



## Russian Federation<sup>\*1</sup>

– Dmitriy Yanin<sup>†</sup>

The Russian Federation is the largest country in the world, spanning 11 time zones. The landscape varies widely, from vast open tracts in the European heartlands and the Taiga and Tundra of Siberia, to mountainous terrain. Agriculture is largely confined to the European regions and the Southern belt of Siberia. Further North, the main industries are forestry and extraction of energy and minerals. The main communications across the country are by air, and the Trans-Siberian railway. The road system is not well developed countrywide. Russia's great rivers also play an important part in transportation as well as in hydroelectric power generation.

In September 1988, Russia became the first Soviet Republic, outside the Baltic, to declare its national sovereignty. This was recognised by Moscow in 1991, following the collapse of the former Soviet Union, of which it had formed a part since 1922. Like the Soviet Union before it, the Russian Federation is a collection of diverse territories at vastly different stages of development.

### Economy

After the collapse of the Russian economy in 1998, the IMF provided US\$22.5bn in a largely unsuccessful attempt to bring stability in the country. In August 1998, the Russian Government announced a devaluation of the rouble, debt defaults and a bank bailout. The reforms boosted Russia's trade competitiveness, whilst high prices for oil and gas (the country's two main exports) saw GDP rise after plunging in the early 1990s. In 2002, some western private-equity investors began returning to Russia.

Growth was strong in 2002 and 2003, but Russia's economy is heavily dependent on oil, and much of its assets are controlled by a handful of oligarchs. Infrastructure desperately needs investment; the financial system needs reform; small-business owners face huge hurdles; and Russia's power industry is close to crisis. Nonetheless, the President, Vladimir Putin, who wants more economic

PROFILE	
Population:	143.4 million ***
GDP (Current US\$):	432.9 billion***
Per Capita Income: (Current US\$)	2,610 (Atlas method)*** 8,230 (at PPP)**
Surface Area:	17.1 million sq. km
Life Expectancy:	66.7 years **
Literacy (%):	99.6 (of ages 15 and above)**
HDI Rank:	57***
Sources:	
- World Development Indicators Database, World Bank, 2004	
- Human Development Report Statistics, UNDP, 2004	
(**) For the year 2002	
(***) For the year 2003	

reform, has done a good job managing Russia's (shrinking) foreign debt. The United States of America designated Russia a market economy, and the EU dropped its long-standing objections to Russia joining the WTO, both of which should ease Russia's path to the membership in the near future.

The economy is dominated by large industrial enterprises, with SMEs, which have acted as an important source of growth in other transition economies, remaining underdeveloped. SMEs account for only 10-15 percent of Russian GDP, compared with typically 50 percent or more in developed market economies and the more advanced transition countries. Small enterprises and start-ups in Russia are held back by stifling taxes and regulations, as well as the strong position of incumbent industrial enterprises, which often exploit their ties to the local bureaucracy to keep weaker competitors at bay.

### Competition Evolution and Environment

In 1990, the first Russian competition authority was created – the Ministry for Antimonopoly Policy and the Support

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† Comments received from Andrei Tzyganov, Deputy Head, Federal Antimonopoly Service

of New Economic Structures (herein after referred to as the MAP) – and the Law “On Competition and the Restriction of Monopolistic Activity on Goods Markets”, (hereinafter referred to as the Law on Competition) was passed in 1991. Support for competition was also expressed in the 1993 Constitution, as well as in other fundamental legislations, for example the Civil Code 1994.

The Law on Competition then contained relatively mild sanctions for most violations, preferring cease and desist orders and disgorgement of improperly received income to direct fines or the punishment of individuals. This was consistent with expectations that the worst potential problems would be controlled by regulation and also reflected fairness concerns about the complete unfamiliarity of competition law concepts and a desire to allow the new rules to become known before severe sanctions were applied.

A long history of planning and coordination, as well as a lack of familiarity with methods used to govern and regulate markets, led to expectations that state bodies of various kinds would attempt to continue to control economic activity. To counter this, the Law on Competition included provisions prohibiting such behaviour. Likewise, the expectation of a need to divide large enterprises or associations was reflected in the inclusion of an article specifically authorising such division after repeated violation of the law.

The early creation of a competition authority contributed to the creation of the necessary environment for competitive markets, both through enforcement actions and through participation in policy formation and legislative drafting efforts. These include a substantial reduction of direct barriers to the movement of goods and services within the country, and the creation of basic legislative frameworks for consumer protection, advertising regulation and other tasks that are necessary to allow markets to function in a reasonable manner.

The then competition authority also played a central role in regulatory reform efforts directed at natural monopoly sectors. It led the initial drafting effort for the law on natural monopolies.

However, some serious structural and legal problems have interfered with the ability of the Russian competition authority to be efficient in its enforcement efforts and to undertake focused competition advocacy.

In 2003, the OECD undertook a detailed assessment of Russia’s decade of experience with competition law and policy. The assessment report concludes that, despite early legislation on the issue and strong expressions of support for competition in the laws, the creation and protection of

competition on domestic markets has not been a policy priority of Russia. Emphasis on rapid privatisation limited the scope of pre-privatisation restructuring to promote competition, and the competition authority has been expected to serve as a general regulator of behaviour in markets; assigned to fill legislative gaps and to enforce against a variety of undesirable practices in markets. Overly broad responsibilities and a lack of credible sanctions have significantly limited the impact of the competition laws<sup>2</sup>.

The initial conception of the competition authority, as broadly responsible for civilising markets, as well as protecting public interest and weaker parties, resulted in task overload, with duties in the areas of consumer protection; advertising regulation; supervision of commodity exchanges; and protection of small business. All these areas require different skill sets and procedures, limiting the effectiveness of the agency. This has been aggravated by the regular addition of enforcement responsibilities under the rubric of competition law.

The substantive competition law, whilst relatively complete in terms of its areas of coverage, does not provide the competition authority with the tools needed to be effective. First, it does not contain credible sanctions. For even the most serious and damaging violations of the competition law, the consequences to a violator are minimal – usually limited to a ‘cease and desist’ order.

Substantive fines are so modest as to have little or no deterrent effect, and are available only for a failure to observe an order or to file required information. Whilst the law provides for criminal sanctions, they have never been applied. Second, the Law fails to provide the competition authority with sufficient investigative powers.

Procedures for obtaining information are cumbersome and rely primarily on written requests. A minor administrative fine and a repeated request are the sole consequences of failure to comply with requests for information. The competition authority cannot compel testimony whilst searches of premises are in theory possible, with the cooperation of local law enforcement, but are in practice complicated and rarely occur.

From a competition perspective, the wave of M&As that has swept through the Russian economy, since 1999, is a cause for concern. Large enterprises have used windfall profits, from high international oil and metal prices, to purchase undervalued manufacturing assets, for example in the automotive sector. Since many of them were badly run by their incumbent managers, even limited improvements led to rapid rises in productivity growth.

Their integration into large industrial conglomerates also provided access to much-needed investment capital, which

2 Based on OECD (2004), Competition Law and Policy in the Russian Federation, Policy Brief, Paris 2004

is still not provided by Russia's ill-functioning banking sector. By 2002, the acquisition wave had moved beyond the industrial sector, with conglomerates buying into insurance, retail and agriculture. Ownership structures are opaque, but according to some estimates, 20 large conglomerates now account for up to 70 percent of Russian GDP.

Many amendments to the Law on Competition were adopted in 2002. The amendments were adopted to tighten the control over anticompetitive agreements, and make the detection and proof of their existence more effective. For example, the Law now imposes a direct ban on the conclusion of agreements between competitors, irrespective of their position in the market, if the implementation of those agreements could lead to the establishment of price (fixing), discounts, mark-ups surcharges, the splitting up of markets along geographical lines or a refusal to enter into agreements with particular vendors or buyers.

In 2004, by a Decree of the President of the Russian Federation "About the system and structure of federal executive power bodies", the Ministry for Antimonopoly Policy and the Support of New Economic Structures (MAP) was abolished. Instead, a Federal Antimonopoly Service (FAS) was established, which inherited the functions of the abolished State Committee, excluding the duties on state support of small business and consumer rights protection.

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## Regulatory Framework

### *Electricity Sector*<sup>3</sup>

Russia, in 2003, embarked on the restructuring of its electricity sector. The reform introduced competition into electricity production and supply. It, however, left dispatch, transmission and distribution as regulated natural monopolies with non-discriminatory third-party access to the networks. This is built on recent experience in the OECD and other countries.

The ultimate aim of the reform is to ensure that supply continues to meet the growing demand by creating

conditions for encouraging both investment in new capacity, and greater efficiency of both production and consumption. This will allow prices to rise to fully cost-reflective levels, ending cross subsidies, and allowing markets to operate where possible.

Broadly speaking, Russia's electricity reform strategy reflects an approach to utility restructuring similar to that implemented in many other countries over the last decade or two. Its core elements include:

- breaking up the vertically integrated monopoly of production, transmission and distribution, and separating the potentially contestable activities from those that have a substantial element of natural monopoly;
- introducing competition into those activities where it is feasible, such as generation and supply; and
- setting regulated tariffs for transmission and distribution, which are natural monopolies, in such a way as to encourage efficiency and not merely cover costs.

### *Telecommunications Sector*<sup>4</sup>

The most important measure to improve the telecom sector's state regulation in Russia has been the adoption of a new version of the *Communications Law*. This law is compliant with the requirements of the WTO; relevant EU directives; recommendations of the OECD and the International Telecommunications Union (ITU), specifically as regards the proposed universal service mechanism.

It is also significant that the Law stipulates that telecom operators shall be reimbursed for economically feasible costs and, given the feasible rate of return on capital applicable to the provisioning of services, if the tariffs on these services are set by the State. Nonetheless, State regulation still does not provide equal conditions for all market participants and does not cope with the problems of distributing the social load, cross-subsidisation and non-efficiency of tariff regulation. All this allows alternative operators to expand at the expense of incumbents.

### *Anticompetitive Business Practices*

In Russia, anticompetitive agreements are generally found in sectors characterised by a high degree of concentration of capital and production capacity, which include natural monopolies.

Until 2002, the provisions of the competition law appeared to make any action, which violated the rights of an entrepreneur or enterprise, a violation, even if there was no effect on competition as a result of the violation. The amendments to the Law made in 2002 appeared to resolve this problem, making requirements for an infringement of rights and a restriction of competition cumulative.

3 [http://www.oecd.org/document/27/0,2340,en\\_2649\\_201185\\_32473755\\_1\\_1\\_1\\_1,00.html](http://www.oecd.org/document/27/0,2340,en_2649_201185_32473755_1_1_1_1,00.html)

4 [http://eng.svyazinvest.ru/telecom\\_industry\\_overview/#3](http://eng.svyazinvest.ru/telecom_industry_overview/#3)

**Box 28.1: Combining Competition and Consumer Protection with Regard to Natural Monopolies<sup>5</sup>**

- An energy provider made a habit of turning off hot water supplies to entire buildings, if any of the customers in the building had not paid the bill; or where they had paid but the housing authority had not transferred the payment to the company. The territorial office of the MAP opened a case, based on the abuse of dominance provisions of the Law on Competition and the provisions of the Consumer Protection Law, and ordered the practice stopped. It also mandated that a statement be published in the papers, informing consumers about their rights.
- A city water provider included, in its contracts for water connection to private houses, a term requiring ‘voluntary participation in shared contribution to development of water system infrastructure’, which was intended to cover costs incurred in laying new pipes, not covered by regulated tariffs. MAP’s territorial office found both an abuse of dominant position and a violation of the Consumer Protection Law. The water company appealed and MAP’s decision was reversed by the Court, on the grounds that the term was not within those regulated, and the parties had the right to agree on whether or not to include such issues, so should conduct negotiations. The Appeal and Cassation Courts reversed the ruling of the Court of First Instance, and agreed with MAP that the term was abusive and was being forced on the customers.

Source: MAP June 2003; MAP Website

**Consumer Protection**

Consumer protection is promoted in Russia, primarily, by the Inter-republican Confederation of Consumers Societies (KonfOP), in cooperation with the MAP, the Ministry of Justice, and a number of other ministries and agencies. KonfOP is a union of national and regional consumer organisations from six CIS countries. Presently, there are 43 member-organisations. KonfOP was set up in 1989, as the Federation of Consumer Societies of USSR, then in 1991, reorganised into a Confederation. KonfOP operates mainly in the following areas:

**Legal Protection of Consumers and Preparation of Law Initiatives**

KonfOP specialists helped prepare the following Laws of the Russian Federation:

- Law on Consumer Protection;

- Law on Advertisement;
- Law on Competition;
- Law on Natural Monopolies; and
- Law on Pharmaceutical Goods and Civil Code.

Since 1992, KonfOP lawyers have won or successfully settled several thousand lawsuits for the protection of individual consumers and an ‘indefinite circle of persons’.

These cases include:

- the first ever Russian lawsuit concerning moral hazard;
- suits against large manufacturers of electronic appliances (Sony, Samsung, Matsushita/Panasonic), for changing the conditions of post-sale service;
- a suit against the Government of Moscow for unlawful evacuation of wrongly parked vehicles, which resulted in the abolition of the relevant Government Decree and amendments to the Administrative Law;
- suits defending the rights of depositors to commercial banks; and
- suits relating to tourism services, housing law, and advertising of pharmaceuticals, amongst others.

**Concluding Observations and Future Scenario**

Shortly after the 2003 assessment report of the OECD was issued, the Russian Government undertook a fundamental restructuring of federal executive bodies that included the creation of the FAS, which has a narrowed focus. The passage of a new competition law has been identified as a priority for the near future, and work on the law is in progress.

However, in order for the new competition authority of Russia to respond effectively to the most serious competition problems, and to meet the challenges of enforcement in newly deregulated sectors of the economy, these problems must be addressed in the design of the new body (FAS) and in the provisions of the new competition law.

**Key Priorities in Drafting the New Competition Law should be:**

- Provision of credible sanctions against violators, e.g. substantial fines, high enough to provide a serious deterrence, possibly using the percentage of turnover measure in use in some jurisdictions;
- Substantially reducing merger control submissions, strengthening economic analysis and structural remedies;
- Increasing the threshold for merger submissions would reduce numbers, allowing more time for the analysis of those that are of greatest concern;
- Focusing state action provisions on conduct that restricts competition, rather than any conduct affecting an entrepreneur or enterprise; and
- Creating clear legal standards for agreements, and priority enforcement against restrictive agreements.

5 OECD Peer Review on Russia’s Competition Law and Policy

***The New Federal Antimonopoly Service (FAS) Can Be Made Effective by:***

- Increasing its investigative powers;
- Reducing the danger that incriminating evidence is destroyed before FAS can receive it. FAS requires either greater investigative powers itself, or more effective mechanisms for cooperation with the police and other bodies;
- Allowing the FAS to focus solely on competition issues;
- Reducing the secondary responsibilities, such as the enforcement of advertising laws for the FAS, so as not to distract it from its primary task;
- Relieving it of the burden of resolving disputes between regulated monopolies and consumers – Industry-specific regulators would be better placed to do this;
- Reducing or eliminating FAS’s responsibility for general oversight of state purchasing;
- Entrusting to state financial and/or auditing bodies the responsibility of ensuring that state bodies use competitive purchasing procedures may stimulate competition in a variety of markets, backed up by a system for private complaints;
- Improving the information gathering and economic analysis capabilities of the staff; and
- Improving the qualification of the FAS staff and increasing practical training for them.

✦ Russia has passed a new competition law that revises the thresholds for determining a company’s monopolistic position. The upper limit is now a 50% market share, unless the company can prove that it doesn’t have unilateral market power. Even the company with a market share below 35% may also be considered a monopoly if demand for its product is inelastic.

*(Source: Global Competition Review, 9<sup>th</sup> August 2006)*

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**Suggested Readings**

*OECD Peer Review Report on Russia’s Competition Policy and Law*, Document CCNM/GF/COMP/WD (2004) 2, retrievable from [http://www.fas.gov.ru/files/1571/Global\\_Forum\\_Final.doc](http://www.fas.gov.ru/files/1571/Global_Forum_Final.doc)

*OECD (2004)*, Policy Brief on Competition Law and Policy in the Russian Federation

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