COORDINATION ISSUES IN RUSSIA'S PRIVATIZATION PROGRAM

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Executive Summary: Coordination Issues in Russia’s Privatization Program

Russian privatization has presented complex issues of coordination, which have been magnified by the attempt to carry out rapid privatization in a context of sharply divergent interest-group representation. Centralization of the privatization decision-making process facilitated the rapid privatization pace that Yeltsin’s reformers wanted, but it did not produce the results that had been anticipated when the objectives of privatization were developed.

Shortly after economic reforms began under Yeltsin, it became apparent that outside pressures on both the legislature and the Yeltsin government would importantly shape the privatization initiative. As the privatization program evolved, Russia’s lawmakers were significantly influenced by the perspectives of enterprise personnel and the administrative bodies that coordinate and supervise enterprises slated for privatization. Yeltsin’s strategists were swayed by the advice of foreign participants in the economic reform arena, as well as by pressures from within Russia.

As the overall scheme of privatization decision-making was conceived, property management committees were structured to represent the interests of the executive branch at each administrative level, from federal to municipal; and property funds, also to be established at each level of administration, were to represent the interests of the legislature. Initially, the interests of the executive and legislative branches were widely regarded as being complementary in terms of the two criteria for reform that were thought the most critical—that privatization should proceed rapidly and that it should be carried out in a way that would improve the country’s economic performance. Ultimately, however, the executive and legislative branches sharply disagreed about the importance of both of these criteria.

During 1993 we interviewed a variety of “stakeholders” in the Russian privatization debate—property management committee and property fund officials, officials in local administrations and soviets, and directors of enterprises that were at different stages of the privatization process. We carried out research which informs this report in Moscow, Ekaterinburg, Voronezh and Smolensk.

We found strong evidence that the divergent interests at every administrative level in Russia contributed importantly to the privatization program’s coordination difficulties. Many local problems among property management committees, property funds, city administrations and city soviets were related to the breakdown of constructive deliberation between Yeltsin’s planners and Russian lawmakers in Moscow. Our research indicated that the property management committee structure is characterized by a high level of compliance with federal-level directives. This administrative hierarchy in the executive branch repeatedly produced conflicts at lower levels. The disadvantage most frequently noted by our respondents to the rigidity of privatization decision-making was that, by enforcing compliance at the local level
with directives from the center, variations among regions and enterprises were not adequately taken into account, and that this flaw was working against effective privatization.

The rapid pace of privatization has been a major issue in all three of our research cities that were operating under the state privatization program. (Moscow is not following the state program.) Tension between those who were especially concerned with privatization efficiency and others whose overriding interest was in the pace of privatization created inevitable conflict. Demands that privatization be carried out through procedures that would stabilize and improve the faltering production system came from many sources, including many members of the Congress of People’s Deputies, local soviets, local property funds, industrial ministries and a number of enterprise directors.

There have been clear winners and losers in Russia’s privatization effort. A number of powerful financial groups have acquired enterprise shares through voucher speculation. Individuals who had liquid assets that were available for investment following price liberalization in January 1992 have been presented with extraordinary opportunities, as have many members of the old Communist Party nomenklatura who have taken advantage of their positions and power to secure valuable assets for themselves. A number of enterprise directors have found themselves strategically placed to acquire control over state property. New business startups have been disappointingly few, however, since the beginning of the privatization program. Russia’s production system has been severely weakened, and the lives of most Russian people have worsened dramatically since the privatization program was initiated—an outcome, we suggest, that is partially attributable to shortcomings of the privatization program itself.

A point of “irreversibility” of reforms has not been reached. The demand for better coordination in Russia’s privatization effort is becoming more urgent, and some of the changes that seem most likely would be at variance with the course of privatization under Chubais.

Serious deficiencies of the privatization program headed by Chubais indicate that major corrective measures are needed. The program’s most fundamental objectives are not being achieved, in most cases. There is strong evidence that critical coordination questions have been neglected by Yeltsin’s reformers. The goals of different stakeholders are often both nontransparent and fluid, and recognition of the complexity of reform objectives and strategies in Russia is a prerequisite to informed policy-making by the US government. Further, analyses of the historical record of foreign policy decisionmaking, and findings from the scholarly literature concerning the biasing effects of closely-held theories, suggest that discussions of issues regarding Russian privatization among US government officials should include a range of perspectives and interpretations that extends well beyond those of stakeholders whose personal or corporate interests are tied to a particular foreign policy outcome.
Coordination Issues in Russia's Privatization Program

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Coordination Issues in Russia’s Privatization Program

Introduction

In October 1991, when Boris Yeltsin asked the RSFSR Congress of People’s Deputies to give him special emergency powers to carry out economic reform, he stated his reasons for the request. First, he said, economic reform would be hard, and he needed extraordinary authority to maintain the reform course during the months when life would be more difficult for nearly everyone. Further, Yeltsin insisted, it was important to preclude the possibility that local governments in Russia might interfere with decisions at the state level. At the same time that Yeltsin was calling for strengthened executive power with a resolutely vertical authority structure, he also emphasized that the work of the parliament and the executive branch would be closely coordinated. ¹After four days of intense discussion, the Congress voted to grant Yeltsin the emergency powers he had requested.

It was not long, however, before clear signs appeared that the expected cooperation among the executive and legislative branches would prove to be elusive. Only 11 days after price liberalization was introduced at the beginning of 1992, Supreme Soviet chairman Ruslan Khasbulatov, speaking to a delegation of Italian senators, said that Yeltsin’s government ministers were proving to be unqualified and might have to be replaced. Already, Khasbulatov was having second thoughts about the parliament’s decision to grant Yeltsin the emergency powers he had requested 10 weeks earlier. What had caused the rapid turnaround in Khasbulatov’s perspective? Most prices had been freed, and after only a few days many citizens were already questioning Yeltsin’s October promise that people’s lives would begin to improve by the next autumn. The initial jolt had been too severe, and the objections of prominent Russian economists to the “shock therapy” idea too urgent, to sustain the unqualified acceptance of Yeltsin’s course that followed from his stance during the August putsch. Khasbulatov’s rapid reversal in January may have been due to a visit he had just made to workers in the city of Riazan. Speaking of this visit, and a similar reversal by Aleksandr Rutskoi after meeting with workers in Siberia, correspondent Nikolai Bodnaruk described the emerging new mood as “populism.”² Whatever its source, this conspicuous crack in the wall of support for Yeltsin’s reform policy was a warning for the future.

Interest Groups and Privatization Policy

These mixed messages in the first days of Yeltsin's reforms highlight the most fundamental coordination issue that has faced Russia's economic reformers. Whose interests, and whose visions for the future, should be most closely heeded as the reform program unfolded? Even among Yeltsin's top strategists, Russia's economic reforms did not begin with a detailed blueprint of how reform should proceed. As Dmitrii Vasilev, a vice-chairman of the State Property Management Committee, told us in the summer, 1992, "We have changed our position over time, partly because of political compromise, and partly because we have learned more about the situation." The reform program that evolved from 1991 onward was even more vaguely apprehended by Russia's lawmakers and Russia's citizens as it was being formulated and as implementation began. Public opinion studies showed strong public support for transition to a market economy. But no one knew how to achieve that goal, and they had accepted Yeltsin's strategy largely on faith. Inevitably, however, outside pressures on both the legislature and Yeltsin's planners were soon felt. The parliament was lobbied heavily by enterprise directors, labor unions, and members of the central planning apparatus. It increasingly responded to pressure from these groups, as well as from growing dissatisfaction among the population with the results of reform. And the executive branch was being urged by foreign advisers to follow the economic strategy that they favored.

In a recent article entitled "The Politics of Russian Privatization," two economic advisers to the executive branch in Russia, Andrei Shleifer and Maxim Boycko, characterize as "stakeholders" the people and groups within Russia who "have existing ownership rights, in the sense of being able to effectively exercise control rights over assets." Their paper is devoted to describing the claims of important stakeholders inside Russia today: executive and legislative branches (including branch ministries), enterprise directors, workers, and the public. 3

An adequate inquiry into the politics of Russian privatization, however, must also consider two additional sets of actors in Russian privatization planning. First, a large number of people and organizations within Russia who work outside the domain of the state enterprise system have a clear stake in privatization. Some, such as financial groups and voucher speculators, have been afforded new moneymaking opportunities through voucher privatization,

as have a number of Russian investors who are interested in acquiring ownership in some of the more desirable properties that are being privatized. Other entrepreneurs have entered the privatization debate in the hope of benefiting indirectly, through more favorable legislation, from the reform climate that prevailed in Russia after the breakup of the Soviet Union.

Further, outside Russia a number of financial institutions, G-7 political leaders and foreign advisers have emphasized their stakeholder interests in Russian reform. In a 1991 Foreign Affairs article, for example, Graham Allison and Robert Blackwill summarize aspects of "America's Stake in the Soviet Future." "The fixed point for our compass must be U.S. interests," they begin. In arguing that the United States should participate in "affect[ing] the outcome of the Soviet domestic struggle," they maintain, "Having spent some five trillion dollars to meet the military challenge of the Soviet Union around the globe, is the United States (and its allies) to opt out now when the Soviet future is being formed?" This theme was prominent in the Window of Opportunity report prepared for the heads of government of the Soviet Union, the United States, and other G-7 heads of state. In his introduction to the document, Allison emphasizes the West's "strategic stakes in Soviet reform." But the "grand bargain" that was proposed by Allison, Russian economist Grigorii Yavlinskii, and others was clearly aimed at furthering the national interests of all countries involved in these discussions—the Soviet Union and G-7 nations. Allison summarized the core of the "bargain" being attempted: "The path of economic transformation Soviet leaders can choose and reasonably hope to succeed in following depends critically on the extent of Western support. Simultaneously, the extent of Western support depends critically on the program of economic reform that the Soviet Union is prepared to choose and follow."

But events that came after the Window of Opportunity report had been completed would fundamentally alter the equation and reshuffle the players in these discussions. We will suggest in a future paper that emphasis on mutual interests among all national parties, which had been a prominent feature of the deliberations surrounding the Window of Opportunity report, was replaced by a new form of dialogue after Gorbachev's resignation and after a number of new

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5 Ibid., 93-4.
participants took key positions in the discussions between Russia and G-7 nations during late 1991 and early 1992. In this next phase, Western interests would be pursued more aggressively, largely unconstrained (now that the USSR had collapsed and Russia's economy was in free-fall) by the former requirement to balance Western and Soviet interests as strategies for Russian economic reform were developed.

A number of outside players in this new phase would solidify personal and corporate stakeholder interests in Russian reform as their proposals were considered and their services to the Russian government provided both professional recognition and financial rewards. Private firms would come on the scene to offer expertise of various types to facilitate Russian economic reform. These activities would often be funded with U.S. dollars — particularly from the U.S. Agency for International Development (USAID). Often, the funding levels for this work have been quite large, as, for example, when the Washington, DC, Sawyer/Miller Group received $7 million to develop a television advertising campaign to promote privatization, and when KPMG Peat Marwick was awarded $98 million in contracts to work with privatized businesses, and when an Arlington, Va., consulting firm, Haglar Bailly, received a $20 million contract to "help privatize Russian utilities and encourage them to install U.S.-made equipment," according to a Wall Street Journal report. The potential bonanza that U.S.-approved Russian privatization made available for consulting firms quickly became obvious as USAID money began to flow. As John Fialka of The Wall Street Journal put it in February 1994, "With so much aid money involved, there has already been a veritable feeding frenzy in Washington," and he adds that USAID "says 1,200 consultants applied to get into the program, a record for the 33-year-old agency."

It is important to note that not all stakeholders within the interest-group categories we have identified have spoken with a unified voice. Especially among enterprise directors, interests have often diverged sharply. "The directors' corps have the most complicated assortment of motives among all of those whose interests are affected by privatization," Vasilev told us, at a time that the privatization of large enterprises was under intensive discussion. "That is because some directors think that they would benefit more by preservation of the command system, while others see greater opportunities in a market environment. One group of directors wants to become the de facto owners of their enterprises, while another

8 Ibid.
group fears negative effects from losing state patronage and Central Bank credits. Some favor ownership among workers’ collectives, and others anticipate benefits from outside investment."

Similarly, changes in the cast of participants in economic planning discussions have critically altered the relative prominence of different perspectives that have been presented to Russian policymakers.9 Further, the relative influence of different stakeholders, both Russian and foreign, has varied through time. Of enormous significance for the future direction of Russian economic reform, for example, was the replacement of Yavlinskii by Egor Gaidar as Russia’s chief economic strategist in the autumn of 1991. Gaidar’s ideas had been endorsed by Swedish economist and former diplomat to the USSR, Anders Åslund,10 and Gaidar’s ascendancy also gave Åslund a leading voice in the direction of Russian economic reform, along with Harvard University’s Jeffrey Sachs. Gaidar developed the main themes of Yeltsin’s October 28, 1991 speech to the Fifth Congress of People’s Deputies, in which price liberalization was announced to initiate the Yeltsin government’s economic program. Sachs and Åslund concurred; Yavlinskii did not. And Yavlinskii’s recommendations diverged markedly from the path Gaidar’s team chose to follow.

In sum, interest group representation has critically influenced the direction of Russia’s economic reforms and the priorities of the privatization initiative. Russia’s lawmakers, at least before the Congress of People’s Deputies was dissolved, have been particularly swayed by the claims of enterprise personnel and the administrative bodies that coordinate and supervise enterprises slated for privatization. Yeltsin’s economic planners, on the other hand, have preferred the advice of foreign participants in the economic reform arena to that of Russian economists and stakeholders in Russia with direct claims on Russian property. Below, we examine processes through which these different interest groups have influenced coordination of privatization among bodies that are responsible for supervising, planning and implementing privatization in Russia.

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9 A significant component of this fluidity has been the changing composition of the Congress of People’s Deputies from 1992 onward, as Yeltsin invited many lawmakers who backed his initiatives to join the executive branch. In that way, the Congress lost between 70 and 100 deputies who could probably have been counted on to support most of Yeltsin’s policies—and whose voices, in many cases, had persuasive influence that is inadequately reflected in these numbers.

The Structure of Coordination and Authority in the Privatization Program

Of course, political cross-currents were nothing new to Russian leaders in the waning days of the Soviet era, and when the RSFSR Supreme Soviet drafted its early privatization legislation in 1991, it built into the structure being created a system of checks to prevent the interests of either the executive or the legislature from becoming dominant. The lawmakers were experienced in the pitfalls of a system where deputies were empowered by law but thoroughly dominated by the executive branch, as had been the case before Gorbachev's political reforms. Thus, as the overall scheme of privatization decision-making was conceived, property management committees were structured to represent the interests of the executive branch at each administrative level, from federal to municipal; and property funds, also to be established at each level of administration, were to represent the interests of the legislature. The soviet at each level was to create the property fund for that level, which was to be comprised of full-time government employees. The property funds were conceived as the sole authorized seller of property being privatized at their level. They were to hold the ownership certificate for an enterprise until shares of the enterprise property were distributed either to enterprise personnel or outside shareholders. In cases in which not all shares of an enterprise were to be distributed, property funds were to be considered the government's representatives in shareholder meetings.

Initially, the interests of the executive and legislative branches were widely regarded as being complementary in terms of the two criteria for reform that were regarded as being the most critical -- that privatization should proceed rapidly and that it should be carried out in a way that would improve the country's economic performance. We return to these points in a later section of this paper, where we outline the considerations that led the executive and legislative branches to diverge and ultimately sharply disagree about the importance of both of these criteria.

The legal basis for the Russian privatization program was articulated in the law On Privatization of State and Municipal Enterprises that was passed by the RSFSR Supreme Soviet

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11 The Federal Property Fund was to be under the authority of the Russian Supreme Soviet.
12 A property fund's responsibility for an enterprise's activity was to be in direct proportion to the percentage of a firm's shares that had not been distributed, up to 20 percent. Elsewhere, we elaborate in more detail about the functions of property management committees, property funds and privatization commissions. See Lynn D. Nelson and Irina Y. Kuzes, Property to the People: The Struggle for Radical Economic Reform in Russia (Armonk, N.Y.: M.E. Sharpe, 1994), 121-25.
on July 3, 1991. This law also specified an organizational structure for carrying out privatization, under the guidance of the State Property Management Committee of the Russian Federation. Local agencies of the State Property Management Committee were to be created in all of the major administrative divisions of Russia (republics, krais, oblasts, autonomous okrugs, and cities with populations of more than one million). This organizational plan closely resembled the structure of administrative authority in the Russian Federation, and was thus intended from the beginning to assure centralized control over the privatization process. At the same time, separate property management committees were to be organized in each of these administrative divisions which would carry out the daily work of privatization -- largely implementation -- in contrast to the task of the local agencies of the State Committee, which was to be largely supervisory.

As they were originally envisioned, the local agencies of the State Property Management Committee were intended to not only supervise the privatization process but also investigate any violations of the state plan at lower levels -- thus insuring complete hierarchical control of the privatization process being directed from the executive branch in Moscow. But this structure proved to be unwieldy, largely because separate property management committee units at the local level were unable, in reality, to maintain the intended division between supervision and implementation functions. As a rule, then, the property management bodies that were developed below the federal level were responsible for both supervising local decisions, based on state guidelines, and for implementing privatization program directives. At every level, property management committees detailed the specific procedures through which the objectives of the state program were to be realized at that level. The state program established priorities for privatization according to sector of economic activities at different stages of the privatization program, for example; and lower-level property management committees identified specific enterprises within their sphere of authority which were to be privatized. Recommendations of the lower-level property management committees about which enterprises would be privatized at specific stages had to be approved by the corresponding soviets.

Property management committees below the federal level were charged by the Supreme Soviet with making decisions about the privatization of enterprises at their level,\textsuperscript{14} and their chairmen were to be vice-heads of the government at that level. The privatization plan for an enterprise was to be submitted for approval to a privatization commission. These commissions were to be created by property management committees at each level of government to review plans for privatizing enterprises at that level. The chairman of each privatization commission was to be on the staff of the related property management committee.

During 1993 we interviewed 105 property management committee officials and 41 property fund personnel in our four research locations who served at the okrug, city and oblast levels. We also interviewed 171 privatization officials in the same four cities during 1992,\textsuperscript{15} as well as observing selected privatization committee meetings. Our 1993 inquiry into the work of property management officials also was carried out among 88 officials in local administrations and soviets,\textsuperscript{16} and 583 directors of enterprises that were at various stages of the privatization process. (In 1992 we interviewed 966 directors.) In selecting the samples of privatization and city officials, our strategy was to identify for interview the most prominent and influential members of these bodies. (Eleven percent refused to be interviewed.) Our 1993 sample of directors includes all production enterprises that had begun or completed privatization by June 1993 in Voronezh and Smolensk, most in Ekaterinburg, and about half of the Moscow total. In this paper we include a number of excerpts from our interviews with these respondents.\textsuperscript{17} In selecting this illustrative material, we consistently attempted to choose statements that represented the characteristic viewpoints and positions which a particular subset of respondents voiced about the particular issue being discussed. This approach has the disadvantage of failing to highlight the full range of positions and views among our respondents, but if it is consistently followed offers the advantage of reflecting the overall trends in our data.

\textsuperscript{14} These decisions may be appealed in court or through arbitration.
\textsuperscript{15} Among these 171 respondents, we reinterviewed 38 in 1993. A large proportion of the privatization decision-makers at work in 1993 had not held their positions a year earlier.
\textsuperscript{16} The n's were 48 and 40, respectively.
\textsuperscript{17} Some details have been changed in the narrative to protect confidentiality.
Stakeholding among Local Officials

We found, in interviews with local privatization officials, that there were a large number of coordination problems involving various units linked together in privatization decision-making, and that frequently those problems interfered significantly with the privatization process (Table 1, page 24). But there is a qualitative difference, of course, between the kinds of coordination problems that result from micro-level organizational inadequacies and those that stem from the larger strategies and objectives of the various stakeholders in Russian privatization. Below, we focus on this second set of problems.

One of the most frequently-voiced complaints among our respondents in property management committees, property funds, and administrations and soviets of local governments was that voucher privatization impeded the task of coordinating the transition from state to non-state ownership. These officials preferred other forms of privatization by a large margin (Table 2, page 25).

Local soviets and administrations in several regions attempted to stop voucher auctions. This effort was based, they insisted, on the need to serve the interests of people in their cities and oblasts. A property fund official in Smolensk told us, "Our city soviet made several decisions which contradict Yeltsin's decree [authorizing voucher auctions]. One was that they decided not to put some of the designated enterprises up for auction. They sometimes thought that the pace of privatization was too fast to ensure that necessary products would still be available locally. The privatization of a bread factory was stopped, for example, because the deputies believed that, after privatization, there wouldn't be any bread." But a property management committee member in Smolensk explained the outcome of that conflict. "We have a major conflict with the local soviet about the list of enterprises to be privatized. They wanted to shorten it. But we are going to proceed with the original list." A Voronezh property management committee official said that her committee disagreed with the local soviet about several aspects of privatization. "They think privatization is too fast, too encompassing, and harmful to the enterprises," she noted. "But we will not deviate from our plan."

We found evidence that resistance to privatization among local administrations was not always based on concerns for community welfare. In some cases, a major factor which contributed to their dissatisfaction with the privatization program was a desire to retain their longstanding control over enterprises. An official in the Voronezh city property fund, whose job was to prepare enterprises for auctioning, observed, "We are experiencing very serious conflict with the local administration. They want to keep the most efficient enterprises under their supervision. They are attempting to slow down privatization of enterprises. At the same
time they are pressuring workers to change their decision about which variant of privatization to choose, how to distribute shares, and who will manage the enterprise. The main theme here is that the administration wants to retain as much control as possible. When we learn that an enterprise’s final privatization plan was influenced too much by local authorities, we either negotiate revisions of the privatization plan or stop the process entirely." A member of the Voronezh oblast property fund stated this point emphatically. "Local soviets and the local administration often try to prevent large enterprises from privatizing in order to preserve 'the state property' from being lost." A Smolensk oblast property management committee member told us, "The chairman of our committee is too subservient to the oblast soviet. He reports to them. And they don't actually understand the privatization process. In their minds, by slowing privatization they are preserving state property from being plundered."

This was the problem that Yeltsin highlighted most pointedly in requesting emergency powers in October 1991. Subsequent developments indicated that this concern was justified -- and not just in Voronezh. In all of our research cities and oblasts, we found evidence of attempts by local administrations and soviets to delay privatization in order to retain control. This problem has been made even more thorny as issues have arisen over whether a particular property is under federal, oblast or city control as privatization begins, and in Moscow that problem is acute.

We also found, however, substantial evidence that the resistance among local stakeholders which Yeltsin had feared was often related to the breakdown of constructive deliberation between Yeltsin’s planners and Russian lawmakers in Moscow. As the Supreme Soviet turned increasingly negative about the way the State Property Management committee was directing the privatization campaign, independently of legislative efforts at oversight, local soviets tended to take the side of the Supreme Soviet. "The uncertainty about who is in charge 'at the top' makes it possible for local soviets to make decisions which contradict privatization regulations and presidential decrees," an Ekaterinburg property management committee member charged. And a number of other respondents in both property management committees and property funds pinpointed the inadequacy of attempts at coordination among federal branches as a critical source of local disputes.

**The Issue of Inflexibility**

Our research indicated that the property management committee structure is characterized by a high level of compliance with federal-level directives. Outside Moscow, exceptions to this generalization were rare in our experience and according to the reports of respondents both
within and outside the privatization decision-making structure. (A Yeltsin decree authorized Moscow officials to develop their own privatization procedure.) This administrative hierarchy in the executive branch repeatedly produced conflicts between local soviets of people's deputies and local property management committees.

The disadvantage most frequently noted by our respondents to the rigidity of privatization decision-making was that, by enforcing compliance at the local level with directives from the center, variations among regions and enterprises were not adequately taken into account, and that this flaw was working against effective privatization. A Smolensk property management official complained to us that "the center should not plan the percentage of enterprises in each sector are to be privatized in local areas. The mix of enterprises is too different from place to place." A Moscow privatization official went further. "There isn't any coordination between the State Property Management Committee and local authorities," he charged. An Ekaterinburg (Sverdlovsk oblast) official concurred, stating, "They [the State Property Management Committee] are eager to decide everything by themselves. They are not taking local interests into account."

The State Committee's unwillingness to allow a large measure of discretion in privatization decision-making below the federal level probably accelerated the pace of privatization of smaller, non-federal enterprises; and rapid privatization was an important objective of privatization planners. But about 60 percent of the large production enterprises that were undergoing privatization in 1993 were federal property, and according to the privatization program the State Committee was required to directly oversee privatization of federal-level enterprises. Even Filippov, who strongly supported the privatization program, faulted this approach. He was concerned that not enough enterprises were offering shares for voucher auction. "The reason for that is excessive centralization of the procedure" for privatizing large enterprises. Filippov insisted.18

Privatization Pace and Concern with Economic Improvement

The rapid pace of privatization was a major issue in all three of our research cities that were operating under the state privatization program. Chubias is directing the program, and justifying its rapid pace, according to an assumption he stated with conviction in our August 1993 interview. "We have had a narrow window of opportunity," he emphasized. "The

18 Petr Filippov, "Chto meshaet 'otovarit' ' privatizatsionnyi chek," Ekonomika i zhizn', no. 37 (September 1993), 10.
parliament started to accept the idea in 1991, but their support faded entirely by the end of 1992." As Chubais saw the situation, if privatization were to be accomplished at all, it would have to be made "irreversible" before the legislature had the opportunity to derail the process.

The idea of "irreversibility" is important to all the reform planners we have interviewed. But when we have pressed for clarification about how a point of "irreversibility" could be identified, or what its defining characteristics would be, responses usually have been nonspecific. But clearly, a guiding principle of the privatization planners has been to move quickly to take advantage of what has been judged to be a short-term opportunity, and thereby to so emphatically dismember the command system that it can never be reconstituted.

"Rapid privatization creates problems," Chubais told us in 1993, "but a slower pace would create more problems." Chubais' position was wholly consistent with the priorities for economic reform that had been articulated by the Yeltsin government's "Economic Policy Memorandum" in February 1992. Written expressly for the International Monetary Fund, this document included a pointed assurance to the IMF that the privatization process would be "considerably speeded up." The reformers' view, that Russian privatization could succeed only if it were rapid, meshed fully with their perceptions about how to meet the IMF's expectations, and thereby increase the likelihood of IMF membership and the opportunity to use Fund-provided resources.

This tension between concern with privatization efficiency and the overriding concern about pace of privatization among government planners created inevitable conflict. Demands that privatization be carried out through procedures that would stabilize and improve the faltering production system came from many sources. In addition to many members of the Congress of People's Deputies, local soviets, and local property funds, it was also widely held among industrial ministries and a number of enterprise directors, that reform should proceed deliberately. Surgery was urgently needed, they argued, to save the Russian economy from further decline, but the surgery should not kill the patient.

Federal-level executives, however, saw privatization as the starting point for economic reform. Eliminating state control over the production system was a necessary precondition, they maintained, for healthy economic development. The "Economic Strategy of the Russian Government," which was issued a month after the "Economic Policy Memorandum,"

19 "Osnovnye napravleniia ekononicheskoi politki Rossiiskoi Federatsii," Kommersant', no. 9 (24 February-2 March, 1992), 22.
20 "Repurchases," in the Fund's terminology, of a member country's soft currency in exchange for hard currency.
underscored this strategy. "We are striving to create a market economy based on private property," the report stated.21 Once ownership of enterprises was transferred into private hands, they believed, real economic reform could begin. This perspective was prominent among foreign advisers to the Yeltsin reformers. Anders Åslund, for example, insists that "the immediate tasks in systematic change in a formerly socialist economy are liberalisation and macroeconomic stabilization." And Åslund's perspective on the efficiency concerns of many of our local officials is that an "extraordinary emphasis on production" is merely a manifestation of "old Marxist values."22

Our respondents did not speak of Marxist values in this regard. Rather, their concerns centered around the ability of enterprises to adapt to the changing economic environment and the necessity, with rapid privatization, for enterprise executives to make administrative decisions for which they were not prepared. A number of officials decried the State Committee's inattention to adequate preparation of enterprises and their personnel for the conditions privatization was quickly creating. According to a property fund official in Ekaterinburg, "The pace of privatization is impeding the development of a business environment that can sustain the privatizing enterprises." Among the property management committee members we interviewed in 1993 -- officials who are directly subordinate to Chubais's State Committee -- a higher percentage judged the then-current pace of privatization to be too rapid (29 percent) than thought that it should be speeded-up (25 percent). Among our property fund respondents, the differential was markedly greater. Fourteen percent of those privatization officials believed that the pace should be quickened. Thirty-three percent believed that the pace should be slowed.

Our results indicate substantial support, however, for the then-current pace of privatization. Thirty-nine percent of property management committee officials thought that no change of pace was needed,23 and among property fund officials the corresponding percentage was 44.24 We repeatedly found divergent perspectives about this issue among members of the same committees and funds, and in our interview we probed in a variety of ways for

21 "Ekonomicheskaia strategiia pravitel'stva Rossii" (part 3), Biznes, Banki, Birzha, no. 14 (1992), 1.
23 Seven percent were undecided.
24 Forty-four percent were satisfied with the then-current pace, and eight percent were undecided.
information that would help us to understand the incompatibilities reflected in the officials’
views about the pace of privatization. In studying the officials’ responses to a large number of
queries during these 45-minute interviews, we identified one characteristic that clearly
differentiated a large number of those who wanted the pace of privatization to be slowed from
many who gave other answers, and that was the thoughtfulness that was reflected in their
responses.

A Voronezh official who believed that privatization’s pace was too rapid argued,
"Privatization needs to be slowed down because the old economic mechanisms are being
destroyed too quickly, and replacements are not being developed." Another suggested, "People
are not psychologically prepared for privatization now. Thus, as it is being carried out now, it
is nothing but a formal act." A Smolensk property management committee member said,
"Privatization needs to be slower, so that the business environment of each enterprise can be
evaluated, and privatization carried out in light of each firm’s particular situation." And a
Moscow official worried that "the legal basis for privatized enterprises is not being provided
with the current rate of privatization." "The vehicle to carry out economic reform has turned
out to be a squanderer of state property," a Moscow property fund member insisted. And
several officials leveled the charge made by a Moscow district property management committee
member: "Today, people are being pushed into privatization the same way they were pushed
into collective farms in another time." An administrator in a Moscow prefecture stated the
point clearly. "We are having serious conflicts with territorial agencies of the Moscow
Property Management committee. They are trying to privatize enterprises as quickly as they
can, and we are trying to preserve the infrastructure. Services and goods are needed after
privatization, and that is our concern." An official in a different okrug prefecture concurred.
"Our people are members of several privatization commissions," she stated, "and they often
complain about experiencing very strong pressure from privatization agencies to make quick
decisions -- not thoughtful, but quick. Such decisions can’t help but lead to negative results."
Such concerns were voiced repeatedly among officials we interviewed in local administrations.

Another property fund member in Voronezh told us that the local property management
committee was accepting assessments of enterprises’ value that were too low, for the purpose
of speeding-up privatization. As the economics chairman of the fund, he was concerned that
these low assessments were having negative consequences. "The low assessments increase the
likelihood that privatization will proceed quickly," he noted. "and they pave the way for either
enterprise workers or an outsider to acquire shares at bargain prices. But in the process the
state is deprived of needed revenue and the enterprise loses a chance for a more deliberate
property transfer that could improve its efficiency."
Justifications for the status quo, or arguments that the pace of privatization should be accelerated, characteristically were phrased in the terms used by the Chubais team, and without the elaborated details that often accompanied the views of officials who were concerned that the pace of privatization was too rapid. A member of the Ekaterinburg property management committee, for example, said, "The fast transition of state property into the hands of owners will become the basis for efficient production." He provided us with no information, however, about how pace and efficiency would be connected in a positive way. "A new class of owners"; "to get to the market as quickly as possible"; "to make the economic situation better." These were typical of the answers provided by officials who favored rapid privatization. "The longer the process the worse the result," a Smolensk property management committee declared.

The Role of Branch Ministries and Departments

During the Soviet period, ministries were at the heart of the economic bureaucracy. Some have been eliminated, and some have been consolidated and restructured. A number of ministries and "departments" remain important to supervision and coordination in the production system at every administrative level. The stakeholder interests of these ministries and departments have become an increasingly important factor in privatization negotiations as the privatization of production enterprises has replaced "small privatization" as the main focus of the privatization effort.

Branch ministries and departments are often reluctant to relinquish their control and planning functions. As a property management committee official in Smolensk put it, "Branch ministries and departments are trying to get their enterprises out of privatization. They especially oppose privatization that breaks up production chains." In a similar vein, branch ministries tend to object to the provision in the state privatization program which permits departments within an enterprise to privatize separately from the larger enterprise. A transportation department of an industrial enterprise, for example, could apply for privatization -- forcing the enterprise to negotiate for transportation services with independent enterprises and thereby increasing their costs. In early 1994, Filippov admitted that the government's provision which would allow departments of enterprises to privatize separately had not been very successful. "All of our attempts to break up enterprises into smaller units . . . have not produced the desired result yet. We will probably have to make some hard decisions, and to
establish progressive taxation on enterprise income according to the number of workers," he added.\textsuperscript{25}

Several officials told us that a strategy of branch ministries is that, if they fail to prevent transformation of enterprises under their authority into joint stock companies, they then attempt to acquire enough shares to be able to control the firms after privatization. Holding companies provide a means of achieving that purpose, and branch ministries often support the proposal to create these umbrella organizations. Opponents of the idea see holding companies as vehicles for preventing competition and to prevent unemployment and production cuts.\textsuperscript{26} Proponents of the idea argue, however, that holding companies would facilitate better coordination and thus improved economic performance.

The State Property Management Committee recognized the potential of branch ministries to modify the Committee’s privatization plans. According to the 1992 privatization program, ministry approval was required for the privatization of some enterprises. Additionally, there was evidence that ministries sometimes were trying to maintain control over certain federal-level enterprises that were being transformed into joint stock companies by retaining 51 percent of the enterprises’ shares. And it was thought within the Committee that, as Vasilev phrased it, ministries wanted "to restore a command economy."\textsuperscript{27} A Yeltsin decree on May 8, 1993, authorized the State Property Management Committee to circumvent the ministries’ authority in many situations.\textsuperscript{28} The Supreme Soviet attempted to prevent the implementation of this decree by appealing its legality to the Constitutional Court. Their basis was clear and persuasive. Yeltsin’s emergency powers had expired in December 1992. The Congress of People’s Deputies had not renewed them. Yeltsin now had no legal right to continue ruling by decree. On July 22, 1993 the Supreme Soviet decided that the authority to supervise the privatization of federal property would now belong to the Council of Ministers. They had given the State Property Management Committee that authority in December 1991, but increasing dissatisfaction with the course and results of privatization caused the lawmakers to reconsider

\textsuperscript{25} Petr Filippov, "Kuda poshel protsess?"
\textsuperscript{26} See, for example, Andrei Shleifer and Maxim Boycko, "The Politics of Russian Privatization," 78-9.
\textsuperscript{27} Igor’ Karpenko, "Programma privatizatsii 1993 goda: sub’ekty federatsii trebuiut vnesti v nee ser’eznye izmeneniia," Izvestiia, no. 93 (20 May 1993), 4.
\textsuperscript{28} "O gosudarstvennykh garantiyakh prava grazhdan Rossii na uchastie v privatizatsii," Ekonomika i zhizn’, no. 20 (May 1993), 15.
and change that arrangement. This decision directly overrode Yeltsin’s May 8 decree which was intended to strengthen the State Property Committee’s hand over ministries.\textsuperscript{29}

Chubais’s reaction was immediate. “The interests of tens of millions of people have been squandered in secret -- behind their backs -- for the political aims of the leaders of the Supreme Soviet and the intransigent, frenzied opposition forces who back them.”\textsuperscript{30} Chubais was attempting to deflect attention away from the important practical and legal issues that had been highlighted. The response of Vladimir Mazaev (then Chairman of the Commission on Economic Reform of the Russian Supreme Soviet) was unequivocal. The Supreme Soviet is not trying to stop privatization. Yeltsin’s decree contradicts the law, Mazaev insisted; and the Supreme Soviet is correct to question the results of privatization as it is now being carried out.

Four days later, just after Yeltsin returned to Moscow, Chubais called a press conference to announce a new Yeltsin decree. This decree repeated the message of Yeltsin’s May 8 decree that the Supreme Soviet had overturned. Informsing those present that the May 8 decree had already been sent to property management committees throughout Russia, Chubais added, “The only change that we have made . . . [is that], whereas the first one stated, ‘In accordance with Presidential Decree No. 640,’ it now reads ‘In accordance with Presidential Decree No. 1108 . . .’”\textsuperscript{31}

\textbf{A Coordination Crisis within the Executive Branch}

Chubais’s defiant public stance could not contain the internal discord that was building within the executive branch, also, during the summer of 1993. And by the end of August, even Yeltsin had been persuaded to consider major changes in the privatization program. Oleg Lobov, who then headed the Ministry of Economics, discussed problems that he and his staff in the Ministry of Economics saw with voucher privatization. Lobov outlined a different approach which he believed would overcome some of the disadvantages of the voucher

\textsuperscript{29} See Mikhail Berger, "Chem grozit pokushenie na vaucher," Izvestiia, no. 135 (21 July 1993), 2; and Ol’ga Berezhnaia, "Deputaty namereny vernut’ gosimushchestvo ministerstvam,” Moskovskie novosti, no. 30 (25 July 1993), 1.

\textsuperscript{30} Igor’ Karpenko, “Parlament pytaetsia otniat’ u naroda pravo vladet’ svoei sobstvennost’iu,” Izvestiia, no. 136 (22 July 1993), 1.

\textsuperscript{31} Igor’ Karpenko, “Protsess privatizatsii vosstanovlen,” Izvestiia, no. 140 (28 July 1993), 2.
program. Yeltsin responded, in writing, "I support this submitted proposal in principle. I ask that the draft for a decree be submitted within 10 days."\(^{32}\)

On September 3, Lobov held a press conference to discuss his ideas. He suggested that the continuing decline in production necessitated a change in Russia’s privatization program. Lobov was unhappy that such a high percentage of state property was being privatized with vouchers, which provided neither enterprises nor the state with needed money. It is important for privatization to be not only a mechanism for changing ownership, Lobov argued, but also a means to reduce the federal budget deficit and provide enterprises with needed capital.

Remembering the "500 Days" proposal, Lobov noted that the idea of selling state property rather than giving a large proportion of it away at no charge had a solid basis in Russian economic reform planning.\(^{33}\)

Lobov’s press conference came at a critical time in the unfolding of Russia’s voucher privatization effort. Many of Russia’s most valuable and productive assets, including major oil and gas enterprises, had not yet been privatized. But now, the time was near for some of Russia’s biggest prizes to be transferred out of state hands. Further, a number of large production enterprises which badly needed modernization were about to lose state subsidies, as they were privatized, that had allowed them to continue operating. Lobov’s idea would either forestall privatization for those companies, if investors were unwilling to pay for shares with cash as opposed to vouchers, or at least bring in needed capital, if they should be sold according to Lobov’s plan. As Lobov knew well, the Supreme Soviet had never approved voucher privatization, and Yeltsin’s authority to continue operating the program by decree had expired.

Two days later Chubais appeared on "Ostankino" television. His back was against the wall, and he knew it. We had met with Chubais only a few days earlier, and he was obviously worried. It was being widely rumored in Moscow that Chubais’s office might soon be vacant. We thought that his chances for survival, this time, were not good; and he seemed to concur. It had not helped Chubais’s cause that a variety of other opinion leaders had quickly rallied behind Lubov. A number of prominent and influential Russian economists supported Lobov’s


proposal. And Moscow's mayor, Yuri Luzhkov declared, "Chubais's privatization qualifies as a crime against city management."34

Chubais responded to Luzhkov on Russian television by accusing Luzhkov and his administration of corruption. He answered Lobov uncompromisingly, insisting that the proposal Lobov had presented was "unacceptable from beginning to end."35 But it soon appeared that Chubais had lost, this time. On September 7, a draft document was published in Nezavisimaia gazeta which called for radical changes in the privatization process, along the lines that Lobov had outlined in his press conference.36 But by September 11 Yeltsin was hedging on the Lobov proposal. He charged Chernomyrdin with the task of meeting with Lobov and Chubais and creating "a common position regarding the proposal of the Economics Ministry directed to implement changes in the current privatization procedure."37 Chernomyrdin had just returned from Washington, DC, where he was trying to secure an agreement to postpone payment on Russia's debts.

The potential for outsider interests in such situations to be expressed in the form of open pressure to follow a particular reform course is underscored in a series of events that followed. On September 13, US Treasury Secretary Lloyd Bentsen cautioned, "There has been slowing down in some areas. That is certainly a concern."38 That day, the Senate Foreign Relations Committee approved a $2.5 billion foreign aid bill for the former Soviet Union, most of which was for Russia. The next day, an under secretary for international affairs at the US Treasury Department, Lawrence Summers, arrived in Moscow. The previous week, Summers had told the US Foreign Relations Committee, "The battle for economic reform in Russia has now entered a new and critical phase in which many of Russia's accomplishments on the economic front are being put at risk. The momentum for Russian reform must be reinvigorated and intensified to ensure sustained multilateral support."39 And Jeffrey Sachs, Harvard professor and then-adviser to the Russian government, warned on September 15 that the drift in the

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36 Ibid.
39 Ibid. Emphasis added.
Russian government was "dreadful," and added, "Things are dead in the water." They were not for long. The next day Yeltsin announced that Gaidar would return, replacing Lobov in the Ministry of Economics. Five days later Yeltsin disbanded Russia's Congress of People's Deputies.

Conclusions

We began this paper by referring to several "stakeholders" in Russian privatization -- people and groups with interests in Russian economic reform. Some groups inside Russia have benefited substantially from the direction of Russian privatization under Chubais's leadership. A number of powerful financial groups have acquired enterprise shares through voucher speculation. Individuals who had liquid assets that were available for investment following price liberalization in January 1992, and there were not many, have been presented with extraordinary opportunities. Many members of the old Communist Party nomenklatura have taken advantage of their positions and power in this time of economic disorder to secure valuable assets for themselves and their associates, and many local officials have also broadened their power in privatization decision-making. A number of enterprise directors have found themselves strategically placed to transfer the control of state property into their own hands. Russians with an entrepreneurial spirit but lacking nomenklatura connections or large sums of money have had less success. New business startups have been disappointingly few since the beginning of the privatization program, and governmental inattention to this critical area has been conspicuous during most of the period since late 1991. Russia's production system, once mighty, has been severely weakened. By the end of 1993, production had declined to 59 percent of its 1990 level, and the severity of economic hardship being endured by Russia's population had been well-documented. The lives of most Russian people have worsened dramatically since 1991, and public opinion research shows that most are fully aware that the promised "social safety net" has not been provided.

The hardship experienced by Russia's citizens has spawned ultranationalist backlash and put at risk fundamental social and cultural institutions. Anti-Western, especially anti-American,

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sentiment has spread rapidly. This sharp turn in public opinion has been fed by both ultranationalism and a large number of mass media analyses in prominent Russian newspapers and journals which suggest a direct link between the economic and military interests of foreign governments and firms, on the one hand, and the rapid deterioration of Russia's economy, on the other.

Recent political developments and the continuing vitality of key elements of the command system demonstrate unambiguously that a point of "irreversibility" of reforms, which has been a prominent justification for rapid privatization, has not been reached. The new privatization program which was approved by a Yeltsin decree on December 24, 1993, for example, gives branch ministries even more control over enterprises than had been the case earlier.43

The branch ministries' proposal for a network of holding companies to smooth coordination among certain production enterprises seems to be gaining momentum, as is their view that the number of enterprises eligible for privatization in some economic sectors should be restricted. They also want to replace standardized privatization procedures with approaches that take into account the particulars of an enterprise and its environment. This would reverse Chubais's emphasis on pace of privatization over considerations of efficiency, and it would decidedly slow the privatization process. Industrial lobbies have favored these innovations for many months, and growing concern over the problems which have accompanied rapid privatization have made these ideas more appealing within the Council of Ministers. Thus, while the demand for better coordination in Russia's privatization effort is becoming more urgent, some, at least, of the changes that seem most likely would be at variance with the course of privatization under Chubais.

Policy Implications for the United States Government

Serious deficiencies of the Russian privatization program indicate that major corrective measures are needed. The program's most fundamental stated objectives are not being achieved in most cases. An important reason, we have concluded, has been the unrealistically rapid pace of privatization in Russia. The objectives stated in the privatization program are important, and they have been neglected in the rush to privatize as quickly as possible. Further, privatization's

43 See "O Gosudarstvennoi programme privatizatsii gosudarstvennykh i munitsipal'nykh predpriiatii v Rossii," and "Gosudarstvennaia programma privatizatsii gosudarstvennykh i munitsipal'nykh predpriiatii v Rossii," "Ekonomika i zhizn'," no. 2 (January 1994), 1, 4-10.
rapid pace has exacerbated coordination problems among agencies and organizations involved in privatization. These problems would be challenging under the best of circumstances, but there is strong evidence that critical coordination questions have been neglected by Yeltsin's reformers. Opposition to Chubais's program, and to the tight control over privatization that his State Property Management Committee has enjoyed, need not signify opposition to constructive economic reform of the Russian economy. Under conditions of rapid change, the strategies of interest groups are played out in a context of divergent priorities and crosscutting loyalties. The real goals of these groups are often both nontransparent and fluid, and recognition of the complexity of reform objectives and strategies in Russia is a prerequisite to informed policymaking the US government. The Russian economic reform debate cannot be accurately viewed as simply a struggle between the Yeltsin reformers and a unitary opposition group that is intent on derailing reforms.

Recently, issues surrounding Russian economic reform have been more informed in the West by the interpretations of advisers and consultants who have themselves been directly involved in Russian privatization than by analysts without a personal or corporate stake in a particular reform course. Yet, there is a substantial scholarly literature on the general biasing effects among scientists of closely-held theories, and on the added burden to objectivity when scholar-advisers apply their theoretical ideas to questions of policy. Additional evidence from the analysis of US foreign policy decisions of the past, such as the Bay of Pigs invasion planned by President John F. Kennedy and his advisers, underscores the critical importance of ensuring a diversity of perspectives in foreign policy deliberations. An important implication of these findings for discussions among US government officials regarding Russian

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privatization merits emphasis. Whether deliberations are concerned with assessing the course of reforms until now, or with exploring possible forms of ongoing participation by the US government in Russian economic planning, the range of perspectives and interpretations that are included in such analysis should deliberately extend beyond that of stakeholders whose personal or corporate interests are tied to a particular foreign policy outcome.\(^{46}\)

\[^{46}\text{See, for example, Irving L. Janis,} \textit{Groupthink: Psychological Studies of Policy Decisions and Fiascoes} (Boston: Houghton Mifflin, 1983).\]
Table 1: Perceived Seriousness of Coordination Problems between Units Involved in Privatization, by Respondent's Organization Type

| Unit Linkages (Percentages Who Responded that there Were Significant Problems [First Subheading] and that the Problems Have Interfered with Privatization [Second Subheading]) | Organization Type |
|---|---|---|
| | Property Mgmt. | Property Committee Fund |
| Respondent's agency and other privatization decision-making bodies | | |
| Coordination problems significant | 55.9 | 59.5 |
| (Column n) | (93) | (37) |
| Probs. have interfered w/priv. | 75.0 | 90.5 |
| (Column n) | (52) | (21) |
| Privatization agencies and federal government ministries | | |
| Coordination problems significant | 50.6 | 40.7 |
| (Column n) | (79) | (27) |
| Probs. have interfered w/priv. | 78.0 | 61.5 |
| (Column n) | (41) | (13) |
| Privatization decision-making bodies (committees, funds, commissions) and privatizing enterprises | | |
| Coordination problems significant | 71.6 | 55.3 |
| (Column n) | (102) | (38) |
| Probs. have interfered w/priv. | 69.7 | 65.0 |
| (Column n) | (66) | (20) |

*aIn this table, respondents were not asked whether or not the particular coordination problem "has interfered with the privatization process in your experience" if they had answered, earlier, that the problems of coordination between the units in question was "not serious at all" or that "there are no problems in this area."

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<tr>
<td>Voucher auctions</td>
<td>22.2</td>
<td>12.1</td>
<td>28.6</td>
<td>20.0</td>
<td>17.0</td>
<td>22.5</td>
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<tr>
<td>Transfer of ownership to enterprise personnel</td>
<td>13.1</td>
<td>9.1</td>
<td>0.0</td>
<td>40.0</td>
<td>21.3</td>
<td>7.5</td>
</tr>
<tr>
<td>Sale of shares to interested buyers</td>
<td>40.4</td>
<td>66.7</td>
<td>50.0</td>
<td>33.3</td>
<td>17.0</td>
<td>37.5</td>
</tr>
<tr>
<td>Opposes privatizing large prod. enterprises</td>
<td>11.1</td>
<td>9.1</td>
<td>21.4</td>
<td>6.7</td>
<td>29.8</td>
<td>25.0</td>
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<tr>
<td>Uncertain</td>
<td>13.1</td>
<td>3.0</td>
<td>0.0</td>
<td>0.0</td>
<td>14.9</td>
<td>7.5</td>
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<td>(Column n)</td>
<td>(99)</td>
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