Chapter 23
Employee Ownership and Corporate Governance in Russia

Yaraslau Kryvoi

Introduction

Russian corporate governance is full of contradictions. For instance, trade unions in Russia have traditionally been tools of corporate management rather than of employees. In effect, managers in the Soviet period were like feudal lords of their enterprise, despite the highly centralized economic system. Workers usually did not play any active role in management, although they had significant blocks of shares in them. Nonetheless, Russian employees ended up better protected from unemployment than their cohorts in other transition economies. These are just a few puzzles of the Russian post-Soviet transition that this chapter analyzes.

For various historical reasons, the idea of employee ownership has traditionally been very popular in Russia. The Soviet system, beginning with the October Revolution, aimed at establishing the dictatorship of proletariat, was built on the rhetoric that a working man is the centre of all government policies. Despite the fall of communism, this Soviet mentality persisted in post-Soviet economy. The designers of Russian privatization, in addition to transferring ownership, also sought to prevent communists from returning to power. To this end, it was necessary to secure wide public support for privatization. Therefore, employee buyouts as the main method of privatization were determined more by political necessity and pressure from directors’ and employees’ groups rather than by considerations of effective economic policy. As a result, employees gained the controlling stakes in most state enterprises.

Russian privatization achieved its main goal – more than half of state enterprises became private and privatization occurred with relatively little social conflict. However, this chapter shows that the redistribution of property via employee buyouts failed to create a new class of effective owners and did not improve corporate
governance. While some described government concessions to workers as “the most generous of any privatization in the world” (Schleifer 2005), in practice directors of enterprises became the sole decision makers while employees remained passive observers. Moreover, most employees ended up deeply dissatisfied with the privatization process, primarily because of low salaries and extreme inequality between the rich and the poor in post-Soviet Russia.

As a result of privatization, directors appointed during the Soviet era often retained their positions and took on enormous responsibility for production and distribution. Directors maintained Soviet tradition and continued to act in a paternalistic role towards employees, who were prepared to obey. Deep economic crises weakened both the Russian state and the controlling market mechanisms that existed in the Soviet era. This created a fertile ground for directors to manipulate and abuse their position of power. Employee ownership helped alleviate social conflicts and reduced unemployment, but the majority of Russian enterprises continued to be overstaffed, which had a negative impact on their profit and competitiveness.

This chapter begins by briefly discussing the main goals and mechanisms of Russian privatization and explaining why employee buyouts became the main method of privatization.2 The section “Why Employee Ownership Does Not Work in Russia” explains the historical and economic reasons why employee ownership did not work in Russia and why employees failed to play any independent role in Russia’s transition.3 The section “The Failure of People’s Enterprises” addresses a contemporary attempt to create employee-owned enterprises in the form of people’s enterprises.4 The section “Lessons Learned from Employee Buyouts in Russia” analyzes the lessons learned from employee buyouts and employee ownership in Russia.5 This chapter concludes with a number of policy recommendations to enable more efficient privatization in transition economies.6

Employee Buyouts in Post-Communist Russia

The Goals and Mechanism of Russian Privatization

Russian privatization was unique in its enormous scale and speed. These characteristics were necessary to achieve state goals of privatization7 – to raise funds for the state budget and to generate investments for restructuring enterprises.8 The overarching

---

2 See Schleifer (2005), pp. 5–16.
7 Audit Chamber of Russia is the main federal supervisory body of the Russian Government. See Federal Law on the Accounts Chamber of the Russian Federation, art. 3 (11 Jan 1995).