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Abstract

Most developing and transition countries adopted statutes prohibiting anticompetitive agreements and abusive practices during the 1980's and 1990's. The effectiveness of these laws is nevertheless widely debated. This paper contributes to the literature by conducting an event study of the adoption of Russian competition laws in the early years of transition, the subsequent economic developments and the legislative reform process of 2002-2006. An examination of the substantive prohibitions and enforcement data reveals that Russian competition laws relied on complex standards and imposed weak constraints on anticompetitive practices. The more recent shift to simpler and more predictable per se prohibitions against collusive agreements substantiates this hypothesis. The evidence has implications for the design of regulatory regimes in other countries with laws similar to those operative in Russia during the transition process.

KEYWORDS: competition law, economic development, market power, Russia

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Introduction

A large number of developing and transition countries adopted laws prohibiting anticompetitive agreements and abusive practices during the 1980s and 1990s.[1] The effectiveness of the new competition regimes remains a subject of considerable controversy in many jurisdictions. This paper offers an event study of competition law reform in Russia as it analyses changes in the legal and economic infrastructure from the early stages of the transition process to statutory reforms implemented in 2006.

The interaction between economic and legal institutions in the Russian Federation provides a rich body of evidence about the dilemmas in the design of competition law as an institution that contributes to the efficiency of a market system. Admittedly, establishing causality between substantive and procedural elements of competition law and economic outcomes is a difficult task given the simultaneous changes in the overall political and macroeconomic situation in Russia following the collapse of central planning. Nevertheless, this study explores the relationships between the substantive and procedural elements of competition laws on one hand, and the development of an economy that exhibits large concentrations, high price setting capacities by incumbent firms, and uneven development on the other.[2]

The working hypothesis of this paper is that the rapid emergence of large industrial agglomerations with price setting powers, the concentration of ownership and control, and the supply bottlenecks that characterized the Russian economy during the transition period justified more robust competition laws from an economic perspective. However, the adoption and implementation of more effective regulations encountered resistance from those who benefited from the present arrangements. When large and well-organized incumbents are prevalent, as is apparently the case in the new Russia, and the general business community is little concerned with the social costs of anticompetitive practices, the development of competition law as an efficiency enhancing institution appears unlikely to occur. In such a setting, the new laws are more likely to replicate old mistakes rather than materially change the previous regulatory regime.[3]

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[1] See Palim (1998) for an analysis of the determinants of the growth of new competition laws, and Maher (2002) on the role of trans-national networks of policy makers actively involved in designing the regulations.

[2] According to the World Bank's World Development Indicators (WDI), Russian per capita GDP fell 9% annually for the 1985-1995 period, and grew around 5% per year between 1995 and 2005. However, recent aggregate figures have been driven primarily by growth in the energy sector. Indicators such as life expectancy and the level of gross capital formation suggest a less optimistic picture.

[3] See Fernandez and Rodrik (1991) for a political economy model where individual specific uncertainty about payoffs from reform generates a status quo bias even when incremental changes

The paper is organized as follows: The next section reviews comparative evidence on the effectiveness of competition regimes across jurisdictions and the theoretical dilemmas in the design of such laws. Subsequently, we explore the Russian experience in greater detail using firm level survey data. The economic conditions are then linked to the substantive prohibitions and enforcement practice as they evolved from the early 1990s to the legislative reform process of 2002-2006.

Comparative evidence on competition law effectiveness

Existing research provides a number of different approaches to the study of competition law and assessing its role as an efficiency enhancing institution. Buchanan and Lee (1992) separate theories of competition law into two generic categories: Public interest theories hypothesize that legal constraints against anticompetitive practices function to serve the general social and economic interest. Private interest theories suggest that the benefits of public regulations often accrue to small and well-organized groups of individuals or industries. In the presence of asymmetric information and regulatory capture, regulations aimed at constraining anticompetitive practices can make entry more difficult and ironically function as restraints against market competition. This basic theoretical ambiguity highlights the importance of empirical research in the design of competition regulation.[4] A number of recent empirical studies have tried to assess the economic role of the new competition laws. This section reviews this literature, describes the basic dilemmas in the design of substantive and procedural features of a competition regime, and details the relevance of the Russian evidence in a comparative context.

Dutz and Vagliasindi (2000) looked at the association between aggregate measures of competition policy implementation and the intensity of market competition for 22 countries in Central and Eastern Europe. They noted a positive correlation between indicators of the competition regime, particularly the effectiveness of legal enforcement, and the intensity of market competition. Their

in the policy framework are socially desirable. Slantchev (2005) offers an empirical assessment of two general political economy models of reform for 25 post-socialist jurisdictions. He finds little evidence that losers have resisted reforms, but robust support for the hypothesis that winners from the status quo have been the prominent opponents of liberal economic policies. Acemoglu and Robinson (2006) develop a model for linking the persistence of inefficient institutions to the presence of an oligarchy that is robust against changes in formal regulations or identities of people in power (i.e. The Iron Law of Oligarchy).

[4] In the case of the Sherman Antitrust tradition in the United States, Buchanan and Lee (1992) argued that empirical research, particularly by scholars associated with the University of Chicago during the 1960s and 1970s, had not provided sufficient support for private interest theories of competition law.

data suggest a certain degree of heterogeneity in the regulatory regimes operative across the region in the post-privatization period and document that Russia had one of the less effective regimes in place during the formative years of the market system. While this analysis does not explain why some jurisdictions implemented ineffective regulatory regimes, their observation serves as the point of departure for the study of the Russian experience presented in this paper.

A broader global study by Kee and Hoekman (2007) focused on assessing the impact of the new competition laws on market outcomes across a wide range of industries in 42 developing and developed economies. Their analysis suggests that both domestic and foreign competition tend to compel market discipline in concentrated industries and lower the mark up of prices over costs. Controlling for the impact of import competition, they find that the adoption of competition statutes did not have a significant direct effect on industry mark up levels. However, they argue that the adoption of competition statutes had indirect economic benefits since it promoted entry by a larger number of domestic firms. When there are more market participants present, anticompetitive practices among incumbent entities may be less sustainable, making price or quantity restrictions less credible. Analogously, concentrated structures can facilitate anticompetitive arrangements because in such environments the transaction costs for sustaining an inefficient private order through time are likely to be lower than in the presence of many participants.

Voigt (2008) studied the association between measures of competition regulations and Total Factor Productivity (TFP) for a sample 97 jurisdictions. His analysis documents a weak positive association between legal indicators capturing the restrictiveness of rules and independence of enforcement institutions, and long-term growth in TFP. He also found that the limited statistical impact of competition laws on TFP tends to dissipate when controlling for broader measures of institutional quality such as corruption. This observation suggests a second indirect channel between legal and economic institutions: Well-designed competition regulations can serve the public interest by enhancing the capacity of other regulatory mechanisms that shape market conduct. For example, the presence of a larger number of firms may limit incentives to bribe officials and capture regulators for a share of the market.

Although this empirical literature documents that competition laws can have possible economic benefits, it does not provide clear support for either public or private interest theories of regulation at the cross-national level. In terms of the transition from central planning, evidence suggests that countries with more effective competition laws also developed relatively more efficient market systems. This paper explores why the Russian competition regime was so ineffective and explores the evolution of its substantive and procedural features.

Regulatory framework for competition policy

Alternative substantive and procedural design features of competition laws are likely to have distinct consequences on how market participants understand the law and incorporate it in their behavior. Before focusing on the specific features operative in Russia since the collapse of central planning, it is important to highlight the generic nature of the dilemmas facing lawmakers in both developed and developing countries.

Rules versus standards in substantive prohibitions

The history of competition law in Western industrialized countries highlights two distinct approaches to designing and interpreting legal prohibitions against anticompetitive agreements and abusive practices.

First, the rule-of-reason approach to the design of substantive prohibitions requires that competition authorities or judges look at the particular circumstances of a case, balance competing economic and social objectives, and determine if the alleged illegal act is reasonable. National legal regimes that evolved in Western Europe after World War II, the Canadian competition regime, as well as most developing and transition countries incorporate this design feature. The presence of a multiplicity of policy objectives in the statutes, an "efficiencies defense", as well as wide-ranging exemptions typically signals the presence of this design approach.[5]

Second, a few countries have diverged from this trend and instead implemented competition law as a set of *per se* (bright-line) rules prohibiting collusive, exclusive or abusive market conduct. A prominent example of this design approach is the Sherman Antitrust tradition in the United States as it evolved following World War II. More recently, the impetus to expand the application of the rule-of-reason approach has been noticeable both in the United States and in the interpretation of relevant European Union treaty provisions.[6]

The economic approach to modeling legal rules and enforcement procedures has long recognized the tradeoffs in the choice between bright-line rules and complex standards. On one hand, general rules against anticompetitive practices tend to be less information intensive to apply than the rule-of-reason

[5] Khemani (2002) provides an overview of exemptions embodied in contemporary competition laws.

[6] For instance, in 2007 the U.S. Supreme Court overruled the nearly century-old precedent established in *Dr. Miles Medical Co. v. John D. Park & Sons Co.*, 220 U.S. 373 (1911) prohibiting resale price maintenance on a *per se* basis. In *Leegin Creative Leather Products, Inc. v. PSKS, Inc. No. 06-480, 551 U.S.(June 28, 2007)* the court declared that minimum price agreements may benefit consumers, and hence should be subject to case by case analysis.

approach to interpreting prohibitions. *Per se* prohibitions are nevertheless costly, since they:

> "….can be expected to give the wrong answer in some specific cases, which means that a general rule will do a worse job of guaranteeing efficient outcomes than would a perfectly wise court deciding each case on its individual merits." Friedman (2000, 43).

This perspective suggests that in the absence of costly information, standards are preferable to rules because they lower the probability of Type I errors (false positives) when implementation of the law prevents socially beneficial transactions because they appear anticompetitive. Flexible standards can allow regulators or judges to balance competing policy objectives and the discretion to decide if particular actions are reasonable in light of specific circumstances. The possibility of Type I errors has been the central argument against the adoption of *per se* prohibitions in both developed and developing countries. Williamson (1983) provided the first of a large body of research in New Institutional Economics (NIE) emphasizing the inhospitality of public competition laws with respect to heterodox organizational forms. In the case of developing and transition economies, Singh (2002) also argues that competition laws should be designed using flexible standards that allow regulators to balance competition and coordination incentives in particular industries since maximizing competition through restrictive rules is not optimal in all areas of the economy.

Christiansen and Kerber (2006) describe the problem of designing competition laws in terms of a continuum of more or less differentiated rules, rather than within the traditional rule-of-reason/*per se* dichotomy. They argue out that the optimal degree of differentiation depends on the relative capacity of rules and standards. Rules have three basic advantages since they have a relatively higher capacity to:

- Stabilize market expectations about the boundary of permissible conduct.
- Restrict the discretion of government entities, hence reducing costs associated with rent seeking behavior.
- Lower the level of expected errors in decision-making that arises in the presence of asymmetric information between the regulators and the regulated.

As detailed in this analysis, the late Soviet and Russian lawmakers did not transplant the U.S. Sherman style system of *per se*/bright line rules, at least until the legislative reforms of 2006. Instead, they replicated the flexible rule-of-reason approach to competition laws.[7] Importantly, many other jurisdictions that adopted competition statutes in the 1980s and 1990, often in times of severe political and economic crises, also replicated a similar model. Understanding the implications of this choice in Russia consequently has broader relevance for designing effective mechanisms for mitigating the costs of anticompetitive practices.

The two distinct approaches highlight uncertainties about the optimal design of substantive prohibitions. However, in practice it is possible to observe the presence of both design features in a particular legal regime. For instance, some jurisdictions impose *per se* prohibitions for horizontal and vertical collusion, and require the application of a rule-of-reason in case of abusive practices by dominant enterprises. An example of this combination is the Sherman Antitrust tradition in the United States. Others have applied less restrictive standards to vertical restraints on competition, but ban horizontal price fixing on a *per se* basis. The usual interpretation of European Union treaty obligations represents an example of this approach. The analysis of Russian competition laws from the early 1990s to 2006 explores the significance of the specific combinations and permutations of the two design strategies relative to regional and global trends.

Enforcement system

In addition to the difficulties in determining the optimal degree of differentiation in rules against anticompetitive practices, lawmakers also design mechanisms employed to implement statutory prohibitions. Theoretically, they can assign the right to bring claims to public or private agents. Outside of the United States however, most jurisdictions have historically provided public prosecutors and competition bureaucracies with the exclusive authority to enforce the law.[8] Debates about the development of European Union competition laws have long focused on the weaknesses of a purely public regime for the enforcement of competition law, stimulating efforts to enhance the standing rights of victims to bring cases against illegal acts in courts. The widely quoted decision by the European Court of Justice (ECJ) in *Courage v. Crehan* summarizes the informational argument for mixed public-private enforcement regimes:

> “The full effectiveness of Article [81] of the Treaty and, in particular, the practical effect of the prohibition laid down in Article [81(1)] would be put at risk if it were not open to any individual to claim damages for loss

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[7] For an analysis of the impact of legal transplantation versus legal origins on development see Berkowitz et al. (2003). Kennedy (2003) provides an overview of recent efforts to associate legal reforms with development policy.
[8] For a history of the U.S. enforcement regime that relies primarily on information and incentives of victims to make direct claims against offenders of competition laws see Lin et al. (2000)

> caused to him by a *contract* or by conduct liable to restrict or distort competition.
>
> Indeed, the existence of such a right strengthens the working of the Community competition rules and discourages agreements or practices, which are *frequently covert*, which are liable to restrict or distort competition."[9]

The ECJ justification for enhanced private rights of access reveals that, even in jurisdictions with established, well-funded, and relatively competent government bureaucracies, knowledge about illegal practices is costly to obtain, interpret, and disseminate. As noted by Tirole (1999), Laffont (2005) and Chen (2006), the need to decentralize mechanisms for enforcing prohibitions against collusion is likely more pressing in developing countries since the relative burden of raising public funds needed to acquire information is higher than in richer jurisdictions. The competition laws adopted during the 1980s and 1990s in general do not incorporate these insights as public competition authorities have been the primary instrument for implementing the rule-of-reason prohibitions. This has been the case in the Russian Federation. Consequently, this paper only studies the implications of the design of public competition authorities.

The analysis of the experience in the immediate post-privatization period by Dutz and Vagliasindi (2000) suggests the presence of some degree of heterogeneity in the effectiveness of public competition authorities across the region. Nevertheless, they do not explore why some jurisdictions failed to produce the type of effective regimes that evolved in Poland or Hungary, for instance. Kovacic (2002) argued that the regulatory regime in some transition economies failed to prevent costly anticompetitive practices and attributed the divergence in economic outcomes to the limited institutional capacity of bureaucracies to interpret complex standards associated with the rule-of-reason approach. This view highlights the importance of Type II errors (false negatives) in the analysis of the relationship between competition regulations and economic institutions in Russia.

This perspective is problematic for two important reasons: First, it assigns blame for past failures primarily to bureaucracies, but does not explain why lawmakers designed competition laws as a set of complex standards, rather than *per se* rules, in the first place. Second, in theory lawmakers could have designed enforcement mechanisms that relied less heavily on the incentives of a centralized bureaucracy for mapping substantive prohibitions into regulatory constraints. Hence, in retrospect it is easy to see that more effective design strategies with

[9] Case C-453/99.

respect to both substantive rules and enforcement could have mitigated the costs of Type II errors.

Existing literature suggests that dilemmas relating to these design features are likely to be interrelated. For instance, consider the difficulties in the choice between rules and standards. In the presence of private rights of access to courts, judges and competition regulators would have overlapping authority in determining if particular practices are in fact inefficient, unreasonable, and consequently illegal. When there are differences in the interpretation of what is reasonable or efficient across the bureaucracy and the judiciary, the boundary of permissible conduct is likely to appear uncertain to market participants. With flexible standards, it would be more difficult to coordinate market expectations when separate public decision makers exercise their regulatory authorities. Since centralization allows for coordination of interpretations, it can mitigate legal uncertainty and the potential for inconsistent decision-making. However, as detailed by Laffont and Martimort (1998) and Laffont (2005), a separation of regulatory powers can increase the transaction costs facing entities that intend to capture regulators and shape state authority to their own private advantage.

Political economy of regulation and transition

Some socialist economies, notably Yugoslavia and China, developed a legal basis for the decentralization of economic activity during the 1960s and 1970s. By contrast, the Soviet central plan remained impervious to such reforms. By the 1980s though, the impetus to develop a mixed socialist economy started to gain support from a new generation of bureaucrats under the radical policy packages of “glasnost” and “perestroika” introduced by the Gorbachev government. According to King (2002), these programs made it increasingly feasible for the bureaucratic elites to imagine how their futures would materialize in a new market economy characterized by private ownership. This change in perceptions explained why incremental reforms did not find much support earlier, but radical restructuring suddenly became popular among the ruling elites. Encouraged by the large expected payoffs from a transition to private ownership, industrial and military managers rapidly embraced the desire of the politburo planners to decentralize economic activity.

Qian et al. (1999, 2006) attribute the radical nature of reform policies in the former Soviet Union to the persistence of centralized hierarchies (U-form) employed to organize economic activity prior to the transition period. In contrast to the multidivisional organization (M-form) of Chinese socialism, the legacy of Soviet central planning made incremental experimentation and learning difficult. Given the historical difficulties in reforming unitary governance mechanisms, this view suggests that it would not be surprising to observe a high degree of persistence in the features of regulatory and economic institutions that evolved after the collapse of the Soviet Union.[10]

Initial institutional and economic conditions are potentially important factors in explaining the Russian legal and economic history after the collapse of central planning. The legacy of the past is likely to be only a partial explanation of the transition from a relatively egalitarian socialist system to one typically characterized by oligarchy and uneven development. Parente and Rios-Rull (2005) offer a theory to explain the different experience with capitalism in Russia and China. They argue that the key impediment to economic growth that explains cross-national income differences relates to the acquisition of monopoly rights by production input suppliers. The strong central government in China successfully managed to resist pressures by upstream firms during the transition process to offer such rights, but the weak post-Soviet state granted associations of incumbent suppliers such legal rights during the controversial privatizations of the mid-1990s.[11]

Boycko, Shleifer and Vishny (1993), authors strongly committed to the privatization policy of the early to mid-1990s, offered early warnings about the prospects for the development of product market competition in Russia. They justified rapid privatization primarily as a good by itself because of its capacity to depoliticize business decisions. Clearly, business remains a political issue in Russia, as in any other market economy. Nonetheless, they also pointed out the limited prospects for the development of product market competition and argued for active competition policies post-privatization. Their justifications for such policies included the concentrated organization of the Soviet economy, which facilitated collusion between recently privatized large enterprises, the collapse of trade with other socialist jurisdictions, a lack of import penetration and the legacy of rigid supply chains where most firms bought their inputs only from one supplier.

Joskow et al. (1994) provided the first comprehensive study of the changing landscape of post-Soviet industrial organization, and challenges to employing competition law. Writing during the rapid privatization process, these authors predicted the formation of a market system that exhibits high levels of concentration in ownership and control, thus facilitating anticompetitive agreements. They argued that the most important factors in determining the long-term prospects of the Russian economy were the inherited industrial and institutional structures. Soviet planners emphasized scale economies and specialization in the organizations they created, and hence had an affinity for

[10] See Gerschenkron (1967) for an analysis of long-term institutional development and the role of a centralized state as an economic actor in Russia.
[11] See Cai and Treisman (2004) for an analysis of the role of federalism as an mechanisms that eroded the power of the state.

increased concentration as a means to improve economic efficiency. They identified emerging private trade associations as a considerable impediment to the formation of product market competition.

Brown and Brown (1999) analyzed the evolution of concentration ratios in the post-privatization period. They found that while concentration in manufacturing had been increasing since the Soviet era, this observation masked other structural changes in the economy. Specifically, they noted that the size distribution of firms across industries in Russia was converging to those present in the United States and product concentration in manufacturing was actually decreasing. They interpret this evidence optimistically, as a sign of emerging competitive pressures on firms operating in the same general product market (i.e. the horizontal dimension). Broadman (2000) reached a more pessimistic conclusion about the prospects for the formation of competitive markets after privatization. This conclusion reflected the finding that by the late 1990s emerging private enterprises in Russia tended to be vertically integrated and able to deter new entry into their market segments. He also noted that the high degree of vertical integration had resulted in increased fragmentation of the national market along regional lines.

Brown and Earle (2000) offer a systematic overview of the evolution of a number of indicators of the competitive environment in Russia during the 1990s. Using a sample of approximately 15,000 industrial firms covering around 75% of total employment in 1993, they document:

- Increased levels of concentration measured in terms of the Herfindahl-Hirschman Index (HHI), as well as 2 firm ratios (CR2) at the 5 digit level of sectoral aggregation over time.
- A rising Gini coefficient in output (measuring inequality or dispersion across firms) suggesting an increased share of production by a subset of firms.
- Increases in regional concentration measures calculated at the oblast level.
- Radically higher levels of import penetration after 1992, inducing competitive pressures in certain product markets.

They further find a positive correlation between the level of product market competition and firm level total factor productivity growth. Their evidence is probably the most robust and complete of the empirical studies on the changing landscape of the Russian economy in the 1990s, and the relationship between the degree of competition and microeconomic growth.

Economic studies typically emphasized the significance of the historical legacy of horizontally and vertically integrated structures under the Soviet central plan in determining the economic outcomes from the transition process. They also show that the trend towards increased agglomeration started before the fragmentation of the Soviet Union and the design of the privatization plan. The competition laws adopted as part of the larger policy program to decentralize economic activity apparently played little part in reversing the general trends in concentration indicators during the 1990s.

The existence of high concentration ratios, or ownership by a small group of oligarchs, may not necessarily harm long-term development of an economy. This is because oligopolies that can extract super-normal rents from downstream firms and final consumers could, at least in theory, employ the retained earnings to invest in improving capital and labor productivity. Guriev and Rachinsky (2005) offer some empirical evidence of this possibility, claiming that consolidated entities owned or controlled by the small group of oligarchs performed better than other private and public Russian organizations in terms of total productivity growth, and at about par with foreign-owned firms in the late 1990s to early 2000s. They take this evidence to mean that the oligarchy is potentially an efficient form of organization and possibly even a credible constraint on the discretion of the government.

However, their conjecture does not account for loss in consumer welfare or other potential negative consequences of the rise of oligarchic economic and political structures. Such negative effects could arise if these agglomerations were to implicitly crowd out access by smaller organizations to skilled labor, capital, and other scarce inputs. In addition to this economic problem, managers of large organizations are likely to be able to coordinate their bargaining with the state or other gatekeepers to essential inputs such as external finance as documented by Beck et al. (2005). Consequently, higher productivity growth rates in oligarch firms relative to other firms may simply reflect the challenges facing potential entrants in the Russian markets.

A comparative view helps shed light on the features of the market system that evolved in the Russian Federation during the 1990s. Table 1-4 provide survey-based indicators of the relative capacity of Russian firms to extract rents from their buyers and perceptions of the costs of anticompetitive practices on firm growth from World Bank Productivity and Investment Climate Surveys (PICS).[12] The surveys questioned firm owners, managers, or accountants across a wide range of topics relating to the business and institutional environment within which they operate. We only focus on two indicators from the surveys that help capture features of the market system and perceptions of the costs of anticompetitive practices on firm level growth. The breadth of the questionnaire and its confidential nature mitigate to some extent against the possibility that the respondents manipulated their answers pertaining to the price setting capacity of

[12] The database has a total sample size of around 30,000 firms. The number of observations across firms of different sizes is broadly similar.

their enterprises or constraints posed by anticompetitive practices to their activities.

Table 1
Price Setting Powers in Comparative Perspective

Country	Percentage of respondents who indicated most customers would stop buying if firms raised prices by 10%.
Albania	29
Armenia	26
Brazil	31
Bulgaria	39
Croatia	23
Czech Republic	29
Guatemala	25
Hungary	35
Indonesia	40
Lithuania	44
Poland	44
Russia	**25**
Slovakia	34
Tanzania	42
Turkey	21
Source: World Bank PICS (2002-03)	

The interpretation of the data follows the basic presumption that in an ideal competitive market, no individual buyer or seller should have the power to influence the price, and hence the firms should act as price takers. If this is not the case, the institutional environment likely facilitates the sustainability of anticompetitive agreements among economic agents. Table 1 shows the percentage of firms that indicated some of their customers would stop buying from them if they increased prices by 10%. To the extent that firm owners and managers know the specific market setting in which they operate, and the responsiveness of their customers, the numbers reflect a consistent picture of the price setting capacity of incumbent firms. A lower indicator value implies higher price setting power. Analogously, a higher number reflects that firms are more likely to be price takers as reflected in the traditional ideal of a competitive market.

The comparative data suggest that along with entities in Turkey and Croatia, Russian firms had a relatively strong capacity to set prices. This picture is consistent with the presence of a high level of concentration and oligarchy outlined in earlier studies.

Besides high concentration ratios and pricing powers, the continued technological sclerosis of the Russian economy remains a central policy concern for economists like Parente and Rios-Rull (2005) as well as for a new generation of policy makers. In initiating a range of legislative projects, including changes to the competition regulations in 2006, the President of the Russian Federation Vladimir Putin (2002) justified the reforms to the Duma by emphasizing the technological angle on the economic problems of transition:[13]

> "Our economy is not yet receptive enough to the achievements of scientific and technical progress. A significant number of enterprises do not invest any funds in creating new technology or in modernizing old technology."

One approach promoted by lawmakers to address technological sclerosis and price setting capacity by incumbents has been to ease entry regulations and the tax burden on new firms and small businesses. The second component of regulatory reform focused on the re-design of rules and procedures for the implementation of prohibitions against anticompetitive agreements and abusive practices by dominant firms. This culminated in the abolition of the Ministry for Antimonopoly Policy (MAP) and the creation of the Federal Antimonopoly Service (FAS) in 2004, followed by the adoption of a new statutory mandate by the Duma in 2006. The Russian case consequently offers two iterations of experiments by lawmakers to enhance the capacity of the economy to implement new technologies and foster long-term development.

Strong perceptions of monopoly capitalism and the powers of an oligarchy partly explain why Russian lawmakers chose to rename the competition agency in 2004, and adopt a new legislative basis two years later. The four years of debates from the introduction of the draft law in 2002 to its final adoption in 2006 nonetheless show that lawmakers and interests that lend them support continued to value specific features of the regime transplanted in Russia during the 1990s and contested the adoption of alternatives into statutes. In addition to outright resistance to the adoption of *per se* prohibitions and privatization of enforcement, the PICS surveys further reveal the potential impact that apathy or ignorance by the business community can have on the design of more effective rules and procedures. Table 2 shows the percentage of incumbent firm managers and owners indicating that anticompetitive/informal practices imposed significant constraints on the growth of their organizations. Similar measures relating to price (interest rate) and access (collateral) to finance provide benchmarks for comparison.

[13] http://www.kremlin.ru/eng/

Table 2
Significance of Perceptions of Financial and Anticompetitive Constraints on Firm Growth
(Cumulative percentage of firms who rank the constraint as major or severe)

Country	Anticompetitive Practices	Access to Financing	Financing Price
Albania	42	14	24
Armenia	16	22	29
Brazil	57	60	83
Bulgaria	46	41	51
China	24	23	22
Croatia	20	25	20
Czech Republic	20	25	21
El Salvador	45	31	28
Guatemala	57	34	24
Hungary	15	22	19
Indonesia	17	17	28
Lithuania	25	18	17
Philippines	24	14	23
Poland	32	33	52
Russia	**15**	**20**	**13**
Slovakia	12	30	30
South Africa	16	13	17
Tanzania	25	48	58
Turkey	23	17	28

Source: World Bank PICS, 2002-2003.

Table 2 shows that the relative level of perceptions relating to the costs of anticompetitive practices was significantly lower in the Russian Federation than many other jurisdictions in the sample. The low level of perceptions relating to the costs of anticompetitive practices to incumbent firms stands in sharp contrast to notions like monopoly capitalism and oligarchy, the traditional concentration ratios used by industrial economists and the high levels of pricing setting capacity captured in Table 1.

To illustrate this point, compare Russian indicators with those of Poland. While the level of pricing power during the 1990s was lower in Poland, perceptions by firm managers about the costs of anticompetitive practices were higher compared to Russia. If incumbent businesses think that anticompetitive practices are costly to their growth, they would have incentives to support the adoption and implementation of more restrictive competition laws. In the absence of such perceptions, individuals and organizations with a strong stake in the status quo features of the regulatory system would likely find it easier to influence the lawmaking process.

The empirical contrast between reality and perceptions generates the working hypothesis explored in this paper. The presence of large agglomerations, supply bottlenecks, and price setting powers can justify the adoption and implementation of restrictive rules against anticompetitive agreements and abusive practices. However, those who benefit from the present regulatory arrangements have incentives to resist the development of competition law as an efficiency enhancing institution described by Buchanan and Lee (1992).

In summary, empirical literature on the evolution of the Russian economy highlights a number of relevant observations about the legacy of the 1990s:

- Traditional concentration measures deteriorated in a consistent manner at least from the late 1980s to the early 2000s.
- Enhanced competitive pressures evolved from import penetration and diversification into new products and services.
- On average, Russian firms exhibit a high degree of price setting capacity relative to their counterparts in other jurisdictions.
- At the same time, managers of existing firms in Russia do not believe that anticompetitive practices pose a significant constraint to the growth of their operations.

To extend the traditional literature on increasing concentration and oligarchy, and to test the sensitivity of comparative observations about the level of price setting powers and perceptions of anticompetitive practices, this section further explores the PICS dataset. Specifically, the analysis decomposes the aggregate results based on the characteristics of incumbent enterprises in Russia and Poland. This comparative analysis helps capture the divergence of the institutional environment for the operation of markets resulting from the privatization and competition policies of the 1990s. It also provides a basis for understanding the motivations behind more recent regulatory reforms in Russia explored in detail in the remainder of this paper.

Table 3 documents the percentage of respondents who indicated that many of their customers would stop buying from them if the firm raised its prices by 10%.[14] While it seems reasonable to assume that managers and accountants have a good grasp of the price responses of their respective customers, it should be still

[14] Please note that the measure of price setting powers in Table 3 differs from the measure supplied in Table 1 since the reference is made to "many" customers in Table 3 and "most" customers Table 1. The decomposition by firm characteristics in Table 3 utilizes the measure referring to "many" customers due to the larger sample size in this category compared to the more restrictive standard set by reference to "most" customers.

acknowledged that they may not have had the right incentives to provide accurate answers, for instance when their market shares were high.

Table 3
Price Setting Powers by Firm Size, Industry, and Ownership
(Percentage of respondents who indicated that many of their customers would stop buying from them if the firm raised prices by 10 %.)

Firm Size	**Poland**	**Russia**
Micro	66	50
Small	50	41
Medium	59	39
Large	38	32
Very Large	47	37
Manufacturing	55	36
Services	53	44
Construction	39	39
Exporter	54	29
Non-exporter	54	40
Domestic Ownership	33	21
Foreign Ownership	60	83
Source: World Bank PICS (2002-2003).		

This measure of the institutional environment reveals a number of interesting observations about the features of the market regimes that evolved after the reforms of the early 1990s and privatization:

- Industrial structure: Service providers exhibit less market power than those in manufacturing and the construction business. Pricing power was relatively similar in the construction sector in both jurisdictions, but is significantly higher in the Russian case in manufacturing and services.
- Firm size: In Russia small firms exhibit price setting powers that exceed those of the very large and micro enterprises. Medium sized organizations exhibit the smallest capacity to set prices and extract rents from buyers. This suggests the presence of a non-linear relationship between firm size and the capacity to engage in anticompetitive practices.
- Sales orientation: Russian exporters have much larger pricing powers than firms that do not export. This can be explained by the composition of Russian exports dominated by energy and commodity supplies to foreign markets. In Poland, where the export structure is more diversified, there is little difference between the two classes of organization.
- Ownership: Firms owned by foreign entities in Russia believe that they are able to set market prices more than those owned by locals. Although a

similar pattern is observable in Poland, the difference in Russia is particularly strong.

Table 4 **Perceptions of Anticompetitive Practices by Firm Size, Industry, and Ownership** (Cumulative percentage of firms who rank the constraint as major or severe)		
Firm Size	**Poland**	**Russia**
Micro	32	18
Small	32	11
Medium	37	21
Large	34	18
Very Large	32	16
Manufacturing	33	18
Services	31	13
Construction	40	17
Exporter	30	15
Non-exporter	33	16
Dom. Ownership	33	16
For. Ownership	30	11
Source: World Bank PICS (2002-2003).		

Table 4 shows the presence of a non-linear size effect in the perception of firm managers about the impact of anticompetitive practices on their growth. Medium sized firms were more susceptible than the very large and small organizations. This observation complements the distribution of price setting powers across firms, suggesting that medium sized entities have relatively less capacity to extract rents from buyers, and a higher exposure to anticompetitive practices by other businesses. Table 4 also documents that the perceptions are highest in the manufacturing and construction sectors. Notably, firms with participation by foreign investors exhibit lower perceptions of anticompetitive practice relative to purely Russian owned organizations and these firms also showed a higher capacity to set prices.

Together the above tables confirm the broad comparative assessment about the dissonance of perceptions and reality not just in Russia, but also in Poland where low price setting powers co-exist with a high level of perceptions about the costs of anticompetitive practices. This puzzling difference may be attributable to the features of the regulatory mechanisms that aim to constrain anticompetitive practices and inform market participants about the risks they pose. The fact that Poland involved the competition bureaucracy in decisions about privatization and implemented competition law as a set of restrictive and predictable *per se* prohibitions highlights the relevance of this hypothesis.[15]

From an economic point of view, the traditional measures of concentration and the PICS-based indicators of evolving market structures seem to justify the reassessment of the Russian competition laws that occurred in the 2000s. But there remains a question about the extent to which the reforms were driven by the interests of incumbent firms. Those benefiting from the emergent structures in the 1990s may have had a lot to lose from substantive changes to the legal regime and thus had strong incentives to resist the adoption of substantive changes to the regulatory regime. As documented by the perception indicators, it is also possible that owners and managers of firms did not perceive a need for change in the regulatory regime. Overall, this evidence suggests that lawmakers may not have had sufficient support from the business community to alter the legal framework for regulating anticompetitive practices and structures that evolved in the 1990s.

Competition regulations in Russia, 1990-2006[16]

The previous section reviewed evidence on the evolution of variables emphasized by economists in the analysis of state and market mechanisms that have a bearing on competition. The economic history of increased concentration in Russia during the 1990s finds a direct counterpart in the evolution of the objectives and instruments of competition law. This section describes the features of state regulatory mechanisms in terms of the substantive and procedural elements adopted and increasingly implemented during the 1990s. In order to characterize the features of Russian competition laws it is imperative to first recall two broader global trends associated with the adoption and formation of such regulatory instruments.

First, Palim (1998) documented that the adoption of new competition laws around the world in the 1980s and 1990s coincided with periods of economic and political crises. Borrowing constraints faced by the public sector led to the acceptance of broad policy reform packages by national lawmakers typically in exchange for access to short-term funds by public and private organizations such as the World Bank (WB) and the International Monetary Fund (IMF). Second, as

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[15] See Pittman (1998) and Varady (1999) for a review of emerging differences in the competition regimes in the first stages of the transition to a market system in Central and Eastern Europe. The fact that both jurisdictions had relatively similar trade and financial liberalization policies further underscores the role of microeconomic policy in explaining divergent paths of development after the shock therapy reforms of the early 1990s.

[16] Primary legal material and translations in this paper are compiled from the publications of the Federal Antimonopoly Service (FAS) available at www.fas.gov.ru. Secondary sources include public communications between Russian officials and the Organization for Economic Cooperation and Development (OECD), available at http://www.oecd.org/russia.

detailed by Maher (2002), the formulation and drafting of the new competition statutes usually involved a good deal of cooperation between local and trans-national networks of experts and bureaucrats. Given the well-understood role of external conditionality to regulatory reform during this period, it is not surprising to see some degree of similarity among the substantive prohibitions of the new competition laws and procedures for their enforcement across transition and developing countries. The homogeneity of the laws hence generates the impression that national legal systems have been simply mimicking fashionable trends rather than searching for an optimal set of regulations and procedures that would reflect their specific requirements.[17]

In relation to the first of the global trends, the adoption of the first competition statutes in the Soviet Union also coincided with a period of rapidly falling production and employment, and rising public sector debt. In particular, the establishment of the State Committee for Antimonopoly Policy and Support of New Economic Structures (hence, SCAP) in 1990 provided the central forum for the management of liberalization policies at the federal level. The Law on Monopolistic Activity in the Goods Market (hence, the Law on Competition) was adopted in 1991 following the recommendations of the SCAP.

In May 1995 amendments to the Law on Competition followed two other products of the post-Soviet political developments: the adoption of a new constitution in 1993 that guaranteed individual economic freedoms and prohibited anticompetitive practices; and the rapid privatization of public assets which typically involved closed auctions and sales to incumbent managers in 1993-1995. Sahlas and Reshetnikova (1997) provide a review of the early stages of the development of the laws and highlight the significant role of advisors from multilateral organizations such as the World Bank and OECD, as well as government representatives from Germany and the United States, in the process. Pittman (1998) also confirms the influential consulting position given to these individuals and organizations in the design of the competition laws.[18]

Hence, both global trends identified by Palim (1998) and Maher (2002) in terms of external influence during an economic crisis were operative in the Russian case. Despite the global origins of the regulatory instruments associated with competition law adopted in the last days of the Soviet Union, the Russian experience presents an interesting anomaly within the context of other Central and East European jurisdictions. Given the evidence of increased post-socialist

[17] See Levi-Faur and Jordana (2005) for a description of this problem in the context of global regulatory and institutional reform.

[18] Kovacic (2002), another observer closely associated with the U.S. government and the so-called technical assistance projects, admits that some of the early laws promoted by Western experts and bureaucrats in Central and Eastern Europe did not match the requirements of those jurisdictions, but blames the local bureaucracies for the failures of the legal instruments.

vertical and horizontal concentration during the 1990s, the mandate assigned to the SCAP and its successor organizations in terms of antimonopoly policy apparently failed to adapt to its local setting.[19]

A study of the regulatory efforts to implement the competition laws in the St. Petersburg region by Sahlas and Reshetnikova (1997) further suggests that local and central competition agencies had difficulties communicating and coordinating their actions in the early stages of transition. Moreover, regulatory responsibilities were routinely shifted across different state agencies by the emerging Russian political system, the names of agencies were changed, and many of the employees of the state agencies functioned in multiple public/private sector capacities (i.e. as consultants, researchers and lobbyists).

The SCAP bureaucracy was initially comprised of about 150 employees and a strong connection to the politburo. The official numbers expanded to around 350 personnel by the mid-1990s. After the bureaucracy was excluded from important policy decisions relating to privatization, the organization was renamed as the State Antimonopoly Committee of the Russian Federation following the Decree of the President of the Russian Federation of March 17, 1997 No. 249 "On perfection of the structure of the federal bodies of executive power". By September 1998, the organization apparently no longer seemed adequate, motivating yet another executive decree, which amalgamated a number of separate agencies involved in regulating natural monopolies, promoting markets and innovative activities. This act brought together employees across the old central planning bureaucracy and enhanced the oversight of the executive over the regulatory apparatus.[20]

The Ministry of the Russian Federation for Antimonopoly Policy and Support to Entrepreneurship (MAP) emerged from this process, which functioned until 2004 when it was replaced with the Federal Antimonopoly Service (FAS) during the second iteration of reforms. In 2002 draft legislation was introduced, culminating in the adoption of Federal Law No. 135-FZ On Protection of Competition in 2006. The contrast between the first draft and the final version of the law provides some signals about the contentious political debates between proponents and detractors of alternative features of the competition regime.[21]

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[19] King (2002) conducted case studies for about 25 firms across different industrial sectors that serve as a good complement to the statistical studies of the 1990s reviewed earlier. His analysis of the transition process at the firm level highlights that the lack of feasible collective solutions to external shocks enhanced the attractiveness of unilateral decisions by managers with privileged access to inputs.

[20] See Kitschelt and Smyth (2002) for a comparative analysis of party platforms and political competition in Poland and Russia during this period.

[21] Legislative changes that influence the powers of federal government to regulate competition have not been limited to the Law on the Protection of Competition. Other reforms of the formal norms that frame the regulatory environment include: Federal Law № 94-FZ "On Placement of

Purpose and scope of the competition law

The 1991 competition statute had the stated objective of “preventing, restricting and stopping monopolistic activity and unfair competition” (Article 1.2). The purpose of the legislation must be viewed in the context of increasingly successful efforts to develop new private economic structures and enhance the legal independence of socialist managers from the central plan. Boycko et al. (1993) argue that prior to 1991 privatization was not a priority on the Soviet reform agenda and only gained prominence with the appointment of Anatoly Chubais to head the State Committee on the Management of State Property (GKI) in that year. Although an analysis of the privatization policies enacted by GKI is beyond the scope of this paper, the procedures developed by this entity consolidated control and ownership structures that persist in the Russian Federation.

The 1991 Law on Competition provided a wide range of specific prohibitions and specified the scope of legal prohibitions and the instruments available to the SCAP for their enforcement, including:

- Many of the formal prohibitions against collusive agreements, concentrations, unfair competition and state actions that are now present in most national jurisdictions.
- Retained the powers of the state bureaucracy to engage in price and margin control regulations.
- Assigned enforcement powers to the bureaucracy rather than granting private rights of standing through the courts or other adjudication venues to implement the laws.

The early competition regulations acted as a bridge between centralized Soviet mechanisms for organizing economic activity and those promoted by interest groups that came to power with the collapse of the Union. Specifically, the competition statute provided state authorities with the opportunity to engage in price and margin control regulations, which have been the primary instruments for the management of the socialist economy prior to privatization. Joskow et al. (1994) describe the operation of margin regulations applicable to firms on the monopoly register as per Russian Federation Regulation 576 of August 1992 by

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Orders for Delivery of Goods, Execution of Works and Provision of Services for Public and Municipal Needs”, Federal Law № 38-FZ “On Advertising”, Federal Law №36-FZ “On Peculiarities of Electric Energy Industry Functioning in Transition Period”, Land Code Articles 30, Water Code Articles 16 and 40, and Resolution of the Government of the Russian Federation № 75 “On the Procedure of Conduct by a Subject of Local Governance of the Open Tender for the Selection of the Managing Organization for Ruling over Tenement-house”. See archives at www.fas.gov.ru.

comparing them to realized margins in the United States as of 1987. Their comparison of the administrative and realized margins across these two distinct economies highlights some important features of the pre- and post-privatization environment in Russia. First, the Russian margin ceilings varied little across distinct industrial sectors. This reflects the difficulties facing price regulators in identifying what margins or prices are desirable given the specific characteristics of different industries. Second, while U.S. and Russian margins were relatively similar in the edible commodities, the realized U.S. outcomes were both higher and more heterogeneous across sectors. A privatized economy consequently offered the prospects of increasing margins in some sectors by increasing prices or reducing costs.

Decisions by the GKI meant that, in contrast to other jurisdictions in Central and Eastern Europe, Russian firms were not restructured prior to the transfer of ownership to managers. This was a direct result of refusals by the GKI to inform the competition authorities in a timely manner of their plans to sell public assets. For example, a 1993 letter by the Russian Federation State Committee for State Property Management indicated that privatization agencies would inform the competition authorities about privatization transactions involving firms with a dominant position. Sahlas and Reshetnikova (1997) note that competition authorities had only a week to respond to the information offered by the privatization agency and little power to alter outcomes even in cases where the given information raised serious concerns. Consequently, the scope of competition regulations over privatization was minimal.

In addition to the 1991 Law on Competition a number of other legal measures were adopted during the height of the GKI privatization program that are relevant to the analysis of the objectives and scope of the regulatory system. These measures include consumer protection statutes, provisions for the regulation of financial markets, and other sector-specific regulatory guidelines to address the natural monopoly problem.

A third class of broader legal rules particularly important for interpreting the purpose and scope of competition regulations consisted of the 1993 Constitution of the Russian Federation and the Civil Code adopted in 1994:

- Article 8 of the 1993 Constitution guaranteed within the Russian Federation: "Unity of economic space, free movement of goods, services and financial resources, support for competition and freedom of any economic activity".
- Article 34: 1. "Everyone shall have the right to freely use his or her abilities and property for entrepreneurial or any other economic activity not prohibited by the law. 2. Economic activity directed towards monopolization and unfair competition shall not be permitted."

Both constitutional provisions are highly general in their scope and application in setting up the framework for the operation of an efficient market economy. The 1993 constitutionalization of prohibitions against activities such as unfair competition during Russian privatization also likely reflects attempts to mitigate public concerns about sensitive decisions relating to the distribution of property rights and the scope for anticompetitive practices in the new economy.

The Civil Code of the Russian Federation adopted in 1994 further specified the scope of prohibitions against anticompetitive practices. It characterized civil economic rights and legal prohibition against restrictive or abusive practices as complementary:

- Article 10.1: "Actions taken solely for the purpose of causing harm to another party, or the abuse of civil rights in other forms, shall not be permitted. The use of civil-law rights for the purposes of restriction of competition or for abuse of a dominant position on a market shall not be permitted."

This provision requires establishing expressed or sole intent for an anticompetitive act or practice to become an offence. If other purposes are present when engaging in anticompetitive or injurious practice, the acts appear justified under the standard set in the Civil Code. The Civil Code configuration thus differs from the *per se* prohibitions mandated under the constitutional agreement and appears to have restricted its scope by implementing a relatively weak liability standard. The requirement for establishing explicit intent in complex business decisions helps protect competent offenders. This provision of the Civil Code guided the interpretation of the constitution in the direction of the rule-of-reason approach to competition law, which had already been favored in the 1991 Law on Competition. Civil procedure hence reshaped the constitutional prohibitions adopted during the implementation of the privatization process.

More than a decade later, Article 1 of the new 2006 law outlines the scope and purpose of its mandate. As the name of the law implies, one aim of the statute is to institute laws that "protect competition" rather than explicitly promote the concept. The first draft extended the scope of the prohibitions to actions by "executive authorities of the Russian Federation", but the adopted version of the law does not include this provision. Importantly, both versions of the new regulations failed to incorporate active qualifiers such as promotion and encouragement of competition in their construction of the purposes of the laws.

The conception of competition law primarily as an instrument for controlling anticompetitive practices by private monopolies remains central to the purposes of the new legislation. This is illustrated generally by the enhancement of regulatory powers relating to the imposition of price controls on dominant firms.

- Article 1.2 of the 2006 law states: "Objectives of the present Federal Law are to ensure common economic area, free movement of goods, protection of competition, freedom of economic activity in the Russian Federation and to create conditions for effective functioning of the commodity markets."

The presence of five potentially competing objectives in the interpretation of the statute highlights the persistence of the rule-of-reason approach under the second iteration of the laws.

Article 4.1 broadened the definition of a commodity as "an object of civil rights (including work, service, and financial service) intended for sale, exchange or trade in another form". Hence, the scope of the law seems to be wider relative to the 1990s. Other updates to the definitions include the expansion of the concept of a geographic market to include anticompetitive activities taking place in regional and global markets, presumably to clear up uncertainties about extraterritorial and local powers of the federal state.

Articles 3 and 4 characterize the law in its antimonopoly functions within the administrative state, providing a long and detailed list of definitions of relevant terms. Article 4.7 defines competition as "a rivalry between economic entities during which the independent actions of each of them exclude or restrict the possibility for each of them to influence unilaterally on the general conditions of circulation of commodities in the relevant commodity market."

Article 2 of the law identifies the Russian Constitution and the Civil Code as the legal foundations for the interpretation of the prohibitions. This article also explicitly relinquishes national legal sovereignty in case there are contradictions between Russian laws and international treaty obligations. This deference to international treaties is consistent across both the first draft and final versions of the text. In summary, we observe an expansion in the range of objectives and the scope of the law.

Anticompetitive agreements

Joskow et al. (1994) identified the absence of *per se* prohibitions against collusive arrangements as one of the significant shortcomings of the legal framework for the implementation of competition policy in the 1991 Law on Competition. They suggested that adoption of such rules may be necessary since industrial consolidation facilitated the ability of firms to engage in explicit or implicit anticompetitive practices. Russian lawmakers did not incorporate this insight into the treatment of anticompetitive agreements until the adoption of the 2006 legislation.

Pittman (1998) identified a second feature of the Russian laws in their separate legal treatment of horizontal and vertical collusion, and the imposition of less restrictive rules on the latter. The discrimination between the two types of restrictive arrangements under Russian laws (as well as those in other Former Soviet Union (FSU) jurisdictions) resulted directly from the choices made by the SCAP in 1990. Article 6 of the 1991 Law on Competition separated the treatment of collusive arrangements across horizontal and vertical categories based on the assertion that vertical integration is usually an efficient solution to the problem of underdeveloped markets.[22] However, this issue remains controversial in the theoretical and empirical literature on industrial organization.[23]

Article 6.1 of the 1991 Law related to arrangements between competing entities or potential competitors. This article did not impose *per se* prohibitions against horizontal collusive agreements but instead allowed the state bureaucracy the competence to define what constitutes an anticompetitive collusive arrangement and to excuse particular practices based on the SCAP's perceptions of their desirability. Moreover, firms with less than 35% share of a relevant market were effectively exempt from the scope of substantive prohibitions. Hence, potential offenders had two relatively easy options to engage in horizontal collusion. First, they could organize their legal forms as to remain below this threshold level, and then engage in anticompetitive practices with implicit immunity from the scope of the standards. Alternatively, firms could engage in collusion and then attempt to convince the public authorities that their anticompetitive agreements did not aim to harm consumers, market competition, and were efficiency enhancing.

Article 6.2 on vertical collusion prohibited concerted practices between "non-competing economic entities, one of which occupies a dominant position, while the other is a supplier or buyer." The incorporation of the qualification of dominance in relation to vertical arrangements extended the rule-of-reason approach to interpreting the restrictions along a supply chain. Sahlas and

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[22] In microeconomic theory, the efficiencies defence for the presence of vertical exclusionary agreements is primarily associated with Williamson (1983). He showed that some vertical exclusionary agreements, such as those between firms, or between firms and unions, can be efficiency enhancing since they augment the institutional environment for trade in the absence of markets. In this context, vertical restraints that may otherwise look anti-competitive may in fact be efficiency enhancing solutions to a "missing market" problem.

[23] In the history of economic thought in the United States for instance, the normative conclusion that public competition laws should treat vertical restraints less suspiciously than those sustained among competitors in a product market is usually associated with arguments from the Chicago School of thought on the subject. Farrell (2005) offers a review of the debate around the so-called Chicago vertical question.

Reshetnikova (1997, 59) criticized the limited nature of the prohibitions under Article 6.2. They pointed out that under the legislative framework of the 1991 Law, "if no party to a vertical distribution agreement is in a dominant position, then such agreements can divide markets by territory or restrict the sale of competing goods."

Hay and Shleifer (1998) identified a more subtle shortcoming of the rule-of-reason approach to interpreting prohibitions against anticompetitive agreements in Russia. Some of the new enterprise owners, later labeled as the oligarchs, readily avoided the concentration measures employed as benchmarks by the competition authorities to monitor large firms. Moreover, individuals and groups intent on tunneling and self-dealing of assets easily constructed interlocking directorate structures that made it difficult for employees and investors to monitor firm ownership and cash flows. Hay and Shleifer (1998) attributed the apprehension of local and foreign investors to extend financing to distressed Russian firms despite apparently high returns to the absence of credible *per se* prohibitions against anticompetitive arrangements by firm insiders.

In addition to basic provisions against anticompetitive agreements in Article 6, the 1991 Law on Competition listed a range of remedies that fell within the competence of the SCAP and its approximately 80 territorial offices. The powers to remedy collusive agreements included the formation, reorganization, and liquidation of commercial entities (Articles 17 and 19) and approval of some direct equity investments in firms. Articles 5 and 12 further provided the bureaucracies with powers to control legally independent economic organizations by terminating or amending contracts and regulating their prices. Consequently, the laws continued to provide public institutions with a wide range of instruments to influence economic conduct including direct price and margin controls.

Article 13 further stipulated the capacity of the public administration to investigate offences by accessing accounting information, for example by entering the physical premises of a firm to obtain evidence. Article 27 established the role of the Federal agencies as the primary enforcers of the specific power to regulate agreements but provided for the possibility that private complaints by individuals, firms, or other government entities may also constitute grounds for a legal claim. This arrangement nevertheless fell short of granting private rights of access to the judicial system. Instead, the public administrators had the exclusive option to decide if reports by claimants are worthy of further investigation and allocation of resources. Consequently, only the administrative bodies were responsible for identifying and prosecuting offences in conformity with the West European tradition to designing competition law enforcement.

The 2002 draft of legislative reforms does not appear to have tried to deal with the problematic differentiation between horizontal and vertical collusion mandated by the lawmakers of the 1990s. Articles 6 and 7 of the draft version continued to distinguish between these two classes of collusive arrangements. As finally adopted in 2006, Article 8 of the law however consolidates the treatment of different classes of agreements and avoids the use of market concentration measures in defining possible offences. The lawmakers thus shifted to a *per se* approach to the treatment of anticompetitive agreements.

The legislation now formally prohibits collusive arrangements of all sorts, by both large and small firms. Under this *per se* formulation, firms retain the right to engage in cooperation, for instance in submitting a bid for a public or private procurement contract on the condition that they disclose the material elements of their relationship. Importantly, this design feature allows potential offenders to avoid liability by exercising prudent information disclosure policies, but simultaneously broadens the scope of the law to apply to all vertical and horizontal arrangements.

Article 8.2 further stipulates that: "Implementation of actions on agreement by an economic entity is not referred to concerted practices". The meaning of this clause does not seem to be clear yet and will likely require interpretation by courts, the bureaucracy, and the executive. In theory, it is easy to see that this article can be interpreted in the context of "passing on" defense when an offender simply blames its anticompetitive practices on the contractual terms in place with third parties. Although the shift in the treatment of anticompetitive agreements signals an important change in the scope and interpretation of the law, it is not certain that it can have a significant effect on collusion given the continued reliance on public enforcement mechanisms to identify and prosecute offences.

Concentrations

While the 1991 law did not function effectively as a constraint on collusion, or offer predictable rules about the boundaries of acceptable commercial agreements, it provided the state authorities with a wide range of instruments for influencing industrial structures. As its name implied, one of the original objectives of the SCAP had been to decentralize socialist monopolies and help create new economic structures. In 1995, after the rapid transformation of the ownership structure of productive assets, some legislative changes to the laws further strengthened federal powers to regulate firms with a dominant position and to monitor the ensuing merger boom. Notably though, the 1995 reforms did not deal with the issues relating to collusive arrangements operating through opaque interlocking directorate structures and hence under the concentration ratio thresholds.

The powers to regulate concentration involved two sets of rules and associated procedures. The first related to anticompetitive arrangements by large firms and the second set of rules implemented merger review provisions. Article 5 of the Law on Competition provided a long list of prohibited actions by dominant firms including those that harm buyers, limit market entry by emergent competition, or discriminate among buyers. The list was not exhaustive, providing the competence to public enforcers to identify and define new forms of abusive practices by dominant firms. Article 5.2 nevertheless mandated that abusive practices would be legal as long as the offending concentration could convincingly argue that their otherwise prohibited actions also involved some positive balancing effect (e.g. efficiency defense).

Articles 17-19 provided a basis to dissolve and reorganize private legal entities pursuant to the prohibitions against abusive practices by dominant firms. Hence, instruments to restructure industries and firms in cases when the emergence of competitive markets appeared unfeasible were available prior and during the privatization process, but were not operative to any material extent.

Recognition of the limitation of the Law on Competition with respect to controlling monopolies led to the adoption of specific statutes and executive regulations on the subject in the mid- to late 1990s. According to Slay and Capelik's (1998) study of the early development of these reforms, the changes did not alter the effective regulatory environment outside the electricity sector. A 1994 State Program reiterated the importance of restructuring large, and now mostly private, dominant incumbents in the Russian economy. This initiative ended the use of the register of large firms that employed margin controls based on self-reported production costs. However, it also provided a list of new justifications that government agencies could use to exempt otherwise illegal practices by large enterprises including considerations of social welfare and unique regional needs. The incorporation of these defenses in the regulations for interpreting the Law on Competition in the mid-1990s complemented the general efficiencies defenses instituted by the SCAP in 1991. These new exemptions also reveal the impact of two important features of Russian history in the mid-1990s, specifically the radical decline in social welfare and the strong pressures for regional autonomy.

To implement the standards, the laws formalized state powers to acquire information from potential offenders under Article 13. These powers allowed state agencies access to accounting information by dominant firms and outlined procedures for the notification of authorities about mergers and equity investments. Under Article 19.8 of the Code of Administrative Violations, failure to provide information required by public authorities was liable to fines. Article 12 of the Law on Competition also delineated a wide range of instruments available to state authorities to remedy or eliminate violations of the law, including the power to amend contracts, set prices, and transfer income resulting from an offence to the federal budget. In short, although the competition authorities did not have effective input into the privatization process, the state did not give up the formal right to regulate abusive practices by dominant firms.

The treatment of dominant firms and their regulation by competition authorities were largely unaffected by the legislative reform process in 2002-2006. The lawmakers continue to provide public enforces with the authority to influence pricing and other contractual terms in cases of dominance.

The emphasis of the law on the regulation of firms with presumed dominance may present a serious problem for innovative industries that implement new technologies. Emerging industries may initially appear dominant to authorities who rely on market share criteria and do not explicitly account for the potential of market entry as a constraint on abusive practices by dominant firms.

The evolution of Article 5 provides special insights about the aims and objectives of the lawmakers responsible for reforming the law in the 2000s. The first reading version of Article 5 stipulated that:

- “Actions (inaction) of an economic entity (group of entities) occupying a dominant position, which result or can result in prevention, restriction or elimination of competition and (or) infringe the interests of other persons shall be prohibited.”

The final version of the law removes the general characterization of prohibited practices and remains reliant on pre-set market share criteria for defining dominance. Lawmakers in fact expanded the scope of the dominance provisions by lowering the threshold level for monopoly regulation from 65% to 50% market share.

Although this headline figure may suggest an expanded scope for the concentration provisions of the law between the 1990s and 2006, Articles 5.1.1 and 5.1.2 of the new law highlight that they function mostly to enhance the power of the bureaucracy to engage in direct price regulation. The provisions suggest that competition law may still be perceived primarily as an exercise in price regulation rather than a tool for influencing market structure and behavior. Passionate arguments against the new laws by observers like Novikov (2004) are usually directed at the high degree of discretion the state institutions exercise in controlling firms that they find to be dominant. The high degree of discretion awarded to the state bureaucracy is evident in the final version of the law adopted in 2006 that contains numerous escape clauses to the 50% market share rule for dominance:

- “The position of an economic entity (except financial organizations) is recognized as dominant: 1) Whose share in the certain commodity market

> exceeds fifty per cent, if only in the course of examination of the case of violation of the antimonopoly legislation or in the course of exercising state control over economic concentration it would be established that despite the excess of the aforementioned quantity position of the economic entity in the commodity market is not dominant;
> 2) Whose share in the certain commodity market is less than fifty per cent in case the dominance of this economic entity was established by the antimonopoly authority."

The law further distinguishes between Article 6 on "Monopolistically High Price of a Commodity" and Article 7 on "Monopolistically Low Price of a Commodity". Importantly, these two articles document the hypothesis that competition regulation tends to be conceived as an instrument for public agencies to regulate the prices of firms that deviate from the norm by charging too low or too high of a price. This feature of the law suggests the persistence of state influence in price setting in the Russian economy. Financial services are generally exempt from the price regulation scheme set out in these two provisions since they are subject to industry specific regimes.

Chapter 2 of the 2006 law further details the scope of authority granted for the regulation of firms found to be dominant. For example, Article 10 prohibits the withdrawal of commodities from circulation if this leads to increased prices or imposing unprofitable contractual terms on third parties that are not economically or technologically justifiable. Article 10 also grants rights to alleged offenders to provide evidence to authorities to justify their actions as economically or technologically efficient.

In summary, the statutes continue to provide broad powers to the bureaucracy for interpreting the boundary of permissible conduct by dominant enterprises. They also allow potential violators to defend themselves against claims of anticompetitive conduct activity by presenting justification for their otherwise illegal acts. The scope for the efficiencies defense appears to have been much narrower in the first reading version of the law introduced to the Duma in 2002, which pointed out that only in exceptional circumstances firms may present evidence that justifies their otherwise illegal actions. Between the first and final versions of the legislative reforms lawmakers enhanced the flexibility of substantive standards against abusive practices by dominant enterprises that emerged from the transition process and strengthened the capacity of public enforcers to implement them.

Other refinements

The reform process that started in 2002 with the introduction of draft legislation resulted in both change and persistence in the manner in which the competition laws treat anticompetitive practices. First, we observe a shift to a *per se* approach for the treatment of horizontal and vertical collusion. These provisions apply to all firms and do not rely on the notion of dominance as captured by market concentration ratios. Second, the lawmakers retained and even enhanced the role of the laws as an instrument for the exercise of direct price regulation by the state and allow administrative agencies broad discretion to exempt otherwise illegal actions ex post. This section reviews some of the more specific procedural refinements that have emerged from the political negotiations over the laws during the 2002-2006 reform process. Specifically, I focus on what the federal administration considers important in the new legislative mandate as described in a presentation by the Federal Antimonopoly Service (FAS) in 2006.[24] Given the lack of private access to courts to enforce the federal prohibitions, the opinion of the state bureaucracy signals how formal rules and procedures are likely to translate into economic constraints on anticompetitive practices.

Although Article 5 in the 2006 law contains a broadly similar approach to the treatment of dominance as the statutes in place in the 1990s, it provides a few new details that enhance the capacity of public enforcers to deal with the well-known problems in using arbitrary threshold limits. For instance, the FAS stresses the importance of the notion of collective dominance and the long list of different classes of economic organizations outlined in Article 9. The presumption of dominance of a natural monopoly further improves the features of the law according to the bureaucracy. Importantly, under the 2006 law the FAS is given the discretion to employ dominance provisions even when a firm has a market share of less than 35%. Under the 1991 law, firms with a market share below 35% were automatically excluded from the scope of the statute.

Other important features of the 2006 law from the perspective of the bureaucracy include the widened exemptions from the general prohibitions with respect to some vertical restraints, concessions on natural resources, and for companies with less than 20% market share. Consequently, the differential treatment of horizontal and vertical collusion instituted first in the early 1990s will likely persist in practice despite the formal consolidation in the substantive treatment of anticompetitive agreements under Article 8 of the 2006 law.

Article 9 is particularly interesting since it tries to deal with the inability of the 1991 law to identify anticompetitive practices by highly competent natural persons who readily managed to exploit the numerous exclusions and market

[24] http://fas.gov.ru/english/legislation/8826.shtml

share thresholds. This Article outlines 14 different types of business partnerships that qualify as groups of persons that are theoretically subject to the prohibitions against agreements and concentration under the law. Given the heavy reliance on concentration criteria for determining dominance, it is not clear how useful the long list will be in helping the public enforcers identify offenders more effectively than before. Article 10 sets rules for non-discriminatory access to markets.

Articles 38 and 51 provide for compulsory division of economic entities in case of egregious violations and transfer of revenues gained from anticompetitive practices to the federal budget. Such provisions clearly increase the expected level of punishment against anticompetitive practices compared to the pre-set fines under the 1991 laws, which rapidly became meaningless with inflation.

Appeals against decisions of the antimonopoly authority are allowed under Article 52. The statutes however do not provide for appeals when the antimonopoly authorities fail to act. Indeed, Article 39 stipulates that the primary authority for the initiation of cases is the federal antimonopoly agency and its local branches, possibly based on complaints by private persons and organizations. Hence, the lawmakers recognized the scarcity of information facing a public bureaucracy, but still granted the agency the option to refuse or take on cases based on its wide-ranging discretion and multiplicity of objectives. This feature of the law suggests that the high level of false negative errors associated with the Russian competition regulations of the early transition period are likely to persist in the future. Much like their predecessors, the lawmakers in charge of the new laws failed to create a credible mechanism that can correct mistakes associated with the failures of public competition authorities to act against costly anticompetitive practices.

Implementation of the law

The first part of this section characterizes the organizational features of the agencies assigned the task of implementing competition laws since the late 1990s. Then we explore how the rule-of-reason approach to the regulation of concentration was practiced by the Ministry for Antimonopoly Policy (MAP) during the decision-making process which culminated in the organizational and legislative reforms of the mid-2000s. This section also includes an illustrative legal case.

Mechanism design

As detailed above, decision makers during the 1990s did not provide competition authorities under the SCAP bureaucracy with a voice in the organization of privatization and in the period immediately following its implementation. This period also witnessed a number of changes to the allocation of tasks across the bureaucracy. By 1998, dissatisfaction with a lack of credible enforcement against costly anticompetitive structures and practices resulted in a consolidation of different regulatory task under the Ministry for Antimonopoly Policy (MAP). The elevation of the competition authority to a ministry level ended with the abolition of the MAP and creation of the Federal Antimonopoly Service (FAS) in 2004. This act made the competition agency formally more independent from executive power, but it is not clear if these changes have altered the degree of political accountability of public enforcers or the effectiveness of the regime.

In terms internal organization, the FAS continues to replicate the unitary hierarchical form that Qian et. al (1999, 2006) associate with the particular model of socialist governance in the former Soviet Union. Evidence of the persistence of U-form administrative hierarchies includes the allocation of regulatory tasks across specific industrial sectors rather than functional lines in terms of different classes of prohibitions. The centralized architecture may have advantages in the application of the rule-of-reason approach, which relies heavily on exemptions to general prohibitions to determine the effective scope of the law. Regulators who specialize in learning about an industry under the given system for allocation of tasks may also be better suited to balance competition and coordination incentives in particular sectors than those focused on prosecuting anticompetitive agreements and abusive practices. However, it also implies that one office is delegated powers to monitor a given industrial sector, thus increasing the likelihood of close coordination between a public enforcer and a possible offender.[25]

Since administrative tasks remain organized along industry lines, the public enforcers in each department must balance the competing objectives set out in the statutes. As an illustration of the challenges posed in the implementation of competition law as a set of flexible standards rather than bright line rules against collusive practices, consider the basic example of the economic conflict between environmental protection and increased concentration. Protecting the environment from hazardous pollutants requires either new technologies or less output. In the absence of new technologies, a centralized authority may correctly presume that a monopolistic market structure is a substitute for environmental regulations since it increases prices and reduces output. In the Russian organizational model, one office must balance these fundamental uncertainties in deciding if an act is legal or illegal. Prohibitions against collusive agreements or abusive practices consequently have little practical meaning without the affirmative opinion of the industry-specific offices and ultimately the director of the agency.

[25] Laffont and Martimort (1998) provide a framework for describing the trade-offs between centralized and decentralized regulatory mechanisms in the presence of asymmetric information between regulators and the regulated.

Moreover, the absence of overlapping jurisdictions within the public enforcement system clearly makes it easy to block the flow of information about potentially costly anticompetitive practices by members of lower level offices. This design feature is consistent with the lack of private standing rights to enforce the prohibitions. Private enforcement could compensate for the failure of public enforcers to act in instances when they do not have the required information about the illegal practices or incentives to pursue them effectively. Similarly, instituting offices with overlapping jurisdiction could limit the credibility of each bargain between the responsible office and the industries it aims to regulate and potentially increase the transaction costs of capture described by Laffont and Martimort (1998).

Administrative practice

This section details the manner in which the public administration interpreted its mandate and prioritized its resources after the financial crises and political transition of the late 1990s. All data relate to the practices of the MAP made public in communications with the Organization for Economic Development and Cooperation (OECD). More recent or disaggregate data in terms of information that would help identify the resources allocated to different industries or the size distribution of the targeted firms are unfortunately not available to the public. Table 5 documents the human and financial resources made available to the MAP after its creation in 1998 and Table 6 shows the level of activities by public enforcers across different classes of prohibitions.

Table 5
Resources for Public Enforcers in Russia

	Persons-year	Budget (Mil. RBL)
2002	1822	310
2001	1857	320
2000	1857	230
1999	1907	137
Source OECD (2004)		

Table 6 Regulatory Activity in Russia						
	2000 A	B	2001 A	B	2002 A	B
Agreements	45	9	45	10	74	26
State action	2386	633	2442	252	3110	707
Mergers	15974	4000	20992	5071	24030	3307
Abuse of dominance	2478	438	3129	538	3566	451
Unfair competition	310	111	343	45	345	80
Source: OECD (2004) A: Matters considered, B: Formal sanctions by MAP						

Table 5 suggests that despite the formal proclamation to raise the profile of competition enforcement by amalgamating a number of functions within the MAP, there were no significant changes to the human resources available for the detection and punishment of offences. Latest human resource data from FAS pertaining to 2005 suggest that the number of employees has remained around 1800, with 350 people in the central office and the remainder distributed across 75 regional offices. On the other hand, the overall expenditures of the bureaucracy increased following the transition in executive power in 2000 supporting claims about enhanced political impetus for developing a more active competition policy regime. Since the number of employees has remained more or less the same, it may be possible to surmise that the increased funds intended to increase the power of incentives for public servants to engage in their tasks diligently. However, given the presence of significant inflationary pressures during the 1990s, the changes in the total budget may have been simply an attempt at indexation with little expected real incentive effects. In terms of the absolute number of investigations and imposed sanctions, the data indicate a rise across all categories of instruments after the increases in funding. Since the numbers of employees did not change in any material way, this observation suggests that the MAP responded to higher-powered incentives in terms of increasing its output.

Significantly, the increased number of investigations did not result in changes to the success rates of the administration to impose sanctions. While most of the bureaucratic resources were channeled through merger and abuse of dominance instruments, the rate of sanctions imposed varied little across the legal categories. The administrators imposed sanctions in a remarkably consistent number of collusion, merger, abuse of dominance, and even unfair competition cases (in about a quarter of all investigations). This fact may be the result of incentive structures within industry specific teams to produce a targeted numbers of investigations and impose a targeted ratio of sanctions.

Tables 5 and 6 on resources and activities allow for an evaluation of the practical relevance of the different classes of legal prohibitions prior to the legislative and organizational reforms of the mid-2000s. The MAP did not deploy much of its resources as constraints against collusive agreements or unfair competition. Instead, a large number of investigations and sanctions were imposed under the abuse of dominant position, merger review and state action provisions. This pattern of practice supports the legal analysis of the features of the regulations that evolved in the 1990s. The rule-of-reason approach made prohibitions against anticompetitive agreements inoperable. The lawmakers instead equipped state administrators with a wide range of instruments to punish, or excuse, abuses by the emerging private oligarchy. The emphasis on state action provisions reflects persistent concerns about the fragmentation of the national economy and efforts by local governments to afford anticompetitive preferences to some firms.[26]

The violation numbers relating to mergers notably include failures to inform the bureaucracy about proposed equity transactions even in the case of smaller firms without economic dominance. Since the MAP was also responsible for functioning as a corporate securities regulator during the period studied here, many of the actions reported under merger control practice pertained to the wide range of financial transactions that required reporting under this sector-specific mandate of the agency. Consequently, it is difficult to describe merger control procedures without more detailed information. Given the documented difficulties in making standards against collusive agreements operative under the 1991 competition statute, it is not be surprising that the agency focused on measures that require establishing dominance. Under the first iteration of the competition laws, once the administration identified an entity as a concentration, the public enforcers had a broad scope for action. The rest of this section illustrates the difficulties present in the implementation of competition law as an instrument primarily used to control the market conduct of large enterprises rather than as a set of predictable *per se* prohibitions against collusive and exclusionary agreements.

Illustration: Rosgosstrakh versus Ministry of Antimonopoly Policy[27]

In 2004 the Moscow Court of Arbitration ruled on an appeal by a group of insurance companies against orders of The Ministry of the Russian Federation for

[26] See Slinko et al. (2004) for an analysis of regulatory preferences granted local governments and its impact on productivity across Russian regions.
[27] Case # 40-20887/04-94-211

Antimonopoly Policy and Support to Entrepreneurship (MAP), the predecessor to the current FAS. The case involved a statement of defense from PLC Rosgosstrakh against an order by the MAP based on findings that this entity had engaged in concerted practices to exclude competitors and restrain competition in the property, casualty and life insurance market in the Republic of Bashkortostan. Since the MAP had been abolished by the time of the appeal, the FAS acted as the respondent to the statement of defense by the firms targeted by the administrative decision.

The first class of evidence used in the finding relates to the special nature of the anticompetitive practices addressed in the original administrative order by the MAP. Following a routine notification of a proposed equity transaction the MAP became suspicious of the presence of restrictive practices by a number of natural persons and corporations. The investigation yielded a wide range of documentary evidence about the practice of appointing members to the board of directors of competing firms without adequate disclosure to their existing owners in order to influence them to enter exclusive vertical distribution contracts with the colluding entities. Essentially, this body of evidence clearly documented the identities and methods of certain individuals and firms aiming to restrain trade in a relatively small regional market. It also shows the intimate connection between horizontal and vertical anticompetitive practices.

Given the lack of *per se* prohibitions regarding collusive arrangements, the Court ruled that this first body of evidence about interlocking directorate structures and failure to disclose the linkages between board appointees was technically insufficient for prosecution. Consequently, the MAP had to find a way to prosecute the case under Article 6 of the 1991 Law on Competition on anticompetitive agreements by dominant enterprises. By defining the relevant market as the Republic of Bashkortostan, they managed to accomplish just that and the Court upheld the order against the offenders.

This case highlights a difficulty in the design of competition law in terms of the rule-of-reason regulation of concentrations. Here, the necessity of proving dominance motivates the narrow and economically arbitrary definition of the relevant market (i.e. The Republic of Bashkortostan) used by the MAP and accepted by the Court. If the relevant market were constructed in regional or national terms, the structural measures would clearly not have produced the necessary threshold concentration ratios. Consequently, the activities of the offenders would have been legal under the competition regime operative during the formative days of the Russian market system in the mid- to late 1990s. The shift to broader *per se* prohibitions against collusion under the 2006 statute detailed earlier may reflect this important weakness in designing competition law as an instrument for implementing complex standards against dominant firms.

Summary of findings and implications

The collapse of employment and production in Central and Eastern Europe in the late 1980s and early 1990s motivated the adoption of broadly similar trade and financial liberalization policies across jurisdictions. As part of these measures lawmakers also implemented laws that prohibited anticompetitive agreements and abusive practices in the market systems that were to emerge. Existing literature suggests a certain degree of heterogeneity in the design of competition laws operative during the formative stages of market development in these jurisdictions (Pittman, 1998 and Varady, 1999). Past studies have also shown that active competition policies were instrumental in shaping divergent market outcomes in the region (Dutz and Vagliasindi, 2000). This paper explored the interaction between state and market institutions that shaped the boundaries of permissible conduct by focusing on the Russian experience with the adoption, implementation and reform of competition regulations since the political and economic transition of the early 1990s.

Economists have long justified the need for effective competition laws in the Russian Federation by documenting increases in industrial concentration ratios and the presence of an oligarchy. This view emphasizes the distribution of usage rights as the source of economic decline in post-Soviet Russia. Heller (1998) and Buchanan and Yoon (2000) have further argued that persistent underdevelopment after privatization may have been caused by the presence of too many exclusion rights in the property regime that evolved in Russia (e.g. the problem of anti-commons).

The growth of large enterprises and increased disparities in the ownership of productive capacity partly explains the impetus for legislative reform in 2002-2006. This paper contributed to the literature by documenting that the legacy of early transition policies also created a market system characterized by a relatively high degree of price setting power by incumbent firms. Ironically, the same surveys suggest that owners and managers of enterprises did not appear to consider anticompetitive practices as a relatively significant constraint to the growth of their operations.

Given the exclusion of the competition authorities from the privatization process in the early to mid-1990s and the policy of privatization before industrial restructuring, it seems reasonable to contend that the lack of effective prohibitions under the 1991 Law on Competition played a role as a determinant of the observed economic outcomes.

The depiction of competition law mainly in terms of an antimonopoly mandate by the state appears to have persisted in the reconfiguration of statutes and enforcement agencies in the 2000s. The Federal Antimonopoly Service remains the exclusive enforcer of the constitutional and statutory prohibitions against anticompetitive practices, and retains a wide range of instruments to implement competition policy by balancing competing considerations in particular sectors and industries. Despite the changes to the name and formal mandate of the bureaucracy, a substantive reorganization of the enforcement agency did not materialize during the reform process. Legislative bargaining that led to the 2006 statute also failed to allow private access rights to general purpose or specialized courts to enforce the new *per se* prohibitions against collusive arrangements.

Overall, the analysis of the post-socialist regime for the regulation of anticompetitive practices in Russia suggests a great deal of persistence in the primary substantive and procedural mechanisms for implementing constitutional prohibitions against anticompetitive practices. A notable exception to this rule is the legislation of relatively broad prohibitions against collusive agreements in the 2006 statutory mandate. The appeal of bright-line rules in terms of a higher degree of predictability and their lower information requirements relative to complex standards help explain this shift in the design of regulations against anticompetitive agreements.

Given the novelty of the 2006 Law on Protection of Competition, there is little evidence to assess what these changes mean in practice as constraints on the behavior of market participants. Because of the persistence of the administrative architecture and the legacy of the rule-of-reason design strategy, it is plausible to expect that the adoption of *per se* prohibitions against collusion will remain formal for sometime to come. Given the legal and economic experience described in this paper, it seems prudent not to overestimate the implications of subtle statutory changes embedded in the 2006 legislation.

Lawmakers can of course resort to a second mechanism for channeling investments into the implementation of legal constraints against anticompetitive practices. Much like Russia during the past 15 years, public enforcement of prohibitions against anticompetitive practices in the U.S. prior to World War II had been sporadic as federal administrators and prosecutors tried to apply a rule-of-reason approach that aimed to balance competing policy objectives.[28] As the U.S. economy began to recover after WWII, the responsibility for enforcing the prohibitions rapidly shifted to the private sector and the Federal bureaucracy started to specialize in merger control. With increased enforceability, *per se* prohibitions against collusion became an integral part of the legal environment for the regulation of private contractual relations. In the Russian case,

[28] See Cole and Ohanian (2004) for an analysis of the dilemmas in the implementation of competition regulation in the United States during the 1930s and associated economic problems. Carlton (2007) reviews recent efforts to change substantive and procedural elements of the Sherman Antitrust regime that evolved after World War II.

experimentation with a mixed public-private enforcement regime will have to wait for further action by lawmakers and the constituencies that support them.[29]

In terms of broader debates about the role of competition law in developing and transition economies, the Russian experience suggests that these jurisdictions may be prudent to revisit the statutes they first adopted in the 1980s and 1990s. As detailed by Palim (1998) and Maher (2002) the new regimes were typically adopted during times of significant financial and political difficulty and with assistance by networks of international experts. As such, many of the new competition regimes implement a rule-of-reason design strategy. Some observers of competition law in developing countries have argued that such a flexible approach is necessary because it allows for an optimization of competition and coordination of incentives depending on the requirements of particular sectors (Singh, 2002). This analysis highlights that while flexibility may be a virtue in terms of lower false positives (Type I errors), clear and predictable per se prohibitions may place more credible constraints against costly anticompetitive practices (Type II errors).

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[29] See Becker (1968), Becker and Stigler (1974), and Friedman (1984) for basic models that capture the limitations of purely public regimes for enforcement of law and regulation.

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