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DEVELOPING THE PUBLIC PROCUREMENT SYSTEM IN THE POST-SOVIET AND MODERN RUSSIA: CHALLENGES AND OPPORTUNITIES

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The paper analyses transformation of Russian public procurement system in the past 25 years. The focus is given to building up the new institutional environment and the main tools and mechanisms of interaction on the emerging quasi-markets. The impact of the international procurement experience, the heritage of Soviet administrative control system as well as macroeconomic and regional factors and social-and-political interests upon procurement regulation are evaluated. The stages of concept evolution and modernization of the regulatory framework in this field are presented from the prospective of the economic policy. Some controversial aspects of regulating the public procurement system and the effect upon conduct of public and municipal customers and suppliers are highlighted. The ideological rationale of the market reforms is identified as aimed at preventing corruption and enhancing the public spending efficiency. It drives a regulatory transition from the industrial policy measures to the policy of competition protection and stimulation, and determines adopting new public procurement technologies to fit the evolving approaches. The authors conclude that the controversies in public procurement are rooted in the basic legal concepts and frameworks that hardly meet the needs of economic agents. Evolution of the institutional environment of the public procurement market proves a low self-control level by the state in the modern Russia.

Keywords: *public procurement; government regulation; economic policy; effectiveness of the contractual system*

JEL classifications: *D02, H30, H57, K20*

РАЗВИТИЕ СИСТЕМЫ ГОСУДАРСТВЕННЫХ ЗАКУПОК В ПОСТСОВЕТСКОЙ РОССИИ: ВЫЗОВЫ И ВОЗМОЖНОСТИ

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В статье анализируется трансформация системы государственных закупок в постсоветской России. Основное внимание уделяется созданию новой институциональной среды, новых инструментов регулирования и механизмов взаимодействия на возникающем квазирынке. Оценивается влияние международного опыта закупок, наследия советской системы административного контроля, а также макроэкономических, региональных факторов и социально-политических интересов при регулировании сферы правительственных закупок. Подчеркиваются некоторые противоречивые аспекты регулирования системы государственных закупок и их влияние на поведение государственных и муниципальных служащих и поставщиков государства. Идеологическое обоснование рыночных реформ определяется направленностью на предотвращение коррупции и повышение эффективности государственных расходов. Это объясняет переход от промышленной политики к политике защиты и стимулирования конкуренции. Авторы заключают, что проблемы в области государственных закупок основаны на базовых правовых концепциях и структурах, которые едва ли удовлетворяют потребности экономических агентов. Эволюция институциональной среды на рынке государственных закупок свидетельствует о низком уровне самоконтроля со стороны государства в современной России.

Ключевые слова: *государственные закупки, государственное регулирование, экономическая политика, эффективность контрактной системы.*

Introduction: Public Procurement in the Swirl of the Emergency Reform

In the early 1990s, transition from centralized provision of physical resources and scheduled product supplies, customary for Soviet enterprises, to procurement under the "market conditions" in Russia was as hectic as the concurrent political transformation. Liberalization of prices, trade and foreign economic relations, freedom of entrepreneurial activity – all those reforms were pushed under the principle: "the more radical and faster – the better"[1]. The approach was typical for the countries with transitional economy, burdened by the priority of politics over economic expediency.

[1] For instance, price liberalization took place "overnight" – on 02.01.1992, when up to 90% of retail and 80% wholesale prices were exempt from government regulation (*Yasin, 2003*).

In terms of the ideology of the market reforms, absence of efficient government control over production and social aspects of the economy could be compensated by the market mechanism designed to facilitate the most efficient interaction between suppliers and consumers. The most important market function, however, is informational: channels of collecting and disseminating objective information about the "opinions" of producers, suppliers and consumers. As a result of the overrated expectations of the Russian government, top-executives of post-Soviet enterprises faced several tough problems: search for counteragents, determining market price and its predictability, competent contracting, and, finally, fulfilling their obligations by the parties to the agreements. Moreover, it had to be achieved under irregular and often unpredictable financing by the decision-makers responsible for budgetary funds.

Heavy under-financing of the government bodies and their procurement, galloping inflation that stemmed from the overnight price liberalization, mushrooming corruption against erratic formal rules and inability of public control over their execution superimposed, preventing not only efficient spending of budgetary funds but procurement in principle.

The supreme authorities saw the issue of product supplies for public needs from a different angle. With the collapse of the Soviet Union, production facilities of the common technological chain were spread out by different countries, the political leadership of which often did not find a better way to achieve political stability of their new statehood rather than a transition to the "economic nationalism" doctrine, opposing to Moscow and Russia as the former centre. Along with the growth of nationalistic sentiments it made impossible reconstruction of the old technological chains under the frame of mutually beneficial cross-country cooperation and creating products required to satisfy public needs. Product supplies from far abroad also were not established due to the significant closeness of the Russian economy from the world markets at the beginning of the 1990s. The system of public regulation of commodity flows to Russia was practically destroyed.

Introduction of domestic convertibility of the Ruble before the external one blocked the entry of Russian currency to the international currency markets and prevented demand for the national MU (*Fetisov, 2006*). It did not make sense for foreign banks to open accounts in Rubles, which additionally contributed to the exchange slump, and aggravated the position of Russian government, while public procurement depended highly on the prices for imported goods.

In the obvious government crisis it was hardly possible to enforce public procurement obligations undertaken by the contractual parties. Already at the beginning of 1991, some companies, particularly, farmers and cooperatives called upon dismissing any targets, assignments or production limits: in their opinion, all products should belong to those who produced them (*Kuzmenko, 1991*). The Arbitration Courts typically avoided such disputes, taking a wait-and-see stand (*Melnikov, 2008, p. 75*).

After the government bodies stopped setting targets on the scope and structure of production and sales turnover, firms were forced to determine the key figures on their own, based on the consumer orders and the current profit margin (*Khanin, 2012*). Producers had to independently search for solvent consumers and resources to support operational activities and capital construction. The essential component for any market-building – systematized information about manufacturers and their products – was absent, which extremely complicated the search for counteragents. The government had only one option: to decline all responsibility for production management and keep just the functions on allocating financial resources, and designate the agents responsible for satisfying public needs at a lower level of public administration.

I. Developing Contractual Relations

At that period Russia started developing new exchange mechanisms: a system of institutions determining the rules and frame of conduct for economic entities (*Volchik & Nechaev, 2015, p. 35*). New regulations dismantled the old system of material support, eliminating centralized supplies and planned economic relations[2]. New approaches to public needs were based on the following principles: 1) A contractual nature of procurement: "public / state contract" should be the main document defining the rights and responsibilities of government customers and supplies[3]; 2) fee-based relations between procurement partners; 3) payment for the goods under contractual market prices (except the goods, for which the government price regulation maintained); 4) the supply volumes depended on effective consumer demand; 5) equality of contractors regardless of the ownership form[4]; 6) equal responsibility of the procurement parties (*Nozdrachev, 1994*).

At the beginning of the 1990s, the economic element was not always in the focus of the reform. Therefore, in the transition from the system of Gosplan [the State Planning Committee of the USSR] and Gossnab [the State Logistics Committee of the USSR] to developing the category of government customers, the legislator did not pay enough attention to the monopsonic nature of the emerging market, which a priori did not imply any intensive competition between suppliers, especially under the initial partiality of the government officials. The starting condition was the critical degree of monopolization and centralization of the Russian economy (*Afanasiev, 2004*).

An idea of mandatory contracts by suppliers that had the dominant market posititon or holders of technological monopoly for particular types of production was introduced. Up to the end of the 1990s, a widespread practice of the regional regulators and municipalities was to limit procurement of products manufactured outside the area, which was related to the numerous problems generated by barter exchange, the nonpayment crisis, irregularity and unpredictability of budget financing as well as an understandable desire to counter local unemployment.

After the New Constitution of the Russian Federation was adopted (1993), it triggered radical reconsideration of the Russian legislation in its entirety, including the regulatory framework for public procurement. Due to the lack of time for strategic reform planning, any changes to the law of that period were often nominal, related to superficial terminology correction. In this context, in spite of the rich international experience in the field of public procurement and the 1993 Model Law of the United Nations Commission on International Trade Law (UNCITRAL) "On procurement of goods, works and services")[5] (in two versions - 1993 and 1994), Russian legislators were not ready to large-scale transformations in the national budgeting, which prevent basing the public procurement regulations on the UN documents.

At the end of 1994, Russia adopted a package of normative acts to develop the regulations on procurement for public needs[6]. However – considering the political crisis and the events in October 1993, Russia was already suffering from increasingly disintegrating trends caused by rejection of the policy pursued by the federal centre as well as the weak-

[2] No. 143 Order of the RSFSR President "On economic relations and supplies of goods and products in 1992" of 15.10.1991, No. 558 Decree of RSFSR Cabinet of Ministers "On organizing inventory-and-logistical support to the national economy of RSFSR in 1992" of 23.10.1991 and No. 2859-I Law of the Supreme Court of the Russian Federation "On supply of goods and products for public needs" of 28.05.1992.

[3] Contacts were supposed to achieve "the best value for money" (*McKevitt & Davis, 2016*).

[4] According to the international practice of regulating public procurement systems, small companies should play a considerable role in intensifying competition on a quasi-market; however, they also need additional support (see, for instance, *Reijonen, Tammi & Saastamoinen, 2016; Loader, 2016; Loader & Norton, 2015; Flynn & Davis, 2016,* etc.).

[5] For more details about UNCITRAL procurement laws see: http://www.uncitral.org/uncitral/ru/uncitral_texts/procurement_infrastructure.html

[6] No. 60-FZ Federal Law "On supplies of products for federal public needs" of 13.12.1994; No. 79- FZ Federal Law "On public inventory reserves" of 29.12.1994; No. 53- FZ Federal Law "On procurement and supplies of agricultural products, raw materials and food products for public needs" of 02.12.1994.

ness of the federal executive power and economic problems locally. A notorious phrase thrown by Boris Yeltsin, the then Chairman of the RSFSR Supreme Council, to the national autonomies on 6 August 1990: "Pick up as much sovereignty as you can swallow", started paying off to the full, blocking the attempts of the federal centre of Russia to control the financial resources of the regions. In terms of the public procurement system, the prevalent position was that the constituent territories of the Russian Federation had the right to determine independently what and how they should acquire for "their own" money. As a result, no common procurement law for all levels of the RF budget system was drafted to replace the obsolete 2859-I.

The new basic No. 60-FZ Federal Law of 13.12.1994 was titled "On supplies of products for federal public needs"[7], which reduced the object of regulation to federal public procurement. The Law set the common legal and economic principles of procurement operations for the federal level of the budget system. No.60-FZ Federal Law formalized the ordering procedure: at companies, organizations and agencies located in the Russian Federation, regardless of their form of ownership, through entering into government contracts; and determined liability for failure to execute them.

Researchers pointed out at the controversies of No.60-FZ Federal Law (see *Nesterovich & Smirnov, 2000; Smirnov at al., 2000*). On the one hand, it encouraged competitive order placement; on the other, the legislators were not fully confident that the market participants would observe the new law (*Shmakov, 2014*). The law contained provisions about mandatory contracts with state-run enterprises, forced placements of public procurement orders for the suppliers possessing monopolistic power. For instance, Articles 4 and 5 of the Law reflected the "carrot and sticks" principle. Article 4 is referred to as "Stimulating product supplies execution …", implying that the legislators suspected possible difficulties with translating the legal act into action. Unfortunately, the Law did not specify a mechanism for building up a national Russian system of public procurement, as announced in 1992. It was not a directly applicable law, and effectively was only a framework document that required further comprehensive refinement.

In spite of the narrower regulatory object from the outset, No.60-FZ Federal Law established an important vector for developing Russian public procurement law. The constituent territories of the Russian Federation were strongly "recommended" to apply it. It meant that regions had to adopt their statutory enactments regulating activity of office holders in the course of procurement, since similar issues of corruption and inefficient budgetary spending were also experienced at the lower administrative levels. On the other hand, the system of transfers forced local ordering parties to apply the federal law, spending the funds allocated under joint project financing using both federal budget and off-budgetary resources.

In accord with Part 4 Article 1 of No.60-FZ Federal Law, "relationship emerging due to procurement and supplies of agricultural products and food products for the federal public needs are regulated by a special law". The situation when the framework law has a restricted scope of application was a consequence of the big leveraging by the agrarian lobby in the State Duma [the lower chamber of the parliament] of that period, as a result of which public procurement on the agricultural market became regulated by a separate enactment, passed several days prior to adopting No.60-FZ Federal Law.

Due to the absence of the culture of competitive bidding in public procurement in the USSR and the Russian Federation at the beginning of the 1990s, the concept of No. 53-FZ Federal Law "On procurement and supplies of agricultural products, raw materials and food products for public needs"[8] turned out to be a system of planning rather that an attempt

[7] No. 60-FZ Federal Law "On supplies of products for federal public needs" of 13.12.1994 // Collected legislative acts of the Laws of the Russian Federation. 1994. No. 34. Art. 3540.

[8] No. 53-FZ Federal Law "On procurement and supplies of agricultural products, raw materials and food products for public needs" of 02.12.1994 // Collected legislative acts of the Laws of the Russian Federation. 1994. No. 32. Art. 3303.

to form a competitive quasi-market for public procurement. It was poorly correlated with the framework Law, which created additional hurdles for the contractual mechanism:

- a number of agricultural items were supposed to be fully procured;
- quotas were established for procurement on the guaranteed fixed prices;
- the Government of the Russian Federation had to determine the regulatory ratio between the cost of the procured raw materials and the costs of the finished products, as well as the maximum sales mark-ups on the product prices in view of the loss-free sales of the finished products.

Therefore, the regulatory acts that determined the economic order at the beginning of the 1990s as well as the political sphere demonstrated two oppositely directed trends: establishing the public procurement markets and restoring the state planning system, initially – in separate sectors of the economy.

II. Thorny Path to Anti-Corruption Enforcement

Along with other countries of the former Soviet Union, in 1995 Russia got the tools to develop the public procurement law in line with the international achievements in the procurement field[9]. The cornerstone in building up the national Russian procurement system was the Presidential Decree "On the priority measures to prevent corruption and reduce budgetary spending in public procurement"[10],[11]. The logic of establishing the regulatory framework suggests that such enactment should have the status of a federal law. Unfortunately, serious contradictions between the Parliament and the President at that period prevented adopting the document in the initially intended format[12].

No. 305 Decree of the RF President was, however, much better that the previous acts in this field. First, it postulated the importance of tendering in product procurement with public funds. Second, its application was extended to relations between suppliers and ordering parties, supported from a particular group of financing sources. Third, it directly requested executive bodies of the subjects of the Russian Federation to adjust their regulations in accord with the Decree. It also contained an Appendix on organizing public procurement of goods, works, services that for the first time specified the procedure and conditions for order placement[13]. Unlike preceding regulations, ordering parties were not required approvals from the superior bodies, which expanded the range of ordering parties significantly. Requirements for potential suppliers in public procurement were formulated. Although such wordings as "to be reliable" or "have a positive reputation" due to their ambiguity were hardly optimal for countering the level of corruption within the system, they determined potential liability of the ordering parties should they opt to work with shell companies, and promoted the general idea to grant contracts to experienced and

[9] Corruption in public procurement is rather widespread: some or other elements of it occur in all countries of the world at all times (*Khramkin, 2011; Mironov & Zhuravskaya, 2016; Auriol, Straub & Flochel, 2016; Mizoguchi & Quyen, 2014; Tucker, 2014*). In terms of economic policy, corruption is manifested in inefficient public spending since representatives of the authorities conclude contracts at overrated prices without competition. The issue tends to gain attention during economic crises, when the income of the population drops down. In the periods of economic growth and sustainable increase of household income it becomes less pronounced.

[10] No. 305 Decree of the President of the Russian Federation "On the priority measures to prevent corruption and reduce budgetary spending in public procurement" of 08.04.1997 // Collected legislative acts of the Laws of the Russian Federation. 1997. No.15. Art. 1756.

[11] It's worth analyzing the concept of "public needs" in more detail. Article 525 Part II of the Civil Code of the Russian Federation, adopted by No. 15-FZ Federal Law "On Part II of the Civil Code of the Russian Federation coming into effect" of 26.01.1996, specified that public needs were the needs of two levels: the needs of the Federation and the needs of the constituent territories of the Russian Federation. Municipal needs and municipal ordering parties, therefore, were not classified as public.

[12] It was demonstrated clearly in No. 97-FZ Federal Law "On tenders for procurement of goods, works, services for public needs" of 06.05.1999, the sense of which was transformed significantly after readings in two Chambers of the Parliament in 1999.

[13] In the absence of business practice of public procurement in Russia and lack of trained specialists in this field, the drafters did not trust that the wordings of No. 305 Presidential Decree would persuade the ordering parties to promptly start applying procurement procedures in accord with the new rules.

highly skilled suppliers. Some of those requirements were incorporated in the federal laws on procurement, adopted at a later stage.

No. 305 Decree of the RF President contained a closed list of procurement methods, with descriptions of their main characteristics and implementation technologies. The ordering parties were given a new opportunity (the right) for bid qualification to identify suppliers that meet the requirements.

The Decree introduced a new concept: of "bid validity" – a period during which a supplier was bound with the obligations to execute all conditions specified in its bid without the right to change them. A reasonable time interval for bid validity was very important for the ordering parties: it should comprise sufficient time for bids evaluation and comparison, signing the contract with the winner, and some additional "insurance" time in case the winner refused to conclude the contract so the contract could be awarded to the next bidder offering the best conditions. It was emphasized that in public procurement, ordering parties must request suppliers to submit tender security simultaneously with the bid (if the procurement sum was below 2 500 MROT[14] the ordering parties had the right to ask to provide such information). Surety had to be no more than 3% of the expected price of the government contract. A closed list of surety forms was compiled: bank guarantee, pledge, and joint surety. Possibility to ensure execution of the government contract was an additional insurance a mechanism for the ordering party at the stage of product supplies.

Between signing No. 305 Decree of the RF President and the State Duma adopting a new federal law regulating public procurement, Russia had gone through two very bad years for the economy, that were full of various events. First, Russia experienced a growing economic crisis that resulted, particularly, in sequestering the expenditure part of 1997 federal budget. Then in August 1998 the Government, which for a long time had been creating a financial pyramid refinancing external debt, announced a default. It triggered a sharp devaluation of the natural currency and soaring imported inflation, putting the import-dependent Russia at the edge of an economic catastrophe and deteriorating drastically the living conditions of the overwhelming part of the population, including the emerging middle class. Confrontation between the President, on the one hand, and the State Duma controlled by the opposition – on the other, became even more aggravated. Lack of confidence in the Government was reflected in a total criticism (albeit not always justified) of their draft laws, especially concerning fiscal policy, budget revenue and expenditures.

In this environment, a public procurement draft submitted to the State Duma in summer 1997 was edited repeatedly, with and then without involvement of the Government, and its quality deteriorated significantly. Ultimately, when the law was passed in spring 1999 it looked nothing but the initial draft and contained numerous conceptual omissions and evident logical lapses. Uncertainty within the public procurement system increased. The regulatory outreach of the new act reduced significantly: No. 97- FZ Federal Law was entitled "On tenders for public procurement…"[15]. Therefore, the Law, first, did not cover any other procurement means except tenders, and, second, Article 2 defined public needs as the needs of the Russian Federation, which was contrary to Article 525 Part I of the Civil Code of the Russian Federation, not reaching the subjects of the Russian Federation and, thus, losing them as an object of regulation. It also did not concern municipal procurement.

[14] Due to a high level of inflation in the 1990s, the thresholds were set in the Statutory Minimum Wage Index (MROT). MROT value at the initial stage of applying No. 305 Decree of the RF President was 83 490 (pre-revaluation) RUB under the federal law, and from 01.01.2000 –100 RUB. Thus, at the time of signing the No. 305 Decree of the RF President 2 500 MROT equaled 208 725.00 pre-revaluation RUB.

[15] No. 97- FZ Federal Law "On tenders for public procurement of goods, works, services" of 6.05.1999 // Collected legislative acts of the Laws of the Russian Federation. 1999. No. 19. Art. 2302.

The Law introduced a concept of "tender organizer" – "government customer in the person of a federal executive body …", which excluded other federal bodies, state agencies and federal state-run companies from its coverage, even the State Duma. Based on the wording of Article 1, special federal laws regulated public procurement in particular sectors of the economy: agricultural products, raw materials and food products, procurement for public reserves, public defence procurement, etc. According to Smirnov and Nesterovich, "the Law self-restricted its coverage to 10–20% of public procurement in Russia (by value)" (*Nesterovich & Smirnov, 2001*). Typically, organizing a tender, an ordering party, based on the source of the allocated funds, was forced to choose a regulatory act to follow: No. 305 Decree of the RF President or No. 97- FZ Federal Law. Moreover, a number of regional and local acts were adopted on their basis, even more fading the legal framework and preventing efficient control over its enforcement.

Overall, procurement specialists considered that the two acts worked in parallel: 1) Procurement for the needs of federal executive bodies in the part of competitive bidding was regulated by No. 97- FZ Federal Law, and in the part of other methods of procurement – by No. 305 Decree of the RF President; 2) Other public procurements, including procurement for the needs of the subjects of the Russian Federation were regulated by the regional laws and No. 305 Decree of the RF President; 3) Municipal procurement was covered by neither the federal, nor the regional law on procurement and instead local enactments applied. Both municipal and regional laws could contain descriptions of other procurement procedures not determined by federal regulations.

In terms of the specified regulatory mechanisms, No. 97- FZ Federal Law was worse than its direct predecessor – the Presidential Decree. The Law did not have a strict requirement on mandatory order placement for public procurement through competitive bidding and applied "in the case of tenders" (Article 1 Part 1). It was a serious attempt to restrict competition since its wordings enabled preventing participation of many potential suppliers in competitive bidding, particularly, the entire distribution segment: "tender participant – supplier (executor) involved in business activity for producing goods (works, services) …" (Article 2), or "tender participant can only be a supplier (executor) that has production capacity and labour resources necessary for production…" (Article 5 Clause 1). There was also an attempt to block involvement of foreign suppliers: they "can take part in a tender if production … in the Russian Federation is absent or economically inexpedient" (Article 6).

At the same time, there were no clear qualifying requirements which led to arbitrary interpretation and possibility to set "additional requirements" by the tender organizers (Article 5), who, in fact, could be legal entities not related to the state (Article 2). The number of the specified types of tenders went down in comparison with No. 305 Decree of the RF President. No. 97- FZ Federal Law did not have direct application and additional bylaws were necessary, clarifying the performance specifics of ordering customers on the numerous aspects of their interaction with the participants of the emerging market. The lower quality of the Law in contrast with the previous acts indicated considerable problems within the law-making process in Russia at that period as well as an overall misbalance of the government system for regulating Russian economy in general. Drafting regulations and standards reminded of "sticking plaster solutions" and fulfillment of obligations to the lobbyists for particular draft laws rather than a system-wide problem-solving approach and a robust strategy for economic development.

In that period intensive efforts to train and retrain public procurement specialists were launched. The responsible organization was designated – National University – Higher School of Economics, Moscow as well as the first retraining centres (St Petersburg, Rostov-on-Don, Nizhny Novgorod, Novosibirsk, etc.) and demand was shaped for their services to ensure that the members and chairmen of the Tender Commissions meet the statutory requirements. These efforts facilitated establishing the expert community in Russia that

is an important prerequisite for successful economic reforms. A noticeable effect, however, would be generated only in several years. At the same time, immediately upon adopting No. 97-FZ Federal Law there was a compelling need for a new law on public procurement and supplies.

III. Transition to the Concept of a "Single Law for All"

Intensive discussions of the new version of the framework law on procurement and supplies for public needs were conducted for several years starting from 2001 in the form of conferences, interdepartmental approvals, discussions in public sources, and so on. The draft law submitted to the State Duma was adopted in the first reading as amended. And then unpredictability of Russian law-making was demonstrated to the full.

In the second version the concept of the law changed significantly. Then after the third reading, a principally new version, unknown to the specialists and the public, was adopted that had not been discussed broadly by the expert community. The new act – No. 94-FZ Federal Law "On procurement …"[16] introduced several technological and substantial novelties. Since the scope of prior discussions was insufficient, the draft was not well-thought, leading to adjustments on a regular basis in terms of both the order-placing technology and some conceptual elements[17].

Let's summarize the positive characteristics of the Law, facilitating evolutionary development and conforming to the international procurement practice[18]:

1. The basic idea of the new law was to stimulate expansion of the public procurement market, by easing entry of potential suppliers, including foreign participants, intermediaries and even physical persons as well increasing the number of ordering parties through unification of municipal procurement rules.

2. For the first time in Russian practice the rules and technologies of federal, regional and municipal procurement were unified.

3. No. 94-FZ Federal Law laid down the foundations of the new system for increasing awareness of market participants by placing information on an official web-site.

4. For the first time the rules for electronic procurement were formulated.

5. Excessive and technically complex approvals by the authorized bodies were eliminated.

6. Small procurements gained the official recognition. In the first edition they were not covered by the Law (Article 1 Part 2).

7. Extrajudicial appeal was reintroduced, after being removed from No. 97-FZ Federal Law. The appeal technology was described in sufficient details.

Unfortunately, the Law also had plenty of shortcomings. The toughest part is that some errors were conceptual, i.e., contrary to the internationally-established efficient procurement practice. Several wordings on procurement rules were quite ill-considered. Some norms had a dual nature: correct in substance but expressed wrongly.

First, the Law did not specify any mechanisms enabling government customers to obtain high-quality products and engage highly-skilled suppliers (that had the required production capacity, experience of similar contracts, and an impeccable reputation).

Second, as the public procurement market accounts for 15–20 % GDP, one can talk about the impact of the new rules, under which the ordering parties set the initial (maxi-

[16] No. 94-FZ Federal Law "On procurement of goods, works, services for public and municipal needs" of 21.07.2005 // Collected legislative acts of the Laws of the Russian Federation. 2005. No. 30(1). Art. 3105.

[17] The latest current edition of 94-FZ Federal Law was the 40th in eight years of its application, which means amendments and additions were made on average five times per year.

[18] In the international practice the term "procurement" (acquiring, supplying) is understood as a set of methods enabling to satisfy the customer's needs in products. Professional analyses of the procurement norms of No. 94-FZ Federal Law can be found in *Karanatova, 2010; Kuznetsova, 2010; Smotritskaya, 2009; Doroshenko et al., 2011; Khramkin, 2011; Belokrylova, 2011, etc.*).

mum) price, on inflation stimulation in Russia. The regulators could estimate in advance that both ordering parties and suppliers would prefer to overrate the initial (maximum) price with regard to the market indicators. For suppliers it is the way to increase their profits, and for customers – to demonstrate a higher scope (share) of saved budgetary funds. In addition, the norm is conducive to corruption within the framework of the law on procurement.

Third, from the main means of procurement, open tenders – the internationally recognized public procurement benchmark – became de facto an equivalent (and in practice – an additional method (Article 10), which reduced significantly the customers' abilities to attract well-balanced bids and increased probability of unconsidered offers.

Forth, the bidders were not obligated to prove their conformity to even a limited set of requirements (Article 11 Parts 1, 6), so the Law contributed to deteriorating the quality of market participants and propelled the emergence of numerous shell firms. An upsurge of financial fraud and counterfeit products supplies could have been expected.

Fifth, the new Law did not provide for a number of procedures and means of procurement that proved their validity under No. 305 Decree of the RF President. For example, such useful mechanisms as pre- and post-qualification of bidders, closed bidding for small sums and two-stage tenders were liquidated.

Sixth, the norms of the Law increased customers' labour costs significantly: for mastering new procurement technologies, observing multiple deadlines and procedures, confirming without being assisted whether bidders meet the requirements, training and retraining specialists, and electronification of particular processes.

Seventh, as mentioned above, the 2005 version of the Law was adopted in haste, which affected the quality of description of various procurement technologies, misleading most of practitioners (*Smirnov, 2006*). Therefore, the legislators were forced to constantly "improve" the Law throughout the entire period of its enforcement, as a result of which customers kept incurring additional procurement costs. "According to government customers, tenders often took place only to report to financial bodies" (*Kuznetsov, 2003*), which was totally contrary to the concerns about the outcome for the society and economic efficiency, and "there were frequent incidents when the tender winner became known long before the bidding".

Evidently, the authors of No. 94-FZ Federal Law lost hopes for the customers' good will and counted on stimulating competition on the emerging market, using budgetary savings as the main indicator of the customer's performance. Since the Law was signed without taking into account the involvement of informal institutions and the psychology of the behaviour of the market players, with time the enforcement practice showed that the legislators' expectations were mostly misplaced.

IV. Conditions for Establishing a Contractual System for Public Procurement

The period for drafting and awaiting the Law on contractual system to come into effect was full of vivid discussions about the results of developing public procurement technologies in Russia[19]. Many were disappointed with the current public procurement rules under No. 94-FZ Federal Law: ordering parties could not purchase the required products in time, their users complained about the low quality of such purchases, suppliers were not keen on taking part in procurement procedures due to the risk of late payment, threat of additional costs because of corruption or the fear to waste time in vain. Finally, government officials and the President criticized the established system for inefficiency and even failures of the budgetary-and-fiscal policy.

Throughout 2011, to fulfill instructions given by the President and the Prime-Minister, several options to modernize the Law were proposed, among which a draft Federal Law

[19] For the concept of establishing and developing a contractual system of the Russian Federation and the international experience in this field see, for example: ipamm.hse.ru/upload/download/library/wp8-2011-02.pdf (*Golovschinsky & Shamrin, 2011*).

"On the federal contractual system", devised by the Ministry for Economic Development, became the most known. Amidst the social support for urgent radical measures, a rising criticism from customers, a reformatory fever of the Ministry for Economic Development against an active resistance from the Federal Antimonopoly Service, that was concerned of a growing risk to lose the control functions over procurement, the draft law still required serious adjustment and refinement.

The first version, proposed by the Ministry, was corruption-prone and cumbersome in terms of its bureaucratic procedures. After a solid portion of criticism, it was returned for further polishing. At the same time, the Federal Antimonopoly Service put forward alternative proposals on modernizing No. 94-FZ Federal Law. As a result, a compromise version was approved and accepted by the Federation Council as No. 44-FZ Federal Law "On the contractual system for procurement of goods, works, services for public and municipal needs" of 05.04.2013, which was signed by the President on the same day to come into force on 01.01.2014.

In comparison with No. 94-FZ Federal Law, the new Law gives an extended understanding of the efficiency principle, in particular, the need to achieve the targets (performance), and introduces a new important principle – stimulating innovations, which means, other conditions being equal, the priority of procurement for innovative and high-technology products[20]. There are also some principal changes in regulation of public and municipal procurement. In accord with the Federal Law "On procurement…", an order was considered placed on the date of concluding a procurement contract (or other civil law contracts under Article 55 Part 2 Clause 14), which increased moral hazards by the customers with regard to the product supply results. According to the concept of No. 94-FZ Federal Law, the procedure was more important that the procurement outcome. The Code on Administrative Violations did not specify fines for the outcome[21].

The field of application of No. 44- FZ Federal Law was expanded considerably. It covered procurement planning, determining suppliers (from publishing a notice to concluding a contract with the winner), the process of procurement (supplies) of products until the contract is executed by the parties as well as accounting and monitoring the results. The Law provides for improving informational support of the contractual system in comparison with the period when procurement fell under No. 94-FZ Federal Law. The national official web-site was designed to expand procurement-support functionalities for both suppliers and bidders. In particular, No. 44- FZ Federal Law mentions such new elements as a library of model contracts and standard contact conditions, a Register of bank guarantees, product catalogues for public and municipal needs, information about prices formed on the markets, etc.

A procurement identification code gives a mechanism of end-to-end observation and data integration from a procurement plan to product supply reports located in the system. Article 5 Part 1 of the Law provides for use a mechanism within the Common Information System (CIS) for exchanging e-documents between suppliers and customers, which offers a necessary groundwork for further electronization of other methods of determining a supplier within the system of purchasing products for public needs.

Now a customer has to justify a purchase. First of all, procurement must conform to a particular target when compiling a procurement plan. The initial (maximum) contract price and the method to determine a supplier must be justified, particularly, any additional requirements to the bidders in a schedule. The Law introduces a rate-setting mechanism

[20] In the modern international practice, regulations associated with an extended use of budgetary funds for the purposes of stimulating innovative activity of companies are very popular. Public procurement is considered one of significant tools for gaining better national and international rankings, and strengthening innovations generation and dissemination (*Markovic-Hribernik & Detelj, 2016; Edler & Yeow, 2016; Detelj, Jagric & Markovic-Hribernik, 2016; Georghiou, Edler, Uyarra & Yeow, 2014; Knutsson & Thomasson, 2014; Kravets, 2016; Ivanova, 2013; etc.*).

[21] Collected legislative acts of the Laws of the Russian Federation. 2002. No. 1. Art. 1. Fines imposed under the Code on Administrative Violations for non-compliance with the law on procurement are specified in Articles 7.29, 7.30, 7.31, 7.32, 19.5, 19.7.2, 19.7.4 and others.

in procurement. The legislator has found it expedient to block public procurement of the products with excessive consumer attributes and luxury items, which implies possible restrictions by the quantity and quality, setting the ceiling prices or standard costs.

For tenders and auctions, customers are now obligated to set the bid security requirements in the form of depositing cash or a bank guarantee [22] at 0.5–5% of the initial price[23]. Under No. 94-FZ Federal Law, to require the bid security was a customer's right.

In the overwhelming majority of procurements, either open or closed, customers have to set the requirement for contract performance security that similarly can be provided in the form of bank guarantee or depositing funds – generally, from 5 to 30% of the initial (maximum) price[24].

Contract execution in accord with No. 44-FZ Federal Law also includes several novelties. A package of measures designed to support procurement comprises product acceptance, expert examination of the supplied goods (using customer's own resources or engaging external experts), payment for the products by the customer and additional stages of product supplies of those stages were specified in an agreement. Customers must put the results of every particular stage of contact execution and the information about the supplied products in a report published in the Unified Information System. The Law "On contractual system …" gives a detailed description of a mechanism of appeal by bidders against unfair conduct of customers and their representatives as well as site operators in case of e-auctions. Particularly, the Law outlines the mechanism for resolving discrepancies in inspection findings between regulators of different levels.

Overall, one can state that the norms of No. 44- FZ Federal Law to a considerable extent support an evolutional development of the rules laid down throughout multiple improvements of No. 94- FZ Federal Law "On procurement…"[25]. The problems, however, are embedded in the procurement concept that is not visible to outsiders.

Conclusions: The Prospects of the State Winning over Itself

According to North, institutions are created to serve the interests of their creators (*North, 1990*). By no means, market inefficiencies of norms and standards always strive for the measures to rectify the situation. A direct confirmation seems to be the stages of establishing the institutional environment for the public procurement market in the Russian Federation.

The evolution of the methods of public and municipal procurement demonstrates how the post-Soviet bureaucracy affected law-making, being some kind of a political mood barometer that reflects, inter alia, the dominant concept of economic policy. Evidently, the legislator's hope for emergence of a new type of Russian officialdom, not inclined to opportunistic behaviour and standing up for the priority of public interests over the group or personal ones, was gradually fading. With time the law on procurement has lost the priority of the industrial policy, mainstreaming instead the competition policy. The balance between anti-corruption efforts and procurement efficiency is also broken. An analysis of the rules and regulations on public procurement exposes nearly all adverse features of Russian law-making process: from bounded rationality of the legislators that leads to unprofessional wordings and statements and destruction of the sense of particular norms through amendments and bylaws, to an incident when after several years of discussing a concept of a particular regulatory instrument, a totally different document was finally adopted. One can notice how easy is to readjust the basic law, which bears the footprints

[22] In electronic auctions – only funds transfer due to technology specifics.

[23] In short e-auctions when the procurement sum does not exceed 3 million RUB – 1% of the initial (maximum) price.

[24] For a detailed description of the technology and conditions for giving bank guarantee under the law and business practice of the Russian Federation see: http://cyberleninka.ru/article/n/primenenie-bankovskoy-garantii-kakinstrumenta-obespecheniya-uchastiya-v-protsedurah-gosudarstvennyh-zakupok.

[25] Still due attention has not been paid to the environmental footprint, the quality of procured products and in general to the factors of influence of public procurement upon sustainable development, which is a pressing issue that is being widely discussed by the international academic community (*Grandia, 2016; Czech et al., 2016; Testa et al., 2016 and others*).

of various lobbying groups: importers, developers, agrarians, certain customer circles, influential government agencies, etc.[26]

Twenty years have passes after the first framework Law on public procurement was adopted – No. 60-FZ Federal Law, and a quarter of a century ago modernization of this field started on the basis of market principles. This is a sufficient period to reach certain generalizations and provide a greater insight into some conceptual issues.

The objectives and methods of public procurement should not be distorted for the purposes of some hypertrophic stimulation of competition. Otherwise, the regulators may forget that a growth of competition on any market is only a means rather than the goal. Yet, even forgetting that the public procurement system can be employed as a mechanism for stimulating production and financing the most efficient domestic producers using budget funds, or that it is necessary to stimulate new jobs in Russia or that there is a need to develop entrepreneurship and increase the tax base, – in any case, the situation when customers are unable to acquire a certain benefit of a required quality for public needs is unacceptable. Finding high quality products at the lowest price is quite difficult. It is a wrongful environment when, due to complexity or inappropriately lengthy procedures, bona fide customers that need to purchase certain products and do not intend to break the framework law are forced to "make arrangements" with suppliers or coordinate their procurement with the authorized regulators. We cannot agree with the idea that more attention should be given to the procurement process (meeting the deadlines, observing the rules for interaction with bidders, and so on) than to the procurement outcome, including possibility to satisfy the current needs.

The system of public and municipal procurement is a powerful demonstration that the attempts by the state to exercise self-control may not be very far-reaching. The foremost expectations for curtailing corruption and increasing attractiveness and accessibility of this market are associated with control by the society, or to put it more precisely, by highly qualified suppliers who have strong interests in becoming the winners, and whom they tried to get rid of rather successfully during the period when the law on procurement had been in effect. Nowadays, 250 000 public and municipal customers and hundreds of thousands bidders in Russia are able to put a significant influence upon transforming the principles of societal cooperation.

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[26] Foreign practice of regulating public procurement demonstrated no less inertia and misalignment. Changing approaches to economic policy requires time and interaction between various authorities, coordination at the government and local levels, due regard to the traditions and a consolidated institutional environment (*Barrett, 2016; Borges, Walter & Santos, 2016; Placek, Schmidt, Ochrana & Pucek, 2016; Sorte, 2016; Ross & Yan, 2015; Ayhan & Ustuner, 2015; Decarolis & Giorgiantonio, 2015* and others).

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