

# Russian Corruption

A Literature Review and Comparison to the Principle-Agent Model: Size, Form, and Scope

By Ian Bogley

## 1. Introduction

Corruption is a core issue of Russian politics, being used as both a mechanism of power as well as representing a debilitating weakness. A diverse literature has studied how Russian President Vladimir Putin has used bribery and the distribution of state assets to maintain control over a country in which the rule of law is weak. (Dawisha, 2015; Lansky and Myles-Primakoff, 2018) The Russian Federation currently ranks 129<sup>th</sup> out of 180 countries according to the Corruption Perceptions Index published by Transparency International. Even before Putin, corruption has been a well-studied topic with respect to the Russian Federation's predecessor, the Soviet Union. (Favarel-Garrigues, 2011; Feldbrugge, 1984; Grossman, 1977)

There are several aspects of Russia which make it susceptible to corruption. The fact that it is well endowed with natural resources leaves it vulnerable to the Dutch Disease, encouraging investment into capital-heavy projects while diverting attention from other sectors of the economy. Even today, Russia is extremely dependent on oil for government revenues and economic stability. The nature of these capital-based projects allows owners to greatly diminish the official price of resources and assets, sell their product, and pocket the profits privately. A prime example of this is the notorious Loans for Shares scheme, in which multiple state companies with near monopolistic control over several natural resources were loaned to wealthy businessmen at extremely low prices in return for the political support of Boris Yeltsin, never to be returned. The owners of these companies would go on to become the new class of Russian oligarchs, a group of wealthy businessmen who used their authority to personally enrich themselves.

However, corruption in Russia is not relegated to the highest levels of power. Bribery is often used to protect access to resources and markets in private business, and to circumnavigate issues in daily life, creating a system structurally dependent on corruption to function. The judicial and enforcement agencies have also taken part, further reducing the legitimacy and stability of societal structure in Russian daily life.

The purpose of this article is to clearly define the shape and prevalence of corruption in the realm of Russian politics, business, and daily life. Section 2 describes the extent of bribery from a macroeconomic perspective, section 3 focuses on the form in which corruption reveals itself in different sectors of Russian life. Section 4 focuses on how prevalent acts of bribery across Russian business, politics, and everyday life. Section 5 describes previous efforts at anti-corruption, the state of mechanisms traditionally shown to check corruption, and recommended cures from external organizations. Section 6 concludes.

## 2. Size

Estimates for total corruption in Russia vary. In 2016, Lieutenant General Andrei Kurnosenko described the amount of annual bribery to be around 298 billion Rubles (5.1 billion USD at the time).<sup>1</sup> In 2010, then-Russian president Dmitry Medvedev's administration estimated the total amount of funds lost through public procurement alone to be around one trillion Rubles (30 billion USD at the time). Another independent report by Milov et al. estimated the total amount of corruption to be closer to 25 percent of Russian GNP in 2010.

While the 1990's are well known to be an era of chaos and corruption in Russia, decade's worth of neglect has increased the magnitude of corruption. Recent numbers from the Prosecutor-General's

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<sup>1</sup> <https://www.nbcnews.com/news/world/russian-bribe-jumps-75-percent-anti-corruption-tsar-tells-newspaper-n734246>

office show that in the first half of 2020, Russia experienced 24,500 cases of alleged corruption,<sup>2</sup> more than the entire number of cases in either 1990 or 2009. (Milov et. al, 2011) This shows how the lack of effective anti-corruption measures have allowed unprecedented spread throughout Russia.

### 3. Form

Many observers have stated that the political structure in Russia is built on corruption. While anti-corruption measures are used on a consistent basis, the selective use to deter Putin's adversaries has been a trademark for his extended reign over the past two decades. One prominent example is the now-defunct Yukos Oil and Gas company, formerly run by an original oligarch named Mikhail Khodorkovsky. Originally a state-owned entity, it was sold to the Khodorkovsky in 1995 under the Loans for Shares scheme. After criticism of and political conflict with Putin, Khodorkovsky and several other shareholders were arrested on tax and corruption charges, prompting a severe drop in the stock price of Yukos and eventual bankruptcy on the back of tax evasion charges. The assets associated with Yukos were auctioned to Rosneft, a separate Russian state-owned company, ensuring greater control over Russia's vital oil supply by the state and Putin's administration.

In comparing this with the models of corruption studied in class, the process of privatization mimics the theft and sale of state properties. Extraordinary circumstances force the value of a company to fall, forcing their sale to other actors at lower prices. Another issue that we studied is that of political agency, which illuminates how electoral incentives can discipline the actions of politicians towards policy and actions which benefit their electorate. However, the efforts of the Russian government to stifle political opposition, censor news media, subvert the electoral process, and ban non-governmental organizations creates hinderances to political discipline.

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<sup>2</sup> <https://www.rferl.org/a/russia-corruption-cases-increase/31436556.html>

## 4. Scope

One issue in Russian corruption is its pervasive existence throughout everyday life, business, and politics. The 2016 Global Corruption Barometer for East and Central Asia surveyed 1507 Russians in early 2016, finding that 27 percent of them had paid a bribe to use a public service over the previous 12 months, and 29 percent engaged in bribery relating to education.<sup>3</sup> Business leaders and organizations are required to keep in favor with regional players or face a dysfunctional bureaucracy and selectively enforced legal system. Even worse, personal connections and bribery are mechanisms through which the current regime maintains power. With everyone in the country participating in illegal activities, there is a multitude of evidence against political players, and those that don't conform or threaten the central power figures are tried using corruption charges.

We can use the principal-agent model to show how the choices of individuals are shaped by this context, as the incentives to engage in extra-judicial racketeering are stuck in a self-reinforcing equilibrium of corruption. Weak institutions and common criminal practice have lessened the disincentives facing local officials, further perpetuating the system. Moreover, the non-benevolent principal view works well, as the bureaucracy is fraught with long and complicated processes which can be softened with well-placed parcels of cash. The introduction of red tape allows bureaucrats to maximize bribery revenue, while avoiding serious punitive measures due to the prevalence of corruption and lack of external oversight.

## 5. Previous and Potential Cures

While anti-corruption measures have been and are currently used to marginalize Kremlin critics, there have been serious attempts at reform. Former president Dmitry Medvedev announced the Anti-Corruption Plan in 2008, which was legislation focused on clearly defining bribery, creating rigorous

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<sup>3</sup> <https://www.transparency.org/en/gcb/europe-and-central-asia/europe-central-asia-2016>

qualifications for public officials, punishing those found guilty through fines, and streamlining the process of reporting corruption.<sup>4</sup> While the plan was updated in 2010, by 2011 it was a self-described failure.<sup>5</sup>

The efforts of Medvedev show that incremental structural change is needed to fight corruption in Russia. This is made difficult by the fact that several of the necessary ingredients for civilian oversight of the issue run against the core structure of the system. To avoid political opposition, Putin's regime has systematically eroded civil liberties through censorship in the media, elimination of political opponents through violence and legal charges, and persecution of non-governmental organizations.<sup>6</sup> Without these checks on government power, the system is reliant on political and economic elites for reform. Under threat from social instability via the emergence of Alexei Navalny and widespread protests, escalation of tensions with the west after the annexation of Crimea, and the rapid spread of COVID-19, it appears that in the near future, Putin's regime must remain in the current high corruption equilibrium to maintain control over political and economic elites.

One possibility for reducing current corruption comes from the principal agent models we studied in class. In theory, increasing public official wages closer to an 'efficiency wage' should reduce the need for raising funds through bribery. This is backed up by Schulze et. al (2016), who find that increasing wages relative to private sector alternatives does indeed reduce corruption.

## 6. Conclusion

Russia is a perfect example of the corruption models we have studied theoretically in class. It gives credence to the idea of efficiency wages in lieu of institutional incentives, it shows the models of bureaucrats using theft of state assets to personally enrich themselves and exemplifies how a country

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<sup>4</sup> <http://www.kremlin.ru/events/councils/996>

<sup>5</sup> <https://www.apnnews.com/russian-president-admits-failure-in-fighting-corruption/>

<sup>6</sup> <https://www.hrw.org/russia-government-against-rights-groups-battle-chronicle#>

like this one can become stuck in a self-reinforcing state of pervasive corruption. With the distribution of state power focused on keeping state actors in line through selective enforcement of the legal system and persecution of potential rivals, it is difficult to see a way out of Russia's current predicament. Serious anti-corruption measures at the top levels of government may weaken Putin's administration, while the other elites have no incentive for incremental reform under a system which benefits them. Potential civilian oversight has been diminished through the erosion of civil liberties and civilian organizations, leaving Russia in a dangerous position which necessitates keeping both elites and the general population happy under an inefficient system ripe with theft and corruption.

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