that, Gasprom bought another 3.016% stake in Sibneft from Gasprombank¹³⁹. Along with completion of the *de-jure* and *de-facto* transition of Yuganskneftegas under Rosneft's control, the deal has substantially changed the balance of forces in the national oil sector. As concerns Rosneft, in addition to establishment of its actual control over Yuganskneftegas, the company was vigorously getting ready for consolidation of its main daughter companies by means of transition to the single share. It should be noted that Rosneft's financial state has been seriously complicated by the need to repay loans it had obtained between 2004 and 2005 to acquire Yuganskneftegas.

Like other natural monopolists, RAO "UES Russia" also embarked on the process of expansion and in late 2005 it acquired a 22.43% stake of "Silovye mashiny" energy construction corporation controlled by Interross. The electricity giant paid USD 101.4m. Given that Lenenrgo, the RAO's subsidiary, by the time had held over 3% of SM stock, the elec-

¹³⁷ Interfax, 29 July 2005, www.rosim.ru.

¹³⁸ The previous version read that the minimum allowed state-owned share was just 35%, however, it was just the government that was allowed to solely, without attracting any JSCs, control the stake.

¹³⁹ MERT RF vneset v pravitelstvo projekt po pokupke "Sibnefti" "Gaspromom"// RIA Nnovosti, 10 October 2005, www.rosim.ru.

tricity monopolist has secured control over a blocking stake and, accordingly, the possibility to influence the respective decision making¹⁴⁰.

Natural monopolists were joined by another serious player that began to acquire earlier privatized assets, namely, PFUE “Rosoboronexport”, the biggest national exporter of military and technical products. The public corporation began focusing on the defense sector and machine building in 2005.

Founded in 2002 by Rosoboronexport and the State Investment Corporation¹⁴¹, the united industrial corporation Oboronprom, in compliance with presidential Decree of November 29, 2004, No. 1481 and Resolution of the RF Government of May 6, 2005, No. 290, has been vigorously working on creation of a helicopter-building holding. In compliance with the above acts, the corporation received in its authorized capital state-owned stakes of Ulan-Ude aircraft maker (UUAZ, 49.18%), Moscow-based helicopter maker named after Mil (MVZ, 31%), Kazan helicopter maker (KVZ, 29.92%), Moscow machine-building plant “Vpered” (MMZ, 38%) and Stupinsky machine-building production enterprise (SMPP, 60%). To raise its share in the companies’ capital up to a control value, Oboronprom acquired additional blocs of UUAZ (25%), MMZ (12.5%) and MVZ (31%). Its last USD 11.8m- worth acquisition became OJSC “Kamov-Holding” from AFK “Systema”. Kamov-Holding holds a 49% stake in OJSC “Kamov”.

In addition to direct acquisitions of stakes in the profile enterprises, in a move to establish control over a number of other enterprises, Oboronprom held an additional stock issuance in the course of which swapped 15.07% of its stock for 29.92% of KVZ owned by the government of Tatarstan. Another new member in the holding became controlled by private investors “Rostvertol” headquartered in Rostov-on-Don. Rosvertol acquired a 2.79% stake in the holding for cash. Meanwhile, the holding is

¹⁴⁰ Following RAO UES Russia’s move, in 2006, Siemens AG acquired another 20.62% stake in Silovye mashiny. With account of a 4.38% stake in SM, the German concern raised its share up to the blocking stake. As a reminder, in spring 2005, the Federal Anti-Trust Service refused Siemens bid for 73.46% of SM stake.

¹⁴¹ After Gosinkor was liquidated in 2003, its share was assigned to Rosimuschestvo, which holds a share in Oboronprom’s capital equal to that of Rosoboronexport.

going to spent the respective proceeds on the redemption of an additional stock issuance of Rostvertol, as the state currently owns only a 3.73% stake in the company. In the future, Oboronprom is going to increase its stake in the company up to a control value, while limiting itself with a blocking stake at the first stage¹⁴². As concerns Oboronprom itself, the additional issuance of its stock resulted in its main stakeholders (in addition to the noted Tatarstan and Rpstvertol) remaining the RF Ministry of State Property (51%) and Rosoboronexport (31.13%) It should be noted that Oboronprom also controls a series of enterprises not associated with manufacturing of helicopters, including OJSC “Oboronitelnye systemy (a 75%-plus stock), CJSC “Oboronpromleasing” (100%) and, via its daughter structures – a 25% stake of a huge machine-building enterprise “Motovilikhinskiye zavody”(Perm).

Later on, it became clear that Rosoboronpromexport’s interests were extending beyond the defense industry, which can be proved by a reshuffle of the executive team at AvtoVaz in late 2005. Representatives of Rosoboronpromexport were co-opted to the new Board of Directors of the leading Russian maker of passenger cars as anti-crisis managers. In 2006, there appeared rumors of Rosoboronpromexport taking interest in KamaZ (which was included in the 2006 privatization plan) and a possible creation of a united National Car-Making Company (by analogy with the United Aircraft-Building Company) immediately after it acquires a full-fledged control over the noted car-making plants. Let us note that Rosoboronpromexport has already got a certain experience of entering boards of directors of a number of enterprises, for instance, a defense plant “Zavod im. Degtyareva (town of Kovrov, Vladimir Oblast), a large stake in which it acquired 2004 after a long-lasting conflict with MDM group.

Another example of the state’s proactive policy with respect to increase of its shares in companies with mixed capital up to control values became announced in June 2005 intentions to raise the federal stake in “ALROSA” diamond holding from 37% to 51% by means of a swap of a newly issued additional stock of the company for state-owned stakes in

¹⁴² Kukushkin M. Gosudarstvo razumno rasporyaditsya vertoletnym aktivom// Vremya novostey, October 4, 2005, www. rosim.ru.

five profile companies (Smolensky krystall (100%), special research and design bureau “Kristall” (100%), Prioksky non-ferrous metal plant (100%), Viluyusk GES-3 (less than 1%) and Almazny mir (52.37%))¹⁴³. ALROSA in turn is regarded as a potential principal stockholder of OJSC “GMK “Norilsk Nickel”. As in the case of Gasprom, this transaction may likewise require attraction of a huge loan under relevant guarantees.

These plans have faced a certain opposition on the part of ALROSA’s other large stakeholder, that is, the government of Yakutia (32% of stock). They do not want to overburden themselves with any efforts to take part in the acquisition of Norilsk Nickel and, furthermore, now they face the need to look for assets to contribute to ALROSA’s capital in order not to let their share diminish. This problem is also complicated by another one, namely, the reassignment under the federal control of a property complex which had earlier belonged to PNO “Yakutalmaz”. Should the arrangement be implemented, Yakutia would lose the right to collect royalty payments from ALROSA, which currently account for up to three-fourths of its budget revenues. To maintain the current balance of forces, Yakutia is ready for a compromise as follows: ALROSA’s capital might be increased at the expense of introduction to its capital of stock of other local enterprises (75% minus 1 share in Yakutugol”, 34.6% of stock of Elgaugol, and 10% of stock in ALROSA-Nyurba)¹⁴⁴.

In 2006, after buying stock from minority shareholders, Vneshtorgbank accumulated a 10.6% state-owned stake in ALROSA. The RF Ministry of State Property filed a lawsuit, on behalf of the Federation, to the Supreme Arbitration Court, on recognition of the RF’s property rights for Yakutalmaz. In autumn 2006, the parties arrived to an amicable agreement that Yakutalmaz should be transferred under the federal property and introduced to ALROSA’s authorized capital, so that to cover an additional stock issuance which would allow the Federation to own a control (51%) stake in the company. To compensate for the loss, the Republic of Sakha (Yakutia), together with Arkhangel’ oblast and

¹⁴³ Shishkunova E. Almazny dosnautsya gosudarstvu // Izvestia [News], 29 June 2005, www.rosim.ru.

¹⁴⁴ Kiseleva E. ALROSA razreshili stat’ neftegazovoy kompaniyey // Kommersant, 8 September, 2005, www.rosim.ru.

Primorsky krai, will collect in full the tax on extraction of natural diamonds (40% of which was earlier collected to the federal budget). The revenue losses of the Republic's budget will also be compensated by a greater fraction of revenues from corporate profit tax, property tax and dividends on the stake owned by the Republic collected to its budget.

The year 2006 saw a fall in the large public corporations' activity on the market for mergers and takeovers vs. 2005. The most significant event in this regard became an acquisition by FPUE "Rosoboronexport" of a 66% stake in OJSC "Avisma", a leading titanium (30% of the global production) and magnesium producer¹⁴⁵. The price of the deal was USD 700m). This purchase overshadowed another one, that is, the acquisition by Oboronprom, the daughter company of Rosoboronexport, of control over "Lepse" machine-building plant, which is one of the largest national producers of electric equipment for the defense and car-making industries.

Rosoboronexport's future expansion plans can be associated with metallurgy, and not only in Russia. Its future shopping list is rumored to include Zaporozhsky titanium and magnesium plant, Volnogorsky and Irshansky mining plants in Ukraine, as well as Krasny Oktyabr metallurgical plant in Volgograd, "Electrostal (Moscow oblast), and "Serp i molot" (Moscow) that produce special kinds of steel for the defense industry¹⁴⁶ – all for the sake of creation of a respective holding.

Rosoboronexport's attempts to increase the volume of assets under control and diversify its sectoral structure, due to different profiles of the recently acquired enterprises (production of helicopters, car-making and defense industries, and metallurgy), form an incentive to a possible reorganization of Rosoboronexport itself. Such reorganization may take the form of establishment of a managing fully public company, with its daughter companies being enterprises it would control, including Rosoboronexport itself in its capacity of monopolist in the area of the intergovernmental military and technical cooperation. It is assumed that some of

¹⁴⁵ In 1998, the control stake in Avisma (town of Berezniki, Perm oblast) was acquired by Verkhne-Saldinsky metallurgical production plant (VSMPO) headquartered in Sverdlovsk oblast, which meant an actual integration of the companies.

¹⁴⁶ Frumkin K. Chabolpo-russki//Kompaniya No. 48–49 (444–445), 25.12.06, p. 22–31.

the daughter companies may launch an additional stock issuance in the future¹⁴⁷.

As highlighted by media, in the past two years the Government has been considering plans of creation other large companies, analogous to the Joint Aircraft-Building Corporation, that should pretend to cover individual segments of the machine-building sector. Like JABC, they should be established on the basis of integration of private and public assets. The Government's plans were to establish a national car-making and energy construction companies, but they have not been realized as yet, though in March 2007 the RF President and Government ruled to create a Joint Ship-Building Company. As concerns the sea transport, the Government is keen to complete the amalgamation of Sovkomflot and Novoship, which was strictly opposed by the Administration of Krasnodar krai in 2006. As concerns air passenger transportation, there were plans to have Aeroflot take over regional (and not only public) air companies, such as Dalavia and Vladivostokavia, among others (as a reminder, since August 2005 Sberbank RF has become a nominal holder of a 25% stake in Aeroflot).

The year of 2006 saw a whole series of other important things happen around huge fuel and energy companies. Gasprom announced its intention to start an independent (of foreign capital) development of Stockmann gas field in the Barents sea. As well, the company acquired 50% + 1 share of Sakhalin Energy, the operator of "Sakhalin-2" project functioning under Production Sharing Agreement, for USD 7.45 bn. As a result of the deal, the stakes of other initial participants in the project shrunk twice: the share of Shell dropped from 55% to 27.5%, Mitsui – from 25% to 12.5%, and Mitsubishi – from 20% to 10%¹⁴⁸.

Rosneft held IPO, and quite successfully. As many as 115,000 individuals subscribed for its shares. According to some estimations¹⁴⁹, that signified the start of the third wave of the population's financial activity over the whole 15-year period of market transformation (after the finan-

¹⁴⁷ www.lenta.ru, 26 January 2007.

¹⁴⁸ Samedova E., Gavshina O. "Gasprom" razdelil Sakhalin na 50%//Gazeta, 22–24 December 2006, p.1.

¹⁴⁹ Sednev V. Narodny capital i fondovy rynek. www.opec.ru, 28 November 2006.

cial pyramids of the early 1990s and placement of the population's savings with commercial banks in the pre-crisis period in 1997–98). The subscribers became a relatively big group of residents who, in the conditions of depreciation of the USD against RUR, low interest rates on bank deposits, lack of accessibility and risks associated with investing in real estate (including the so-called “shared housing construction”) are ready to transform their savings into new securities. They orient towards a long period of holding of those and opt for the strategy of a low return on investments under a greater reliability, which can be ensured by a direct (bypassing intermediaries and collective investors) holding of the property right for shares and prevalence of the state in such companies, which they conceive as an additional warrant of safety for their investment. The companies, which have received a great number of private individuals as their shareholders after holding additional issuances, now can capitalize on the opportunity for seeking a governmental support in the event of various kinds of financial cataclysms.

Such a mood fuels bright prospects for Russian companies in terms of holding new additional issuances in the future. More specifically, in 2007 state-controlled Sberbank and Vneshtorgbank (that recently took over St. Petersburg-based Promstroybank) followed Rosneft on this path.

Thus, a main distinguishing feature of the period between 2005 and 2006 became a notable rise in activity of large holdings with the state participation, which expanded their business by means of its diversification and horizontal and vertical integration. In parallel with that, there continued integration of dispersed state-owned assets and creation of new holding structures. Against such a backdrop there was noted a slowdown in the process of restructuring of natural monopolists that earlier had been main players in the area of mergers and takeovers.

In all the cases cited above one cannot maintain it was nationalization in the direct sense of the term, as the state formally did not become an owner of new assets by means of their confiscation or redemption at the expense of budgetary funds¹⁵⁰.

¹⁵⁰ Except for the case of a possible liquidation of Rosneftegas in the future and the consequent reassigning of a 10.74% of Gasprom stock to the state.

Holdings with the state participation, as main subjects of the process, were acquiring property rights for new assets resulting from market transactions that were cleared with government agencies (including the RF Government and the Ministry of Economic Development and Trade). To purchase the said assets they used their own and, chiefly, attracted funds in the form of loans disbursed mostly by overseas banks, rather than national ones. That by and large conformed to the stand repetitiously declared by the nation's supreme leadership.

Such activities naturally can have an indirect impact on the property and financial state of the nation. Under a favorable scenario, as an owner of huge holding companies, the state can count on growth in their capitalization, which would indirectly mean greater budget revenues in the event of future sales of state-owned blocs in those. There also are certain prerequisites of growth in current dividend payments to the budget, which can be fueled by proceeds the holding structures collect from their daughter or controlled companies or their sales. However, that requires an adequate degree of corporate governance, transparency and manageability of executive management in relations between the state and holdings, as well as between the latter and their daughter companies.

At present it is hard to unambiguously assess all the above from the perspective of influence the aforementioned factors exercise on the situation in individual industries and in the economy on the whole. Time will show to what extent huge holdings with the state participation are capable to effectively run a great number of acquired or otherwise received assets of different profiles. An examination of the comparative efficiency of different forms of property constitutes a separate object of research and is not considered in this paper. Let us just note that, while evaluating general trends of the dynamic of property structure in the corporate sector and results of the process, numerous Russian researchers (though not in every paper on this subject) would arrive to the conclusion that public corporations and economic companies with the state participation appeared less efficient than veritably private and completely privatized companies. There also are some papers on this subject published overseas. Thus, on the basis of their research A. Boardman and A. Vining concluded that under similar conditions private companies exhibit sub-

stantially greater performance than public ones¹⁵¹. As concerns Russia, after the shifts in 2004–06, this conclusion, of course, requires empiric evidence basing on new data, as well as certain caution when it comes to interpretation of that, especially with account of peculiarities of the sectors dominated in the property area by companies with the state participation.

Given the above, there arises an important question as to how one should measure the boundaries of the public sector in Russia's economy.

On the one hand, as read in Resolution of the RF Government of January 4, 1999, No. 1, the national public sector comprises economic subjects of three basic types at the federal and regional level:

- public unitary enterprises whose operations rest upon the right for economic control;
- public institutions;
- economic companies over 50% of whose authorized capital is owned by the state.

The amended version of the document adopted by Resolution of the RF Government of December 30, 2002, No. 939, also attributes to the public sector of the economy economic companies over 50% of whose authorized capital is owned by economic companies that fall under the public sector, i.e. those ones the state-owned share in the authorized capital of which exceeds 50%.

On the other hand, it should be noted that, according to the definition of public property Rosstat employes in its reports and publications, the category of public property comprises assets belonging, on the basis of property right, to the Russian Federation (the federal property) and assets belonging, on the basis of the property right, to Republics, Krai, Oblasts, cities of the federal status, Autonomous Okrugs and Oblasts (property of the RF Subjects). Under such approaches, the statistical monitoring and attribution to the public property covers federal and regional institutions, unitary enterprises and only those economic companies whose capital (at 100%) belongs to RF and its Subjects.

¹⁵¹ Boardman A.E., A.R. Vining: Ownership and Performance in Competitive Environment: a Comparison of the Performance of Private, Mixed and State-Owned Enterprises. – Journal of Law and Economics. Vol. 32, p. 29.

Meanwhile, Rosstat defines “the mixed Russian property” as property belongs, on the basis of the respective right, to a Russian legal entity. This category includes property of various kinds. With such definitions, naturally, it is fairly hard to single out from the mass of economic subjects the specific group of enterprises and organizations with a state-owned share in their capital (and, moreover, differentiate them by size of the share), albeit it is logical to assume it is they that form the bulk of the mixed Russian property¹⁵².

According to Rosstat, with the use of the new classification of kinds of economic activity (OKVED) instead of the former classification of sectors of the national economy (OKONKH), in 2005, the public form of property in terms of the proportion of shipment of goods of one’s own production, completion of works and services by one’s own operations was particularly notable in the processing industries (8.3%), production of means of transportation and equipment (17.9%), coke and petroleum derivatives (15.3%), paper and pulp production, publishing and poly-graphic operations (12.5%), production of electrical equipment, electronic and optical equipment (12%), and production and distribution of electricity, natural gas and water (14.5%).

As concerns the contribution made by the mixed Russian property to the national economy, one can single out mineral production (15.6%) (including fuel and energy sources –13.5% and other minerals – 30.6%), processing production (14.7%), production of means of transportation and equipment (35.4%), chemical production (25.8%), production of electric equipment, electronics and optical equipment (15.9%), rubber and plastic goods (13.1%), metallurgical production and production of finished metal goods (12.8%), production of other non-metal goods (12%), machinery and equipment (11.9%), as well as production and distribution of electricity, natural gas and water (24%). In all other industries and kinds of activity wherein Rosstat employs the classification of forms of property the proportion of the public and mixed Russian property accounts for under 10%¹⁵³.

¹⁵² In addition, the state-owned share can be present in enterprises that fall under the category of the joint Russian and foreign property.

¹⁵³ Rossiysky statistichesky ezhegodnik. 2006: Stat. sb. / Rosstat. M., 2006, p. 380–383.

Meanwhile, the statistical monitoring has so far failed to present the public sector proceeding from the definition contained in the Government Resolution of 1999. However, the aforementioned definition of the public sector suffers from a series of defects, specifically:

- it fails to embrace commercial and non-for-the-profit organizations with participation of the federal and regional unitary enterprises, at least, those ones in which the share of unitary enterprises accounts for more than 50%;
- in practice, to exercise control over an economic company, one does not necessarily have to own more than 50% of its stock (shares) – it is more accurate to speak of more than a half of voting shares. This is quite urgent a challenge for the enterprises one-fourth of whose capital in the course of the mass privatization in 1992–94 was assigned to their labor collectives as privileged shares (similarly to the arrangement made under the 1st variant of benefits under transformation of enterprises into joint-stock companies), but restrictions on privatization caused by the sectoral peculiarities (for instance, in the defense industry) required keeping control blocs in the state property. As a result, the size of the share fixed with the state accounted for 38% of an enterprise’s authorized capital, but more than 50% of voting shares;
- outside the public sector, there remained economic companies in which the aggregate share of the state and economic companies, whose 50% of stock (shares) is owned by the state, exceeds 50% of their capital, while the state-owned share and that of the economic companies with the prevalence of the state capital individually account for less than 50% each;
- the same can also be attributed to the situation of economic companies, wherein an aggregate proportion in excess of 50% of capital is owned by the state and the economic companies in which more than 50% of stock (shares) is owned by the state are in the property of economic companies that falls under the public sector, i.e. to those companies in which the government share in the authorized capital exceed 50%, while their individual proportions account for less than

50%¹⁵⁴, as well as to situations when control over economic companies can be ensured by addition of shares of the economic companies that fall under the public sector with shares of economic companies they control.

In the circumstances, it is imperative to bring the system of statistical monitoring in line with attribution of a given company to a particular sector of the economy (and, primarily, the public sector definition¹⁵⁵), though it is evident that it is hard to locate poles of real control over (vis-à-vis formal property rights for) a given enterprise. For instance, OJSC “Atomenergomash” (a 100% daughter company to JSC “TVEL”) owns 50% + 1 share of “EMA Alyans-Atom”, which in turn holds a 78.6% stake in “Zio-Podolsk” and 96% one – in engineering company “Ziomar”. At present “Atomenergomash” is going to found a joint venture with Alstom (France) to produce steam-turbine equipment for nuclear power plants¹⁵⁶. For reference, 100% of TVEL is owned by the state and may form a contribution to the authorized capital of “Atomenergoprom”, the holding currently being formed by the Government. One so far can speak of just a calculation of shares of various business groups and companies (including state-controlled ones) on specific markets for goods and services by means of special applied research.

According to findings of the research into property concentration in the framework of the project entitled “Memorandum of Economic Situation of the Russian Federation” implemented by the World bank Moscow Office in 2003 that focused on 45 sectors of the economy, including 32 industry branches that represented over $\frac{3}{4}$ of the national industrial sector, the federal government controlled 26% of the volume of output (with the proportion of employees accounting for 15%), while regional authori-

¹⁵⁴ With great reserve this concerned the structure of capital of CJSC “Gasprom” prior to implementation of the plan on raising the state-owned share up to a control value, albeit the federal stake accounted for less than 50%.

¹⁵⁵ All the above can also be attributed to the municipal level and participation of local self-governance bodies in the economic companies’ capital.

¹⁵⁶ Malkova I. Rosatom vybral Alstom/Vedomosti, 3 April 2007, B2.

ties controlled 6% (with the equal proportion of employment)¹⁵⁷. Let us stress that the data belongs to the period when companies with the state share had not yet started conducting vigorous operations in the area of takeovers and mergers.

To exemplify such an approach, one can provide Brunswick Warburg's assessments of the proportion of the state in capital of the companies whose securities are traded on the stock market among other categories of owners (*Table 41*).

Table 41

Structure of Capital of Companies with the Greatest Market Capitalization and the Most Attractive for Investing

Period	Domestic portfolio investors*	State	Strategic investors**	Foreign portfolio investors*	Companies' Staff (including Managers)
1998	24	23	21	17	15
1999	21	28	18	16	17
2005	15	23	37***	16	9

* – for 2005 these categories are labeled merely as investors;

** – including shares owned by holding in daughter companies (for instance, RAO UES Russia's share in Mosenergo, etc.);

*** – for 2005 this category is labeled as strategic investors and controlling owners.

Source: Russian Equity Guide, 1998/99, Brunswick Warburg, 1998, p. 12; Russian Equity Guide, 1999/2000, Brunswick Warburg, 1999, p. 12; Russian Equity Guide, 2005/06, Brunswick Warburg, 2005, p. 10.

Table 41 makes it evident that in early 1990s the state was a large stockholder in companies that were most attractive from the perspective of investing in their securities, and kept its position in the mid-2000s as well. In both periods the state was the second biggest stockholder (in 1998 it followed domestic portfolio investors and in 2005 – strategic investors and controlling shareholders), while in 1999, right in the aftermath of the financial crisis, it controlled the biggest proportion of stakes (28%). At this point, it should be remembered that as long as strategic

¹⁵⁷ Guriev S., Rachinsky A. Kotsentratsia sobstvennosti v rossiyskoy ekonomike. In: Transition – Ekonomichesky vestnik o voprosakh perekhodnoy ekonomiki. October-November 2004. Issue 4 (2004), p. 11–13.

investors and controlling stockholders are concerned, there might be state-controlled holding among them.

These data quite well correspond to the recent ones on the rise in the specific weight of the state in capitalization of the national stock market. Over 2.5 years (between mid-2003 and early 2006) the proportion of the state-owned stock portfolio in the amount of capitalization rose from 20% to 30%, while its size in absolute terms posted a nearly 4-fold growth (from USD 48bn up to USD 190bn)¹⁵⁸. The year of 2006 saw continuation of the trend, and the state share ultimately grew to 35%. One can reckon that investors have begun to conceive the presence of the state-owned stake in corporations' capital as an additional factor of their reliability and stability.

In conjunction with that, there arises a logical question as to how one should interpret the intensification of the public companies' impact on the economy from the theoretical and practical perspective.

If one considers the process of establishment of new public holdings from the purely organizational and management perspective, he will spot an attempt to optimize the state presence in the economy, which, proceeding from formal quantitative characteristics, was had become quite extensive by late 1990s- early 2000s. However, the state property was very much dispersed and existed in the form of thousands of separate and poorly controlled (or not controlled at all) unitary enterprises and stakes in newly created joint-stock companies operating practically in all the industry branches.

It is far harder to discuss the motivation behind the expansion of the public sector in the economy as a whole. It has never been enunciated as a consistent policy, and one can suggest several possible variants of it:

- hope for the possibility to improve manageability of state-owned assets. This hope takes its roots in a banal logic that it is easier for the government and its staff to exercise a managing influence on several (a few dozens) of large companies, rather than on thousands of uni-

¹⁵⁸ Yassin E.G. Rol' gosudarstva v ekonomike na etape modernizatsii. In: Modernizatsia ekonomiki i gosudarstvo. In three volumes. Volume 1. M., GU-VShE Publishers, 2007, p. 44.

- tary enterprises and hundreds of economic companies with the state-owned share in their capital;
- pursuance of a structural and industrial policy focused on the intended modernization of individual sectors of the economy:
 - for the military-industrial complex – the restoration of the broken in the 1990s production cooperation and specialization, and the renewal of the ability to produce numerous kinds of armaments and military equipment to rearm the national armed forces and promote these goods on overseas markets;
 - for some industries of the processing subs-sector – as a quasi-protectionist measure in light of the intensification of competition on the domestic market due to Russia’s accession to WTO;
 - for the fuel and energy complex (FEC) – solidification of Russia’s position on the world market and in its relationship with the leading developed nations as an “energy power” and guarantor of “energy security”;
 - as one of the measures in the context of the whole complex of efforts to redistribute the natural rent, windfall profits collected by mining industries and natural monopolies (mostly those operating in FEC), but as a merely additional and supporting measure, as presently it is tax administration and regulation of foreign trade activities (export duties, etc.) that play a main part in this particular area;
 - as a method of exercising influence on the stock market and increasing stability of the public finance, when, on the one hand, creation of public companies and their acquisition of other assets can keep the stock market intact, while on the other hand, these assets and companies themselves may be fully or in part sold in a period of the budget crisis (a kind of modification of the Stabilization Fund); the concept of using state-owned blocs in the most attractive companies to support the pension system likewise pursues the same goal;
 - a way to solidify political positions of the present leadership on the eve of next election cycle, which does not exclude future possibilities to deploy public companies as a springboard to promote individuals to supreme posts in the government and ensure “golden parachutes” and rent-seeking behavior in pursuance of personal goals.

All the aforementioned groups of arguments that underlie the intensification of the state's participation in the economy in terms of property rights in practice appear closely interlacing and mutually complementary.

Theoretically, both pluses and minuses of a large public company (regardless of its organizational and legal form) depend on its belonging to the public property, as well as its size.

Pluses of a large public property are:

- a possibility for the state to exercise influence, by means of the functioning of large companies, on the nation's ongoing socio-economic development without an additional burden on and risks for the budgetary system along a whole series of avenues (for instance, pricing, loan disbursement, implementation of certain investment projects, to name a few);
- amalgamation of internal resources of several smaller by size economic agents and their concentration for the sake of making investment in the areas which, as the Government believes, should ensure critical for the national economy structural shifts and dumping of any collapses of the market;
- common for all huge holding companies effect of increase in predictability and stability of economic ties, decrease of transaction costs and expansion of horizons of planning at the level of a given corporation, and increase in its competitive stability thanks to its acquisition of control over a greater share of the market;
- possibility to ensure, in the event of amalgamation of smaller economic agents into an integrated structure, economies of scale (boosting the volume of output and the respective economy of scale, integration and joint use of sales channels, centralization and diversification of supplies, redistribution of orders, maneuvering with temporarily free resources, including cash and staff, transfer of technical documentation, R&D results and rights for intellectual property in the framework of a big structure);
- financial effects generated by the existence of a huge integrated structure (greater (vs. separate economic agents) opportunities for getting access to external financing through bank loans and stock market, the potential of working with large investors and creditors, growth in

capitalization, more ample and diversified opportunities for collateral-based operations, mutual guarantees for counterparts united under the auspices of an integrated structure, the image of a borrower with lower risks and an opportunity for being granted a favorable credit rating).

Minuses of a large public company in many ways appear an extension of its pluses:

- an large economic structure faces risks of lower efficiency after its business has overstep a certain threshold: there are numerous examples when over time large private corporations would loose their flexibility, aptness to innovations, while in the case of the public company these risks appear aggravated by its specific shortcomings, such as, specifically;
- from the perspective of management, the state controls the company's management more loosely and less efficiently, which gives rise to corruption;
- risks of political interference on the part of government agencies may compel the management to shift the focus of their attention towards solving non-commercial tasks, which are different from maximization of profit in the prejudice of the latter;
- natural connections with the government staff that allow the company to count on a budgetary or any other form of state support (bank loans, state order, etc.) generate the effect of soft budget constraints, depreciate the threat of takeover and bankruptcy, which discipline managers in the private sector, foster unequal competitive conditions for different economic agents.

Never the less, one currently already can speak of such a negative phenomenon as growth of indebtedness of companies with the state participation. In all fairness, this is inherent in the national corporate sector on the whole and an insufficient transparency of recent deals in particular, which in many cases were concluded by the companies' affiliated and daughter structures, rather than by themselves.

According to Mr. A. Savatugin, Director of the Department for Financial Policy of the RF Ministry of Finance, the aggregate debt accumulated by Russian public companies grew from USD 570 m in 2000 to

1.75 bn in 2002 and, according to some preliminary estimations, exceeded 20 bn in 2005, which makes it comparable to the nation's debt before the Paris Club¹⁵⁹. There also exist yet more frightening figures of the debt volume in question, for instance, USD 12 bn and 28 bn in 2002 and 2005, respectively¹⁶⁰. Thus, the pace of the debt accumulation is on the rise: given that it grew 3.1 times over the period of 2000–02, the respective rate over 2002–2005 accounted already for 11.4 times. Comparing these figures with the total amount of the debt accumulated by the national nonfinancial organizations (before nonresidents) as presented by Rosstat, one can note a sharp rise in the proportion of public companies in it – from 2.6% as of early 2001 to 5.2% as of early 2003 and 15.9% as of early 2001¹⁶¹. According to Mr. Savatyugin, the state should be held responsible for such companies' activities and develop uniform approaches to domestic and foreign borrowings the public companies make. There should be no ban on overseas loans in principle, but some quantitative restrictions should be introduced and, wherever possible, such loans should be replaced by borrowings on the domestic financial market. As the problem of attraction of borrowed capital is closely related to proportions of distribution of the companies' net profit on saving and consumption (dividend payments, including the state), the Government is designing a package of documents on creation of a uniform system of borrowings and a uniform dividend policy¹⁶².

A poor transparency in operations of companies with state participation can be exemplified by the organization of exportation of the Russian

¹⁵⁹ Opec. Ru; citing materials of RIA "Novosti", 8 December 2005.

¹⁶⁰ Radygin A., Malginov G. Rynok korporativnogo kontrolya i gosudarstvo // Voprosy ekonomiki, 2006, No. 3, p. 83.

¹⁶¹ The data on the volume of external debt accumulated by Russia's non-financial organizations (exclusive of participation in capital) before non-residents (as of beginning of the year) quoted from: Rossiysky statistichesky ezhegodnik. 2006: Stat. sb. / Rostat. M., 2006, p. 618 (with the ref. to CBR). If compared with data on public companies' external debt, the data may appear insufficiently accurate, due to the fact that banks (of which some are controlled by the state) are singled out in a separate category of borrowers.

¹⁶² At this point, one should remember that in 2005, Rosimushchestvo, while implementing procedures of corporate governance, oriented state representatives to focus on ensuring an indicator of 10% of net profit that should be transferred as dividends and declared that the future target indicators would be even greater.

gas and transit of the Middle-Asian gas to Ukraine and other post-Soviet states, which manifested itself in the course of recent negotiations Gasprom was holding between 2005–2006. Yet more illustrative was the polemics between an official representative of Gasprom and one of its minority stockholders (Hermitage Capital) in “Voprosy ekonomiki”¹⁶³, one of the leading Russian economic journals. The polemics in question concerned not only Gasprom’s operations in the post-Soviet zone, but practically the whole spectrum of issues related to the gas monopolist’s functioning. The expansion of natural monopolists into other sectors exposes a clear contradiction with earlier efforts to diminish their participation in non-profile businesses that distract their funds from investing into main kinds of operations, thus having an indirect pressure on production costs and on pricing for their goods and services.

One can also note a positive fact, that is, the expansion of companies with the state participation was unfolding, at least on the surface, without an evident consumption of budgetary funds. However, one may be in need for budgetary finds some time later, when new circumstances would necessitate restructuring of assets in such industries of the processing sector as the aircraft building and car making, which, depleted by the scarce financing in the 1990s, display a low level of competitiveness, their prospects remain uncertain in light of Russia’s potential accession to WTO.

The future advancement of the noted companies with the state participation will be determined by their capability to repay loans already disbursed to them. At the moment, this seems fairly doable, given the current prices for energy sources, the Government’s efforts to ensure return on its share in companies’ capital by means of its dividend policy and its involvement in the corporate governance procedures, as well as selection of sector-specific structural and industrial policy options by the Government.

¹⁶³ Kleiner B. Korporativnoye upravleniye i effektivnost deyatelnosti kompanii (na primere OAO “Gasprom”) // Voprosy ekonomiki, 2006, No. 3, p. 86–103. Kupriyanov S. Otvet “Gasproma”: kritika effektivna, kogda ona obosnovanna // Voprosy ekonomiki, 2006, No. 3, p. 104–110.

2.5. Conclusions

Certain positive outcomes from implementation of the Concept of Management of State Property and Privatization (1999), promulgation of new laws – on privatization in 2001 and unitary enterprises in 2002, which granted the executive power with a greater freedom of action in the privatization area, laid grounds for discussing in 2002–2003 new initiatives that concerned the problem of public sector management. As concerns economic companies with the state participation, the RF Ministry of State Property formulated annual reference points for sales of state-owned stakes of a certain group: in 2004 – selling all the state-owned blocs that account for 25% of companies' authorized capital; in 2005 – selling all the state-owned blocs that account for 50% of companies' authorized capital, and selling of the rest state-owned packages, except for those of strategic companies – in 2006. According to the RF Ministry of State Property, this ambitious program required annual sales of state-owned stakes in 4,000 joint-stock companies (including reorganized FPUEs). As a result, by late-2008 the government shall keep under its control not more than 2,000 FPUEs and 500 various stakes. However, the success with the program implementation was fairly poor. During three years after its adoption the above reference points became far less specific and reiterated statements of the prior year.

In 2004-2006 the legal base that regulates the functioning of state-owned assets in the framework of the corporate sector has undergone dramatic modifications, such as:

- approval of the list of strategic joint-stock companies, the privatization of state-owned stakes in which requires consent of the RF President, and the list of enterprises and organizations (including economic companies with the state-owned share in their capital) that fall under effect of special provisions of the 2002 act on insolvency (bankruptcy);
- adoption of a new statute on procedures of management of shares belonging to the federal Government, which determines the place and role of different agencies in the process in the aftermath of the recent administrative reform, with a clear solidification of the RF MEDT's position of an arbiter in relationship between the RF Ministry of State

Property and sectoral agencies and an author of proposals for the Cabinet, when the state needs to identify its stance with regard to the most important companies;

- enactment of a series of model documents that constitute a concrete apparatus and guidance in terms of regulation of state representatives' activities (model forms of directives, proxy votes, decisions, recommendations on mobilizing a stance on a given issue, passport of the meeting of a company's executive body);
- elimination of restrictions for economic companies with a considerable state-owned share in their capital to redeem land lots and softening of restrictions on their holding additional issuances, along with regulation of procedures of reduction in the state-owned share.

In practical terms, the process of management of public assets in the corporate sector has found itself under a notable impact of: (1) the struggle around the list of strategic enterprises and joint-stock companies; (2) the conflict between the RF Ministry of State Property and the Russian Federal Property Fund, and (3) the start of optimization of the network of FPUEs and federal public institutions (FPIs) subordinated to the federal agencies of executive power, which was carried out under the aegis of the Government Commission on implementation of the administrative reform.

If compared with its original version of 2004, the list of strategic enterprises and joint-stock companies has somewhat shrunk, which, however, to a greater extent is true, so far as the subsector of unitary enterprises, rather than the one of economic companies, is concerned. That can be mostly attributed to inclusion of the earlier excluded from the list enterprises and companies into newly formed integrated structures; as well, there were cases in which new enterprises and institutions appeared in the list. Unfolded in the course of the administrative reform and made public, the conflict between the Ministry of State Property and the Russian Federal Property Fund was resolved by late 2006, with the compromise being based mostly on the Ministry's proposals. That was evidenced by newly introduced amendments to the Fund's Charter that substantially limited its autonomy. The optimization of the network of FPUEs and FPIs subordinated to the federal agencies of executive power, which was carried out

under the aegis of the Government commission on implementation of the administrative reform, had an indirect relation to the problems of management of the state-owned property in the corporate sector, as it forms the field of a potential incorporation by means of classification enterprises into unitary enterprises due to remain in the federal property (including in this group enterprises subject to transformation into joint-stock companies with their 100% stake remaining in the federal property) and enterprises subject to privatization, one of the options being their incorporation. A possible enactment of amendments to the act on privatization that would allow one to privatize public and municipal institutions would have a great impact on the magnitude of the sector of economic companies with the state participation. According to the bill in question, they should become subject to transformation into open joint-stock companies, as it currently practiced with regard to unitary enterprises.

Distinguishing features of the period of 2004–06 became: (1) the government policy on integration of its assets in holding structures moved to the shadow; (2) the already existing holdings have intensified their activities and took the path of expansion of the scope of their operations and diversification of their business by means of mergers and takeovers; (3) the state itself also intensified its activity, particularly, along the avenue of increasing its shares in companies' authorized capital to a value that allows it to exercise a critical influence on the companies' operations. In practice, the three avenues appear closely interlaced and mutually complementing. The group of new active players in the field of mergers and takeovers was dominated by natural monopolists (Gasprom, RAO UES Russia and FPUE "Rosnoboronexport"). A large-scale project on increasing the state-owned stake in Gasprom to a control value is particularly worth noting in this respect. The expansion of business by companies with the state-owned share in their capital by means of its diversification, horizontal and vertical integration continued being accompanied with integration of dispersed public assets and creation of new holding structures. Against such a backdrop there occurred a notable deceleration of the pace of restructuring of natural monopolists that, as noted above, were major players in the process of mergers and takeovers.

Today, it is premature to draw any certain conclusions as to how the public companies' contribution to mergers and takeovers has affected their efficiency and the situation in particular industries. The problem with assessing public corporations, as well as other holding structures', performance, lies with the fact that the composition of their daughter, affiliate and controlled assets is unstable –it can change, thus seriously affecting the performance of the group as a whole. Another challenges is the problem of evaluation of the degree of consolidation of certain assets in a holding (for instance, it is hard to assess the contribution of enterprises and organizations with participation of structures which are controlled by the holding indirectly, via a network of daughter and affiliated companies, rather than directly. This and other problems form one of the reasons why it is fairly hard to accurately draw the current boundaries of the public sector in the Russian economy.

Nonetheless, one can presently argue that one of results of the national public companies' vigorous operations on the market for mergers and takeovers became a dramatic growth of their external debt. But analogous phenomena have appeared characteristic of the national corporate sector on the whole, and they can be dumped, providing the current price situation for energy sources on the world market remains unchanged.

3. State Participation in Corporate Sector at Local Level and in the Context of Relations between Federal Center and the Regions

The issues of local government authorities participating in the capital of economic societies has not been receiving sufficient attention during scientific research. Various corporate governance studies tended to focus on analyzing the share of the RF subjects and of municipalities in such capital, and on their representatives participation in the boards of directors. As rule, no comprehensive analysis of situations in particular regions has been ever performed with the exception of the study by Azarova (Azarova, 2000).

3.1. Participation of the regions and municipalities in economic societies: background, sources, scale

In the course of privatization regional and local authorities, just like the federal government, have received the possibility to receive shares of privatized enterprises and keep them as their property. They have also received the possibility to use their special right to participate in managing such enterprises through the “golden share” rule.

The question is – which level of government was the most active in exercising this tool? Below the consolidated of official Russian statistics on this process are presented in relation to the enterprises of state and municipal property (*Table 42*).

As shown in *Table 42*, during the period of period 1993–2002 in the process of transformation into a joint-stock companies the decision on fixing the stake of shares was applied to nearly 16% of federal enterprises, which is 2 times more than to enterprises being in regional (8,4%) and municipal (7,6%) property. However, this result was obtained mostly during 1993–1994, when fixing of blocks of shares was used pretty rarely at the local level. It is enough to say that in 1993 according to official statistics there was no fixing of municipal enterprises shares at all when

transforming them into joint-stock companies and the “golden share” was issued only in 2 cases.

Table 42

Maintaining State Participation in the Capital when Establishing Joint-Stock Companies Based on the Form of Property in 1993–2002

Period, form of property before transform- ation into a joint- stock company	OJSC, total	OJSC with stake shares in federal, re- gional and municipal property		OJSC with 100% shares fixed as state and municipal property		OJSC with the “golden share” rule and hav- ing the special right		OJSC in which all the shares planned for sale have been sold	
		units.	%	units.	%	units.	%	units.	%
		1993	13,547	439	3,2			204	1,5	2,242	16,5
- federal	5,419	381	7,0			141	2,6	582	10,7
- regional	6,028	58	1,0			61	1,0	1,116	18,5
- municipal	2,100					2	0,1	544	25,9
1994	9,814	1,496	15,2			792	8,1	3,061	31,2
- federal	4,921	1,080	21,9			484	9,8	1,506	30,6
- regional	3,744	369	9,9			255	6,8	1,192	31,8
- municipal	1,149	47	4,1			53	4,6	363	31,6
1995	2,816	698	24,8			429	15,2	1,071	38,0
- federal	1,326	373	28,1			178	13,4	501	37,8
- regional	859	182	21,2			139	16,2	374	43,5
- municipal	631	143	22,7			112	17,7	196	31,1
1996	1,123	190	16,9			132	11,8	532	47,4
- federal	538	85	15,8			68	12,6	249	46,3
- regional	393	59	15,0			42	10,7	202	51,4
- municipal	192	46	24,0			22	11,5	81	42,2
1993-1996	27,300	2,823	10,3			1128	4,1	6,906	25,3
- federal	12,204	1,919	15,7			693	5,7	2,838	23,3
- regional	11,024	668	6,1			358	3,2	2,884	26,2
- municipal	4,072	236	5,8			77	1,9	1,184	29,1
1997	496	84	16,9			58	11,7	206	41,5
- federal	180	23	12,8			13	7,2	86	47,8
- regional	221	32	14,5			36	16,3	88	39,8
- municipal	95	29	30,5			9	9,5	32	33,7
1998	360	142	39,4	18	5,0	28	7,8	124	34,4
- federal	101	31	30,7	1	1,0	3	3,0	32	31,7
- regional	178	73	41,0	9	5,1	21	11,8	56	31,5
- municipal	81	38	46,9	8	9,9	4	4,9	36	44,4
1999	258	101	39,1	10	3,9	42	16,3	101	39,1
- federal	31	2	6,5	-	-	6	19,4	13	41,9
- regional	203	87	42,9	9	4,4	36	17,7	71	35,0

Period, form of property before transformation into a joint-stock company	OJSC, total	OJSC with stake shares in federal, regional and municipal property		OJSC with 100% shares fixed as state and municipal property		OJSC with the "golden share" rule and having the special right		OJSC in which all the shares planned for sale have been sold	
		units.	%	units.	%	units.	%	units.	%
- municipal	24	12	50,0	1	4,2	-	-	17	70,8
1997-1999	1,114	327	29,4	28	2,5	128	11,5	431	38,7
- federal	312	56	17,9	1	0,3	37	11,9	131	42,0
- regional	602	192	31,9	18	3,0	81	13,5	215	35,7
- municipal	200	79	39,5	9	4,5	10	5,0	85	42,5
2000	199	72	36,2	6	3,0	8	4,0	96	48,2
- federal	36	9	25,0	-	-	3	8,3	12	33,3
- regional	138	58	42,0	5	3,6	5	3,6	71	51,4
- municipal	25	5	20,0	1	4,0	-	-	13	52,0
2001	125	59	47,2	12	9,6	2	1,6	55	44,0
- federal	11	5	45,5	-	-	-	-	6	54,5
- regional	93	51	54,8	12	12,9	1	1,1	37	39,8
- municipal	21	3	14,3	-	-	1	4,8	12	57,1
2002	125	38	30,4	16	12,8	1	0,8	44	35,2
- federal	10	1	10,0	1	10,0	-	-	2	20,0
- regional	94	29	30,9	10	10,6	-	-	22	23,4
- municipal	21	8	38,1	5	23,8	1	4,8	20	95,2
2000-2002	449	169	37,6	34	7,6	11	2,4	195	43,4
- federal	57	15	26,3	1	1,8	3	5,3	20	35,1
- regional	325	138	42,5	27	8,3	6	1,8	130	40,0
- municipal	67	16	23,9	6	8,9	2	3,0	45	67,2
1993-2002	28,863	3,319*	11,5	62**	0,2**	1696*	5,9	7,532	26,1
- federal	12,573	1,990*	15,8	2**	0,01**	896*	7,1	2,989	23,8
- regional	11,951	998*	8,4	45**	0,4**	596*	5,0	3,229	27,0
- municipal	4,339	331*	7,6	15**	0,3**	204*	4,7	1,314	30,3

* – calculated as grand total of the amounts per each year of the specified period and does not mean the number of JSC with state/municipal participation by the start of 2003, because part of blocks of shares could have been sold, and the right to use the "golden share" rule could have been stopped;

** – only for the period 1998–2002.

Sources: Russian Statistics Almanac, 2003: Art. M., The Goskomstat Russia, 2003, p. 335; Statistical Bulletins (Data) on the course of privatization of state and municipal enterprises (subjects) during January–December 1993 (p. 65), 1994. (pp. 31–33), 1995. (p. 66), 1996 (p. 66), 1997 (p. 66), 1998 (pp.78–80), 1999 (p. 78–80), 2000 (p. 64–66), 2001 (pp. 63–65), 2002 (pp. 63–65). M., The Goskomstat Russia; the authors' estimations.

However, in 1995 the share of JSCs created within the framework of privatization with fixed stakes of shares at regional and municipal levels reached already 21–22% – close to the number achieved when transforming federal enterprises into joint-stock companies (28%). In 1996–1999 the share of federal enterprises with fixed blocks of shares during transformation into joint-stock companies was consequently lower compared to regional and municipal enterprises. In 2000–2001 the situation changed slightly: the share of JSC with fixed stakes among former federal enterprises exceeded the share of municipal enterprises with fixed stakes. However, it was still below the share of former regional enterprises with fixed stakes. In 2002 the general picture was pretty similar to that of the period between 1996 and 1999.

Eventually, the maximum shares of enterprises with fixed stakes were seen:

- among former federal enterprises in 2001 (45.5%),
- among former regional enterprises in 2001 (approximately 55%), it was also high in 1998–2000 (40–42%);
- among former municipal enterprises in 1998–1999 (47–50%).

As for application of the “golden share” rule, the overall trends are pretty similar to those of the blocks of shares. Starting from 1995 the “golden share” rule is more actively used during the period of transforming regional and municipal enterprises into joint-stock companies. However, during certain years (e.g., in 1996 and 1999) the share of federal enterprises with this instrument was slightly exceeding the share of regional and municipal enterprises with such rule (or at least the share among one of those two groups). Starting from 1999 the practice of using the “golden share” rule started to diminish: in 1999–2000 it was not applied to any municipal enterprises at all, in 2001 it was not applied to any federal enterprises, and in 2002 – neither to any federal nor to any regional enterprises.

Eventually, the peaks of the shares of privatized enterprises with the “golden share” rule were noticed with regards to:

- former federal enterprises in 2001 (19.4%);
- former regional enterprises in 1995, 1997 and 1999 (16–18%);
- former municipal enterprises in 1995 (17.7%).

It is also interesting that the biggest share of OJSC all shares of which were sold during one calendar year (meaning the shares initially planned for sale) was seen among former municipal enterprises (over 30%), and the lowest share – among former federal enterprises (less than 24%), with regional enterprises taking the interim position (27%). Respectively, the JSC with remaining stakes of shares were mostly characteristics for federal enterprises. As for former regional enterprises, more than half of the shares subject to sale were sold in 1996 and in 2000. For former municipal enterprises most of such shares were sold in 1999–2002. As for former federal enterprises, such situation was observed only in 2001.

The above listed data may be supplemented by the following. The practice of transforming state and municipal enterprises into joint-stock companies with 100% of shares fixed as state property was more actively applied to regional enterprises, while as the practice of contributing to the charter capitals of economic societies – at municipal level. Transferring blocks of shares either into trust management or to a holding company (judging by somewhat limited data for 1998–1999) was pretty actively used at both federal and regional levels.

Fixing blocks of shares as regional and municipal property during the process of transforming respective enterprises into joint-stock companies was not the only source to form portfolios of shares (equity, participatory interest) at the local level.

The other sources were: contributing state and municipal property into charter capitals of economic societies within the course of their privatization in exchange for budget investment. In addition there were cases when blocks of shares were obtained within the process of enterprises' debts restructuring in case those were debts to local budgets (e.g., Krasnoyarsk non-ferrous metal plant) and their buying-out from the new owners (e.g., in 1996 Moscow City bought out the control stake of shares of "ZiL" truck manufacturing plant from Microdin trading company).

Receiving blocks of shares from the federal government is worth a special comment. That was done due to the fact that the central government was not providing enough funds to the regions in the crisis environment of mid-1990ies. Concentration of the federal government's efforts on the attempt to achieve formal financial stabilization in 1995–1998 (the "fight for

Ruble” lost by the federal government was partially funded out of privatization cash returns) naturally led to less attention being paid to local problems (in some cases the federal government specifically demonstrated its unwillingness to deal with them). This explains the increasing impact on the privatization process and on the property relations within Russian regions. There were certain fair reasons for this (e.g., the vast dimensions of the country and significant differentiation between the regions); however, the root cause was a different one. The lengthy election campaign at the national level during 1995–1996 without any obvious chances for the eclipsing ruling party in the federal center made the support of the leaders of the subjects of the Federation critically important (the legitimacy and autonomy of those leaders became even higher after direct regional elections of 1995–1998 which had taken place practically everywhere).

The redistribution of state property (mainly, the blocks of shares of enterprises having for various reasons not been sold during voucher and cash privatization) between different levels of government constituted an obvious available resource in the context of informal trade-offs between the federal center and the regions. Based on the Edict of the RF President No. 292 of February 27, 1996, and in the RF Government Resolution No. 554 of May 8, 1996, RFPF reviewed the documents on 250 from 29 regions (the suspension of divestment process related to such possibility actually impacted 600 enterprises from 34 regions), which resulted in transferring federally owned blocks of shares to Kirovskaya, Sverdlovskaya, Novosibirskaya Oblasts and to Krasnoyarskiy Krai as an offset of the federal debt to the regions.

Similar decisions were made later as well. The following examples may be observed during the period of 1997–1998: the blocks of shares of JSC Moscow Refinery and of JSC “Mosnefteprodukt” (constituting 38% each) were contributed to set-up “Central Fuel Company” (“Tsentralnaya Toplivnaya Kompaniya”), the blocks of shares of JSC “Sverdlovsknefteprodukt” and of JSC “Yekaterinburgnefteprodukt” (constituting 38% each) were contributed to set-up “Uralnefteprodukt” company (in both cases regional authorities were setting up integrated fuel companies to participate in business activities at the highly profitable market at highly

profitable market); also blocks of shares of JSC “Kirovo-Chepetsky Chemical Plant” (19%), Samara International Airport (25.5%), Kalneft (38%) were transferred to the regions. At that time federal center was rather willingly re-distributing part of its property in favor of the regions, which may be explained by the fact of those enterprises not being those with high yield or unambiguously attractive, so they were not of priority interest for oligarchic capital.

Eventually, the pool of regional governments’ property, including stakes of shares (equity, participatory interest), started to grow gradually.

After 2000 the federal center’s policy switched to building the power vertical, and the practice of transferring shares to the regions was terminated. There are very few examples of transferring federal property into the City of Moscow property on the basis of the Edicts of the RF President relating to the period 2002–2003: blocks of shares of 6 federally owned enterprises for the overall amount of 4,086.5 mln. rubles were transferred to the City of Moscow as compensation for the expenses to perform the Russian Federation capital function. Those enterprises were: Vnukovo airport (60.88%), JSC “Khimavtomatika” (60%), JSC “Svoboda” (49%), Tushinsky machine-building plant (38%), Cold-storage facility No.7 (25.5%), Moscow non-ferrous metals processing plant (19%).

It is clear, that both regional and municipal governments organized privatization, just like the federal center, and stakes of shares (equity, participatory interest) in economic societies were important subjects of this process. Nevertheless, the regional and local government assets remained very significant, and thus direct data about their numerical indicators became available only in 2004 (*Table 43*), while as similar data about municipal assets is still closed.

Table 43

**Structure of Joint-Stock Companies, with Russian Federation
and the Subjects of Federation Participating in their Capital
for the Period of 2004–2005 (Broken by the Amount
of Stakes of Shares)**

Type of property	total		less 50% interest + JSCs with special “golden share” right		50% – 100 %		100 %	
	units	%	units	%	units	%	units	%
Property of the subjects of the RF (2004)	4,021	100	1,743	43.3	1590*	39.5	688*	17.1
Federal property (as of March 1 2005)	4,075	100	3,135	76.9	487**	12.0	453**	11.1

* – estimate of the overall number of blocks of shares and equity exceeding 50% for 1362 units is available;

** – estimate of the overall number of blocks of shares and equity exceeding 50% for 1419 units is available.

Source: A. Gazetov, E. Ditrich, A. Kotlyarova, D. Skripichnikov. Report about government management of state enterprises in Russia // Round table on corporate governance in Russia, June 2–3, 2005 (in the framework of TACIS Program and Global Forum on Corporate Governance), pp. 18–19, 25.

As *Table 43* shows, the scale of regional governments’ participation in the capitals of economic societies is quite compatible to that of the federal center. At the same time it necessary to state that participation of regional authorities from the point of view of exercising control over the activities of such economic societies looks much more optimal compared to the level of federal participation. The share of economic societies, in which regional government have either controlling or 100% interest, is much higher at the regional level. Respectively, the share of economic societies, where regional governments do not have controlling stake is less at the regional level – 43% versus approximately 77% at the federal level. It will be fair to say, that the structure of economic societies with RF participation in their capital has undergone significant change by mid-2006 and became closer to that observed at the regional level.

It is highly probable to assume that the federal portfolio of shares has much more weight to it in regards of its value, even though some regions

were or still are in possession of the stakes of shares of some pretty attractive enterprises having been transformed into JSCs during privatization. The examples are: stakes of shares belonging to Tatarstan Republic in Tatneft, Nizhnekamskneftekhim, Kazan helicopter plant, KAMAZ; stake of shares belonging to Moscow City in “Krasny Oktyabr”, TsUM; stakes of shares belonging to Bashkortostan Republic in a whole series of fuel-and-energy companies, in Bashinformsvyaz and Ufa motor-building association. There are also examples of regional authorities participating in newly established companies – created beyond privatization process. Thus, Udmurtia Republic participated in OJSC Belkamneft together with Bashneft, Udmurtgeologiya and JSC Baikal, while as Irkutskaya Oblast participate in RUSIA Petroleum company – the holder of the license to develop the major Kovykta gas field together with Interros and TNK.

Currently two contradictory trends of managing shares may be observed at both regional and municipal levels. On one hand, regional and municipal governments analyze the value of possessing the stakes of shares for municipalities and regions; they optimize their investment portfolios by partial divestment of some blocks of shares. On the other hand, the process of government and municipal sectors restructuring is currently underway, in the context of which part of unitary enterprises are being privatized by transforming them into open joint-stock companies, including open joint-stock companies with 100% participation of respective region/municipality.

The process of demarcation of authorities between different levels of government serves as a catalyst for privatization at the local level. We should remember that effective legislation allows regions and municipalities to participate in economic societies, however, limits such participation by the purposes of them exercising just their authorities and resolving the issues of local importance as they are defined by the federal laws: Law on general principles of organizing legislative (representative) and executive power bodies in the subjects of the Russian Federation [enacted in 1999] and Law on local self-government organization [enacted in 2003] – and by their numerous succeeding versions. In such environment most regions and municipalities implement the strategy of selling most of the blocks of shares belonging to them (first of all, the minority ones, of

course). However, selling blocks of shares owned by regions and municipalities often faces serious challenges, one of them being lack of sufficient demand for such shares due to the structure of property in economic societies, due to insignificant value of stakes offered for sale and due to difficult financial and economic status of a number of enterprises.

3.2. Aspects of Managing State and Municipal Assets in the Corporate Sector at Local Level

To manage the stakes of shares (equity, interest participation) of economic societies, subjects of the RF and municipalities which own these shares, just like the federal center, engage three mechanisms ensuring state participation in controlling economic societies:

- representing the interests of the respective regions and municipalities by including their representatives into managing and controlling bodies of economic societies;
- putting shares into trust management of commercial companies and entrepreneurs on a commercial basis;
- setting-up holding companies, including by way of contributing blocks of shares owned by the state into their charter capitals.

The most common is the first mechanism allowing representatives of regions and municipalities to participate in the companies' management – just like at the federal level. There are a lot of problems arising from this, which are also very similar to the challenges faced by the federal center. Other mechanisms are not used very often.

At the end of 90-ies the active participation of the RF subjects' leaders in property management was observed including the process of using the respective assets to set up regional and local holding companies. The stakes of shares remaining in state property after privatization often became the core of such holdings, however, regional and local governments made contributions into their charter capital in other forms as well¹⁶⁴.

¹⁶⁴ Other new areas of strengthening regional authorities' impact over developing property relations (in addition to the ones mentioned above) were the following: participation in JSC internal corporate conflicts inside JSC, manipulation with bankruptcy procedures, creation of new sub-national and municipal enterprises including by way of using assets

Bashkortostan Republic really became the leader of establishing such holding companies. For example, on September 7, 1998, Bashkirskaya Toplivnaya Kompaniya (Bashkir Fuel Company) was established by way of consolidating blocks of shares belonging to the state in JSCs Bashneft (63.5%), Bashenergo» (32%), Bashneftekhim (including 3 core subsidiaries), Transneft and Transnefteprodukt regional branches. This Bashkir Fuel Company quickly moved to the 4th position in Russian market as for level of sales of refined products (in 1999 – 6th position). There are other examples as well. In 1998 (the crisis year) Vladimir Oblast government decided to create 4 sector holding companies by consolidating 51% shares of enterprises operating in glass industry (22 enterprises), cotton and textile industry (20 units), flax industry at first – 20 enterprises, but only 5 decided to consolidate in the summer) and defense industry (15 units) to restructure them and to bring them out of crisis. Another example is a project of creating JSC “Moscow TV-set” (to implement the program of revival of TV manufacturing in Moscow and Zelenograd) with participation of local authorities in the capital of the newly established JSC (50%). Another example is creating JSC “Samaraagrokhimprom” (founders: Samara Oblast Government and “Resoyrce-Mezhregiongaz” 25.5% capital each, Samaraenergo (14%), 4 chemical enterprises 5–10% each) to introduce new system of procuring fertilizers for agriculture in the region and coordinate financial flows of the holding participants. Next year Novosibirsk Oblast proposed to consolidate state-owned enterprises manufacturing construction materials into a single financial-industrial group. The economic effects of such consolidation were not at all obvious. In some cases pragmatism and common sense stopped similar initiatives of regional authorities after some negative outcomes at the initial stage.

It is also necessary to note, that many regions just did not own the sufficient amount of assets to establish holdings. First of all, it related to the

received within bankruptcy procedures as pay-back for non-state sector debts, capitalization of debt with exchanging them for shares in capital, certain enterprises buy-out, initiating actions and influencing decisions of law-enforcing and judicial authorities on cancellation of privatization deals and secondary transaction. Such areas are not reviewed in this document.

regions with insufficient economic development or those implementing the privatization policy in the most active way.

Very little data is available about the specific practices of transferring blocks of shares owned by regional and municipal authorities into trust management. Riding a bit before the hounds, we can note here that after enacting the Law on privatization of 2001 Moscow City organized tenders for transferring blocks of shares into trust management with further possibility to buy out these blocks dependent of the management performance. However, the shares of only 3 OJSCs were put under the trust management at that time (“MIC Zelenogradsky JSC “Kuryanovskoye” and “Mosrybkombinat”), and for other 4 companies some similar options were reviewed.

In 1999 Russian government adopted the Concept of Management of State Property and Privatization in the RF, which was a certain incentive for regional and local authorities to improve their own property management, including management of economic societies with regional/municipal participation in the capital.

One of the examples is adoption of the Concept of Management of Moscow City Property and of Interaction with Other Property Holders in the City up till 2005 by the Resolution of Moscow City Government No.977 of October 26, 1999, and the Resolution of Moscow City Duma No.108 of October 18, 2000. It is necessary to note that the capital of Russia even back in early 90-ies positioned itself as a major property holder at the same level as republics which had distanced themselves from the federal center a long time ago. Starting from mid-1994 Moscow City leaders initiated a harsh open criticism campaign against the overall Russian privatization model, and then in 1995 drawn the permission from the Federal government to implement Moscow-special cash privatization using its specific scheme (Edict of the RF President No.96 of February 6, 1995).

The Report about the outcomes of implementing the Concept of Management of Moscow City Property and of Interaction with Other Property Holders in the City up till 2005 approved by the Resolution of Moscow City Government No. 327-PP on May 23, 2006, states that managing the companies with stakes of shares owned by Moscow City is implemented

according to the Federal Law No. 2098-FZ of December 26, 1995, “On Joint-Stock Companies” and with the Regulations on the Procedure of appointing and on the operations of Moscow City representatives in governance bodies and audit committees of open joint-stock companies, the shares of which fully or partially belong to Moscow City, including those created during the privatization, and which are subject to special right of Moscow City to participate in managing/controlling them (“golden share”) enacted by the Resolution of Moscow City Government No. 689 of August 29, 2000.

In 2006 Moscow City was participating in 509 economic societies, and out of those 509 had a package less than the controlling stake in 281 economic societies. The City exercised “the golden share” right with regards to 101 joint-stock companies.

The key objectives of managing the stocks and stakes of shares owned by Moscow City are: improving the performance of economic societies targeted at increasing the tax and non-tax revenues into the city budget, generating income from the city-owned blocks of shares economic societies, rising the level of capitalization of the City portfolio of shares and making its structure manageable, feasible and efficiently responsive to the market situation, so its profitability for Moscow City can be accurately estimated.

Achieving all those objectives is directly related with the measures targeted at developing the market for securities issued by various economic societies with Moscow City shares, at streamlining the systems of accounting, reporting and analyzing financial and economic status of economic societies.

Moscow City Government has enacted a number of regulatory documents including those on streamlining the systems of accounting, reporting and analyzing financial and economic status of economic societies, on developing the securities market infra-structure, on increasing the level of investment activity of Moscow citizens. The system of representing the City’s interests in economic societies has been formed; the procedure of transferring the City’s shares (blocks of shares) under trust management has been defined, as well as the order of Moscow City participation in economic societies.

The centralized storing of the City-owned blocks of shares has been organized in the Bank of Moscow depositary.

The following measures have been undertaken with regards to managing the stakes of shares owned by Moscow City:

- classification of economic societies with the City's participation by industries and assigning economic societies with the City's participation to sector/industry managerial agencies of Moscow City executive branch of power;
- proposals on candidates to boards of directors and audit commissions representing Moscow City are being annually submitted to the joint-stock companies, in which Moscow City is a shareholder;
- proposals on presenting the annual financial statements and business plans of the respective economic societies to Moscow City Government are being annually introduced into the agendas of general shareholders' meetings;
- Register of the City's representatives in managerial bodies of economic societies is re-approved on an annual basis based on the results of the general shareholders' meetings;
- reporting discipline of the City's representatives in managerial bodies of economic societies has been improved (thus, in 2003 performance reports from 87% enterprises were submitted into Moscow City Property Management Department);
- financial status of economic societies with City's participation is being monitored;
- Annual report analyzing financial and economic performance of enterprises with Moscow city's share in their charter capital is being generated;
- dividend policy is being implemented in joint-stock economic societies with shares owned by Moscow City (amount of dividends, received by the city based on 2004 performance increased the level of 12% of net profit of business entities with the city participation again (7.3% by the outcomes of 2002));
- training and certification of City representatives in the field of corporate governance at the regional branch of Federal Service for Finan-

cial Markets (FSFM) in the Central Federal District is being organized on a permanent basis.

176 persons have been trained in the field of “Management of Joint-Stock Companies and Representing State (Municipal) Interests in Corporate Governance”, the total number of certified City representatives as of December 1, 2005, made 361 persons.

There are some examples of independent third-party directors being elected to corporate governing bodies due to support of city authorities. Thus, in 2004 City Property Management Department promoted representatives of Association for Protection of Interests of Shareholders and Investors (APISI) to the boards of several companies, OJSCs “Legavotrans”, “5th Automotive Company”, “14th Taxi Park” and Household Coolers Plant being among them¹⁶⁵.

City Property Management Department, Moscow Government Economic Security Division, Moscow City Committee for Insolvency (Bankruptcy), City Department of Land Resources, sector departments, committees and divisions of Moscow City, Regional branch of FSFM in the Central Federal District are providing for the following measures targeted at prevention, settlement and liquidation of corporate conflicts consequences; at avoidance of social tension caused by such conflicts; at maintaining and expanding the City taxation base:

- collection, summarization and analytical processing of data about corporate conflicts in the City of Moscow with the purpose of identifying their root causes and key features;
- developing municipal policy targeted at prevention of corporate conflicts based on analysis;
- develop the Moscow City regulatory framework with the purpose of liquidation of possible gaps and inaccuracies of regulation creating the possibility for corporate conflicts.

The key tasks of improving the system of City property management are material increase of their profitability and incremental value, as well as raising the level of capitalization of the companies with Moscow city shares by public offering of their securities at the stock market.

¹⁶⁵ Is State an Efficient Owner? // Securities Market, 2004, No. 16 (271), p. 53; In the Interest of the State // Journal for Shareholders, 2004, No. 11–12, p. 17.

It has been identified that most important areas of improving the system of Moscow City property management in the future shall be:

- engaging managing companies through application of legal trust management mechanism with regards to Moscow City assets;
- creation of holding companies for managing enterprises operating in one market segment, as well as enterprises with integration potential with regards to operations and business;
- forming investment funds for the system of City property management with the purpose of managing City property with low liquidity, managing complex assets and implementing major investment projects.

With the purpose of restructuring of the stock portfolio, Methodology Principles of forming the list of blocks of shares owned by the City of Moscow and subject to privatization (sale) in 2005–2007, as well as the order for putting municipal property under trust management.

The following normative documents regulating transferring blocks of shares under trust management in compliance with the effective laws:

- Regulation on the Procedure of organizing tenders for transferring shares (participatory interest) in economic societies owned by Moscow City under trust management;
- Regulation on the Procedure of interaction between executive power bodies of Moscow City when setting-up trust management of city-owned shares in open joint-stock companies with further sales based on the results of trust management;
- Framework requirements to Standard Trust Management Plan for shares (participatory interest) of Moscow City transferred under trust management based on tender results;
- Regulation on organizing control over the activity of trustees for Moscow City property;
- Regulation on the procedure of paying compensation and reimbursement of expenses to the trustee for the property of Moscow City.

To increase Moscow City budget revenues by way of efficient management and rising the level of capitalization of City securities portfolio, it was decided to set up investment funds with Moscow City participation

and Regulation on the order of interaction between executive agencies of the City Government when establishing management of the City property using the financial market instruments and mutual investment institutes.

Within the framework of the City stock portfolio restructuring a set of measures is being implemented to bundle subjects of governance by way of consolidating low-profit blocks of shares by sectors/industries. This will allow reducing the costs of maintaining and administering the City portfolio of shares, increasing its level of capitalization and of liquidity upon consolidating low-profit shares of small and medium-sized companies. Consolidation by sectors/industries is being implemented based on the newly created joint-stock investment funds of shares with 100% interest of the City in their charter capital and with engaging professional managing companies on a tender basis. Such approach was approved by Moscow City Government Resolution No. 400-PP of June 7, 2005, "On Consolidation by Sectors/Industries Low-Profit Blocks of Shares Owned by the City of Moscow".

The story with establishing OJSC "United Hotel Company" (UHC) in 2006 by Moscow City Government may be regarded as an illustration of the way new approaches to managing economic societies are being implemented in Russian capital¹⁶⁶. The City's share in this OJSC is 49%, and LLC "Naphtha Co." will have the controlling interest.

It is planned that UHC will comprise the assets of OJSC DecMos (which is currently constructing "Moskva" hotel with the City's share of 49%); of hotels "Sayany" (the City's share is 100%), "Balchug" (the City's share is 69%), "Metropol" and "Budapest" (the City's share is 30%), "Baikal" (the City's share is 15%); of hotels "National", "Kuzminki", "Tunist", "Voskhod", "Orekhovo" being SUEs, etc. UHC will have possession over "GAO Moscow" company (the City's share is 100%) established for efficient managing of the City's shares in various hotels. More than one third of the hotels which are planned for inclusion into UHC are in unsatisfactory condition; they do not have a category assigned and require very big investment. After establishing UHC the

¹⁶⁶ Should not be confused with power generating companies (in Russian – same abbreviation) established within the process of restructuring RJSC "United Energy Systems of Russia (RAO EES)".

City authorities plan to terminate the practice of selling municipal hotels at auctions counting on future IPO for UHC. On the whole, Moscow City owns (fully or partially) the stocks of about 30 hotels.

3.3. Conclusions

Just like at the federal level, the power bodies of the RF subjects and of local self-government have been fixing their ownership of the blocks of shares of privatized enterprises during the process of privatization and used their special “golden share” right. Overall, this instrument was used less often with regards to regional and municipal property versus federal enterprises. Among other sources of opportunities for the regions one should note transferring federal blocks of shares to them as matter of compensation for the federal budget debts in the second half of the 90-ies. As a result, the number of economic societies with participation of regions turned out to be comparable with the number of economic societies with federal participation. As for the level of regional authorities’ control, the scale of their blocks of shares (participatory interest) provides for higher influence over the respective enterprises.

Currently the scale of regions and municipalities participation in the capital of economic societies is based on two major factors. First of all, state and municipally owned blocks of shares appeared due to privatization of state property. At the same time special attention should be paid to transforming state and municipal enterprises providing public services into joint-stock companies with 100% participation of regions and municipalities – with further privatization of parts of their shares. Secondly, the policy of selling shares (participatory interest) often is challenged with very poor demand.

The currently going on process of dividing the authorities between the levels of government is the background for all this. This process is regulated by effective legislation requirements of limited participation of regional and local authorities in economic societies depending on their level of authorities and the need to resolve the issues of local importance. To manage stakes of shares becoming regional and municipal property upon transforming state and municipal unitary enterprises into joint-stock companies, the mechanisms and instruments used at regional and local

levels are the same as at the federal level. Some RF subjects (e.g., Moscow) are approaching these problems within the context of a more general objective to improve the management of their property in general trying to influence the operation of economic societies more actively (including the use of certain instruments which had not been previously in demand for various reasons).

4. Legal Framework and Regulation of Conflicts around Mixed Property Management

Similar to other spheres of socio-economic development of Russia, the issues of managing state assets in the corporate sector being at the crossroads of the interests of various government and business groups have inevitably become the source of various legal collisions. In the environment, where the legislation is inefficient, where there are so many gaps in the legal framework, and where so many business entities with mixed capital deliberately violate the effective norms and regulations, enterprises with mixed capital have become, on one hand, the subject of thorough attention on behalf of law enforcing agencies supervising the compliance, and on the other hand – the sphere of conflicts between different players.

4.1. Companies with Mixed Capital in the Context of Compliance Supervision and Controlling Efforts of Government

It's worth a separate note, that the sources of significant portion of violations related to managing state assets in the corporate sector are imbedded into the model of property reform implemented in Russia in 1990-ies.

The very well known Report by the RF Accounting Chamber “Analysis of State Property Privatization Processes in the Russian Federation for the period 1993–2003”¹⁶⁷ states the following violations in the course of activities of executive agencies within the course of privatization:

- misuse of powers assigned to executive agencies by law with regards to state property disposal;
- failure of executive agencies to perform their direct duties in the sphere of privatization;

¹⁶⁷ Analyzing the Process of Privatization of State Property in the Russian Federation in 1993–2003 (expert analytical evaluation) / Team Leader – S.V. Stepashin, Chairman of the RF Accounting Chamber. – M.: “Olita” Publishers, 2004.

- illegitimate under pricing of disposed state assets, artificial tenders and poor efficiency of divestment;
- lack of independent external control over pre-privatization preparation of state assets and of the privatization deals outcomes;
- corruption and lack of system of opposing crime in the sphere of privatization.

Due to the scale of privatization practically all types of violations have to that or another extent influenced the establishment and functioning of the whole corporate sector of Russian economy, including companies with mixed capital. The RF Accounting Chamber Report contains numerous examples of violations, which provide sufficient grounds to challenge the legacy of transforming many state enterprises into joint-stock companies, the fairness of their primary capital distribution, of selling or other disposition of state-owned stakes of shares.

With regards to companies with mixed capital where the state has maintained a certain share, one can note a great number of direct violations and misuse of executive agencies' authorities in the process of privatization strategic enterprises (in defense industry most of all), including their transfer under control of foreign entities due to ignoring restrictions set by law, not fixing blocks of shares as state property or fixing blocks of shares in the amount insufficient for state control.

Another source summarizing the Accounting Chamber materials for the period of 1998–2001 about violations in the course of privatization is the document titles “Management Issues and Regulation Objectives in the Sector of State Unitary Enterprises”¹⁶⁸. It lists some examples of violations in identifying the structure of the assets subject to transfer to JSCs at the point of their setting-up. They include unlawful inclusion of state property into the charter capital of the newly established JSCs (which is especially relevant in relation to the social and cultural assets, as well as assets not qualified for privatization being the property of the fiscal authorities); underestimation of the state property value due to imperfect procedures and deliberate violations of property assessment methodology; arbitrary amendment of previously made decisions with regards to

¹⁶⁸ Management Issues and Regulation Objectives in the Sector of State Unitary Enterprises. M., IET, 2003, pp. 75–77.

various types of property. Such violations were taking place in joint-stock companies, in which the state either remained one of the shareholders or exercised property control through the “golden share” rule (e.g., Moscow Helicopter Plant named after M.L. Mille, All-Russian Institute of Light Alloys (Moscow), Sheremetyevo International Airport).

Another type of violations and conflicts related – among other property – to state-owned stakes of shares, results from division between different levels of government when regional authorities were obviously misusing their rights when they were making decisions contradictory to Russian law and interfering with the federal center’s sphere of authorities.

First of all this relates to such republics within the Russian Federation as Tatarstan, Bashkortostan, Sakha (Yakutia), which at the very start of market reforms distanced themselves of the federal center, chose their own privatization model and made a preliminary announcement about making the major bulk of the state property based in their territory the property of the Republic. S.D. Migranov’s work (2005) is dedicated to comprehensive analysis of similar violations in Bashkortostan Republic for the period 1991–2004¹⁶⁹. As one could expect, the transactions with state-owned stakes of shares in fuel and energy enterprises are in the main focus, mostly – of Bashneft and refineries. However, one could not say that there were no violations in other sectors of the economy.

A striking example of legal collisions resulting from division of property between different levels of power is a situation with 40% shares of OJSC Irkutskenergo, which the government of Irkutsk Oblast had been claiming starting from early 90-ies. When the relations between the federal center and the regions changed after 2000, the RF Ministry of State Property instituted an action with the High Arbitration Court of the RF about recognizing its rights (as a representative of the federal center) for this particular stake. Irkutsk Oblast at that point instituted a counter action claiming for recognizing share property of the federal center and the region. The High Arbitration Court judgment of February 5, 2001, was of a compromise character: the Russian Federation’s right for 40% shares was acknowledged, but at the same time Irkutsk Oblast was granted the rights

¹⁶⁹ S.D. Migranov, *Invalidity of State and Municipal Property Privatization Transactions*. M., Logos Publishing House, 2005.

of occupation, use and disposition, including the shareholder's rights for 15.5% shares without the right of divesting, pledging and handing over management functions with regards to this asset. The General Prosecutor's Office of the RF was not satisfied with this and filed its protest with the High Arbitration Court Presidium. Eventually, on July 9, 2001, the protest was sustained and the provisions relating to the rights of Irkutsk Oblast were excluded from the judgment. The Presidium based its decision on the following: Agreement of May 27, 1996, on division of authorities between the RF and Irkutsk Oblast, allowing for the possibility of giving the region the right to manage the disputable stake of shares, required the Parties to enter into a special agreement on the matter which had not been done. As for the Federal center's ownership rights for these shares, they are unimpeachable. However, another two-year period was required to finalize the issue, so that the federal authorities could start to exercise their rights and responsibilities with regards to this given stake of shares.

This example obviously demonstrates the important role of Prosecutor's Offices in controlling the activities of enterprises with mixed capital from the point of view of compliance.

Thus, the following issues are being inspected within the course of Prosecutor's compliance audits featuring implementation of the RF shareholder's rights:

- legality of inclusion of state/municipal property into a charter capitals of JSCs and other enterprises of mixed forms of property;
- compliance with budget regulation requirements about remitting dividends (payments) on shares (contributions, participatory interest) owned by the state/municipality;
- lawfulness of state representatives participation in managing bodies of economic societies and in their operations;
- reports by territorial bodies of municipal and state property management (currently at the federal level this body is called the RF Ministry of State Property) about meetings of boards of directors of JSCs reviewing the issues of preparation for shareholders meetings and decisions to be supported at such meetings;

- forwarding if necessary letters to boards of directors of JSCs by territorial bodies of municipal and state property management with proposals to be included into the agenda, with draft decisions and support;
- timely provision of state authorities opinions about the voting procedure at shareholders' meetings for the state representatives;
- provision of adequate data in shareholders' meetings minutes (date, time and location of the event, total number of voting shares and the number of those participating in the respective meeting);
- application of responsibility measures to JSCs' management bodies in case shareholders' meetings resolutions are not observed (officially notifying JSCs' management bodies about unacceptability of such situation and about applying possible enforcement measures, applying provisions of JSCs charters to their officials in case they fail to observe resolution of shareholders' meetings, including early termination of individual authorities or management bodies' powers, initiation of filing suits with courts on behalf of state property management bodies);
- compatibility between the wording of issues raised within the context of JSCs management bodies operations and those listed in the respective documents and the wording developed at the preliminary preparation stage;
- availability of voting by power of attorney for state representatives (for persons not holding positions of state officials the contract for representing the state's interests is also required), timeliness of their issue;
- the voting procedure for the state representatives on the issues included into shareholders' meetings agendas, its compliance with the instructions issued by the respective state property managing body (for companies included into a special list – by the RF Government);
- keeping necessary records about participation of state representatives in JSCs management bodies activities.

The following documents shall constitute the necessary documentary basis for analyzing the implementation of the state's rights as one of the

shareholders: annual reports, financial statements, profit and loss accounts, statements by audit commissions and auditors, lists of persons qualified for voting at shareholders' meetings, minutes of shareholders' meetings, reports from representatives of the state in JSCs management bodies, their proposals on various issues, information on the outcomes of state representatives' activities¹⁷⁰. The prosecutor shall react to identify incompliance with the following legal acts: notice of opposition, recommendation, resolution, warning and finally – statement of claim filed with the respective Arbitration (Commercial) Court.

4.2. Companies with Mixed Capital in the Focus of Arbitration Practice in 2000-s

Arbitration practice on litigations involving joint-stock companies with the state being a shareholder in many cases reveals insufficiency of effective legislation and provides solutions to disputes arising between the state and other economic subjects.

The presented analysis of arbitration practices¹⁷¹ demonstrates a wide range of various forms and ways used by shareholders, economic subjects and other stakeholders when seeking legal remedy. Because of this wide range it was impossible to select the most typical cases, so only the existing trends will be analyzed and the most common legal structures will be presented here (their various combinations form the current arbitration practice on the issues).

¹⁷⁰ Gosudarstvennaia sobstvennost' v Rossiiskoi Federatsii (Pravovoe regulirovanie, pravoprimenitel'naiia i prokurorskaia praktika: nauchno-prakticheskii kommentarii [State Property in the Russian Federation (Legal regulation, practice of law-enforcement and public prosecution: scientific and practical comments)]). M., OLMA-PRESS, 2004, p. 170–173.

¹⁷¹ This research was carried out based on special sample consisting of 105 Resolutions of Federal Arbitration Courts (FACs) issued during the period between January 1, 2000, and September 1, 2006, in 4 Federal Arbitration Districts: Volgo-Vyatsky, East-Siberian, Far East and Moscow. Such courts have the cassation jurisdiction over the judgments of lower level arbitration courts and of cassation courts established in the respective judicial districts. The sampling criteria was that the participants of the arbitration process had state share in their company's capital.

The key trend of arbitration practice on litigations involving joint-stock companies with the state being a shareholder is that the fact of property divestment is the most common grounds for filing petitions with the arbitration courts, as the plaintiffs claim such divestments are violating their interests. Violations are most of all related with not following the order of closing a property divestment deal as set by the law or with underestimating the value of property subject to divestment. The company itself is usually a plaintiff, shareholders or state authorities do it more rarely. These circumstances define further legal development of the situation.

Based on such factors as the specific JSC body having decided on the disputable deal, the value of divested property, the value of the state's stake of shares, the legal grounds for claims and legal remedies are selected for defending the infringed rights of the plaintiffs.

The most common legal remedies to protect the infringed rights are:

- filing a claim about recognizing the decision of the company management body (General Shareholders' Meeting, Board of Directors) as void;
- filing a claim about recognizing the deal as void (Articles 167, 169, 170 of the RF Civil Code) or about using the implication of the void deal (Article 168 of the RF Civil Code).

The specifics of each of the remedies shall be reviewed below. Let us now review the key legal norms which are most often used as the grounds for filing claims on such group of cases.

1. Violation of the property pricing (cash valuation) procedure as set in Section 3 of Article 77 of the Federal Law “On Joint-Stock Companies”.

2. Violation of special procedure for closing major deals as set in Articles 78–79 of the Federal Law “On Joint-Stock Companies”.

3. Violation of provisions regulating the order of special “golden share” rule application by either the RF or by the RF subject.

Let us review them in greater detail:

1) The most common grounds for recognizing the property divestment deals or the respective decisions of companies' management bodies is violation of the procedure for its cash valuation (pricing).

The current arbitration practice on claims related to violation of market valuation procedure for the property of JSCs with state shares has got certain specifics.

This is related with a special order of market valuation of property in joint-stock companies with + 2% of voting shares owned by the state and/or municipality. This order is set by item 3 of Article 77 of the Federal Law “On Joint-Stock Companies”. Specifically, the most frequent violations constituting the grounds for legal claims are failure to receive the endorsement from state financial body (the State Property Management Committee) and to engage Federal Service for Financial Rehabilitation and Bankruptcy and starting from December 11, 2004 – Federal Property Management Agency (FAFPM – The RF Ministry of State Property) and its territorial branches in market evaluation of property. Such legal situations to a great extent arise from the non-specificity of legal provisions, which fail to regulate the form of state financial control body participation in property valuation, as well as from the lack of efficient compliance control.

Besides, a number of claims also refer to the RG President Edict No. 1210 of August 18 1996 “On Assurance of Shareholders’ Rights and Interests of the State as an Owner and a Shareholder”¹⁷². This law stipulates that in joint-stock companies with over 25% voting shares owned by the state BoD shall invite an independent third-party assessor for market evaluation of property on the request of either state representatives or of the respective government agency.

The courts assessing the justification of the claims by non-state party and referring to Part 3 of Article 77 of the Federal Law “On Joint-Stock Companies” may end up with quite different judgments. Thus, according to the judgment of Moscow District Arbitration Court No. KG-A40/1789-03 of April 8, 2003 “the provision of Part 3 of Article 77 on mandatory engagement of state financial control body in market valuation of JSCs property is focused on protection of the state interests and thus *the plaintiff* (not being a state body) *does not have the substantive rights for chal-*

¹⁷² Currently out of effect due to the RF President Edict No. 116 of February 2, 2005.

lenging the BoD resolution on the grounds of such state body had not been engaged in the evaluation”.

However, in most cases the claims of the plaintiff not being a state body grounded on violation of Part 3 of Article 77 of the Federal Law "On Joint-Stock Companies" by the defendant are satisfied by the court provided sufficient legal grounds and evidence are presented.

For example, the judgment of Khabarovsk Krai Arbitration Court satisfied the demands of relief from OJSC RZhD (“Russian Railways”) to OJSC “Golden Link”¹⁷³ about calling void the OJSC “Golden Link” GSM decision about increasing the charter capital by way of additional private offering of shares. One of the grounds for calling the GSM decision void was non-observance of the pricing procedures for the offered shares.

Federal Arbitration Court of the Far East District reviewed the cassation claim of OJSC “Golden Link” challenging the judgment of Khabarovsk Krai Arbitration Court and decide that the judgment was fair and should remain effective, emphasizing the following with regards to the pricing procedure:

“Judicial authorities have also ascertained that at the moment of GSM making the decision on the pricing for private offering of additional shares the state owned more than 2% of OJSC “Golden Link”. Respectively, by virtue of item 3 of Article 77 of the Federal Law "On Joint-Stock Companies" the defendant should have engaged state financial controlling body in the process of pricing additional shares meant for private offering.

At the same time the GSM decision on the pricing for private offering of additional shares was made without any engagement of such body.

¹⁷³ “Golden Link” is the first business entity in Russia outside the perimeter of Federal Railway Transportation System to be granted property rights not only for the rolling stock, but also for general purpose railways (20 km) for carrying cargoes over Russian-Chinese border constructed at the expense of JSC. This entity used to be discriminated by the RF Ministry of Railways, which formed the grounds for application to the anti-monopoly authorities. They issued a Directive forbidding creating discrimination limiting fair competition. In the spring of 2002 Moscow City Arbitration Court reviewed the claim of the RF Ministry of Railways challenging this Directive and judged to keep the Directive in effect. Starting from spring of 2003 “Golden Link” was granted the rights to provide services as a private railway.

Consequently, the Court reasonably alleged the illegitimacy of the GSM decision with regards to pricing for private offering of additional shares (Resolution of Federal Arbitration Court of Far East District No. FZ-A73/04-1/4285 of February 8, 2005).

Neither is there a uniform approach in judicial practice to answering the question: which should be the cases of application of Para 3 of Article 77 of the Federal Law “On Joint-Stock Companies”. There are a number of approaches, in particular:

- it is necessary to engage state financial controlling body in the process of property evaluation *only in case a partner is buying out shares owned by either the state or a municipality*;
- it is necessary to engage state financial controlling body in the process of property evaluation *only in case the law prescribes the property value to be established by the Board of Directors*. These requirements are prescribed for the cases when the Board of Directors approves major deals and related party transactions. Besides, the law directly stipulates that the price for offering of shares or for buying-out the company equity securities shall be determined by virtue of the resolution of the Board of Directors. (Such an approach dominates in real judicial practice).

To eliminate uncertainty of regulating such issues amendments to the Federal Law “On Joint-Stock Companies” were introduced by Federal Law No. 146-FZ of July 27, 2006. Now the new version of this norm comes into effect on July 1, 2007, stipulating receiving agreement of the respective state controlling body with the established property value by way of notification of such body about the respective resolution of the Board of Directors. This norm applies to cases when the resolutions are made about value of property, price for the company securities offering, price for buying-out the company’s shares. This norm shall be applied by the companies with the state being the owner of 2–50% of the voting shares. In addition, the new version of Para 3 of Article 77 of the Federal Law “On Joint-Stock Companies” stipulates:

- the list of documents to be submitted to justify the decision made about the property value;

- the deadline for serving the documents to the respective authorized government body, and the deadline for their review by this body;
- criteria for auditing documents relating to property evaluation;
- right of appeal against the resolution of the authorized state body;
- expert evaluation of the property evaluation report;
- consequences of violation of evaluation process by a partner;
- some other aspects.

Overall incorporating into the law a list of cases when the norm about agreeing the property value applies and the mechanism for such achieving such agreement is a positive fact, because it defines the subjects of such legal relations, as well as their rights and ways to exercise them for both parties of the process. Thus, the amendments should allow for more efficient exercising of rights and for more efficient protection of them.

A substantial series of disputable issues arise due to the uncertainty of application of the law. As has been stated earlier, there is a general order of defining the market value of property of joint-stock companies with the state or/and municipality holding more than 2% of the voting shares. This order is prescribed by Para 3 of Article 77 of the Federal Law “On Joint-Stock Companies”.

However, according to Para 5 of Article 1 of the Federal Law “On Joint-Stock Companies”, this norm shall not apply to joint-stock companies set-up within the framework of privatization process, if more than 25% of shares remain owned by the state – the Russian Federation or its constituent entities; or if the special “golden share” rule is used (meaning the right for the Federation or its entities to participate in JSC management). Before the state or municipality divests 75 % of shares of such JSC, but no later than expiry of privatization term as set by privatization plan of the respective enterprise, the legal status of such joint-stock companies shall be governed by the Federal Law and State and Municipal Property Privatization.

In reality, privatization timelines may be rather lengthy, and its expiry is often not known to another Party (especially because such timelines are subject to frequent change). This results in uncertainty of the legal status of a company, and as a consequence – deals may often be concluded with

violations to the process of property evaluation, as well as in difficulties when protecting the rights of the stakeholders.

Thus, the arbitration court reviewing the claim instituted by CJSC “Truboprovodnaya armatura and spetzoborudovaniye” (Pipeline Armature and Special Equipment) against OJSC “Ussolyekhimprom” and OJSC “Irkutskenergo” about recognizing the decisions of extraordinary OJSC “Ussolyekhimprom” shareholders meeting and two related surety agreements as null and void, disallowed the claim. The Federal Arbitration Court of East Siberia District expedited the cause for repeated review, including identifying the norms applicable to disputable legal relations. This judgment was justified as follows:

“Instituting the claim the plaintiff referred to legal status of OJSC “Ussolyekhimprom” is defined based on privatization law.

The first instance arbitration court based its judgment on the norms of the RF Law “On Joint-Stock Companies”.

Resolution of the issue of application of the norms of the Federal Law “On Joint-Stock Companies” to the activities of OJSC “Ussolyekhimprom” should have been based on the fact that Para 2 of item 5 of Article 1 of the Law limits the period when special legal status norms apply to such companies. This special legal status shall be valid starting from the moment of privatization decision until the moment the state divests 75% of its shares in the respective joint-stock company, but no later than the end of privatization period as it is defined by privatization plan of this specific enterprise. According to item 10 of the Edict of the President of the Russian Federation No. 1210 of August 18, 1996¹⁷⁴ the point of finishing the privatization period should be regarded as the last date of completion of selling the shares (date of completion the final tender or auction). In case a certain portion of the newly established joint-stock company (51, 38 or 25.5%) is fixed as the state property for a certain period of time in accordance with the privatization law, the end of privatization period shall be regarded as the end of the period for which those shares were fixed as state property.

¹⁷⁴ Lost effect based on the Edict of the RF President No. 116 of February 2, 2005.

Upon the end of privatization period or upon the moment when the number of state-owned shares makes no more than 25% of their overall number, the activities of the joint-stock company established on the basis of privatized state-owned enterprise shall be fully regulated by the Federal Law “On Joint-Stock Companies”.

The first instance arbitration court did not review the issue whether the privatization period for OJSC “Ussolyekhimprom” was finished, the case materials do not comprise documents certifying the period for which a stake of OJSC “Ussolyekhimprom” shares is fixed as state property (item 10 of the Edict of the President of the Russian Federation No. 1022 of August 9, 1999).

The case materials also lack evidence of the number of shares in state property (Resolution of the Federal Arbitration Court of East Siberia District No. A-19-13139/03-9-ΦO2-2571/04-C2 of July 6, 2004).

The above described case is not the only one. In such situations the undefined legal status of an enterprise leads to high judicial costs for joint-stock companies, to losing their control over a portion of their property, which is very difficult to restore. Besides, in such situations the possibility for the respective joint-stock companies to exercise their business activities within the framework of the legal norms also becomes impeded, because business is differently regulated by the RF Law “On Joint-Stock Companies” No. 2098-FZ of December 26, 1995, and by the RF Law “On Privatization of State and Municipal Property” No. 178-FZ of December 21, 2001.

2) There is another considerable group of cases related to entering into major deals. Which deals should be classified as major ones? This is one of the most problematic areas of legal regulation of JSCs’ activities. This is mostly due to some very unfortunate wording found in Para 1 of Article 78 of the Federal Law “On Joint-Stock Companies”. The ambiguity of terminology used by the legislator (“a series of mutually related transactions”, “deals closed in the process of normal business”) leads to very much divergent interpretation of this concept and to different explanation by the courts. As a result, similar cases may be judged very differently. Besides, such situation creates favorable environment for various

abuse, including abuse of law, thus actually impeding the protection of the violated rights.

The most contradictory practice is observed in the situations related to mutually related transactions. Thus, it is pretty typical to find one of the parties to the litigation to base its claims about recognizing deals as mutually related on the following grounds:

- “all deals relate to the same kind of property (e.g., real estate)”;
- “all 4 deals were closed within a short period of time (11 days)”;
- “all deals are represented by contracts of the same type (e.g., alienation of property for compensation);
- “the Seller is one and the same entity”;
- “all premises subject to deals are located in one building”;
- “all deals are targeted at one objective – alienation of premises owned by the Plaintiff”.

Defendants would base their responses in opposition to such claims on the following grounds:

- “the premises are not connected by a single technology cycle”;
- “some premises have separate entrances”;
- “prior to executing the contracts the premises had not been engaged in business, so their divestment did not lead to interruption of the operations”;
- “the contracts were signed by different buyers with the intent to use the premises for different purposes”;
- “the deals were not concluded with the objective to consolidate all assets in the hands of one entity”

(Resolution of the Federal Arbitration Court of Volgo-Vyatsky District No. A43-12790/2004-2-469/of May 3, 2005).

When evaluating the arguments of the parties to the litigation, courts sometimes are inclined to agree with the Plaintiff, and in other cases – with the Defendant. In such case the Plaintiff’s position seems to be correct, because all the transactions were targeted at achieving one business objective, however, the arguments used by the Plaintiff are more in the sphere of general logic and dominating judicial practice, but not in the sphere of a specific legal norm, thus leading to above mentioned contradictions.

The arbitration court of cassation expressed its position on interrelated transactions as follows:

“This given provision within the Law (Para 1 of Article 78 of the Federal Law “On Joint-Stock Companies”) does not elaborate on which deals/transactions should be regarded as interrelated ones. It means the adequate interpretation may be provided by the court on a –case-by-case basis. Not a single attribute identified by courts is of absolute character and thus may be used as an evidence of interrelation between contracts only in combination with other circumstances of each particular case, because all the proposed attributes are external, while as interrelation is a casual connection (i.e., internal connection)” (Resolution of the Federal Arbitration Court of Volgo-Vyatsky District No. A43-12790/2004-2-469/of May 3, 2005).

Because of the lack of common criteria for identifying interrelated transactions, claims are often dismissed by the courts: if the deals are not interrelated they cannot be viewed as a major deal in aggregate, that means they cannot be regulated by the provisions of Article 79 of the Federal Law “On Joint-Stock Companies” covering the issues of approving deals by either Board of directors or by general shareholders meeting. In the situation of non-abiding by the norms and principles of fiduciary liability¹⁷⁵ in corporate governance this leads to violation of shareholders’ rights (including the rights of the state) when significant part of a company’s assets may be divested at the price substantially below the market price (sometimes – dozens of times lower).

The judicial practice of such types of litigations also includes some cases associated with illegal changes in the ratio between the cost of the deal and the value of the company’s assets. It is connected with the following: if the value of the property subject to divestment does not exceed 25% of the book value of all the company’s assets as of the last reporting date (with certain exceptions stipulated by Para 1 of Article 78 of the Federal Law “On Joint-Stock Companies”), the procedure for approving such a deal as defined by Article 79 of the Federal Law “On Joint-Stock Companies” does not apply. Thus, the parties to the litigation may either

¹⁷⁵ Using courts for punishing managers in case of violation or abuse of their responsibilities to shareholders.

illegally overestimate the book value of the assets and in this way decrease the share of the assets subject to the transaction; or may illegally undervalue the deal per se.

Thus, for example, the Resolution by the Court of Appeal cancelled the Moscow Arbitration Court judgment about dismissing the claim by OJSC of All-Russian Research Institute for Textile and Soft Goods Machine Building (hereinafter – OJSC VNIILTECMASH) to LLC Corus about recognizing the real estate transfer deal as null and void and about nullification of the LLC Corus right of ownership with regards to this property.

The conclusion by the Court of Appeal was that “the Plaintiff was illegally accounting for and booking the intellectual property assets not belonging to OJSC VNIILTECMASH, and thus the book value of the Company’s assets was illegally overestimated. In relation to this, the total value of divested property made over 25% of the Plaintiff’s assets booked value, and thus the contested Sales-and-Purchase Agreement was qualified as a major deal and was subject to review and approval of the OJSC VNIILTECMASH BoD in accordance with Article 79 of the Federal Law “On Joint-Stock Companies”.

Because the transaction of real property divestments was closed in violation of Articles 77, 78 and 79 of the Federal Law “On Joint-Stock Companies”, the Court of Appeals recognized it as void, and as a consequence nullified the state registration of re-assignment of property rights.

The Resolution of Moscow District Federal Arbitration Court No. KG-A40/3728-06 of May 15, 2006, recognized the judgments of the previous appellation instance about nullification the transaction of state property divestment as lawful and sufficient.

As for the term “deals closed in the normal course of business”, according to clarifications by the Supreme Arbitration Court, “ deals closed in the normal course of business may, in particular, include deals of purchasing feedstock and materials required for business performance, products sales deals, obtaining loans for financing operational expenditures (e.g., for acquiring wholesale batches of goods for their further re-selling through retail network)” (item 30 of the Resolution No. 19 of the Plenum

of November 18, 2003 “Some Issues of Application of the Federal Law ‘On Joint-Stock Companies’”).

3) Judicial practice on litigations related with implementation of the special “Golden Share” Rule providing the RF Government and state power bodies of the RF subjects with the right of participation in managing joint-stock companies is represented by two major groups of cases.

The first group is related to claiming against the legality of property divestment deals.

These cases are pretty similar to those reviewed above. But one may notice that the fact of violation Article 38 of the RF Law “On State and Municipal Property Privatization” No. 178-FZ of December 21, 2001, by joint-stock companies subject to the “Golden Share” Rule is very seldom used as the grounds for challenging the legality of the divestment deals. That means, that the norm requiring notification of RF/subjects representatives about the dates and the agenda of the general shareholders meetings, as well as RF/subjects representatives’ rights to participate in OJSC management (the right to appoint an RF/subjects representative to the BoD, participation of such representative in the general shareholders meeting with the right of veto on key issues, etc.) are either most often abided by or are not used by the companies to justify their claims against illegal divestment of their property.

The second group of cases is related to situations when RF subjects’ right to apply the “Golden Share” Rule is challenged, and is completely different from all other categories of cases. In particular, such claims are not related to property divestment, but to legality of using the right of the state (as one of the shareholders) to participate in managing the company.

Mostly claims of this category of cases (additionally used for analysis: Resolutions of the Federal Arbitration Court of Povolzhye District and Resolutions of the Presidium of Supreme Arbitration Court of the RF) are targeted either at calling void directives of Governors and of Property Management Committees of Oblasts (from December 11, 2004 – territorial bodies of the RF Ministry of State Property) on the application of the “Golden Share” Rule, or at recognizing Resolutions of RF subjects’ power bodies on the same issues as contradictory with the federal law.

Different claims – about recognizing the RF subject’s actions on applying the “Golden Share” Rule as illegitimate – are found not that often.

This category of cases appeared due to numerous changes of the “Golden Share” regulation, which before July 28, 1997, stipulated for 3-year fixing of the “Golden Share” in state property (item 4 of the RF President Edict No. 1392 of November 16, 1992 “On Measures to Implement Industrial Policy during State Enterprises Privatization” and item 2.3 of State Program of State and Municipal Enterprises Privatization in the RF, approved by the RF President Edict No. 2284 of December 24, 1993).

By the time the RF Law “On State Property Privatization and on the Basics of Municipal Property Privatization in the RF” No. 123-FZ of July 21, 1997¹⁷⁶ was enacted, a number of enterprises appeared for which the 3-year fixing of the “Golden Share” in state property had expired prior to July 28, 1997. In such case their legal status was defined not by privatization laws, but by the laws on joint-stock companies (item 5 of Article 1 of the Federal Law “On Joint-Stock Companies”). However, the RF subject representatives continue to interfere in the company’ business via participation in the general shareholders meeting, by applying the “veto” right to their resolutions and in certain other ways. With this the government officials substantiate their actions on the existing respective Directive (Resolution) of the Governor or of the Property Management Committee (currently – territorial body of the RF Ministry of State Property), fixing the “Golden Share” rule of the respective RF subject. Such situations are especially typical for Chuvashia, Tatarstan, East Siberia and Far East regions.

Thus, the judgment of the Arbitration Court of Tatarstan Republic recognized as illegal item 2 of the Resolution by the Tatarstan Republic Cabinet No. 75 of February 12, 2001, stipulating introduction of special right for Tatarstan Republic to participate in managing OJSC Kazan Research and Production Association “Vertolet Mi” (helicopter).

The Resolution of the Court of Appeal changed the judgment with recognizing the part in appeals as void, and the Federal Arbitration Court

¹⁷⁶ Became invalid due to enactment of third law on privatization No. 178-FZ of December 21, 2001.

of Povolzhye District No. A65-9944/2002-SG1-30K of April 17–21, 2003, left it unchanged.

The Cassation Instance issued the Resolution stating the following:

Article 5 of the Federal Law of July 21, 1997 “On State Property Privatization and on the Basics of Municipal Property Privatization in the RF” stipulates a special right – the “Golden Share” Rule.

However, in connection to item 5 of Article 1 of the Federal Law “On Joint-Stock Companies”, such kind of decision may be made prior to when the state divests 75% of its shares.

For the moment of the challenges Act by the Tatarstan Republic Cabinet, only 20,638% of a third party shares were owned by the state.

Thus, the Court has come up with a valid conclusion about violation of a number of the RF Laws by way of enacting item 2 of the Resolution by the Tatarstan Republic Cabinet No. 75 of February 12, 2001, and lawfully recognized the above mentioned item of the Resolution as void (Resolution of Federal Arbitration Court of Povolzhye District No. A65-9944/2002-SG1-30K of April 17–21, 2003).

All other legal grounds used for seeking remedy in courts are represented in this group with very small numbers of cases and may not be qualified as typical.

And then there is one more, not a very numerous one, category of cases which deserves reviewing: *cases related to violating the order of closing the related party transactions.*

The fact that there are very few applications to court on this grounds is already a sign that, as a rule, the requirements of Article 82 of the Federal Law “On Joint-Stock Companies” about disclosure of related parties information are not followed. With this, execution of numerous deals between affiliated entities and/or between companies owned/controlled by the same persons is a generally known fact.

But even very scarce claims associated with related party transactions were not sustained. Why? First of all, it is related to the fact that the party bringing this case to court usually has got information about an interest in the deal and assumes the other party receives a hidden benefit due to significant undervalue of the divested (or leased) property vs. market value. However, the Plaintiff does not have direct evidence of such profit to the

other party and cannot prove this other party being the beneficiary and the intermediate, as it is required by Article 81 of the Federal Law “On Joint-Stock Companies”. Under such circumstances the transaction would not be recognized as a related party transaction, so it is not necessary to obtain the BoD/GSM approval for it.

In addition, judicial practice comprises cases when one of the parties in a deal closed by a joint-stock company is a judicial entity, in which this company’s BoD member used to be (one month ago or less) a founder or also a BoD member. However, the effective wording of Article 81 of the Federal Law “On Joint-Stock Companies” does not allow for recognizing persons who used to hold management positions in entities participating in the deals as related parties.

Thus, Russian Federal Property Fund (RFPF) represented by it Kirovsky Regional Branch instituted a claim against OJSC Wellcont and LLC Alevit about recognizing as void the deal of sales-and-purchase of operational premises and applying the consequences of nullifying the deal. However, the court dismissed the Fund’s claim and both court of appeals and the cassation court left this judgment unchanged. The Claimant (RFPF) substantiated its claim on an interest of an OJSC Wellcont BoD member who performed as an intermediary for the disputable transaction.

The Federal Arbitration Court of Volgo-Vyatsky District left the judgment of the arbitration court unchanged and stated the following:

According to item 33 of the Resolution by the Plenum of Supreme Arbitration Court of the RF No. 19 of November 18, 2003, resolution of disputes related to closing deals with participation of related parties listed in Para 1 of item 1 of Article 81 of the Federal Law “On Joint-Stock Companies” should necessarily take into account that the rules for such transactions as prescribed by the Law shall apply in case of circumstances listed in Para 2 of the same item, specifically: in case the persons listed as related parties, their relatives mentioned by the Law (family members) or affiliated persons are parties, beneficiaries, intermediaries or representatives in the transaction; in case any of these persons is the owner (either individually or jointly and severally) of + 20% of shares (participatory interest) of a legal entity which in this given transaction is a party, bene-

ficiary, intermediary or representative; in case any of the listed persons holds a position in management bodies of a legal entity being either a party or a beneficiary in this given transaction, or positions in management bodies of a managing company of such entity.

To recognize the transaction falling under all the requirements of Article 81 of the Law as void it is necessary to prove that the respective person was a related party as of the date of closing the deal.

The documents of the case contain evidence that as of the moment of closing the deal A.F. Varankin (OJSC Wellcont BoD member) was not a party to the disputable transaction and was excluded from the list of LLC Alevit partners according to the General Shareholders Meeting Minutes No. 10 of December 10, 2002, amendments to constituent documents being registered on January 5, 2003. Real property Sales-and-Purchase Agreement was preliminary approved by the company BoD and the property value was estimated by a third-party assessor, due to which the Court has come to lawful conclusion about A.F. Varankin not being a related party to the given deal.

The Claimant's reference to CJSC "PO Resource" Director A.F. Varankin performing as an intermediary in the disputable transaction between OJSC Wellcont and LLC Alevit shall be dismissed as not having substantiation in the materials of the case (the Resolution of the Federal Arbitration Court of Volgo-Vyatsky District No. A-28-1247/2003-412/9 of August 19, 2004).

Thus, the accomplished analysis allows for the following conclusions:

- real property assets as the biggest and most liquid ones are most often the subjects of disputable legal relations involving JSCs with the state as one of the shareholders (these assets were passed to the JSCs in the process of privatization of state enterprises);
- in case of executing transactions against the interests of JSCs with the state as one of the shareholders, the claims seeking to protect the state's interests are most often initiated by companies themselves rather than by the representatives of the state;
- legal substantiation of claims related with violation of the state's interests is usually more efficient during litigation versus claims related with violation of the interests of physical or legal persons;

- we can witness significant number of cases when property of JSCs with the state as one of the shareholders is being divested against the interests of their shareholders. These divestures are most often based on insufficient legal norms regulating participation of state power bodies in evaluation of JSCs' property, as well as regulating major deals and related party transactions procedures.

It's worth noting separately that the activities of the state representatives (territorial branches of the RF Ministry of State Property) are often inefficient with regards to protection of the state's interests in the process of divesting assets of JSCs with the state as one of the shareholders. The activities of FAFPM with regards to representing the interests of the state in courts may also be characterized as inefficient, which leads to violation of the periods of limitations, failures to submit adequate evidence and thus – causing damage to the state as the owner and the shareholder.

Getting back to legal remedies, it's worth noting their special features related to the fact that JSCs with the state as one of the shareholders are very special subjects of disputable legal relations, so let us describe those special features with more detail:

a) Claims to recognize as void the decisions of JSCs' managing bodies are pretty frequently related to challenging the legality of decisions about execution of major deals. They may also be related with violation of the procedure of cash evaluation of the property vs. the one prescribed in Para 3 of Article 77 of the Federal Law "On Joint-Stock Companies".

Other violations of the Law are related to violation of the General Shareholders' Meetings or the BoD meetings procedures. They are not frequently used in judicial practice to substantiate claims; their role is mostly auxiliary to the ones mentioned above despite the clarifications by the Supreme Arbitration Court of the RF. Item 24 of the Resolution by the Plenum of the Supreme Arbitration Court No. 19 of November 18, 2003, emphasized that when reviewing the claims about recognizing GSM decisions as void the following may be *qualified as breach of Law, which may be used as the grounds for satisfying such claims*:

- untimely notification (non-notification) of the shareholder about the date of the General Shareholders Meeting (item 1 of Article 52 of the Law);

- failure to provide the shareholder with the opportunity to review the necessary information (materials) on the issues included into the GSM agenda (item 3 of Article 52 of the Law);
- untimely provision of voting ballots (item 2 of Article 60 of the Law) etc.”

“These violations ... may serve as legal grounds ...”, however, they very seldom do in real practice. So in this case the conclusion is: under the existing regulation the shareholders’ rights are not secured.

This is related mostly with the fact that Para 7 of Article 49 of the Federal Law “On Joint-Stock Companies” allows the court “to leave the challenged resolution unchanged in case the vote of the given shareholder could not have influenced the results of voting, the violations are not material and the resolution has not caused any loss/damage for this given shareholder”. And the courts are indeed actively applying this norm to minority shareholders’ rights, because a major stake of shares can always “influence the results of the voting” meaning Para 7 of Article 49 of the Federal Law “On Joint-Stock Companies” cannot be applied because one of the mandatory conditions for this norm is missing.

However, the problem is not related just with this. To a great extent it is difficult for shareholders to protect their rights because there is no common understanding (either specified by the law or developed by judicial practice) of the term “the shareholder’s loss/damage”. The Supreme Arbitration Court does not provide clarifications on this issue, just stating that “the claim needs to be satisfied in case *the committed violations of the Law, of other legal acts, of the company Charter derogate from the rights and lawful interests of shareholders* either having voted against this resolution or having not participated in this voting” (item 24 of the Resolution by the Plenum of the Supreme Arbitration Court of the RF No. 19 of November 18, 2003 “On Some Issues of Application of the Federal Law ‘On Joint-Stock Companies’”).

In the existing circumstances the gap could be filled with a general civil law norm defining the term “loss”. However, decrease of the shares value cannot be viewed as the shareholder’s loss (see Article 15 of the Civil Code of the RF). Neither can the courts view the dividends not received by a shareholder as non-derived income, because it is impossible

to state that “the person (shareholder) could have received them had their rights not been violated”, as dividends could be not distributed even in case the company received more significant income from selling property.

Besides, whenever a deal is executed against the interests of a joint-stock company, it is the company that suffers loss, and according to Para 2 of Article 48 of the Civil Code of the RF, the shareholders’ rights with regards to the JSC are of promissory nature.

Under such circumstances little success may be expected from protecting the minority shareholders’ rights in court, as it significantly depends on the judge’s opinion about materiality or immateriality of violations committed during organization and conducting the General Shareholders’ Meeting.

Nevertheless, sometimes the courts cancel resolutions of General Shareholders Meetings (sometimes – in part) due to violation of the general procedure of their calling, organization and conducting.

Thus, individual shareholders instituted a claim against OJSC “Orbita” and OJSC “Registrator R.O.S.T” about recognizing as void the resolution of the General Shareholders Meeting and the voting ballots, as well as about restoring the entry in the Shareholders Register.

The contested GSM resolution was about introducing amendments and supplements to the JSC Charter, as well as about consolidation of equity stock and preferred stock.

The Plaintiffs substantiated their claims by the fact that the requirements of Item 3 of Article 52 of the Federal Law “On Joint-Stock Companies” had been violated within the course of preparation to the General Shareholders Meeting: the shareholders did not receive information required for participating in the meeting, which resulted in them losing their shares.

The judgment of the Supreme Arbitration Court of Mordovia Republic recognized the Resolution of OJSC “Orbita” GSM about consolidation of stock as void, obliging OJSC “Registrator R.O.S.T” to restore the entry about the Plaintiffs’ shares in the Shareholders Register.

The appellation instance partially changed this judgment: the Plaintiffs’ claim about restoring the entry in the Shareholders Register was

dismissed, with regards to all other aspects the judgment was left the same. The Resolution of the Federal Arbitration Court of Volgo-Vyatsky District left the decision of the appeal instance without any changes.

The Federal Arbitration Court of Volgo-Vyatsky District agreed with the reasoning of the appeal instance and stated the following:

“According to Article 54 of the Federal Law “On Joint-Stock Companies” the BoD when preparing the General Shareholders Meeting defines the list of information (materials) to be provided to the shareholders in the process of such preparation.

The materials of the case witness that no such list of materials was timely submitted to the shareholders and no procedure for such submission had been identified. One day prior to the General Shareholders Meeting the “Izvestiya Mordovia” newspaper published information with the list of materials and the price for which the fractional shares were to be sold. However, such notification did not comply with the requirements of item 2 of Article 52 of the Federal Law “On Joint-Stock Companies” prescribing the JSC management to submit such information 30 prior to the GSM date.

V.S. Lysyakov being the owner of 170 shares voted against the disputable resolution, V.I. Pechnikov (65 shares) did not participate in the voting, T.P. Kozlova (169 shares) and R.D. Adeeva (231 shares) voted “for” the proposed resolution. The Plaintiffs claimed not being aware of what kind of information they specifically needed to review prior to GSM.

The reference memo provided by OJSC “Registrar R.O.S.T” states that equity stock and preferred stock of “A” type with the nominal value of RUR 1 were cancelled based on the contested Resolution of GSM.

According to item 8 of Article 49 of the Federal Law “On Joint-Stock Companies”, the shareholder is entitled to protest against the GSM Resolution in court in case he/she voted against such resolution and this resolution abrogates his/her rights and lawful interests. The contested Resolution of OJSC “Orbita” managing body affects the Plaintiffs’ rights and lawful interests related to owning the shares of this OJSC.

According to item 8 of the Resolution of Plenums No. 4/8, failure to provide shareholders with the opportunity to review the necessary infor-

mation (materials) on the issues of GSM agenda shall be recognized as lawful grounds for recognizing the decisions of such GSM void.

Given these circumstances, it should be assumed that the court had sufficient grounds to settle the claim in part related to the second item of the GSM agenda” (Resolution of the Federal Arbitration Court of Volgo-Vyatsky District No. A39-2774/02-155/2 of April 7, 2003).

It worth noting that such a decision is to a great extent substantiated by the fact, that in this case the shareholders’ rights were violated in a very rude form and resulted in the maximum possible negative effects – loss of shares. Less rude violations of shareholders’ rights related to decrease of the value of their property or to decrease of the amount of income may in some other cases remain without any judicial remedies.

A significant number of cases associated with violation of the shareholders’ interests during consolidation of shares, provided such violations had not been eliminated in the process of previous litigations stipulated review of this specific issue by the Constitutional Court of the RF. Its position was expressed in Resolution No. 3-P of February 24, 2004, stating the following:

“Consolidation of stock applying conversion ratios leading to fractional shares appearance and to their further buy-out against the will of their holders is currently performed in the environment of lack of well-established securities market, and when BoDs lack sufficient number of third-party members. Under such circumstances *the Resolution of a General Shareholders Meeting about consolidation of stock means pretty serious (from the point of view of its effect) interference into the sphere of economic interests of minority shareholders similar to loss of their property.*

Due to specific features of business in the format of a joint-stock company *the grounds for divestment the property of some shareholders may be the interests of the joint-stock company in general* as long as this is done for the benefit of the company. With this it is necessary to take into account that *as a result of stock consolidation in the interests of the joint-stock company in general, the shareholders with significant stakes of shares usually find themselves in a more beneficial situation, at the same time minority shareholders usually suffer from negative effects.* The

fact that different groups of shareholders have different interests in the process of stock consolidation is inevitably leading to the growing importance of legal procedures in economic decision-making, importance of efficient (not just formalistic) judicial control, all this being the guarantee for minority shareholders' rights.

In relation to this judicial control over stock consolidation procedure compliance becomes more and more important. *Special level of responsibilities of courts is explained by the fact, that the legislator defined the legal procedures for decision-making on stock consolidation issue in very general terms without any detail*".

As for nullifying Resolutions of BoD or of some other managing body of a joint-stock company (individual or collegial), the position of the Supreme Arbitration Court of the RF was stated in item 27 of the Resolution by its Plenum No. 19 of November 18, 2003 "On Some Issues of Application of the Federal Law 'On Joint-Stock Companies'". According to this clarification, it is possible *"both in case when the law stipulates for the possibility to challenge these decisions, and in case the law does not contain any such direct reference, provided such resolution does not comply with the requirements of respective laws and regulations and violates the shareholders' rights and interests protected by law"*.

There is a special case of challenging the decisions of BoD or GSM. It relates to nullifying the decisions of increasing charter capital by issuing additional shares. The following cases happen in practice:

– BoD decides to increase charter capital before the completion of privatization (in violation of Article 21 of the RF Law "On State Property Privatization and on the Basics of Municipal Property privatization", according to which "OJSC for which the investment and/or social conditions have not been fully completed are not entitled to make a decision about increasing their charter capital, about issuing additional shares or other securities that could be converted into shares);

– BoD decides to increase charter capital by issuing additional shares, which results in decreasing share of the state in the given JSC.

Thus, the RF Ministry for Property Relations instituted with Moscow Arbitration Court a claim against OJSC "Novaya Investitsionnaya Initsiativa Delta" (hereinafter referred to as OJSC NII Delta) about nullifying

its BoD Resolution about increasing charter capital by issuing additional shares.

As was ascertained by the first instance court and by the court of appeals, the OJSC NII Delta BoD decided to increase charter capital by issuing additional shares, and all 7 BoD members elected at the General Shareholders' Meeting voted unanimously for that decision.

However, the representative of the Russian Federation appointed to represent the state in the BoD in accordance with the RF Government Resolution No. 388 of April 7, 1998 "On Appointing the State representatives in Joint-Stock Companies of the Military-Industrial Complex Companies" was not a participant in that given GSM.

The Federal Arbitration Court of Moscow District agreed with the judgment by Moscow Arbitration Court and with the resolution by the Court of Appeals recognizing the BoD Resolution as void and stated one of the arguments as follows:

"... the contested BoD Resolution was adopted without taking into account the requirements of item 6 of Article of the Federal Law No. 208-FZ of December 26, 1995 "On Joint-Stock Companies", according to which increase of charter capital by way of issuing additional shares in case a stake of shares representing over 25% of votes at the General Shareholders Meeting is fixed as state/municipal property by legal acts of the RF on privatization may be done during the period for which such state/municipal property is fixed only in case the state/municipal share in the charter capital is preserved.

Because the Defendant's BoD decided to have a private offering of additional shares with payment according to the procedure prescribed by the law, the share of the state may be preserved only under condition, that the state itself acquires (for an established price) a respective stake of shares. The Court of Appeals ascertained that there were no sources paying for such shares out of the federal budget, because such funding had not been stipulated by Privatization Plan approved by the RF Government Resolution No. 1165-r of August 15, 2003. Thus, additional issue of shares shall in such case inevitably result in decrease of the stake of shares owned by the state.

Thus, substantiation of the cassation appeal is faulty.

Taking into account all the above, the Cassation Court has no grounds for canceling the previous judgments on the given case stipulated by Article 288 of AIC of the RF (Resolution of the Federal Arbitration Court of Moscow District No. KG-A40/5404-04 of June 29, 2004).

The RF Law No. 155-FZ of July 27, 2006 introduced amendments to the law on privatization regulating the procedure of increasing the charter capital of OJSCs established within the process of privatization and having 25% or more shares fixed as state/municipal property. Besides, the new law stipulated the procedure for public offering of such shares and for their listing with stock exchanges, as well as for offering shares beyond the borders of the RF (Articles 40, 40.1 of the RF Law “On State and Municipal Property Privatization”).

According to the general rule, the increase of the charter capital of such companies by way of additional issue of shares may be done only under the condition of preserving the state’s/municipality’s share.

However, the Law defines a number of state power bodies (the President of the RF, the RF Government, state power bodies of the subjects of the RF, local self-government bodies), *entitled to make decisions about increasing charter capital resulting in decreasing the stake of shares owned by the state/municipality* – Article 40 of the RF Law “On State and Municipal Property Privatization”. Delineation of authorities of each of the above listed power bodies is based on the size of the stake of shares owned by the state and/or taking into account the fact of qualifying the company in question as a strategic one.

Quite similar the state power bodies are entitled to define the state’s share in the charter capital during IPOs and listing of shares at stock exchanges shares, as well as during offering of the shares beyond the borders of the RF (Article 40.1).

Strengthening of the state control over its shares and the most competitive enterprises could be evaluated as a positive factor, had the bureaucrats of different levels not obtained the right to make the final decision about the possibility to decrease the state’s share in the charter capital of the respective OJSC. The importance of this issue for OJSC and for its shareholders, high value of blocks of shares of a number of enterprises (or their high social importance) combined with personal interests of cer-

tain government officials may create a favorable environment for either illegal or unfeasible decisions, for re-distribution of part of the state's property in favor of third parties (including bureaucrats themselves).

b) Claims about calling the deals void with regards to JSCs with state as one of the shareholders are most often related either to violation of the procedure for closing major deals as prescribed by Article 79 of the Federal Law "On Joint-Stock Companies", or to violation of the procedure of cash evaluation of property as prescribed by Para 3 of Article 77 of the Federal Law "On Joint-Stock Companies".

The most significant difficulty when instituting such a claim is qualifying the disputable deal as either void or voidable. Clarification of this issue is very important not only for selecting the correct legal grounds for claims substantiation, but also for defining the period of limitations. According to Article 181 of the RF Civil Code, the period of limitations for a voidable deal makes 1 year, and for a void deal – 3 years (until July 21, 2005, this period made 10 years).

Article 168 of the RF Civil Code stipulates recognizing the deal as void in case it does not comply with the requirements of laws and other legal acts, "provided the law does not state that such deal is voidable and does not stipulate other consequences of non-compliance". Such vague wording and lack of direct definition of "voidable deal" in regulatory documents (including Federal Law "On Joint-Stock Companies", RF Civil Code) leads to qualifying any sort of non-compliance (which may take place during execution of voidable deals) as the grounds for claiming the deals as void and for applying the respective consequences prescribed by Article 168 of the RF Civil Code.

In some cases such error may lead to violating the period of limitations, and as a consequence – to impossibility of protecting the violated right; in other cases it may become the reason for abusing the rights (instituting claims and initiating litigations on voidable deals within the period of limitations for void deals), which could be avoided in case of having clarity with regards to the terms "void deal" and "voidable deal", especially when they are used in the texts of legal acts and regulations.

Another category of cases is worth noting: they are related with invalidity of legal transactions performed with a goal contradicting the basic principles of law and order and of morals (Article 169 of the RF Civil Code).

Most often risks of such type are initiated by state bodies – Federal Agency for Federal Property Management (FAFPM) and its territorial branches, tax inspectorates. However, they most often fail to provide convincing evidence of the fact that the true goal of the Defendant was not just derivation of profit, but *a goal contradictory to law-and-order or morals* (e.g., the goal of understating taxable income).

The reason for this is vague wording of provisions of Article 169 of the RF Civil Code, connecting the invalidity of the deal not with the actual consequences of the executed deal, but with a specific goal contradictory to either law-and-order or to morals, which it makes it necessary to prove it and thus makes it more difficult to apply this norm.

Another way of protecting the violated law is to institute a claim for applying the consequences of the deal being void in connection with its contradiction to the requirements of privatization regulations effective as of the moment of closing the deal.

The 10-year period of limitations effective prior to Federal Law No. 109-FZ of July 21, 2005 allowed the Plaintiffs to claim the application of the consequences of void deals related to divestment major assets of joint-stock companies (mostly – real property) during the period of 1993–1996, thus actually challenging the legality of obtaining property by current shareholders. Decreasing period of limitations down to 3 years starting from July 25, 2005, was of very positive character because it facilitated protection of property rights and maintaining the stability in business community. It is even more true, because claims of such categories are most often dismissed.

The analysis of arbitration practice identified that there are two ways of legal regulation of business of JSCs with state as one of the shareholders.

The first one may be conventionally called “private-legal”. It treats the state equally as other shareholders with certain reservations, which may be justified by some economic and social conditions, regulating business

activities based on the principles of freedom, autonomy and equality of all participants of the legal relations. Private-legal regulation is applied in the sphere of legal relations regulated by the Federal Law “On Joint-Stock Companies”.

The second way of legal regulation may be conventionally called “public-legal”. It treats the interests of the state being a shareholder as priority ones versus the interests of other private shareholders, and all the key issues of business of such JSCs are to be controlled by the state. In this case the state regulation of business is pretty obvious. Public-legal regulation is applied in the sphere of legal relations regulated by the Federal Law “On State and Municipal Property Privatization” No. 178-FZ of December 21, 2001, and to a significant number of the joint-stock companies established within the process of privatization provided the state (or the subject of the Federation) owns 25% and more of shares of the given JSC or the special “Golden Share” Rule is present.

Besides, the arbitration practice with regards to cases on joint-stock companies with state as one of the shareholders evidently demonstrates the following:

- inefficient management of state property (shares) expressed in devaluation of shares due to divestment of JSCs assets in prejudice of the shareholders interests;
- illegal interference of regional authorities into business of JSCs;
- fewer legal possibilities for protecting the minority shareholders’ interests in court.

4.3. Conclusions

In the environment of imperfect legal regulations and of a number of gaps in Russian legal framework, as well as purposeful violation of legal norms and requirements on behalf of numerous business entities, the mixed capital companies have been placed in the focus of government attention from the point of view of compliance. On the other hand, such companies have also become the field of conflict situations in the relations of business participants. Many violations of law with regards to state assets in the corporate sector turned out to be connected with violations during privatization in the 90-ies (e.g., during the process of de-

lineation of state property between different levels of government, when regional power bodies were exceeding their competence and making decisions contradictory to the effective Russian laws and interfered with the competence of the federal center).

The fact of the state having a share in the capital of many business entities is for many government agencies (including the law-enforcing ones) an additional incentive for thorough study of compliance with the norms regulating the implementation of the shareholder's rights of the RF. Sufficient case studies on this matter may be found in the materials of prosecutor's office and in arbitration practice on cases associated with joint-stock companies with the state as one of the shareholders.

In the process of studying arbitration practice a number of legal problems were identified as requiring amendments to the effective legislation with the purpose assuring more efficient protection of the shareholders' rights. The following measures seem to be required for resolving those problems:

1. It is necessary to introduce amendments to Articles 38 and 39 of the Federal Law "On State and Municipal Property Privatization" No. 1 78-FZ of December 21, 2001, and item 5 of Article 1 the Federal Law "On Joint-Stock Companies" No. 208 of December 26, 1995, with the purpose of applying regulations on joint-stock companies to those established within the process of state and municipal enterprises privatization.

Under the effective legal regulation, enterprises regulated by laws on privatization, as well as their shareholders with the exception of the state during rather long period (not limited by reasonable time) are practically beyond the sphere of civil legal relations with regards to resolving the corporate governance issues. They are managed within the limits of state regulation in unjustifiably discriminating conditions.

When provisions of the Federal Law "On Joint-Stock Companies" are applied to the JSCs created within the process of privatization, special norms, if necessary, may be stipulated with regards to legal status of strategic enterprises, as well as other mechanisms for implementing the interests of the state in relation to economically valuable enterprises, which have major stakes of shares owned by the state or municipalities.

Currently the legal status of enterprises created in the process of privatization is not always obvious, which leads to execution of deals contradictory to the law and violating the interests of shareholders, as well as creating difficulties with protection of the violated rights.

2. A definitive norm needs to be introduced into the Federal Law on “Joint-Stock Companies”¹⁷⁷, defining the concept of “shareholder’s loss”, as well as incorporation of this concept into the formulation of general concept of loss as stipulated by Article 15 of the RF Civil Code.

Under the existing wording the remedies for shareholders’ rights is difficult. This is related to the fact that causing loss to the company by execution of a deal contradictory to the company’s interests is not recognized as loss of shareholders (participants of the company), because their rights with regards to the company are of promissory character (Para 2 of Article 48 of the RF Civil Code). In addition, the real loss as defined by Article 15 of the RF Civil Code either is not caused to shareholders or is very difficult to prove, and the wording of “opportunity cost” concept does not allow for qualifying neither non-derived dividends nor increase of the shares value as such (because they could not have been necessarily obtained under normal development of the situation).

In addition to the above mentioned, such definition of loss leads to arbitration courts preserving many of GSM resolutions as valid even when they are enacted with violations of the law. With this the courts are based on Para 7 of Article 49 the Federal Law on “Joint-Stock Companies”, because “the disputable resolution does not cause loss to shareholders”. It means that the court can effectively cancel the GSM unlawful resolution only on the initiative of some major shareholders – owners of significant blocks of shares, whose votes may really affect the result.

3. It is necessary to identify and recognize as illegal directives by administrations of the subjects of the RF, as well as by the RF Ministry of State Property and by its territorial branches, stipulating fixing the “Golden Share” Rule with the subject of the RF, provided the 3-year term of its application expired before July 21, 1997.

¹⁷⁷ I.e., legal norms setting the definitions of certain legal concepts.

Implementation of this measure will allow putting a limit to illegal action of regional bureaucrats interfering into the companies' business.

4. It is necessary to introduce amendments to Para 7 of Article 49 of the Federal Law on "Joint-Stock Companies" stipulating the shareholders' rights for instituting an appeal against the GSM resolutions. The introduced amendments should be targeted at eliminating the possibility for minority shareholders discrimination related to insignificant number of their shares, not impacting the results of the voting, which would actually mean implementation of fiduciary responsibility principle (specifically – the principle of shareholders equality irrespective of the size of their assets). Besides, it is necessary either for the legislator to define or for the Supreme Arbitration Court to clarify the concept of "material violation" with regards to organizing/conducting General Shareholders Meetings and to adoption of their resolutions.

The existing uncertainty in this sphere leads to dismissal of claims about nullifying the resolutions of the General Shareholders Meetings conducted with violations of effective legislation and the respective Company Charter abrogating the interests of shareholders (especially the minority ones).

5. It is necessary to introduce amendments to Para 1 of Article 78 of the Federal Law on "Joint-Stock Companies" with regards to the concept of "major deal" defining the criteria for qualifying the deals as interrelated and excluding the term "deals executed in the process of normal business".

Currently significant number of deals is executed with violations of the major deals procedure prescribed by law. However, the shareholders are not always successful in protecting their rights at courts due to unclear definition of the "major deal" concept and importance of judges' perceptions (without the required experience) when qualifying the deal as the one "executed in the process of normal business".

6. It is necessary to amend the concept of a void deal stipulated in Article 168 of the RF Civil Code, setting a clear delineation between void and voidable deals. Because both kinds of deals may be executed with violations of the law (or other regulatory acts) the parties do not always succeed in defining the legal status of the deal. Besides, "voidable deal"

is the term which is not used in regulatory documents creating inconvenience in practice. The outcome of this, among others, may be missing the period of limitations, which excludes the possibility to protect the violated rights.

7. It is necessary to amend the wording of Article 169 of the RF Civil Code in such a way, so that qualifying the deal as void is not related with identifying the purpose of the deal (whether it is contradictory with the basic principles of law-and-order and morals), but is rather based on actual negative consequences of the deal (e.g., causing loss to the state).

The current wording does not allow for recognizing the deals as void based on such grounds because it is extremely difficult to ascertain and prove this kind of purpose.

5. Companies with Mixed Property in Canada¹⁷⁸

A consequence of the privatization process adopted by Russia in the mid-1990s is the persistence of a large number of enterprises with mixed public and private ownership. Questions of performance, governance, accountability, and improper conversion of assets and control have arisen in the Russian context. The purpose of this note is to examine Canadian instances of mixed ownership to see whether they might suggest fruitful avenues for reform of corporate governance.

5.1. Place and Role of Mixed-Ownership Corporations in Canada

5.1.1. Canadian Corporate Structures

In Canada, organizations may be chartered under federal or provincial law. Provincial law for the most part follows the principles established under federal law, the main features of which are as follows:

- Ordinary joint stock companies are registered under the *Canada Corporations Act*, Part 1, or the *Canada Business Corporations Act*. They may have one or more classes of stock with different economic and governance rights. Their legal personality rests in a board of directors, who carry ultimate responsibility for running the company and are elected by the shareholders. Directors' fiduciary obligation is to the best interests of the company. There is an extensive set of behavioural norms and obligations laid out in such statutes as the *Canada Business Corporations Act*, the *Income Tax Act*, the *Canadian Environmental Protection Act*, employment law, the *Bankruptcy and Insolvency Act*, and many others. Provincial securities commissions regulate their issuance of equity and debt, and their obligations to disclose material information. The principal provincial statute, and a model for other provinces, is the *Ontario Securities Act*.

¹⁷⁸ Author – Harry Sveine. Global Research Center with Victoria University. Report prepared within the framework of participation in Project 51, CEPRA, “Issues of Managing Corporations with State Participation”, headed by Professor Alexander Radygin (Institute of Transition Economy, Moscow).

- Non-profit companies can be chartered under Part 2 of the *Canada Corporations Act*. They may operate in a commercial manner but must devote any surplus of revenues to the typically charitable interests they are organized to serve. In these cases the members of the society elect a board of directors who “are” the corporation in the usual way. These directors have the same kinds of duties and liabilities as do directors of ordinary profit-oriented joint stock companies. These companies are sometimes called “non-share corporations” as they do not issue equity to investors. If such an organization has some directors named by the government and some of its assets provided by appropriations, it may be an example of shared governance, if not ownership.
- From time to time, though infrequently in recent years, Parliament may by statute establish a corporation. Such “special act” companies normally have all the powers of an ordinary company except for certain specific constraints, which typically relate to corporate objectives – in effect, the allowed fields of endeavour – or to obligations to perform certain functions as a matter of public policy. Official language requirements, limits on borrowing powers and the issuance of securities or the location of offices are common examples of such obligations. When all the shares of such a corporation are owned by the government the company is referred to as a Crown corporation. If any shares are owned by a private party it is a mixed enterprise. If shares are held by a province it is referred to as a joint enterprise.

5.1.2. *Mixed-Ownership Corporations*

Stephen Brooks, writing in 1987, remarked that the literature on mixed-ownership corporations was scanty¹⁷⁹. His brief historical and analytical overview remains the best in the literature almost two decades later. Drawing on French and British as well as Canadian experience, he makes the point that such companies, in the crunch, are often disobedient. Elf and BP both disobeyed their national government shareholders to look after national customers first during the 1973–74 oil embargo, and

¹⁷⁹ Stephen Brooks, “The mixed ownership corporation as an instrument of public policy,” *Comparative Politics* 19 (January 1987): 173–91.

the Canada Development Corporation refused to invest in the failing Massey-Ferguson company in 1981. All were highly public confrontations. The directors of mixed enterprises are well within their statutory rights to decline to take actions that are not in the best interests of the company, and with the possible exception of France, Western publics will generally not support the government in such an affray.

Boardman and Davis, canvassing a large number of mixed, private, and state-owned enterprises in western Europe, North America and Japan, assessed their performance on a wide range of measures, concluding that “large industrial state-owned enterprises and mixed enterprises perform substantially worse than private corporations”¹⁸⁰. Their quantitative conclusion seems sound; less convincing, since the evidence is fragmented and anecdotal, is why this should be. They nonetheless describe the more compelling theories in an introduction to the empirical analysis.

5.1.3. *The Canadian Situation*

Of the small number of mixed-ownership commercial companies in Canada, many tend to be temporary: they were acknowledged at the outset as way stations on the route to complete privatization. Nonetheless, the period of mixed ownership can be lengthy – long enough to expose the peculiarities and difficulties inherent in the model.

Private investment in public corporations in Canada comes through debt as well as equity. Debt is seen as safe, given the existence of formal or assumed guarantees and the priority of debtors over equity holders in the case of a wind-up. On the other hand, most private investors prefer to avoid taking shares in companies whose motives include public policy or political objectives. Such purposes are seen as reducing the potential for profit and unfit objects for private investment.

The Canadian government classifies its corporate holdings into wholly-owned Crown corporations and “other” holdings. This category includes mixed-ownership corporations as defined above; corporations jointly owned with a province; shares in international organizations such

¹⁸⁰ Anthony E. Boardman and Aidan R. Vining, “Ownership and performance in competitive environments: a comparison of the performance of private, mixed, and state-owned enterprises,” *Journal of Law and Economics* 32 (April 1989): 1–33.

as the development banks; “shared-governance” organizations¹⁸¹; and the securities of organizations under the *Bankruptcy and Insolvency Act* which have fallen into federal hands pending liquidation.

As may be seen, mixed enterprises have not been popular in recent years (*Table 44*), and the last one, Petro Canada, was fully privatized in 2004.

Table 44

**“Other” corporate holdings of the government of Canada,
fiscal year-ends 1999–2005**

Type of company	2005	2004	2003	2002	2001	2000	1999
Mixed enterprises	0	1	1	1	1	1	1
Joint enterprises	3	3	3	3	3	3	3
International organizations	18	18	18	18	18	17	17
Shared-governance corporations	144	141	139	139	133	133	112
Corporations in bankruptcy	40	35	29	25	20	20	17

This was not always the case. As recently as 1985 there were about ten such corporations (*Table 45*).

Some were incidents in a larger restructuring: the numbered companies in *Table 45* were used to acquire the assets of failing fishery companies in the perennially troubled Atlantic region. The federal government negotiated an arrangement in which it invested new money, the owners of failing companies were given some shares to recognize the value of their assets, and a substantial new company, Fishery Products International, was created to carry on the fishery. The federal government sold its shares in FPI as soon as it was able to, but for a time, virtually the entire Atlantic fishery was under mixed ownership. Such were the obvious requirements of an emergency situation, as well as the daily public visibil-

¹⁸¹ These are typically industrial promotion boards or minor management or regulatory agencies organized under the non-profit provisions of the *Canada Corporations Act* or provincial Societies acts to whose finances the government may have made a contribution and in return is awarded a seat or two on the governing body for accountability and transparency purposes.

ity of the restructuring of the region's principal primary industry, that improprieties, even conflicts, in governance were avoided. After all, the alternative to partial federal ownership during restructuring was bankruptcy, a fact which had the virtue of simplifying negotiations.

Table 45

Canadian Mixed Enterprises, 1985

Название компании	История и основные характеристики компании
125457 Canada Limited, later NSHOLDCO Limited	with 125459 Canada Limited, sold to Fishery Products International as part of the restructuring of the Atlantic fishery in 1982–84
«125459 Canada Limited» Canada Development Corporation	as 125457 Canada Limited, later NSHOLDCO Limited Chartered 1971 as holding company with investments in Canadian manufacturing and resource companies; initial public offering (IPO) 1975; by 1985 government owned 47 percent of voting shares; later sold 23 of 30.7 million remaining shares to the public by installment receipts, taking voting power to 11 percent; remainder privatized in 1986.
Canadian Arctic Producers Limited	1965; set up to market art and carvings of Inuit and Dene communities; shares transferred to corporation in 1982, now a division of Arctic Co-operatives Limited.
Cooperative Energy Corporation	Chartered 1982 as means for co-operatives to invest in oil and gas; wholly privatized in 1995
La Société du parc industriel et commercial aéroportuaire de Mirabel Mohawk St. Régis Lacrosse Ltd. Nanisivik Mines Ltd.	Set up to manage airport lands inside the perimeter of Mirabel airport, Montreal. Sold 1982–83 Inactive by 1985 Canada earned 18 percent of equity through infrastructural investment and related services. Mine played out and property sold to Breakwater Resources Inc. about 1996.
Panarctic Oils Ltd.	Chartered 1966 to explore for and develop oil and gas in the Arctic Archipelago; became a subsidiary of Petro Canada in 1976
Petro Canada	Chartered as a Crown corporation in 1976; partially privatized 1991 and 1995; remaining shares sold 2004
Telesat Canada	Chartered 1969. Provides satellite broadcasting and related services for Canada and other countries in the Americas. Bell Canada, its long-time private shareholder and a principal telephone company in Canada, became sole owner in 1998.

Sources: Canada, Auditor General, *Report*, 1985, chapter 5, "Mixed and Joint Enterprises," Ottawa and company reports.

Other companies were set up with specific local development purposes, often in situations where access to capital in the ordinary way was difficult because of risk, lack of collateral, or the inability of banks to price and manage risks appropriately. This would account for Canadian Arctic Producers, which virtually created the market for Inuit art, today a principal source of income for far Northern communities; or for Mohawk St. Régis Lacrosse, where a native Indian community faced difficulty raising capital. The Mirabel industrial park was a shared ownership company set up to develop part of the vast acreage expropriated for the eventually unsuccessful Mirabel Airport, 50 km north of Montreal. Likewise, the Cooperative Energy Corporation was an offshoot of a doomed federal policy initiative, the National Energy Policy of 1980. Eager to create some Western approval for its confiscatory and only dubiously constitutional energy strategy, the federal government created a subsidized vehicle with which (principally agricultural) cooperatives could buy into the oil and gas industry. An election in 1984 reversed the policy and incidentally sealed the fate of Cooperative Energy as a mixed-ownership corporation. In contrast, the federal 18 percent share in a rich but remote lead-zinc mine, Nanisivik, was earned in a normal commercial manner through the provision of shipping services. The government, through a Crown corporation, CanArctic Shipping, had a monopoly on ice-strengthened freighters. The mine has since played out and the property was sold to a junior mining company, Breakwater Resources.

This leaves four large companies on the 1985 list. PanArctic Oils was created as a mixed enterprise in 1967 to explore for oil in the Arctic Archipelago, an area of great prospectivity but also great expense, where conventional oil companies would not venture alone under the prices prevailing at the time. PanArctic was later rolled under the umbrella of Petro Canada, but has kept its corporate identity and mandate as a subsidiary of that now large corporation. Telesat was also a child of the 1960s, founded as one of a string of federal attempts to conquer Canada's challenging geography¹⁸², in this case by making data and broadcasting services available across the country by means of geostationary satellites. Founded in

¹⁸² Canada has, after all, fully half as many time zones as Russia.

partnership with Bell Canada, the principal telephone company in Canada, the federal equity has since been sold to Bell. As regulated utilities, both companies are legally required to operate as “common carriers” that is, their monopoly ownership cannot interfere with access to the signal relay capacity of Telesat. A public regulatory body, the Canadian Radio-television and Telecommunications Commission, polices their business practices in a highly public fashion.

A few years later, in 1971, the Trudeau government created the Canada Development Corporation to invest government money, and later the savings of eventually 31,000 ordinary citizens, in a portfolio of private companies, principally in industrial and resource development. The officials who ran the company were some of the brightest, most aggressive, and most committed Liberals of their day. While the company enjoyed a number of investment successes, they also sustained losses. The appeal of supposedly strategic sectors where Canada might not otherwise have a “player” or might forfeit early-mover advantages was strong, and hard-eyed risk assessment and management was not a principal recruitment criterion. One of the later uses of the company was as a restructurer and seller of failing industrial enterprises, such as Canadair or de Havilland, companies in the aerospace business. Either way, CDC’s portfolio too often called to mind the comment of a distinguished Canadian public servant of the time, Sylvia Ostry, who observed that civil servants were no worse than anyone else at picking winners, but that “losers were pretty good at picking governments”.

That leaves Petro Canada, the principal focus of the rest of this report.

5.2. Petro Canada

The most recent example of straightforward mixed ownership is Petro Canada, founded as a Crown corporation in 1975, in the wake of the Arab oil embargo, as “a window on the industry”. This richly endowed company was intended to make sure that there was a Canadian corporation of scale in the rapidly consolidating international oil industry of the day.

The principal questions are how the federal government exercised its rights as owner during three distinct periods and whether corporate behaviour changed as ownership changed.

5.2.1. *History of Petro Canada Development*

When Parliament created Petro Canada in 1975, its initial endowment was the government's share of PanArctic Oils and its holding in Syncrude, the pioneering Tar Sands developer, then still in pre-production mode. The initial board of directors, all directly appointed by the government, was chaired by Maurice Strong, a businessman with strong public policy interests who was well acquainted with senior ministers in Ottawa. Strong was also President. The Executive Vice President and Strong's successor as President, Wilbert Hopper, was a former senior government official. The two started business on January 1, 1976 in Calgary. They were soon joined as vice president of corporate planning by Joel Bell, an ambitious young man from the Prime minister's Office¹⁸³.

Petro Canada had a mandate to grow big, and to do it quickly. At the same time they had a mandate to invest in those national resources which were just beyond the fringe of what the private industry of the time would contemplate. So their first investments were farm-ins – shares of projects owned and operated by other companies – on expensive and risky exploration plays on the Scotia Shelf and on the Grand Banks of Newfoundland, and the acquisition of the less risky Canadian assets of Atlantic Richfield, which was then under financial stress from the development of the Prudhoe Bay field in Alaska. Investment in Syncrude was stepped up. In this case the risk was not with exploration results but with technology.

Then came a mistake. In 1978 Petro Canada tried to buy Husky Oil, a major Western Basin producer, but execution of the deal fell apart, largely because of errors by the relatively inexperienced Petro Canada team¹⁸⁴. On the rebound, Hopper and Bell (Strong had left in 1978) bought Pacific Petroleum in 1979 through a purchase of the 48 percent holding of Phillips Petroleum and a subsequent public offer for the rest of the float. For the first time Petro Canada had moved away from being a pure upstream play, as Pacific Pete had some small refining and marketing assets.

¹⁸³ Peter Foster, *The Blue-Eyed Sheiks: The Canadian Oil Establishment*, Collins, Toronto, 1979, pp. 139–64.

¹⁸⁴ *Op. cit.*, p. 157.

At this point Petro Canada's existence was threatened. A Progressive Conservative government under Joe Clark was elected in May 1979 which was philosophically opposed to direct government investment in the sector and which had promised to privatize the company. Even exploration success off the east coast in both oil (Hibernia) and gas (Scotia Shelf) was not going to deter the new government. Fortunately – from the point of view of company management – the government fell in November, before it could pass privatization legislation, and the more interventionist Liberals were re-elected. In the wake of further disruptions in the international oil economy, the Liberals were bent on expanding Petro Canada and, incidentally, expropriating the rents from high prices hitherto accruing principally to the province of Alberta¹⁸⁵. Expansion came in the form of the purchase of the large Canadian assets of the Belgian Fina corporation, which added greatly to Petro Canada's retail marketing and refining base. In 1982 Petro Canada discovered a large new oilfield, Valhalla, in its home province and in 1983 bought the refining and marketing assets of BP Canada. By now it was by several measures the second biggest integrated oil and gas company in the country and nearing its goal of being "too big to privatize"¹⁸⁶.

With the election of Brian Mulroney's Progressive Conservative government in 1984, the priority was unwinding the Liberals' unfortunate National Energy Policy. Petro Canada, whose acquisition and frontier drilling budgets had been underwritten by the federal government, was unhitched from that source and instructed thenceforth to behave in a purely commercial manner. The next acquisition, Gulf Canada Limited, was financed from ordinary cash flow and borrowings. Not until Mr.

¹⁸⁵ This may have been the single most wrong-headed policy decision by any Canadian government. Regional anger was enormous, set the stage for a Conservative landslide in 1984, and persists to the present. The seizure, moreover, was predicated on oil and gas prices continuing to escalate from their 1979 highs, hardly something to be predicted from an unstable cartel faced with resource and technological alternatives. The story of the NEP is told in another volume by Peter Foster, *The Sorcerer's Apprentices: Canada's Super-Bureaucrats and the Energy Mess*, Collins, 1982.

¹⁸⁶ A phrase used by the CEO, W. Hopper, to the author that summer. Petro Canada would have been by far the biggest IPO on the Canadian market at the time, had it been sold all at once.

Mulroney’s second term did the government get around to passing privatization legislation, and in July 1991, the first shares were sold to the public. From then until 2004, Petro Canada was a classic mixed enterprise.

In 1995, another 50 percent was sold, leaving the federal government with approximately 19 percent. The remainder was sold in 2004. There is thus a period of 16 years in which the federal government was sole owner of one of the largest integrated oil and gas firms in the country, 4 during which it was the majority owner but pledged to proceed at some point to complete divestiture, and 9 during which it was a minority shareholder. The company continues to thrive in private ownership (*Table 46*) and has lately been discussing a large liquefied natural gas (LNG) deal with Gazprom.

Table 46

Petro Canada 2005: a snapshot

Indicator	Billions of Canadian\$ except where indicated
Assets	20,7
Long-term debt	2,9
Shareholders’ equity	9,8
Cash flow	3,8
Net profit	1,7
Return on capital employed	16%
Proven reserves	1,232 MMboe

Source: Petro Canada Annual Report, 2005.

5.2.2. Petro Canada as a Crown Corporation

It will be apparent that the company’s first 15 years were a period of exceptional expansion, driven by a public policy (and a public purse) that wanted to see a major Canadian presence in an industry which had been overwhelmingly – over 90 percent – in foreign hands, and which in the globally highly politicized markets of the day did not put Canadian consumer interests first. It is fair to say that the board and senior management were initially not as experienced as their competitors. This showed itself in risk- and quality-adjusted prices for farm-ins with those competitors which were somewhat more expensive than they should have been, rather than in the prices paid for major acquisitions. Here, management

was prepared to be opportunistic. With deep pockets and an ability to pay cash for the assets of competitors experiencing squeezes of their own, they were able to be skilful buyers, the Husky fiasco aside. Very quickly, the best brains in the investment banking and legal businesses came on-side.

Foster relates an incident from the 1979 purchase of Pacific Pete which illustrates the sometimes delicate problems of governance and propriety that can arise even in these relatively simple circumstances¹⁸⁷. The board of directors, consisting principally of experienced businesspeople who were not unfriendly to the government of the day, also included the Deputy Minister of Finance, Tommy Shoyama. The financial instrument used to make the purchase was so-called “term-preferred” shares, an after-tax device that allowed the payment of significantly lower dividends. The federal government, concerned about the loss of tax revenues through what was seen as a loophole, ended their use in the November 1978 Budget – just days after Petro Canada had arranged its financing. Mr. Shoyama, a man of unimpeachable reputation, knew what both the company and the government were doing, but said nothing to the company.

Mr. Shoyama was in a difficult spot¹⁸⁸. He had to respect his oath of office in respect of Cabinet secrets, and he had a legal obligation as a board member to act always in the best interests of the corporation. He resolved it by keeping secret the intention of the government, even though there were subsequent accusations of improper behaviour. There had been much speculation in the press about the possibility of closing the loophole, however, and any prudent management would have hastened to make its financing activity a *fait accompli* before the date of the Budget.

During its period as a Crown corporation, Petro Canada acted as an instrument of national policy. It is clear that no other company was will-

¹⁸⁷ Foster, *Blue-Eyed Sheiks*, p. 161.

¹⁸⁸ The conflicts faced by senior officials when they are appointed to corporate boards, even those of Crown corporations, can be severe and may be best avoided altogether. H. Swain, “Eyes on governance: governing our Crown corporations,” *Globe & Mail*, 21 October 2004 p. B6.

ing to take on its portfolio of frontier (Arctic and offshore) exploration, technology development (Tar Sands), and conventional exploration and development while at the same time striving to grow a presence in every facet of the business – exploration, production, refining, distribution, and retail marketing – in a single country. No private company attempted anything of the sort, even within the extraordinarily generous fiscal climate of the times.

5.2.3. Petro Canada as a Mixed-Ownership Corporation

In July 1991 the first shares were sold to the public. There had already been changes in senior management and the board. Strong, Hopper and Bell had left years before, and the board and senior management were oil industry professionals. The federal government still appointed a director, a senior lawyer from a prominent Calgary firm with a large energy practice, J.F. Cordeau. A modest program of investment abroad began with an oil discovery at Tamadanet, Algeria. Rebranding and marketing in Canada got a boost, along with refining capacity that allowed the production of a full line of lubricants as well as gasoline and diesel fuel. In 1996 the Canadian upstream activities of Amerada Hess were acquired, and an alliance was formed with Norsk Hydro in respect of North Sea oil and gas. Offshore (Hibernia) oil and Tar Sands production reached 250,000 barrels per day (b/d) by the turn of the century, and in 2002 international operations were greatly expanded through the acquisition of the exploration and production assets of Germany's Veba Oil and Gas GmbH. In 2004 a plan for a liquefied natural gas plant, using LNG from Gazprom, was announced for a site in the Gulf of St. Lawrence. The same year saw the sale of the remaining 19 percent government holding. The next year some of the Veba assets in Syria were divested to a joint venture of Chinese and Indian companies.

The story from the announcement of privatization in 1990 forwards, in other words, is that of a normal large company in this sector. It spread risk by acquiring an exploration and production portfolio abroad, both by acquisition and by direct investment. It diversified its domestic upstream investment among offshore, Tar Sands and conventional production, and built a portfolio of natural gas assets to complement oil. It sought to make its marketing activities reliably profitable by investing in brand develop-

ment and by building or acquiring refining capacity to serve a wide range of petroleum, oil and lubricant markets in its home territory. All of this was financed from internally generated cash flow and normal market operations, and with the rewards of a conservative balance sheet in mind (see *Table 46*). No extraordinary attention was paid to public policy objectives, although like all large companies striving to be seen as good corporate citizens, it began to pay attention to its environmental footprint and its community relations, and since 2001 to report on these good deeds. It is today a well-regarded senior integrated oil company whose stock price has rewarded investors well in recent years and whose dividend has grown steadily since its inception in 1994. In other words, there has been no difference in corporate strategy and behaviour, in terms of prudent risk management, between the periods of mixed ownership and wholly private ownership.

Finally, it should be noted that mixed or wholly private enterprises operate by exactly the same rules and the same oversight by securities commissions, occupational health and safety regimes, employment and environmental laws and so on. Directors have the same duty of loyalty to the best interests of the corporation and liabilities with respect to third parties. An alert legal profession, public regulators, and an apparently incorruptible judiciary enforce the law.

5.3. Other Types of Mixed-Ownership Companies

5.3.1. P3s: Mixed Ownership?

In recent years, following on the success of the British Private Finance Initiative, there have been a number of “public-private partnerships” (P3s) in Canada. The federal government somewhat inadvertently pioneered the form more than twenty years ago with its innovative approach to financing the Confederation Bridge, a 13-km bridge across the Northumberland Strait connecting Nova Scotia with Prince Edward Island. Since then two provinces, British Columbia and Ontario, have established Crown corporations to arrange P3s. But these are less true partnerships or mixed-ownership enterprises than they are a sophisticated way of acquiring infrastructural services. There is a large literature on the topic; suffice to say that in their fullest flowering, P3s involve a transfer of risk and

related financial responsibilities to the private sector providers of necessary infrastructure, in which the (usually) higher cost of private capital is offset by innovation in design and economies in operation. A hospital, for instance, may be commissioned by a public authority under a “design-build-finance-operate” model, under which (a) the authority specifies the outputs or performance required, (b) transfers substantial financial, completion and operating risk to the private sector, (c) seeks innovative design and operating efficiencies through an open bidding process, (d) requires the builder to be the operator and capital maintenance provider for a period measured in decades, while (e) the public authority provides all clinical services. This model has been applied as well to roads, bridges, airports, prisons, schools and other discrete pieces of infrastructure in a number of European countries, the US, Canada and Australia. But while they involve substantial transfer of risk, the sharing of risk is trivial, there is no mixing of interests as would happen through a formal partnership (much less shared ownership of equity) in the venture, and the roles and responsibilities of all the entities involved is set out exhaustively in contracts. At bottom, there is no pooling of interest in a single organization, which is the essence of the mixed-ownership corporation¹⁸⁹.

5.3.2. Pension Funds

In recent years public pension funds operated by the provinces and by the federal government have become major investors. Conservatively invested, much of the cash used to be in fixed-income securities, often of the very governments that sponsor the funds. In recent decades, however, a more professional approach to investment has taken hold, with decisions on investment policy and specific transactions delegated to professional managers. In consequence most now devote more than half of their holdings to corporate equities. And the sums involved are staggering: about \$800 billion in total. The Canada Pension Plan Investment Board alone administers \$103 billion of workers’ assets.

¹⁸⁹ We assert this despite arguments to the contrary in, e.g., Alessandro Marra, “Mixed public-private enterprises in Europe: economic theory and an empirical analysis of Italian water utilities,” *Bruges European Economic Research Papers* 4, July 2006; www.coleurop.be/eco/publications.htm.

The leader in equity investment among pension funds has been the Caisse de depot et placement du Québec. Over the period from the 1970s to the turn of the century it actively sought, consistent with a good rate of return, to invest in Quebec companies, with the idea of creating ‘national’ champions. This *dirigiste* idea was shipwrecked on shoals of losses – \$8.5 billion in 2002 alone – which led to a revolution in management and the establishment of a new goal: creating the best possible retirement for its annuitants. The conflict, in other words, between maximizing returns and funding provincial economic development came to an abrupt end when the conflict between goals was resolved in favour of the people to whom the trustees of the fund owed a fiduciary duty.

In many ways the story of the Caisse has been salutary for its peers, none of whom take an active role in the affairs of their investee companies. In general their holdings in individual publicly traded companies are small – a few percent of any one company, perhaps, and highly diversified. The Canada Pension Plan Investment Board has tended simply to ‘buy the index’ – i.e., not to exercise any discretion about individual companies but to buy across the board in proportion to market capitalization. There are pressures on these boards to vote their shares in favour of a variety of good causes: good corporate governance practices (though these are now much more closely regulated by law than a decade ago, when that particular pressure began to be felt), or good environmental performance. These pressures are for the most part resisted, although there is some movement in that direction.

The bottom line is that the investee companies are not mixed-ownership corporations of the classic sort. The pension boards may well be Crown agencies, but their objective is maximizing return within a set of investment and risk guidelines for the pension plan beneficiaries, a matter which is thought not to involve an active role in management.

5.3.3. *Provincial Cases of Mixed Ownership*

Provincial experiments in mixed ownership are few, and there is no central registry of them. As with the federal government, they were more popular in the 1970s than before or since. In Saskatchewan, for example, a Crown-owned corporation has long overseen the affairs of the provincial government’s more-or-less commercial corporations, but private in-

vestment in these vehicles is minor and mostly at arm's length. British Columbia also experimented with a holding company for Crown corporations but tended to see this as a step on the way to privatization.

5.3.4. *Minor Sources of Mixed Ownership*

There is a program of the federal government, Technology Partnerships Canada, which can result in short-term government ownership of some of the equity of private companies. Conditional loans are made to companies meeting fairly strict guidelines; these loans are repayable if the technological development in question is successful, usually under some sort of royalty arrangement. In the case of a wildfire success, the government may reserve some warrants on company stock. Usually these turn out to have no value; in the rare cases when they do, they are disposed of as soon as practicable.

Technically, the federal government may find itself sharing equity with other creditors through the workings of the *Bankruptcy and Insolvency Act*; but as the entity in question has already failed, this hardly gives rise to policy or governance questions.

Finally, Crown corporations themselves may have non-wholly-owned subsidiaries¹⁹⁰. Thus Canada Post owns 80.41 percent of Purolator Courier Ltd., 51 percent of Innovapost Inc., and 6.1 percent of Co-operative Vereniging International Post Corp. The Canadian Broadcasting Corporation owns 20 percent of Look Communications Inc. and 29 percent of The Canadian Documentary Channel. These and others are minor entities, for the most part, operated with strategic partners rather than financial investors in an unreservedly commercial manner.

5.4. Concluding Observations

Why are there so few mixed ownership corporations in Canada? The answer lies in the structure of incentives for private investors. In this economy, the expectation is that the only reason that government invests in anything that looks like a corporate enterprise is because it is not some-

¹⁹⁰ Canada, Treasury Board, *2004 Report to Parliament – Crown Corporations and Other Corporate Interests of Canada*, Ottawa, 2005.

thing the private sector would normally invest in. The enterprise is freighted with objectives that have little to do with private profit; or the risk is beyond the frontiers of rational private investment; or it may be subject to whimsical operational decisions based on the personalities of individuals who are appointed by the government to the board or management. These persons may not be motivated by the pure flame of profit maximization. The question private investors would ask is why anyone would want to invest in a mixed enterprise?

Private entities may lend money to government operations, especially when, as is usual, they pledge the “full faith and credit” of the government to the repayment of principal and interest but still pay a few basis points more than government bonds. In such cases the return to the private investor is entirely independent of the success or failure of the enterprise. Equity investment carries no such guarantee.

Shared-governance entities are different. These are typically industrial or regional promotional bodies, or entities with quasi-regulatory or sectoral management functions, which are in essence representative of the sectors being regulated or promoted¹⁹¹. In these cases, there are no real assets to be diverted, only operational funds, to which the government typically makes a contribution in return for a seat or two on the board. The purpose of such representation is essentially informational, though it may be supposed that the mere presence of such members may keep self-dealing to a decent minimum.

It would appear that the purpose of government investment affects governance and whether or not conflicts arise in the minds of managers and observers. Where shares are acquired simply in order to take advantage of private sector management in a search for superior returns, as is the case with the pension plans, no conflicts arise. Where shares are held temporarily with the purpose of sale, as in Petro Canada during the period of mixed ownership, objectives are also strongly aligned. It is when the government wants to avail itself of private investment in competitive

¹⁹¹ These are listed in the annual report of the Treasury Board to Parliament, “Crown Corporations and Other Corporate Interests of Canada,” available on the website www.tbs-sct.gc.ca/report/CROWN/.

markets in the pursuit of goals which may inhibit profit maximization that instability may be expected.

In Canada, when governments wish to avail themselves of the disciplines of ordinary commercial markets for a policy purpose, they normally do it through wholly-owned Crown corporations. If they wish the enterprise to be carried on by a genuinely private firm or by private managers, government generally arranges it through fairly sophisticated contractual arrangements, or more generally through the creation of private financial advantage through direct or tax expenditures. The private sector avoids mixed enterprises unless there is some advantage – monopoly, monopsony, self-regulation, sectoral or regional promotion, insider information, procurement preference, tax or financial penalty avoidance – of a more than ordinarily commercial sort granted in the process. In this sense, the Canadian example is either of little use to Russia, or a great deal. The example might be helpful if Russians were to decide to unwind the sometimes unhealthy connections between public and private interests in ordinary commercial enterprises.

6. Current Tasks and Key Areas of Improving Management of Mixed Property Companies in the Corporate Sector

By now 8 years have already passed since the Concept of State Property Management and Privatization in the RF was adopted in 1999. That is why it would be quite logical to evaluate the outcomes of the first several years of implementation of this document, as well as to identify the existing problems.

6.1. Intermediate Outcomes of Reforming the System of State Property Management in the Corporate Sector in 2000-es

The Concept of 1999 connected exercising control over efficient management of state-owned shares with evaluation of the following factors:

- dynamics of growth of income from managing shares in federal property;
- decreasing the size of blocks of shares fixed as federal property;
- functioning of accounting and control mechanisms with regards to activities of companies with state participation, as well as accounting and control over managers;
- comprehensiveness of the register of blocks of shares;
- outcomes of the process of decreasing the number of small non-liquid blocks of shares fixed as federal property.

Being based on the recommended criteria and indicators, one may note that the state was able to achieve growth of income from managing state-owned stakes of shares, which was reflected in significant increase of paid dividend amounts. However, one shouldn't forget that the objective basis of all that process is the renewed growth of Russian economy in general, leading to increase of dividends in the private sector as well. One may also assume with certain confidence that by now the register of state-owned blocks of shares is more or less complete.

At the same time, the overall numbers of blocks of shares fixed as federal property did not decrease versus 1999, while the number of minority (up to 25% of capital) blocks of shares grew, just like their relative share in the overall bulk of federal blocks of shares.

Eventually, after enactment of a series of legal acts and undertaking significant administrative efforts, the mechanism of managing shares in joint-stock companies with state participation was finally formed, including the required controls.

If we were to evaluate the degree and the efficiency of practical implementation of the Concept-1999 from the point of view of a conversion instrument, the mechanisms that it offered were not utilized to a full extent. *Appendix* contains a full-scale comprehensive evaluation of the outcomes of Concept-1999 implementation by key areas of achieving the objectives set by the state.

Classification of business entities with state participating in their capital was achieved only partially. Some relatively complete information is available only about the structure of companies dependent on the size of the state's share, which defines the level of the state's influence, and dependent on the sector of the economy. With regards to classification of companies based on the objectives of the state, the list of strategic JSCs was approved in 2004; however, the objectives of the state in other companies where the state is one of the shareholders are not completely clear, which makes the perspectives of divesting the state's blocks of shares non-transparent. There is no information about classification of business entities with the state participating in their capital dependent on the level of the liquidity of their stock, on their financial status, headcount and sizes of their capital assets.

The government was undertaking some pretty basic measures when exercising general state functions of managing the shares owned by the state. They were: coordination of the activities by the ministries and departments, appointing government officials to serve on management bodies of respective business entities and issuing written voting instructions for them, in some cases charters of business entities with the state participating in their capital were reviewed in order to assure the state's interests.

However, the certification of the state representatives was not performed; government officials appointed to represent the state's interests in major companies of strategic importance were supposed to have this task as their major job – but that has not been implemented. Financial resources to support government officials representing the state in respective JSCs were supposed to be allocated out of the dividends derived from the state-owned shares, however, this wasn't accomplished either.

Consolidation of blocks of shares of JSCs operating in similar areas or having similar objectives was performed on a vast scale within the integration framework. Acquisition of shares to strengthen the state's participation in JSCs (or making the state-owned block of shares the controlling package in some other way) was required to implement some general state objectives. However, until 2004 that was done on a rather random basis; and only later it turned into active expansion of companies with the state's participation effecting a rather wide spectrum of sectors and areas of business.

There is no information about establishing the procedure for using the state-owned blocks of shares as guarantees on behalf of the Russian Federation with their allocation to the state debt secured by the state's property rather than by the federal budget revenues; nor is there information on substituting stakes of shares fixed as federal property with the special "Golden Share" right.

The measures of the Concept-1999 relating to increasing the non-tax revenues into the federal budget, to attracting investment into real economy and to supporting domestic manufacturers were implemented to an even smaller extent.

In essence, one may be sure only about certain cases of transferring shares into the property of the RF subjects as an offset against financial obligations of the federal government¹⁹², about acquiring shares by the state as a result of capitalizing the tax arrears (without putting them under the trust management) and about some attempts to attract an effective owner within the course of standard privatization procedures.

¹⁹² At the same time nothing is known about regions presenting their programs for developing such companies, which in the Concept-1999 was qualified as a mandatory condition for transferring blocks of shares.

There is no information of any kind about any of the following measures:

- purchasing shares with the purpose to consolidate them into stakes, further selling of which would assure the highest income to the federal budget;
- issuing and offering derivative securities covered by shares;
- issuing derivative securities providing the right to acquire shares after a certain period of time with simultaneous transfer of the mentioned shares into the trust management by the Buyer of derivative securities;
- selling shares upon pre-market preparation and rehabilitation of joint-stock companies;
- exit from LLC and LP receiving the effective share of their value defined on the basis of calculating the net assets of the company¹⁹³;
- using state-owned shares to secure investment or loans allocated for special targeted projects;
- using shares to attract investment to vertically integrated organizations (shares introduced into charter capital of the vertically integrated organization are in such case used as security).

Speaking about G&A costs optimization, one may state only that the number of federally-owned blocks of shares was decreased down to the level allowing for implementing the regulatory and control functions of the state by way of selling shares, their consolidation within vertically integrated organizations utilizing similar technology or operating at the same markets, as well as their transferring to the regional (municipal) level. However, the share of minority blocks of shares (which do not allow the state to exercise its management functions) still remains rather big, and Privatization Program for 2007–2009 is focused at selling first of all complete (100%) state-owned blocks of shares.

Nothing is known about introducing minor blocks of shares (the decision to sell them was made, but they weren't sold) and blocks of shares which won't bring significant income to the state budget in case they are sold into charter capital of the companies created in a way similar to port-

¹⁹³ In practice the state's share in LLC and LP were included into the Forecast Plan (Program) for Property Privatization similar to the state-owned blocks of shares in JSCs.

folio funds. There is no information either about selling small non-liquid blocks of shares to the issuer and to the company employees at privileged price.

In order to support institutional changes in the economy, certain measures were implemented into practice.

Some cases were observed, when the government facilitated decision-making about reorganization or bankruptcy of enterprises with material budget payments arrears at the initiative of the owners with the purpose of further capitalizing the arrears into liquid shares of the newly established effective companies. Often enough the government supported restructuring of major enterprises delineating the assets required for exercising strategic state functions (and selling all the remaining assets) with the purpose of future transformation of such enterprises into 100% state-owned joint-stock companies to launch new production or to diversify the existing production. Another measure exercised by the government was acquisition of shares at the expense of contributing land plots into charter capital of joint-stock companies.

Vertically-integrated organizations were actively established at that time, other areas of managing state-owned stakes of shares were also improving. Same may be said about increasing investment attractiveness of Russian companies for domestic and foreign investors by way of decreasing the state's share in their charter capitals. The mechanism for preserving the size of the state's share during additional issues of shares established in 2006 may play an important role in this process.

The only thing to add is that the analysis of causes for inefficiency of managing state-owned shares through state representatives performed within Concept-1999 still remains valid.

Partial classification of business entities with the state participation was accomplished allowing for identifying realistic opportunities for assuring the state impacting the decisions made by the managing bodies of such companies. Certain efforts were undertaken to bring the constituent documents of joint-stock companies in compliance with the state's objectives and with the task of protecting the state's interests.

The acuteness of the problem of poor quality and inefficiency of managing state-owned shares through the state representatives (being in most

part government servants) was to a certain extent eliminated. The key cause for such poor quality and inefficiency was the gap between the size of the state's share in the capital and the capacity of the existing management system, as well as resources allocated for such management, because the number of state representatives had grown significantly compared to the 1990-ies and material growth of government officials' salaries was also observed (especially, at the very top level). Within the approved interfaces with state power bodies the spheres of authorities of the state representatives were defined, as well as the order of preparation for operations of managing bodies of the business entities with the state participation and the format/profile of reporting documents.

However, the mission and the operations of government officials in the capacity of the state representatives still do not provide for any mechanisms of their professional certification and special training based on the specifics of a certain company. There is no clear and uniform system of selection, training and performance evaluation of the state representatives. The last factor impedes exercising effective control and applying disciplinary measures.

In the mean time, the performance discipline of the state representatives still remains at very low level. Thus, the materials of the RF Accounting Chamber Board meeting on October 27, 2006 to discuss the outcomes of auditing the activities of the RF Ministry of State Property and other federal executive agencies in the sphere of assuring the state's interests with regards to managing and disposing federal property in 2003–2005 stated some rather significant drawbacks in organizing the activities of the state's representatives in managing state-owned stakes of shares. In 2004 the state's representatives overall missed 68.5% of general shareholders meetings. As a result, the decisions on paying out dividends, on their amounts and forms of payment were in most cases made without participation of the state's representatives¹⁹⁴.

Because the objectives and interests of the state with regards to a specific business entities are not always clearly defined by the state power bodies, the activities of its representatives without specific tasks being set

¹⁹⁴ Low Efficiency of Control // Financial Control, December 2006, No. 12 (61), p. 107.

is often based on their own understanding of the state's objectives and interests leading to their misinterpretation and distortion, giving way to opportunistic and biased behaviors without any risk to be called liable for inefficient management.

The practice of engaging trustees and managing companies to managing the state-owned stakes of shares has not been developed, even though it is to a greater extent in line with professional management requirements and assures responsibility for management outcomes, as well as providing opportunities for better reward and compensation of managing expenses to the trustees/managing companies from the respective company's profit dependent on achieving certain financial results.

The order of putting the federally-owned shares under trust management as approved in 1997 was not in any way changed. Its major advantage (tender-based process of selecting the trustees) does not make this mechanism completely free from such drawbacks as lack of normative provisions about tender participants mandatory submitting their proposals about the best way to achieve the objective, about reporting procedures, control, grounds for applying liability measures with regards to the trustee.

Information about situations in business entities with state-owned shares obtained by state power bodies from the reports of the state representatives is not systematized and generalized to a sufficient extent; a comprehensive analysis of economic performance of such companies is not available.

Summarizing all the above, it is possible to say that with regards to achieving the objectives of state management of the state-owned stakes of shares (participatory interest) as defined in Concept-1999 certain progress was evident in the 2000-es, especially in the sphere of increasing the non-tax revenues into the state budget and carrying out institutional transformation in the economy, if only development of vertically-integrated organizations in order to restructure certain sectors of the economy. In relation to this one may with a great level of certainty speak about G&A costs optimization as well. At the same time, it is not at all obvious that some business entities improved their performance in the sphere of general state functions and of achieving other objectives set by the state. Special studies are required to answer the question: were there any posi-

tive changes made with regards to improving financial and economic performance indicators, providing incentives for production and operational growth, attracting investment, etc.

It is also worth noting that the objectives of improving the management of business entities with the state's share were also set among others by the RF Government in its mid-term development programs throughout the 2000-es.

These objectives were implemented into practice to a very different extent. Thus, one may consider partially implemented the tasks set forth in the RF Government Action Plan in the sphere of social policy and modernization of the economy for 2000–2001 (approved by the RF Government Resolution No. 1072-r of July 26, 2000), which were in a very general way formulated as protection of the state's interests in managing bodies of joint-stock companies and as taking inventory holdings of all assets and liabilities of the state (with regards to respective business entities). However, this is not to the same extent true with regards to the Program of Social and Economic Development of the Russian Federation for the Mid-Term Perspective (2002–2004) approved by the RF Government Resolution No. 190-r of July 10, 2001.

This document stipulated the following measures targeted at improving the efficiency of managing the state-owned shares:

- exercising a set of measures to improve professional qualifications of government officials representing the state in joint-stock companies, raising the level of their responsibility by way of enacting appropriate legal documents;
- forming the institute of professional state representatives with their main function being to assure the interests of the state in joint-stock companies;
- resolving the issue of funding the activities of the state representatives in the sphere of managing the state-owned blocks of shares;
- monitoring, analysis and planning of financial and operational activities of the joint-stock companies with over 50% of shares owned by the state;
- performing consolidated, industrial and regional analysis of activities of the joint-stock companies with participation of the state, analysis

of the efficiency of their operations , defining the estimated amount of dividends to be remitted into federal budget, as well as performing other calculations required for timely justified management decisions by the state representatives in joint-stock companies.

In essence, it is possible to say that there were no any efforts made to resolve the first two tasks. As for the third one – some attempts to solve it were made (however, the format of resolving by way of including a separate line-item into the budget to represent allocations for managing state-owned stakes of shares does not exactly comply with the approaches of Concept-1999). It is very difficult to judge the efficiency of resolving tasks No. 4 and No 5 related to monitoring and analysis of performance of business entities with state participation. The only thing to add is just to mention the continuation of selling state-owned blocks of shares in joint-stock companies, which are not associated with the state's interests on protecting national security. However, the pace of this work was obviously behind the planned ones.

As the Program of Social and Economic Development of the Russian Federation for the Mid-Term Perspective (2006–2008) approved by the RF Government Resolution No. 38-r of January 19, 2006, it does not specifically mention business entities with state participation with the exception of the already traditional task of further decrease of excessive state and municipal sectors of economy, which does not facilitate implementation of functions and authorities of the Russian Federation, its subjects and local self-government bodies.

6.2. Key Issues and Recommendations to Improve State Property Management in the Corporate Sector

The number of business entities with state participation – those with significant weight in Russian economy in general – will remain quite significant in the foreseeable future, which makes it necessary to improve the whole system of management of such companies. Let us now review in greater detail the most important issues arising along this way and the key areas of such improvement.

- Restructuring of portfolios of state-owned shares (participatory interest) in the context of transformation of the state sector of economy in general;

Resolution of such task stipulates defining the group of joint-stock companies of special value for the state from the point of view of its strategic interests, in which state-owned stakes of shares are not subject to sale in the long-term perspective and for which the possibility of maintaining the size of the state's share at the expense of the state budget needs to be provided in the light of the most recent changes in privatization regulatory framework.

In essence, there is a need to expand optimization processes actively implemented by the government in departmental federal unitary enterprises and institutions in the context of administrative reform to cover the sub-sector of business entities with government participation. In relation to this it is absolutely possible to adjust the list of strategic JSCs – both in the way of incorporating certain companies into that list and in the way of excluding certain companies from it (the newly incorporated entities may be the recently incorporated federal unitary enterprises and newly established integrated organizations), but doing just that won't be enough. It is also necessary to clarify the status of companies with state's share in their capital not qualified as strategic ones from the standpoint of the state's objectives, the feasibility and possibility for divesting the state-owned blocks of shares.

Sector-based concepts need to be adopted as the basis for such work to substantiate the objectives and tasks of the state's participation in various sectors of economy linked to the tasks of structure policy, with plans to reform certain sectors, with authorities of the respective departments. The objectives and tasks of state participation in the capital of business entities need to be set, financial and economic situations of business entities need to be analyzed, as well as current practice of corporate governance with regards to compliance with the legislation provisions and the requirements of Corporate Code of Behavior, and situations at the markets where they operate.

With regards to state-owned blocks of shares of business entities, operations of which cannot provide for resolving the tasks set for the

power bodies based on the objectives of the state in this given sector and on the legally-established authorities, it will make sense to develop proposals on privatizing the state-owned shares of joint-stock companies setting the sequence and the terms of selling.

First of all, this relates to the companies, where the size of the state's share (minority stakes) does not allow for influencing management decisions, and companies operating in the environment of the already competitive market.

The interim options might be: transferring the state-owned blocks of shares (participatory interest) under trust management by managing companies (including the option of further sale based on the outcomes of such trust management), to holding companies and investment funds.

Using the trust management mechanism is feasible for rather big sizes of the stakes (not smaller than blocking packages), which are subject to privatization, but cannot be sold in the near future due to certain reasons (e.g., need for pre-sale rehabilitation, unfavorable situation at the stock market, etc.).

Contributing the state-owned blocks of shares into charter capitals of holding companies is targeted at resolving the tasks of integration and managing enterprises producing similar goods or operating in the same market sector – it relates mostly to structure policy requiring participation of the state. In the opposite case simple selling of state-owned shares seems to be more efficient and more transparent solution.

Forming investment funds with the purpose of managing low-liquidity stakes of shares will allow for decrease of expenses required for maintaining and administering the state-owned portfolio of shares, for increase of capitalization and of liquidity of the blocks of shares upon consolidating low-profit shares of minor companies applying the instruments of financial market and group investment mechanism.

- Sales policy

As has been mentioned earlier, the state-owned stakes of shares (either minority ones or blocking ones) have been the key subjects to sales within the course of privatization procedures during the recent years.

Implementing the policy of selling minor blocks of shares not providing the state with the possibility to influence management of the respec-

tive companies is a rather difficult task, because as a rule such stakes do not represent any particular interest for potential investors not only due to their minor size, but often – due to the profile of the companies' business or their financial and economic situation. Provided the financial and economic situation is favorable, the motivation of investor could be not just aspiration for establishing corporate control, but even more so – expectations about significant dividends and about growth of their shares market value. However, despite all positive changes of the recent years, such situations still remain true only for a small number of companies, in which the dominating groups of shareholders are already established (including the state as a shareholder in some of the companies).

An abrupt shift towards selling full stakes (100% shares) in the Forecast Plan (Program) for Federal Property Privatization in 2007 may significantly change the whole privatization picture. However, in the environment where a big number of minority stakes is owned by the RF such a shift doesn't seem to be very feasible, plus one may question how realistic this task really is.

From the point of view of organizing the sales process and for the sake of facilitating the selling of state-owned blocks of shares, the following needs to be taken into account:

- grouping blocks of shares of several joint-stock companies of different sizes forming lots for further sales may be quite feasible, as it may allow for using the motivation of potential buyer associated with acquiring the desirable stake of shares of significant size – for the purpose of selling low-liquidity minority stakes;
- proposals of the RF Ministry for Economic Development and Trade (MEDT) with regards to simplifying the procedure of selling single shares without announcing the price skipping the auction and IPO phases may also be considered as pretty feasible;
- it is desirable to synchronize implementation of proposals from MEDT about simplifying the procedure for privatizing unitary enterprises by way of excluding for some of them mandatory procedure of transformation into a joint-stock company (the smaller businesses criteria are proposed as the threshold) and about simplifying transformation into a joint-stock company during privatization – to avoid situa-

- tions when the process of transformation into a joint-stock company is simplified, but the norms about mandatory transformation of unitary enterprises into joint-stock companies is still in place (if their book value exceeds the minimal charter capital of OJSC [RUR 100 K]). In such case there will be no guarantees that the required level of transparency is assured with regards to certain unitary enterprises;
- the analysis of actual pace of selling federally-owned blocks of shares and of privatizing unitary enterprises has proved that under existing conditions the maximum possible figures of sales and privatization made 500–600 units (for each of the procedures). As a rule, the real number of the blocks of shares sold within a calendar year has always been below the initial projections. Hence the recommendation to reject the practice of multiple adjustment of initial parameters of the Program for selling blocks of shares by way of mechanical inclusion all stakes not sold during the previous year, because the real pace of sales are still within the initial parameters, but the administration challenges grow. It is also very unlikely that stakes of shares not having raised any interest on behalf of the buyers may be then demanded just after several months. It seems that the program of selling the state-owned stakes of shares for the next year should be expanded by way of including the stakes which were not actually offered for sale due to certain technical reasons;
 - including attractive blocks of shares (controlling packages, shares of companies with very good financial-economic situations) into privatization program should be performed very carefully, because of significant risk that having sold the liquid shares the state may remain the owner of non-demanded blocks of shares, which will not create any interest on behalf of business community in the future;
 - the analysis of actual pace of privatization (actually – only of incorporation) of Federal State Unitary Enterprises (FSUEs) and of selling federal blocks of shares arises serious doubts about the feasibility of practice of transforming federal state institutions into joint-stock companies, as it may lead to increase of the burden on certain departments due to the need to assure representation in managing bodies of the newly established JSCs; the probability of quick selling of

their shares is extremely low because of low liquidity of the assets (shares of many institutions just like of the majority of unitary enterprises will become “stock rubbish”); in any case it’s worth postponing the issue of transforming those institutions into joint-stock companies – at least until the moment when significant decrease of the number of FSUEs is achieved;

- the possibility to increase the volume of sales is linked to expanding the circle of sellers, and the conflict between the RF Ministry of State Property and RFPF proved that such action would require some serious amendments to the effective legislation to allow for engaging non-government organizations on a tender basis – but only after several pilot projects are implemented to highlight the “pros” and “cons” of this approach.
- Forming and implementing an adequate system of corporate governance in JSCs with stakes of shares owned by the state – to assure the state’s right for managing, influencing a business entity and exercising adequate control for the process of making and implementing managerial decisions

In principle, this task may be resolved within the existing legal framework with the Federal Law “On Joint-Stock Companies” enacted in 1995 being the core of such system (taking into account its numerous amendments later on). The state as a shareholder is entitled to set issues at BoD or GSM about improving the performance of the respective JSC, increasing its role in management and to seek respective resolutions based on its own stake of shares – either independently or by way of forming alliances with other shareholders in case the state-owned stake is not enough.

However, the state’s ambitions with regards to strengthening its influence based on the state-owned stakes of shares may realistically be implemented into practice only in case adequate normative and regulatory instruments are available inside the respective JSC. That is why the task of building and fine-tuning corporate governance model for such companies requires development, adoption and implementation of State Corporate Behavior Standards based on the effective Code of Corporate Behav-

ior and on a number of standard documents regulating the operations of business entities with state participation.

The first group of documents may include standard sample charters for joint-stock companies and internal regulations (Terms of Reference for General Shareholders Meeting, Board of Directors, for Sole executive Body (managing company), for Audit Committee [General Auditor], Corporate Secretary, for Foundations and Committees with the Board of Directors).

The second group of documents may include standard forms of internal regulations of joint-stock companies with state-owned shares on strategic and scenario planning, budgeting, credit policy, management accounting, business and financial analysis, corporate reporting; as well as documents on the same issues that should direct the power bodies when they exercise their authorities as shareholders.

To implement the corporate governance model for the companies with state participation into practice the following is required:

- state power bodies should initiate and state representatives in JSCs should submit the above mentioned documents for the companies' managing bodies to review and approve (provided the given JSC already has got such internal documents, new versions may be provided);
- state power bodies should initiate through state representatives in JSCs BoDs the work on developing and reviewing annual budget plans for the next fiscal year and mid-term budget plans; the position of the state representative with regards to approving these documents should be preliminary agreed with the respective power bodies.

As for the companies, in which the state is either a majority or a sole complete shareholder, these measures should be viewed as mandatory; in other cases they are strongly recommended, and the state representatives should implement them fully or partially into the practice of functioning companies, in which the state does not have the opportunity for their guaranteed implementation.

In addition to that the state representatives should systematically participate in JSCs managing bodies (including Audit Committees), in auditing their financial/accounting reporting, in completing the forma-

tion and in keeping the Register of JSCs performance indicators, in assuring application of Corporate Behavior Code in the practice of JSCs.

The efforts of the state representatives in JSCs managing bodies together with the dividend policy of the state as a shareholder should become an effective instrument regulating the amount of cash allocated by JSCs for consumption (including top executives compensation); controlling the investment targets with regards to compliance with the JSC strategy and its business profile in general, as well as with the objectives set by the state when fixing its share in the capital; controlling the feasibility of additional assets acquisitions at the open markets (M&A activities) from the point of view of key areas of the state economic policy.

- Dividend Policy

To improve the efficiency of managing JSCs with state participation feasible dividend policy should be developed in each company.

Let us remember that the dividend policy model proposed by the RF MEDT (and prior to it – by the RF Ministry of State Property) stipulates distribution of net profit effectively received by the company according to the following algorithm. After deducting the mandatory payments and charges (including payments to the funds established by this particular company) from the amount of the effectively received profit, a fixed part of profit should be allocated for paying out the dividends. After that investment projects funding at the expense of the net profit is reviewed. The remaining part of net profit should be also allocated for paying out the dividends. When reviewing the investment project a whole set of factors should be taken into account, including their compliance with target economic indicators established for the given JSC (target IRR), economic efficiency of allocating net profit to fund investment projects vs. other purposes, the amount of loans used for funding investment projects in case of insufficient buffer resources.

Overall this approach seems feasible. However, the concerns about weakening the investment potential of JSCs by such dividend policy may be to a certain extent true. Nevertheless, taking into account the entrepreneurial character of JSCs, the deeply rooted in the Russian corporate sector (back from the 90-ies) informal practice of deriving income by way of capturing financial flows through subsidiaries and dummies, the

active dividend policy of the state may be viewed as a positive factor targeted at rehabilitation of corporate governance in general.

In this case dividends in this case are indicating relative financial prosperity of business entities rather than serving just fiscal purposes. Even though fiscal interest of the state towards a lot of companies is obvious, especially – in the fuel-and-energy sector, the dividend payments into the budget may be viewed as auxiliary instrument of collecting the resource rent, of re-distribution of monopoly profit. Of course, to do this, the state as a shareholder needs to exercise active dividend policy, but doing just that won't be sufficient.

- Possible options for the state to manage its assets in business entities

As of today, the main way to manage companies with the state's share in their capital is still through representatives of the state (all of them being government officials).

Using this mechanism is feasible only with regards to a limited number of companies, which operate in the sphere of strategic interests of the state.

At the same time, for most of the JSCs with state participation oriented mostly towards commercial targets the activity of the state representatives does not bring the expected results, because such representatives, on one hand, need to operate within the context of corporate regulation targeted at meeting the dynamic demands of market mechanisms, on the other hand – they are loaded with the need to fulfill their obligations as for their position in the government.

That is why further improvement of the quality of managing JSCs with state participation seems to be most feasible in the following two ways:

- improving the tools for activities of state representatives;
- little by little broadening different options of representing the state's interests at the expense of: (1) expansion of trust management practices, (2) engaging managing companies in playing the sole executive body role in JSCs, and (3) engaging third-party professional directors in managing the state-owned stakes of shares.

In all the cases mentioned above it is necessary to develop and approve (by way of either enacting appropriate legal and regulatory frame-

work or by introducing amendments to effective acts and documents) the incentive mechanism for individuals and legal entities representing the state's interests in business entities with state participation, including approaches to setting performance indicators, the procedure of calculating and paying out bonuses and awards, liability measures for non-performance and failure to achieve the key performance indicators set for such companies.

In the most general terms, the key performance indicators for evaluating the activity of such state representatives (on top of dividend payments to the state budget) may include the dynamics of the market value of state-owned stake of shares (or company capitalization in general), lack of the threat of bankruptcy, and in certain cases – production of certain volumes of goods (work, services) and successful implementation of capital projects.

- Improving functioning of the institute of state's representative

Because the institute of the state representatives, at least in the mid-term perspective, will remain the key functioning instrument of managing the state assets in the corporate sector, some serious improvement of professional qualifications of employees of various departments is required along with increasing their motivation towards honest and high-quality performance against their professional responsibilities. The HR policy of the state becomes more and more important in this context.

The following may be proposed as personnel policy measures:

- developing the mechanism for selecting government officials to represent the state's interests in business entities (a clear set of professional and ethical criteria for appointment);
- special attention is required for selecting the state's representatives to serve on Audit Committees (they need to have special professional skills);
- organize training and professional up-grading of the state's representatives in the sphere of corporate regulation and effective legislation, corporate governance, stock exchange markets, etc.;
- organize regular special certification procedure for government officials representing the state in managing bodies of business entities

(analogous to professional certification of state unitary enterprises directors);

- set limits for representing the state’s interests by one government official simultaneously with regards to a number of companies and timeline;
- switch to representation of the state’s interests in major companies of key importance by government officials for whom this activity becomes the core one, with simultaneous approval of their annual activities programs by the Government (introduction of the authorized state’s representatives institute); in case the state representatives are transferred to professional basis, it will be necessary to develop a standard framework contract for representing the interests of the state for those representatives which are not government officials (agents, attorneys);
- bring the effective framework contract for representing the interests of the state (enacted in 1996) in compliance with the recent legal acts;
- to minimize opportunistic and biased behavior of the state’s representatives their right to independently make decisions on a number of issues (in case there are no instructions on behalf of the government) needs to be cancelled – both for government officials and third-party agents/attorneys, and the limits for independent adjustments to the issued directives need to be set;
- incorporate activities of the state representatives into the general framework of civil service (reflecting their functions in employment contracts, establishing the scale of disciplinary sanctions allowing for imposing financial fines, setting not just the current salary but social guarantees).

Creating the system of incentives for the state representatives in JSCs will require not only stricter requirements for selecting the candidates for representing the state’s interests in BoDs, but also definition of sources to fund their activities.

In principle two sources are possible: (1) effective salaries of government employees with allocation of certain additional payments (bonuses) for conscientious efforts to represent the state’s interests in managing

bodies of JSCs, and (2) compensation for good work from the JSCs themselves.

In case the first type of the funding source is used, then it is better to make special appropriations allocate a separate line-item in the annual budget of the respective department. Significant increase of government officials salaries after the administrative reform has opened some very good opportunity for providing additional incentives to state representatives through various mark-ups, annual performance-based bonuses, etc. A modification of the same option could be using dividends paid by JSCs with state participation to the state budget, so that employees of respective ministries and departments could get a fixed percentage of those – similar to percentage of privatization income received by government property management agencies and by some other organizations within the course of privatization.

In case the second type of the funding source is used, then some amendments to the legislation are required, because effective laws and regulations prohibit the state representatives to receive any cash funds from the business entities they are assigned to. A half-way option could be to set the ceiling for bonuses/awards received by government officials for their activities in JSCs with state participation.

One shouldn't forget about the possibility of using quasi-monetary mechanisms as incentives for government officials. They may include regulating the access to various social benefits at the core job, preferences with regards to future pensions, entering the data about serving at a JSC into a labor record book, etc.

- Other options of managing state assets in business entities

Trust Management

The currently effective mechanism of trust management of the state-owned shares was developed back in 1997, however, it has not been yet widely applied.

To improve this mechanism would mean to establish more detailed criteria for selecting winners of respective tenders, to define the amounts of compensation for the trustees, and to establish details of the trustees' liabilities to the trustor (settler of the trust). Some legal acts need to be ad-

ditionally developed for this purpose to set some standard requirements for the trustees' programs, as well as the mechanisms of monitoring and controlling their activities; the order of paying out the reward and compensating for the expenses also needs to be established. There is also a need to resolve the issue of licensing trust management activities based on the RF Law "On Securities Market" with establishing and organizing the Register of Trustees.

On this basis the practice of applying the trust management mechanism could be expanded with regards to federally-owned blocks of shares of non-strategic JSCs. Such mechanism does not stipulate for the divestment of shares put under trust management during the period the Trust Agreement is valid and upon its expiry provided all the conditions of trust management have been met. In this regards it is necessary to state, that selling shares by way of preliminary putting them under trust management (stipulate by the Privatization Law of 2001) has not yet been legally fixed in respective resolutions by the RF Government, due to which this mechanism cannot be applied during privatization of not only state, but municipal property either. Meanwhile the proposed mechanism could potentially become an additional channel for selling state-owned blocks of shares.

Engaging managing companies in exercising the sole executive bodies functions in JSCs

This opportunity is stipulated by the Federal Law "On Joint-Stock Companies" (item 1 of Article 69). Based on the GSM decision the sole executive bodies functions in the given JSC may be transferred to a commercial company or to an individual entrepreneur (manager) based on the respective contract. This kind of resolution may be adopted at a General Shareholders Meeting only at the Board of Directors' initiative (Supervisory Board) of the respective JSC. With that the law does not require mandatory special majority at the GSM when passing such resolution.

Using this option may be considered feasible when establishing holdings, because in such case the participation of the state in a parent company will allow for influencing subsidiaries and branches having trans-

ferred their management bodies' authorities to this parent company. It is also feasible for resolving immediate tasks of receivership. Another advantage of having such sole managing company could be the fact that the relations with the JSC executive body regulation is beyond the perimeter of Labor Legislation.

To assure adequate legal and regulatory support for such a process a standard agreement for transferring the authority of a sole executive body by JSCs with state participation will be required, so that the state representatives might be based on such an agreement when initiating this process at the managing bodies of JSCs.

Engaging third-party professional directors in managing the state-owned stakes of shares

This option of managing the state-owned stakes of shares may be regarded as a rather new one, because it was not of high demand up till very recently (including private JSCs without state participation). The demand for such third-party professionals was initiated by minority shareholders, whose rights were often violated in the context of struggling for corporate control.

With regards to JSCs with state participation, one may only talk about the government nominating (supporting) a third-party director as one of the candidates to be elected to the Board (Audit Committee). Definitely, in case of nominating such a candidate, the issue of executing the Contract to represent the state's interests and the issue of funding sources will arise again.

Certain guarantees with regards to government-nominated third-party directors (auditors) may be found in cooperation of the state with such self-regulated organizations (CPOs) as Russian Institute of Directors (RID), Association of Independent Directors (AID), Institute of Professional Directors, and Association to Protect the Interests of Shareholders (APIS). Provided a contract is executed with such CPO, this organization could recommend several candidates from its members to be nominated as candidates to managing bodies of JSCs with state participation¹⁹⁵. A

¹⁹⁵ One of the options is to use National Register of Corporate Directors.

separate issue in this case will be the level of responsibilities of CPOs for the professional activities of their members.

External experts could also be engaged to analyzing situations in certain specific companies with state participation, to developing recommendations and directives for government officials representing the state in managing bodies of such companies.

- Management enforcement

In today's environment besides professional up-grading and improvement of incentives for management professionals, the issues of selecting HR potential and of determined preclusion of abuse are also of tremendous importance.

With regards to this issue the following measures are to be considered:

- initiating by government bodies acting on the basis of respective laws and regulations the discussions on early termination of authorities of executive bodies in JSCs with state participation, as well as election of the new executive bodies on the grounds of poor performance identified within the course of audits, facts of assets stripping, of position abuse, using insiders' information, etc.;
- defining the list of threshold (pre-critical) situations when the state representatives are obliged to initiate calling an extraordinary meeting of a JSC executive bodies for pro-active review of problems of further development;
- developing the Register of State Representatives in managing bodies of business entities as a part of a comprehensive database containing full information on each and every person representing the state's interests in managing the assets (relates not only to the state representatives in JSCs and to trustees, but also to state unitary enterprises and institutions directors);
- including the provisions on the state representatives liabilities into legal acts regulating the activities of individuals and legal entities representing the state's interests in managing bodies of the respective business entities (with detailed description of violations and consequent sanctions), including mandatory exclusion of persons previously dismissed from their positions due to bad business practices and unfairness from the state representatives corps;

- standard employment contracts with top executives may become important instruments to implement the state’s policy in JSCs where the state holds a controlling interest or a full (100%) stake of shares may be (in addition to a whole series of standard internal regulatory documents of the company already referred to in the context of forming the corporate governance model); such contracts may stipulate a number of limitations set for state unitary enterprises directors, as well as an additional incentive in the form of a system of options granting the managers the right to acquire shares of the respective company at a discounted price, this becoming more and more relevant in connection with the growing practice of IPO by Russian companies;
- standard employment contracts with top executives should be incorporated into the general scheme of salaries and compensations either for members of collective managing bodies or for those performing as sole executive bodies; such scheme should also set the key performance indicators, the order of calculation and payment of bonuses and awards, liability measures for failure to perform against the assigned functions and to achieve corporate KPIs;
- introduction of a universal norm prescribing mandatory disclosure of personal income/property to state power bodies could become an important mechanism for monitoring/controlling the activities of persons associated with JSCs with government participation; this norm could be applied to state representatives in managing bodies of all categories and to directors of companies with state participation (dependent on the size of a state-owned share);
- special amendments may be introduced into civil and criminal legislation.

Application of various enforcement measures by the state with regards to JSCs with state participation may be objectively based on the outcomes of monitoring, analyzing and planning of business activities of such JSCs (especially those where the state is either a majority or a full shareholder), which in its turn requires development of methods for analyzing and evaluating their performance taking into account the specifics of the given sector of economy.

The system of regular monitoring and analysis of financial-economic situations in JSCs with state participation should be based on analyzing the dynamics of specific company's KPIs, should be also compared with the KPIs of similar companies (at least, with those of the same status) and average industry indicators characterizing the efficiency of managing particular assets. Such benchmarking against the industry-average indicators, which comprise the performance of private companies as well, provides the possibility for unbiased evaluation of the company situation, which then may be used for deciding on the feasibility of assets divestment (including the state-owned blocks of shares).

A very important condition for that is gathering, monitoring and analyzing a massive amount of data with the purpose to calculate the efficiency indicators representative to various groups of companies. Significant deviation of the company's KPIs to a negative side should become the grounds for a set of measures to improve performance and for initiating respective actions by state representatives, including resolving of personnel issues. Performance monitoring and analysis is especially important for the companies operating in non-competitive sectors, where the managers cannot be based on market signals. In such case KPIs of Russian companies can justifiably be benchmarked against the KPIs of similar foreign companies.

Developing a uniform approach in the area of mandatory audits, organization and methodology for Audit Committees (at least, for JSCs with the state's share exceeding 50%) should also provide for improving the quality of managing the state-owned stakes of shares. Switching to electing Audit Committee by cumulative voting could open the opportunities for better effective control over such JSCs.

- Organizing interaction between the state and companies with its participatory interest

In the environment of lack of traditions of alliances with active non-government shareholders, the practice of agreements between government executive agencies and companies with state participation pretty popular in other countries (e.g., targeted contracts in France) could become of special importance in Russia.

Such contracts could be approved by the RF Government on an annual basis simultaneously with the next year budget, assuring compatibility with other areas of government activities with regards to setting the key economic priorities (ensuring sufficient budget revenues and fiscal discipline, products/services pricing and elimination of cross-subsidies, protecting the shareholders' rights and anti-monopoly regulation, productive sector restructuring and investment into its up-grading, forming the demand for capital equipment in the context a leasing schemes, supporting domestic machine-building and R&D funding). Switching to mid-term budgeting has opened significant opportunities in this sphere allowing for execution of agreements with companies in which the state owns shares not just for one-year term, but for longer periods.

Of course, interaction in this format may be efficient only in case the state's interests in the above mentioned companies are represented on a permanent basis (not necessarily by government officials) fixing the obligations in the respective agreements and in the programs of such representatives approved by the government.

- Interaction between the state and other shareholders in the context of common problem of protecting property rights and corporate governance development

Demonstration of best corporate governance practices should become the core objective in interaction between the state and other shareholders in the process of managing mixed property companies. Such best practices should be targeted at:

- increasing the transparency by way of complete information disclosure in compliance with the legislation requirements (especially at execution of major deals and related party transactions, reorganization, participation in M&A activities);
- engaging third-party evaluators for preparation and execution of transactions with the company assets;
- introduction within the company and practical application of liability mechanisms for BoD members, controllers and other officials of JSCs for causing any kind of damage to either JSC or to its specific shareholder;

- improving accounting and reporting systems, including introduction of International Accounting Standards.

The state could use this as a basis for pilot strategic alliances with active non-government shareholders in a number of companies, primarily – in those where the state is not a majority shareholder.

Amendments to the RF Civil Code and to the Federal Law “On Joint-Stock Companies” clarifying the concepts of “shareholder’s loss”, “major deal”, “void deal” and the grounds for nullification of deals could play an important role in harmonizing the relations between the state and other categories of shareholders.

It is also absolutely necessary to expand application of the joint-stock regulations to cover the companies established within the course of state and municipal enterprises privatization, as well as to revise the resolutions of state power bodies at different levels on applying the “Golden Share” Rule assuring the special right of the state to participate in managing joint-stock companies with the purpose to bring them to compliance with the amendments to the legislation and with the changing social-economic environment.

Thorough efforts are required from state power bodies to collect, consolidate and analyze information about corporate conflicts arising in JSCs with state participation, to implement measures allowing for avoidance of such conflicts, including defining the liabilities of the state representative and of heads of power bodies having appointed them for making decisions leading to corporate conflicts.

- Ensuring the required level of transparency in business entities with state participation

The following measures and approaches are required to resolve this kind of task:

- state power bodies’ commitment to achieving the level of transparency and information disclosure in JSCs with state participation similar to the level of public companies with stocks listed at the stock markets;
- public disclosure of information about the outcomes of state representatives’ performance review (including government officials and legal entities representing the state’s interests in the respective JSCs);

- completion of comprehensive classification of business entities with state participation based on criteria of the Concept of State Property Management and Privatization in the RF of 1999 adding the information about distribution of such companies by regions and by the sources of the state-owned shares (transformation into JSCs during privatization, contribution of the state's property into charter capital, provision of budget investment in the exchange for getting a share in the capital, tax arrears or accounts payable restructuring, restitution of the state's property during de-privatization listing specific reasons, acquisition of share through additional issue of stock or at the secondary stock exchange market);
- annual publication of the RF Government, the RF Ministry of State Property and MEDT report about the annual performance of business entities with state participation, including consolidated analysis of their financial-economic situations;
- incorporation of the above-mentioned report into the report on state sector economic performance in general, which should be presented to the Parliament and published for public access;
- serious improvement of the economic and business statistics system by forms of property, organizational-legal forms of business entities of by sectors of the economy; this system should provide adequate information about the scale of the state sector of the economy meaning not just the limits as set in the effective definition of the state sector, but also taking into account the scale of the state's participatory interest in the capital of business entities, sizes of state unitary enterprises, of integrated and holding companies controlled by the state, size of network of subsidiaries, branches and affiliations of the parent companies belonging to the state sector.

6.3. Conclusions

Evaluating the level of practical implementation of the Concept of State Property Management and Privatization in the RF of 1999 with regards to business entities with state participation one may state, that the objectives set forth in this document were only partially achieved (dividends contribution in the non-tax revenues of the federal budget was

raised, institutional changes in the economy were implemented mostly by creating integrated organizations).

At the same time it is obviously premature to speak about G&A costs optimization, about improvement of exercising general government functions by the respective business entities, even though the state anticipated those performing such functions when fixing its share in the capitals of those companies. It is also too early to evaluate positive changes in key indicators of financial and economic performance of those companies, as well as mechanisms of incentives for production growth and for attracting investment. The control mechanisms with regards to JSCs with state participation and with regards to engaged managers has some very serious drawbacks. The evaluation of reasons for inefficiency of the system of managing the state-owned stakes of shares included into Concept-1999 is still to a great extent relevant. Even though the process of the Concept implementation grew active starting from 2000, some very important issues remain open, such as incentives for state representatives, decision-making principles, performance evaluation criteria, assuring the necessary transparency of the whole process. Management mechanism and decisions offered by Concept-1999 with regards to business entities with state participation were not to a full extent demanded in practice.

In the near future the significant number of business entities with state participation will remain and their value in Russian economy will continue to be pretty serious – all this emphasizes the urgent need for comprehensive improvement of the system of managing such companies.

It is feasible to exercise such improvement in the following areas:

- restructure the portfolio of state-owned shares based on various sectors development concepts substantiating the objectives and tasks of state participation aligned with the structural policy, with plans to reform certain industries, with the authorities of respective departments on preparation for privatization of state-owned blocks of shares (participatory interest) in the business entities, the operations of which do not provide for achieving the objectives set by the state when fixing its shares in their capitals – based on the objectives of the state in the given sector/industry and on its legally established authorities;

- improve the privatization tools as the means for solving the set objectives with the focus on selling blocks of shares not achieving the size of control package;
- forming and introducing the adequate corporate governance system in JSCs with state-owned shares, allowing for the right of the state to participate in managing activities, to influence the business entity and to monitor/control the decision-making and decision-implementing process (develop, adopt and implement Corporate Behavioral Standards based on the effective Corporate Behavior Code and on a number of standard internal documents regulating the activities of business entities with state participation);
- consistent implementation of the dividend policy based on the agreed approaches and on methodology for defining the position of the Russian Federation as a shareholder in a JSC with regards to dividends payment issues;
- improving the organization and operations of state representatives institution (develop the mechanism for selecting appropriate government officials for representing the state's interests in JSCs; organize training and professional up-grading for state representatives; organize regular special certification of government officials representing the state's interests in JSCs; switch to representation of the state's interests in major companies of key importance by government officials for whom this activity becomes the core one; resolve the problem of assuring incentives for state representatives);
- expand the sphere of applying different mechanisms of managing the state's assets in business entities (on top of the institution of state representatives), such as trust management, engaging managing companies and third-party professional directors – with preceding development of the appropriate legal framework;
- assure management enforcement target at selecting HR potential and determined preclusion of abuse (early termination of authorities of executive bodies in JSCs with state participation, as well as election of the new executive bodies on the grounds of poor performance; defining the list of threshold (pre-critical) situations when the state representatives are obliged to initiate calling an extraordinary meeting of

- a JSC executive bodies for pro-active review of problems; developing the Register of State Representatives in managing bodies of business entities, etc.);
- organizing appropriate interaction between the state and companies with state participation by way of executing respective agreements;
 - build the system of interaction between the state and other categories of shareholders in the process of managing mixed-property companies on the basis of best corporate governance practices (improving transparency through complete information disclosure; introduction and practical implementation inside a JSC the mechanisms of liabilities of BoD members controlling bodies and other for causing loss/damage to a JSC or to a shareholder; improving accounting reporting systems including IAS implementation; introducing amendments to the legislation to clarify such concepts as “shareholder’s loss”, “major deal”, “void transaction” as well as the criteria for nullifying transactions; revise the decisions made by power bodies of different levels with regards to applying the “Golden Share” Rule providing the state with the right to manage JSCs to assure compliance with recent amendments to the legislation and changes in social-economic environment);
 - assuring the appropriate transparency level in business entities with state participation (public disclosure of information about the outcomes of state representatives’ performance review [including government officials and legal entities representing the state’s interests in the respective JSCs]; completion of comprehensive classification of business entities with state participation; annual publication of the RF Government, the RF Ministry of State Property and MEDT report about the annual performance of business entities with state participation; serious improvement of the economic and business statistics system).

7. Final Conclusion

1. Analyzing the government's policy in the sphere of managing state-owned stakes of shares in Russian corporate sector at the federal level during the last 8 years after approving the Concept of State Property Management and Privatization leads to the following conclusions:

- The relevancy of all measures undertaken starting from 1999 to improve managing mixed-property JSCs is indubitable; however, they were all late by at least 3–4 years. The period right after completion mass-scale privatization back in 1994–1995 was obviously the most appropriate time for all these measures.
- The time between the adoption of the Concept of State Property Management and Privatization in the RF in 1999 and today is quite sufficient to state certain improvement of the situation in this sphere. In particular, both absolute and relative growth of budget revenues from state-owned blocks of shares is a solid evidence.
- The following trends were observed in the dynamics of the amount and structure of business entities with state participation over the last 8 years:
 - there was no decrease in the number of business entities with state participation;
 - at the same time the scale of current application and coverage of such instrument for controlling the state assets as the special “Golden Share” Rule decreased, just like the level of state participation in business entities other than OJSC;
 - in 2005–2006 the relative number of business entities with the state owning over 50% interest has increased significantly – at the expense of growth of companies with 100% of shares owned by the state due to broad application of procedures of transforming state unitary enterprises into JSCs;
 - as a result, by 2006 the state owned more than half of the capital in 44% of all business entities with state participation (vs. 25% in 1999), which significantly broadens the opportunity of full-scale majority control;

- at the same time, substantial share of business entities with the state owning minority packages remained at the same level, while the share of business entities with the state owning controlling interest decreased, which may be evaluated as a negative factor as it weakens the opportunities for both the state as a shareholder and potential buyer due to low liquidity of minority stakes;
- the profile of federally-owned blocks of shares as of mid-2006 is approximately the same as estimated by the RF Ministry of State Property for the period after implementing 2003 Privatization Program;
- in 2003–2005 it was possible to increase the sales of federally-owned blocks of shares within the framework of privatization; however, the real number of blocks of shares per calendar year was always less than preliminary estimations, not to mention upwardly adjusted plans;
- in the structure of sales of federally-owned blocks of shares the share of stakes sold by way of new privatization mechanisms (IPO and unannounced sales) increased; the share of minority, controlling and full stakes in the overall number of the sold stakes of shares increased with simultaneous decrease of the blocking stakes.
- Legal and regulatory framework was substantially amended:
 - the regulation of state representatives' activities in mixed-property companies strengthened significantly vs. 1990-ies, opportunities for their arbitrary and biased actions deviating from government requirements were decreased;
 - legislative gaps (between privatization and bankruptcy laws) were closed;
 - the fact of at least 3 lists of companies (special, strategic and those with exclusive insolvency treatment) with different levels of state assets control (business entities and state unitary enterprises) subject to the state regulation means, in essence, the beginning of creating a new legal framework for the enterprises comprising the core of the state sector of the economy.

- Effective practice of managing state assets in the corporate sector was not significantly changed vs. 1990-ies:
 - the institute of state representatives (government officials employed by various departments) in managing bodies of business entities with state participation is still the key instrument for managing state-owned stakes of shares;
 - the policy of state assets integration by way of creating holding companies received its further development; however, its focus was shifted from fuel-and-energy complex in 1990-ies towards defense industry and a number of other industries producing goods for domestic consumption; in this context launching of natural monopolies restructuring has become distinguishable step in the economic development of the Russian Federation;
 - the key executives of many of such companies were replaced with new people, including state representatives in their managing bodies (in addition to government officials the President's Administration representatives are currently occupying important positions);
 - state representatives in mixed capital companies became more active, which often led to corporate conflicts between different groups of shareholders; similar conflicts also accompanied the process of setting-up holding companies and other integrated organizations on the basis of consolidating the state's assets; however, often enough these conflicts in their essence were based on confrontation of different government executive agencies rather than conflicts with private shareholders.
- With regards to realization of the state's right for receiving dividends from participation in various joint-stock companies, the following should be stated:
 - significant increase of dividend payments to the federal budget was achieved; in 2006 such payments grew more than 17 times vs. 1999, which is within the streamline of Russian corporate sector trends;
 - the key role in assuring dividend payments belongs to fuel-and-energy complex and to JSCs with more than 25% of shares

- owned by the state; the trend shows that with increasing the size of the state-owned stake of shares amounts of dividend payments into the budget also increased, as the number of companies paying out the dividends;
- the level of concentration of dividend payments was very high: in 2001–2004 at least 80% of payments were covered by 10 companies;
 - despite the most recent positive changes in dividend policy, there is still very high potential with regards to payments into the budget, which is confirmed by the outcomes of proactive audits.
- Administrative reform started to significantly impact the process of managing mixed capital companies;
 - the RF Ministry for Economic Development and Trade became the new subject of property policy with regards to enterprises of the state sector of the economy; MEDT is qualified to perform as an arbitrator between the RF Ministry of State Property and executive agencies in various sectors and to submit initiatives and proposals to the RF Government on many issues of managing business entities with state participation;
 - the efforts on optimizing the network of organizations subordinate to federal power bodies broaden the potential field of state property in the corporate sector, taking into account that not only unitary enterprises, but institutions as well, may be transformed into joint-stock companies;
 - the conflict between the RF Ministry of State Property and RFPF being a consequence of unresolved issue of possible expansion of federal property seriously slowed down the privatization process, including selling of federally-owned blocks of shares.
 - During the last year visible expansion of companies with state participation is taking place in a number of industries, while the trend for establishing integrated organizations by way of consolidating state-owned assets is preserved. However, implementation of such projects and creation of integrated organizations in defense industry is rather problematic (as has been demonstrated by unsuccessful attempt to merge Gazprom and Rosneft).

2. Thus, despite the fact that management of federally-owned shares in joint-stock companies is to a great extent regulated, the control targets of improving management of mixed capital companies as they were set by Concept-1999 were only partially achieved.

One of the success stories is increasing the amount of dividend payments into the budget and assuring relative comprehensiveness of the Register of blocks of shares. At the same time the attempt to decrease the overall number of federally-owned blocks of shares failed; the number of minority (up to 25% capital) blocks of shares grew significantly vs. 1999, just like their share in the federally-owned blocks of shares. Even though the controlling mechanisms in JSCs with government participation function more or less sufficiently, personal motivation and controls of their managers are very weak.

3. The following issues of improving management of business entities with state participation may be regarded as the most relevant:

- consistent implementation of the course towards gradual selling of state-owned minority blocks of shares, which do not allow for state influence of these companies;
- formulating the objectives of state participation in managing business entities aligned with the overall scheme of administrative reform;
- development of dividend policy allowing for more non-tax budget revenues from this particular source and for reproduction of capital assets of the mentioned business entities with the purpose of high-quality performance of functions, which the state assigned to these companies when preserving that or another form of assets control;
- simplifying the procedure of managerial decision-making with regards to business entities, which do not constitute special importance for the state;
- resolving the problem of motivation and incentives for state representatives in managing bodies of business entities with simultaneous introduction of mandatory mechanisms for evaluating their performance and for selecting appropriate human resources;
- gradual engagement of private business managers in the process of managing business entities with state participation on the basis of trust management arrangements, engaging management companies,

alliances with active non-government shareholders, appointment of professional directors;

- talking about interdependency of state participation in business entities and structure policy, the following factors are of crucial importance: 1) forming integrated organizations of holding type to improve competitiveness; and 2) possible implementation of investment projects by way of granting budget funds in exchange of the share in the capital of newly established companies.

Detailed regulation of activities of state representatives in mixed property companies based on comprehensive measures just like other requirements of the state towards companies with its participation do not guarantee automatic radical improvement of the situation with managing mixed property companies.

In the conditions of developed market economy the immanent drawbacks of state property stipulate the that companies with mixed capital are falling behind more efficient private sector. However, in the conditions of Russian transitional economy, where many already privatized enterprises fail to demonstrate expected efficiency and best practices of management by their new owners, implementation of the state's interests (besides the objective of non-tax budget revenues and structure policy implementation) is capable of providing a positive impulse for improving corporate governance in general based on consistent abiding by the spirit and the letter of law.

It is impossible to implement the state's impact on the economy, first of all, by way of expanding legal norms and procedures through major national corporations with state participation, significant economic value and big number of subsidiaries; secondly, by way of indirect impact on formation of the overall legal framework for JSC activities.

From the point of view of assuring efficient performance, state participation in the economy with regards to property relations needs to be brought in compliance with real, pretty modest managerial capacities of the government.

As a result, the government priorities should be focused on the efforts to optimize the profile of already existing state assets, to improve the efficiency of managing already operating state-owned companies by way of

defining their position in the system of government priorities, to assure transparency of cash flows, to disseminate the best practices and corporate governance standards, to limit non-core acquisitions, to approach more carefully the issue of which decisions need to be approved by government agencies, to assure participation of state-owned companies at M&A markets.

As for further promulgation of institutional reform in the sphere of property relations, in the context of today's realities it is connected not only with implementation of annual privatization programs, but with the process of reforming natural monopolies, primarily – in electric power industry and in railway transport with regards to achieving positive results from attracting outside investors (including private ones) to highly competitive market segments and from expanding the activities of independent generators (carriers).

It is impossible to achieve all the above mentioned objectives without elimination of narrow group interests (private or public). In practice it may be implemented only through special laws and other normative documents addressing not only changes in managing state-owned shares in JSCs and other mixed property companies, but also development and adoption of the Structural and Industrial Policies, and reforming the overall system of government service. Contracts with state representatives and with trustees need to reflect the whole set of managerial effects, development and implementation of the system for achieving agreement between all state power bodies and government agencies. Obviously, sufficient political will is needed for creating transparent and strict controls and responsibility mechanisms, as well as for protecting it from criminal and lobbying elements.

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Appendix

Evaluation of the Extent of Implementing the Concept of State Property Management and Privatization in the RF of 1999

Measures	Degree of Implementation
<i>Classification of business entities by quantitative and qualitative indicators</i>	
- based on the level of liquidity of shares, including: (1) providing for quick remittance of significant cash amounts to the state budget upon selling the shares; (2) shares which will not bring substantial income to the budget; (3) shares impossible (or unfeasible) to sell under the legally established conditions	information n/a
- based on industry in which the company operates	done
- based on the objectives of the state in the activities of business entities, including: (1) strategic ones for implementation of state objectives (defense, security), (2) ones included into social programs, (3) ones implementing high potential projects, (4) natural monopolies	partially implemented: list of strategic JSCs approved in 2004
- based on the possibility for influencing the activities of business entities and partnerships depending on the number of shares (the number of votes in managing bodies of the respective companies)	done
- based on financial status of the company with state participation: (1) ones with financial stability; (2) ones with bankruptcy risks (arrears exceeding 3 months, arrears to federal budget and extra-budgetary funds, or salary arrears); (3) ones subject to bankruptcy litigation	information n/a
- based on headcount and size of capital assets	information n/a
<i>Exercising general government functions when managing federally-owned shares</i>	
- coordination of activities of ministries and departments in the process of managing stakes of shares by a federal agency for state property management	was in the process of implementation, though in an insufficient scale
- establishing the order and conducting certifica-	wasn't implemented

Measures	Degree of Implementation
tion of specialists in the sphere of managing business entities	
- appointing state representatives to managing bodies of OJSCs with federally-owned shares selecting them from industry professionals of federal bodies of executive power, the RF Ministry of State Property, as well as executive power bodies of the RF subjects, in the territory of which the respective OJSCs are located	was in the process of implementation
- assuring the RF interests in managing bodies of the most major joint-stock companies producing goods/services of strategic importance for national security, as a rule – through government officials on a permanent basis	wasn't implemented
- issuing written voting instructions by the RF Ministry of State Property to state representatives in OJSCs with federally-owned shares – in coordination and agreement with line ministries and departments	was in the process of implementation
- allocating at least 10% of dividends paid into the budget for the RF Ministry of State Property and line ministries and departments to finance expenses associated with managing federally-owned shares. At least have of the allocated amount should go to line ministries and departments	allocations were made from the federal budget to fund management of state-owned shares in OJSCs (irrespective of the amount of dividends on federally-owned shares)
- establishing the order of using blocks of shares as guarantees on behalf of the Russian Federation accounting for those guarantees as government debt backed by state assets versus federal budget revenues	information n/a
- consolidation of blocks of shares of JSCs operating in similar areas or having similar objectives	was in the process of implementation fin the context of forming integrated organizations
- acquisition of shares in JSCs with state participation to enhance such participation in case this is required to resolve general state functions and provided the necessary resources are in place	until 2004 – single instances, later – within the framework of growing activity of JSCs with state participation at M&A markets
- establishing the mechanism for maintaining the size of state-owned stake of shares (charter capital participation) during additional issue of shares	2006 amendments into federal laws on privatization and on joint-stock companies regulating the order of decreasing the state's share
- replacing federally-owned stakes of shares	information n/a

Measures	Degree of Implementation
<p>with the special “Golden Share” Rule</p> <ul style="list-style-type: none"> - undertaking measures to review business entities’ charters to assure protection of the state’s interests 	<p>was in the process of implementation, though in an insufficient scale</p>
<p><i>Measures targeted at increasing non-tax budget with regards to JSCs operating in highly-profitable industries, making sellable products, having got stable financial situation and not requiring significant capex</i></p>	
<ul style="list-style-type: none"> - passing shares to the RF subjects to offset financial obligations of the federal government provided the regions present their enterprises development programs 	<p>single instances (information about regions providing development programs is n/a)</p>
<ul style="list-style-type: none"> - acquisition of shares for consolidating them into stakes with the purpose of further selling with the highest budget revenues 	<p>information n/a</p>
<ul style="list-style-type: none"> - issuing and selling derivative securities backed by shares 	<p>information n/a</p>
<ul style="list-style-type: none"> - issuing derivative securities providing the right to acquire shares upon a certain period of time with simultaneous transfer of the above mentioned shares under trust management of derivatives buyer 	<p>information n/a</p>
<ul style="list-style-type: none"> - selling shares upon pre-sale treatment and rehabilitation of joint-stock companies; 	<p>information n/a</p>
<ul style="list-style-type: none"> - exit from partnerships and LLCs with receiving the effective share calculated based on net assets of the company 	<p>was in the process of implementation within the context of privatization programs</p>
<p><i>Attracting investment into real sector of economy and supporting domestic manufacturers</i></p>	
<ul style="list-style-type: none"> - using state-owned shares for securing investment or loans allocated for special target projects 	<p>information n/a</p>
<p>using state-owned shares to attract investment into vertically-integrated organizations (shares contributed to the charter capital of an integrated company will become the security)</p>	<p>information n/a</p>
<ul style="list-style-type: none"> - engaging efficient owner, acquiring shares within privatization process under conditions of investing them into the company’s activities 	<p>was in the process of implementation within the context of privatization programs</p>
<ul style="list-style-type: none"> - improving investment attractiveness of enterprises for domestic and foreign investors by decreasing the state’s share in their charter capitals 	<p>was in the process of implementation within the context of privatization programs, amendments to Federal Laws on Privatization and on Joint-Stock Companies of 2006 regulating the proce-</p>

Measures	Degree of Implementation
<ul style="list-style-type: none"> - acquisition of shares by the state resulting from capitalization of tax arrears with further selling of these shares or putting them under trust management 	<p>degree of decreasing the size of the state's share</p> <p>single instances without putting under trust management</p>
<i>G&A costs optimization</i>	
<ul style="list-style-type: none"> - decreasing the number of federally-owned blocks of shares down to the level allowing to implement regulating and controlling functions of the state – by way of selling shares, their consolidation into vertically-integrated organizations with similar technologies or markets, as well as by transferring shares to regional or municipal level 	<p>was in the process of implementation within the context of privatization programs (deviation from the plan – over 2 years behind)</p>
<ul style="list-style-type: none"> - contributing minor blocks of shares to charter capital of the companies established similar to “portfolio funds” provided the decision with regards to selling these blocks has already been made, but no actual sale took place. Such company will receive a certain degree of freedom provided the controllers are in place (Supervisory Board, Board of trustees) 	<p>information n/a</p>
<ul style="list-style-type: none"> - selling minor non-liquid blocks of shares with their further buy-out at market value defined according to the Federal Laws “On Joint-Stock Companies” and “On Evaluation Activities in the Russian Federation” 	<p>information n/a</p>
<ul style="list-style-type: none"> - selling minor non-liquid blocks of shares to JSC employees at nominal value in case of impossibility to sell those stakes at an auction 	<p>information n/a</p>
<i>Institutional changes in the economy</i>	
<ul style="list-style-type: none"> - forming vertically-integrated organizations 	<p>implementation already started on a broad scale, serious plans for mid-term perspective</p>
<ul style="list-style-type: none"> - facilitating of decision-making with regards to restructuring or bankruptcy of enterprises with significant arrears to the state budget – on the initiative of the owners with the purpose to capitalize the arrears into liquid shares of newly established through re-organization clean efficient companies 	<p>single instances</p>
<ul style="list-style-type: none"> - restructuring major enterprises with delineation of assets required for the state to implement 	<p>single instances</p>

Measures	Degree of Implementation
its general functions with further creation on this basis 100% state-owned JSC and selling the remaining assets to either develop new production or to diversify the existing one	
- acquisition and further selling of shares in exchange for the land plots contributed into charter capital of joint-stock companies	single instances without selling shares