The Politics of Post-Communist Pension Reform:
The Influence of Business Lobbying on Policy Outcomes

Dissertation

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Abstract

A question of perennial interest to social scientists is how and when businesses can influence policy outcomes. Related to this is the question of whether democracy alters the political power of commercial interests. Debates over pension privatization in the post-communist countries provide a useful empirical context in which to examine these questions. Private pension funds and investment companies in the post-communist countries lobbied for pension privatization from which they potentially stood to enjoy substantial financial gains. In some countries their efforts were successful, while in others the private financial sector was excluded from policymaking circles.

I draw on existing explanations of business lobbying to develop my theory of conditional influence. At the adoption stage, lobbying by businesses in the financial sector is more likely to be influential in less democratic systems, and vice versa. Being influential on adoption, however, does not ensure that businesses will be able to secure influence on regulatory issues. In cases where political power has been thoroughly consolidated within the state apparatus, even if the private financial sector successfully pushed for pension privatization, they are unlikely to maintain their political sway over subsequent regulatory policy. Additionally, my theory produces a unique empirical prediction about the influence of the capital market on the decision to privatize pensions. A larger capital market should strengthen the claims of the financial sector about the
positive benefits of pension privatization in securing long-term capital investment in the country. We should, however, only see a larger capital market making pension privatization more likely in less democratic countries in which lobbying by businesses in the financial sector is more likely to be influential.

I present cross-national statistical evidence from 25 post-communist countries which indicates that a larger capital market does increase the probability of pension privatization in less democratic countries. Building on this, I use case studies to offer more insight into the causal mechanism of lobbying. I examine the development of pension policy in Russia over three distinct political eras which vary on the level of democracy. These case studies are based on extensive field research in Russia including interviews with politicians, policymakers, and businesspeople including representatives of the relevant state ministries, investment companies, and private pension funds. The case studies bolster the cross-national evidence and support my theoretical expectations.

The findings have important implications for three areas of research—lobbying, the politics of economic reform, and the welfare state. First, this research counters welfare state research in which demographics are thought to be the primary determining factor in reform. Although demographic conditions like aging populations get pension reform onto the political agenda, they do not determine the ultimate policy outcomes. Second, this research indicates that the lobbying efforts of certain businesses will be less successful in more democratic contexts. Indeed, a central finding of this dissertation is that money only buys power some of the time.
Dedication

Dedicated to my parents, Eugene C. Wilson, Jr. and Julia A. Wilson

and

To the memory of my grandparents, James C. and Kate Willis Anderson and Elva Wilson
Acknowledgements

A major perk of finishing my dissertation is that I finally have the opportunity to formally, and somewhat publicly, thank the many people who have helped me throughout my graduate years.

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I am deeply indebted to all of my interviewees in Russia who took the time to explain to me the development and workings of Russian social policy. While I will not
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ix
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# Table of Contents

Abstract .......................................................................................................................... ii  
Dedication ..................................................................................................................... iv  
Acknowledgments ......................................................................................................... v  
Vita ................................................................................................................................... x  
List of Tables .................................................................................................................. xiv  
List of Figures ............................................................................................................... xv  

Chapters:  

1. Introduction ............................................................................................................... 1  
   1.1 Pension Reform Pressures in the Post-Communist Countries ....................... 3  
   1.2 The Financial Sector as an Interest Group in Pension Reform ................. 21  
      1.2.1 Political Importance of the Financial Sector in Pension Reform .......... 21  
      1.2.2 Studying Lobbying Influence on Policy Choice ................................. 25  
   1.3 Organization of the Dissertation ................................................................... 26  

2. Theoretical Framework: The Market as Interest Group .................................. 30  
   2.1 The Overlooked Role of the Private Financial Sector in Pension Reform ....... 33  
   2.2 Existing Explanations of Business Lobbying ........................................... 39  
   2.3 A Theory of Conditional Influence ............................................................ 46  
      2.3.1 Adoption of Pension Privatization ..................................................... 47  
      2.3.2 Regulation of Pension Privatization .................................................. 50  
      2.3.3 The Effect of the Capital Market on Pension Privatization .............. 57  
      2.3.4 Summary of Argument ...................................................................... 62  
   2.4 Research Design of Dissertation ................................................................. 64  

3. Cross-National Evidence of How Lobbying Mediates Pressures to Reform ...... 74  
   3.1 Empirical Test: Determinants of Pension Privatization .............................. 76  
      3.1.1 Choice of Cox Models ....................................................................... 76  
      3.1.2 Variables ......................................................................................... 77  
      3.1.3 Results of Analysis ......................................................................... 81  
      3.1.4 Interaction of Market Capitalization and Democracy ....................... 84  
      3.1.5 Other Significant Predictors of Pension Privatization ...................... 92  
   3.2 Conclusion ......................................................................................................... 95
List of Tables

<table>
<thead>
<tr>
<th>Table</th>
<th>Title</th>
<th>Page</th>
</tr>
</thead>
<tbody>
<tr>
<td>1.1</td>
<td>Adoption of Structural Reforms in Post-Communist Pension</td>
<td>13</td>
</tr>
<tr>
<td>2.1</td>
<td>Expectations regarding Regime Type &amp; Policy Stage</td>
<td>62</td>
</tr>
<tr>
<td>2.2</td>
<td>Sources of Political Support &amp; Opposition in Russia, 1991-2008</td>
<td>68</td>
</tr>
<tr>
<td>3.1</td>
<td>Privatization across the Post-Communist Countries</td>
<td>78</td>
</tr>
<tr>
<td>3.2</td>
<td>Determinants of Pension Privatization</td>
<td>82</td>
</tr>
<tr>
<td>4.1</td>
<td>Competing Pressures for and against Market-Oriented Pension Reform during the Yeltsin era</td>
<td>111</td>
</tr>
<tr>
<td>4.2</td>
<td>Evolution of Official Pension Reform Plans in Russia, 1992-1998</td>
<td>129</td>
</tr>
<tr>
<td>5.1</td>
<td>Russian Pension System Adopted in 2001 (implemented in 2002)</td>
<td>164</td>
</tr>
</tbody>
</table>
List of Figures

<table>
<thead>
<tr>
<th>Figure</th>
<th>Title</th>
<th>Page</th>
</tr>
</thead>
<tbody>
<tr>
<td>1.1</td>
<td>Old-Age Dependency Ratio in 1960, 1990, and 2000</td>
<td>5</td>
</tr>
<tr>
<td>2.1</td>
<td>Theoretical Expectations regarding the Link between Market Capitalization and Pension Privatization</td>
<td>59</td>
</tr>
<tr>
<td>3.1</td>
<td>Hazard Functions Showing the Effect of Market Capitalization at Different Levels of Democracy (based on Model 2)</td>
<td>85</td>
</tr>
<tr>
<td>3.2</td>
<td>Hazard Function of Pension Privatization at Different Levels of Covariates (based on Model 2)</td>
<td>94</td>
</tr>
<tr>
<td>4.1</td>
<td>Number of Private Pension Funds, 1995-2008</td>
<td>114</td>
</tr>
<tr>
<td>4.2</td>
<td>Number of Participants in Private Pension Funds, 1999-2009</td>
<td>115</td>
</tr>
<tr>
<td>4.3</td>
<td>Private Pension Fund Indicators, 1999-2009</td>
<td>116</td>
</tr>
<tr>
<td>5.1</td>
<td>Market Capitalization in Russia, 1991-2008</td>
<td>154</td>
</tr>
<tr>
<td>5.2</td>
<td>Size of Contributions to the Accumulated Portion of Pension (in the 2nd Tier)</td>
<td>167</td>
</tr>
</tbody>
</table>
Chapter 1

Introduction

Pension reform is one of the most complicated and painful problems of the transitional period as it affects the entire population.\(^1\)

A central part of the transition after the fall of communist regimes in Eastern Europe and the countries of the former Soviet Union was the development of a market-based economy. Although the post-communist countries varied tremendously in the speed and nature of market reforms, the first wave of reforms included privatization and stabilization measures intended to free price controls and keep government spending within hard budget constraints (Przeworski 1991). Powerful business lobbyists, particularly the directors of formerly state-owned enterprises, posed significant hurdles in the progress of these first wave reforms. In countries where these “short-term winners” were influential, both political and economic reforms stagnated (Hellman 1998).

The second wave of economic reforms included a revision of the social welfare systems which were often inefficient and sometimes were significant burdens on government coffers. In contrast to theories about the first wave of reforms, however, the role of private businesses lobbying was given much less attention in explaining this second wave of economic reform. Instead, scholars focused on the role of domestic politics,

\(^1\) Pavel Orlov-Karba, *Vse o Pensionnoi Reforme*, Moscow: Gardariki, 2005; author’s translation from the original Russian.
international pressures, and economic conditions in explaining why some countries took different paths in welfare policy (i.e., Inglot 2008 among many others).

In fact, battles over pension reform offer a useful empirical context in which to examine whether private businesses played a role in welfare state reforms. One reason is that the stakes of pension reform are high for all of those involved. Advocates of market-oriented reforms attached great importance to the revision of pension systems. For instance, Yegor Gaidar, one of the architect’s of Russia’s shock therapy, suggested that a heavy pension burden had even contributed to the fall of the Roman Empire (Gaidar 2005: 514). For retirees, both present and future, pension systems are a large component of their quality of life. Domestic pension savings constitute a large pot of money over which bureaucrats and businesspeople compete for access. Pension privatization is among the many options for pension reform from which the government can choose. The private financial sector could enjoy considerable profits from a private pension system through managing and investing mandatory retirement contributions, or it could be largely excluded from national pension plans. Given the stakes of reform for the private financial sector, I seek to address the following question: Under what conditions were businesses in the financial sector able to successfully lobby politicians and bureaucrats regarding pension policy?
In answering this question, I address three literatures in political science—lobbying, the politics of economic reform, and the welfare state. Regarding the lobbying literature, I address the question of how and when businesses will be influential. For the politics of economic reform, this research grapples with the question of when potential stakeholders will influence solution to what have been labeled as “crises”. In the area of welfare state literature, I examine how state-led reforms have the possibility of creating new private markets. Answering my central research question, therefore, has wide-reaching implications in several important areas.

1.1 Pension Reform Pressures in the Post-Communist Countries

The problem of pensions was not new when it was taken up in the post-communist countries after the fall of communism. Communist systems were characterized by a comprehensive and centralized public pension system that covered the vast majority of populations. Pensions were small but adequate, as the level of benefits was set with the assumption that housing and utility costs were minimal (Kornai 1992). The post-communist systems often provided for a number of special categories and benefits depending on occupation, but were consistently characterized by low retirement ages – often 60 for men and 55 for women (McAuley 1977). Such systems are referred to as defined-benefits (DB) systems, in which a certain level of benefit is guaranteed. Communist systems are also financed on a pay-as-you-go (PAYG) basis, so that current tax revenues finance current benefits, although such systems are typically not fiscally balanced in practice.

Aging populations increasingly strained the communist PAYG pension systems.
Even before the collapse of communism, communist governments realized that they were unable to continue financing such a generous welfare state—these governments typically had other priorities including industrial development and the arms industry (Kornai 1992: 171-178). When communism fell in the early 1990s, in addition to high national debts, there were several pressing problems on pension systems including weak administrative capacities and a falling number of contributors due to high unemployment (Fox and Palmer 2001). The need for reform—while apparent before the fall—became glaring after it.

The 2007 World Bank Report—*From Red to Gray: The “Third Transition” of Aging Populations in Eastern Europe and the Former Soviet Union*—details the aging trends in the post-communist countries and their policy consequences including the impact on pension systems (Chawla et al. 2007). By 2025, in many of the post-communist countries nearly one-fifth of the population will be over the age of 65. From 2000 to 2005, the countries of Eastern Europe were also the most rapidly shrinking populations in the world. The estimated impact of this on pension systems is quite large. On average, pension system dependency rates for these countries are at least three times higher than old-age population dependency rates. The implication of this is that the growth of the pension system will rapidly outstrip the ability of the working age population to finance state-provided retirement benefits. In countries that have not adopted major structural reforms such as the Czech Republic, it is estimated that pension expenditures will rise from 8 to 16 percent of GDP by 2025. The pension problem was and is real in that these are rapidly aging populations with pension systems that have been increasingly strained. The possible solutions varied to what was framed by international
advocates and some politicians as a pension “crisis”.

Slowing rates of growth during the market transition in the 1990s further exacerbated the difficulty of the working population to support retirees. On strictly demographic and financial criteria, the pension systems of some countries were under more strain than others. From 1960 to 1990, the populations of the Communist countries got much older and, therefore, more expensive to support. Figure 1.1 below shows the change in the old-age dependency ratio—the ratio of those over the age of 65 to the working population—in 1960, 1990, and 2000 in the post-communist countries.

Source: Chawla et al. (2007)

**Figure 1.1: Old-Age Dependency Ratio in 1960, 1990, and 2000**

In Poland, the old-age dependency ratio in 1960 was 9.5 which increased to 15.5 by 1990 and to 17.8 in 2000. Likewise, Hungary experienced an increase from 13.8 to 20
between 1960 and 1990. The only populations that did not shrink were those of the Central Asian countries and Caucuses—Kazakhstan, Kyrgyzstan, Turkmenistan, Tajikistan, Uzbekistan, Georgia, Armenia, and Azerbaijan—and these countries nonetheless had aging populations. Although the populations of some countries were not aging as rapidly as others, almost all were and are faced with demographic pressure which made the generous Communist pension systems more difficult to maintain. From the government’s perspective, these demographic trends created the pressure to alter PAYG systems.

Projections regarding demographic trends further linked aging population to large increases in pension spending, particularly in the older countries (Chawla et al. 2007, 158). Older populations translate into more spending. For instance, for a country like the Czech Republic which has not privatized pensions, spending is projected to increase from 8 to 13 percent of GDP between 2004 and 2025. In Slovenia, which has also not privatized pensions, pension spending is expected to increase from 10 to 15 percent between 2004 and 2035. Pension spending is relevant because the “crisis” did not arise solely from demographic pressures, but also from fiscal constraints on the government. Fiscal constraints on the government stemmed from a decline in revenue (due to a drop in output in the early 1990s) and increasing costs; the ability of post-communist governments to borrow more money was decreasing. For instance, Hungary had one of the highest levels of foreign debt. Despite efforts to curb the growing debt, in the 1980s it had one of the highest levels of foreign debt in the world which doubled in the 1980s (Stark 1990, 357). Such high foreign debt limited the ability to continue financing

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2 The generosity of pension benefits is also relevant for projecting spending increases although this was roughly equivalent across the post-communist countries.
generous social benefits through public borrowing, although it also capped its resources to finance any transitional costs.

These pressures were several-fold. First, these systems became increasingly expensive to maintain for governments that faced tighter budget constraints than under communism. Second, as part of the transition to a market economy, pension privatization was a way to send a signal of commitment to market-oriented reforms. Politicians, thus, were motivated by a combination of factors including finding a policy to satisfy current pensioners and current workers, limit state expenditures on pensions, and send a positive signal about a commitment to market-oriented reforms to international organizations like the World Bank and the EU and to potential investors. Reforming pension systems was also touted as a means of promoting economic growth, so that another motivation was to improve economic conditions more generally. The key issue was the question of how to change the system.

The pressures on post-communist politicians are consistent with the “age of retrenchment” in which a combination of maturing welfare state systems and political shifts to the right—in the post-communist countries this meant pro-democracy, pro market-oriented parties that gained varying degrees of power across countries—generated proposals for cutting the welfare state (Pierson 1994, 1996). Similarly, post-communist politicians were motivated by both ideological moves to the market and the increasingly costly pension systems that strained government finances. Pierson further notes that pro-market politicians often garnered support from the business community indicating that this is an important interest group to take into consideration.

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3 Kornai (1992) refers to the “soft budget constraints” which meant that Communist government did not have unlimited spending capacity but were much less constrained than they would be under market-based economies.
Post-communist countries seeking to reform their pension systems faced two major types of changes: parametric and structural. These types of reform were not exclusive of each other and many countries chose to combine parametric and structural reforms. Following the name, parametric reforms change the parameters of the system. These include measures such as increasing the retirement age, changing pension indexation, cutting benefits, and improving the collection of contributions (Cangiano et al. 1998). Almost all of the post-communist countries have chosen to make parametric cuts including increases in the retirement age. Because wages tend to grow faster than prices, a number of post-communist countries have shifted pension indexation from gross wages to prices although changing the indexation formula can be extremely unpopular if the public is aware of it (which is often not the case). Cutting benefits typically involves measures such as lengthening the minimum contribution period, decreasing the use of noncontributory periods for pension calculations, and raising the number of years over which to calculate pension benefits. Finally, improving the collection of contributions involves expanding the contribution base and improving tax administration. One way to achieve this is to include pension contributions within the personal income tax base, thus making collection easier.

In contrast, structural reforms overhaul the underlying design of the system, and therefore, can be more politically difficult and expensive. The extent to which such reforms are politically unpopular and expensive depends on the nature of the political system and the extent of reform. Structural changes alter the social contract, shifting the

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4 A notable exception is Latvia where there are strong incentives to work longer because doing so can mean that an additional ten years of work can double the amount of pension received.

5 For instance, Hungary chose a mixed system in which half of pensions are indexed to wages and the other half to prices (Ferge and Juhasz 2004).
burden of old age provision from the government to citizens (World Bank 1994). The privatization of communist pension systems constitutes a radical overhaul to social security systems shifting away from a system based on defined benefits to one of defined contributions. In a privatized system, some or all of one’s retirement benefits come from mandatory savings that are privately invested. Private pension funds—created by investment firms, banks, and other financial intermediaries—profit from management fees, commissions, and profits associated with investing these savings. This means that private pension funds are the most direct winners of reform, at least in the short-term. Pension privatization is typically phased-in so that the costs are not fully imposed on current retirees, if at all. Current retirees, therefore, are usually neither winners nor losers of pension privatization.

The net effect for current workers (i.e., future retirees) is less clear as a privatized system introduces uncertainty about future benefits. Pension privatization has the potential to affect current workers negatively if the returns to their retirement investments are lower than defined benefits guaranteed by the state. In the short-term, current workers could be considered the losers if they are required to make higher payroll contributions in order to continue financing the benefits of current retirees and their own future benefits. In the long-term, current workers may be winners if the returns to their contributions are positive. In the event of negative return or returns lower than the previous defined benefit scheme, current workers will be the losers. Private pension schemes do not ensure a rate of return on contributions, although the government may

6 Lindbeck and Persson (2003, 105) explain that the distribution of the costs and benefits depends on how a newly introduced fully funded system is financed and returns to mandatory pension savings. They contend that, contingent on the proper design of the system, “a shift from pay-as-you-go” to a fully funded system can be designed in such a way that rather modest sacrifices of early generations will result in large gains for future generations.”
provide for a minimum level of state support for the poorest retirees. The result is that there is a great deal of uncertainty about future benefits.

In 1980, Chile became the first country to pass legislation privatizing its pension system. Chile’s reforms constituted a radical overhaul that made the average wage of worker’s retirement benefits based entirely on their mandatory contributions which would be privately invested (Edwards 1998; Vittas and Igelsias 1992). To partially offset the consequences for those in the lowest income bracket, the Chilean state does provide a top-up subsidy that is a guaranteed minimum pension (MPG) for men over the age of 65 and women over the age of 60 who have contributed to the system for 20 years but have below a minimum level of income (Kritzer 2008). Having begun in Latin America in the 1980s, pension privatization has spread including developed democracies such as Australia, Denmark, the Netherlands, Sweden, the UK, and the post-communist countries of Eastern Europe, Russia, and Central Asia (James and Brooks 2001).

Pension privatization was an approach strongly advocated by the World Bank in the 1980s and 1990s, as described in the report, *Averting the Old Age Crisis: Policies to Protect the Old and Promote Growth* (World Bank 1994; emphasis in the original). While the World Bank has since modified its position and diversified its advice, the initial recommendations advocated the adoption of a system in which a person’s retirement benefits would be based upon three tiers. The system would also be based on a funded-defined contribution scheme (FDC) so that current contributions finance future

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7 In Hungary’s privatized pension system, funds that yield too little are to be closed and individuals’ investments should be transferred to better yielding funds (Simonovits 2000, 523).
8 MPG may also cover individuals who have outlived their “actuarial life expectancy”. Disabled citizens must have contributed for 10 years to receive MPG payments. There is another program (PASIS) that covers low-income individuals who are disabled or over the age of 65 but do not qualify for other pension payments.
benefits. The first tier consists of defined benefits provided by the government. Because these defined benefits would be funded by general tax revenue on a pay-as-you-go basis (PAYG), they are referred to as unfunded. The second tier is the FDC component and is based on defined contributions. Benefits paid from this tier would come from mandatory savings that would be privately invested; this was the fully-funded portion of an individual’s retirement. The third tier consists of voluntary contributions to provide supplementary assistance in old age.

In the mid-1990s, the World Bank began advocating another variant of structural reform which is the notional-defined contribution (NDC) scheme (also known as a non-financial defined contribution scheme). In an NDC scheme, contributions are attributed to individual accounts and credited with a rate of return set by the government. Unlike a fully funded system, however, the system is still pay-as-you-go (PAYG) because current contributions are used to finance current pension benefits. Thus, like a fully funded privatized system, the NDC system is based on defined contributions. Significantly, it does not provide for private investment of individuals’ retirement savings. The NDC option is a less radical structural reform. Four post-communist countries have chosen some version of a NDC system including Poland, Latvia, Kyrgyzstan, and Russia.

In part because of the many possible ways in which government could address aging populations and the subsequent rising pension costs, post-communist pension reform is a useful empirical context in which to examine the lobbying of private businesses. This is also a useful empirical context because there is wide variation in the types of countries which have and have not privatized pensions. The pattern of pension

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privatization also runs counter to our typical classification of the post-communist countries regarding other market-oriented and democratic reforms. This variation allows us to separate the standard explanations of reform from the conditions under which the private financial sector would be more or less influential. Table 1.1 presents the 15 post-communist countries that have adopted structural changes to their pension systems. I have noted in parentheses which countries adopted a NDC system.
Table 1.1: Adoption of Structural Reforms in Post-Communist Pension Systems

<table>
<thead>
<tr>
<th>Year</th>
<th>Country</th>
</tr>
</thead>
<tbody>
<tr>
<td>1998</td>
<td>Hungary (FDC), Kazakhstan (FDC), Kyrgyzstan (NDC)</td>
</tr>
<tr>
<td>1999</td>
<td>Croatia (FDC), Poland (NDC+FDC)</td>
</tr>
<tr>
<td>2000</td>
<td>Bulgaria (FDC), Macedonia (FDC)</td>
</tr>
<tr>
<td>2001</td>
<td>Estonia (FDC), Latvia (NDC+FDC), Russia (NDC+FDC)</td>
</tr>
<tr>
<td>2002</td>
<td>Lithuania (FDC)</td>
</tr>
<tr>
<td>2003</td>
<td>Slovakia (FDC), Ukraine (FDC)</td>
</tr>
<tr>
<td>2004</td>
<td>Romania (FDC), Uzbekistan (FDC)</td>
</tr>
</tbody>
</table>

Did Not Privatize Pensions

Albania, Armenia, Azerbaijan, Belarus, Bosnia & Herzegovina, Czech Republic, Georgia, Moldova, Serbia & Montenegro, Slovenia, Tajikistan, Turkmenistan

NDC = notional defined contribution; FDC = funded defined contribution

Sources: I take the date for which legislation was passed (not implemented). General sources include Orenstein (2008), Holzmann and Hinz (2005) and Brooks (2007). For Ukraine, see USAID (2005) and World Bank (2005); for Slovakia see International Center for Policy Studies (2005); for Croatia see the official legislation (Croatian State Parliament 1999); Croatia did not implement the legislation until several years later; for Estonia, Latvia, and Lithuania see Natali (2004), for Bulgaria see Asenova and McKinnon (2007); for Macedonia see OECD (2007) (did not implement until 2005). Romania did not implement pension privatization until 2007 even though it passed the initial legislation in 2004.

While variation exists in the nature and degree of private pension systems adopted, all of these countries adopting structural reforms share the common experience of having adopted major overhauls of a long-standing system of social support.\textsuperscript{10} Amongst the countries that did not privatize pensions are some of the most and least market-oriented and democratic countries. Pension privatization did not occur in countries like the Czech

\textsuperscript{10} Kazakhstan, Hungary and Poland chose to follow a more Latin American pension model and offer citizens a choice between a limited number of funds. Croatia and Latvia followed a “clearinghouse model” according to which there was individual choice among a number of investment funds (Fox and Palmer 2001). Poland, Latvia, Russia and Kyrgyzstan have chosen different forms of NDC systems.
Republic and Slovenia in which we would think that the government was more prone to be pro-market oriented and interested in serving the interests of the private financial sector. In contrast, pension privatization measures were taken in Uzbekistan and Bulgaria, two countries which have not been among the more advanced economic reformers and which have very small private financial sectors.

There are several major sets of explanations for pension privatization which focus on the costs of current pension systems, domestic political conditions, globalization, and the role of international organizations. First, the cost of the current pension system is both an impetus and hindrance to pension privatization. The cost of pension systems is determined by the generosity and maturity of the current system. The cost imposed by pension systems, particularly communist pension systems which consist of defined benefit schemes, is directly related to the age dependency ratio which is the ratio of the working age population to dependents. A smaller age dependency ratio indicates that there is a larger working age population that is contributing to the system and the system is more sustainable. Conversely, a state with a high age dependency ratio will have difficulty providing sufficient resources to cover benefit payments. Demographic pressures can be used by politicians, bureaucrats, and other policy advocates to claim that there is a “crisis” which merits attention. Empirical evidence supports that aging populations create pressures to reform. For instance, research has shown that a shift in the proportion of the population over the age of 65 from only 9 to 12 percent increases the likelihood of privatization by about 26 percent (Brooks 2009: 56).

However, the rising costs of the current pension system also make it difficult for a government to afford the higher transitional costs associated with pension privatization.
As governments transition from a PAYG system to a defined contribution system of private individual accounts, the government must continue paying current benefits while current contributions finance future benefits. As populations age and the PAYG system becomes more mature and costly, therefore, the cost of privatization may become prohibitively high (James and Brooks 2001; Myles and Pierson 2001; Pierson 1996). The administrative costs of managing a new private system, in which the government often maintains oversight over individual accounts, can be quite high as well (Kay 2003). The transitional costs of structural pension reforms can be even higher depending on their depth of reform, meaning the extent to which the government shifts the responsibility of future pensions to private individual accounts. Pension privatization is typically financed through debt, so that as a government’s debt rises, it should be less able to finance expensive privatization costs even if doing so would provide long-term benefits. In short, the rising costs of pension systems provide an impetus to reform up to a point, but in the most costly systems the government will be unable to finance high transitional costs.  

Second, the pressures posed by *globalization* created a double-bind for developing countries that are considering some market-oriented reforms (Brooks 2009). On the one hand, pension privatization is touted as a means of increasing domestic savings and thereby improving investment although the link between defined contributions and national savings has been contested (Holzmann et al. 2001; Orszag and Stiglitz 2001). On the other hand, pension privatization is extremely costly and, if it is financed by increasing government deficits, then the country runs the risk of instigating capital flight by investors who fear a government that will default on its loans. Brooks

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11 The administrative costs of individual accounts may also erode the value of retirement savings. In the UK, it was estimated that 40 to 45 percent of the value of individual accounts was taken up by fees and costs associated with their management (Murthi et al. 2001).
(2009) concludes that while globalization and fiscal crisis, partially due to aging populations, got the issue of pension reform on the agenda, they did not determine the final outcome. This is particularly evidenced by the fact that, while crises in pension systems triggered reform debates, both countries with relatively young populations and those with much older populations pursued structural reforms and the countries with the oldest populations did not necessarily pursue the most extensive reforms (Chłoń - Dominczak and Gora 2003).

Third, the partisanship of the government has long thought to influence the direction of welfare state reform (Allan and Scruggs 2004). While theory and empirical evidence suggest that partisanship will influence the odds that pension privatization measures are adopted, research also indicates that it will not necessarily do so in a direct manner. Right-wing governments are more ideologically prone to adopt privatization measures, although this is not always the case in the post-communist context. In Poland, for example, the desire to signal a commitment to market-oriented reforms helped to overcome the influence of partisanship (Müller 2003). Empirical research grounded in the Latin American context has shown under certain contexts, large left-wing coalitions are the most likely to pursue pension privatization according to a “Nixon in China” type logic (Brooks 2009). Left-wing administrations are more likely to be able to characterize such reforms as necessary for objective reasons, while right-wing will be blamed for ideological motivations rather than a true concern with social well-being. While evidence suggests that partisanship should matter, the direction of its influence is unclear.

Fourth, a long stream of literature has pointed to the importance of diffusion effects of policies, particularly innovative ones, so that as more countries adopt a
particular policy solution the odds of it being adopted in other countries become higher (Dolowitz and Marsh 1996; Heclo 1974; Meseguer 2005; Walker 1969; Simmons and Elkins 2004). Research on diffusion includes studies specific to the diffusion of pension reforms (as in Weyland 2005). Brooks (2007) finds, however, that diffusion effects are different for reforms like fully funded pension privatization in which the sunk costs are high versus NDC policies in which the costs are much lower and are reversible. When costs are high, diffusion is more likely to be an influential factor because diffusion constitutes a learning process, providing important policy information to other countries about the best (or worst) ways in which to adopt pension privatization measures. In contrast, when the sunk costs are lower—as they are for the adoption of NDC pension systems—we see diffusion playing much less of a role. As the number of countries that have adopted pension privatization measures increase, a country is more likely to put the policy on the agenda thereby increasing, though not definitively securing, its ultimate adoption.

Fifth, international influences are also likely to influence the adoption of pension privatization. Although the World Bank has since modified its position to include a wider range of policies than privatization, the publication of *Averting the Old Age Crisis* in 1994 established the World Bank as the main advocate of pension privatization promotion around the world (World Bank 1994). The option of systems of notional defined contributions (NDC) has been offered as a possible alternative to true privatization (Holzman and Palmer, eds. 2006; see also Williamson and Williams 2005).

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12 In *Old-Age Income Support in the 21st Century*, World Bank experts referred to their recommendations as a “benchmark not a blueprint,” signifying a shift in its advocacy regarding pension privatization measures (Holzmann and Hinz 2005. The option of systems of notional defined contributions (NDC) has been offered as a possible alternative to true privatization (Holzman and Palmer, eds. 2006; see also Williamson and Williams 2005).
resources for countries wishing to privatize (Dowers et al. 2001; Holzmann and Hinz 2005: 1; Kay 2000; Madrid 2003; Müller 2001; Queisser 1998). Pension privatization was promoted as a type of magic pill, or “prevailing nostrum,” which could not only solve the problem of high pension burdens, but also increase domestic investment and economic growth (Orenstein 2009). While the World Bank has been influential, the role of international institutions may be more limited than is typically thought and domestic political and economic factors are often determining factors even in a highly globalized era (Nelson 1996, 2004; Garret 1998; Vreeland 2003). International advice was not uniformly pro-privatization. The International Labor Organization (ILO) took very different stances regarding the proper course of pension reform and did not support privatization, but they did not enjoy the resources of the World Bank nor its ability to offer loans in return for the promise of reform (Orenstein 2009). Therefore, in countries where World Bank involvement was greater—as observed by the presence of larger loans from the Bank—it is more likely that pension privatization was at least considered as an option.

The European Union (EU) is another international organization that might influence the adoption of pension privatization, albeit indirectly. EU candidate countries faced pressures that non-EU countries did not. The EU did not have an official policy on pension systems and binding EU legislation of pensions was limited because this was considered to be an issue falling within the purview of national governments. There were, however, broad objectives laid out including those of adequate support and sustainable systems (Barr and Rutkowski 2005). For countries like Hungary which adopted pension reform measures in 1998, earlier than other countries, the EU did not
significantly influence reforms (Ferge and Juhasz 2004). The EU did, however, require countries to maintain low deficits, which required governments to cut spending. Pension privatization was touted by the World Bank and other pro-market reform advocates as one way to do this although, as noted above, privatization raises costs in the short to medium-term.

While few of the Western European EU member countries have privatized pension systems, privatization could be seen as a policy consistent with a larger agenda for market-oriented reforms amongst the East European countries. Pension privatization was also a way to signal commitment to market-oriented reforms and was included in country’s investment rankings (Rodrik 1998). Pension reform, therefore, was a way to send a signal to the EU about commitment to market-oriented reforms. For instance, the former deputy prime minister of Poland and the Minister of Finance, Leszek Balcerowicz, stated that, “I am not entirely sure whether our pension reform will really deliver on all its promises. However, as long as it gives me another serious argument to reduce unnecessary spending now, I support it” (quoted in Barr and Rutkowski 2005, 158). This is why Polish pension reforms, for example, were undertaken by an unlikely government of the left, under the administration of President Kwaśniewski that needed to signal such a commitment to market-oriented measures to the EU (Müller 2003). Likewise, although the EU did not play a significant role in Hungarian reforms, market-oriented advisors promoted the development of private pension funds (Kornai 1992).

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13 Only six Western European countries have adopted structural, as opposed to parametric, pension reforms. Italy Sweden adopted a more market-oriented system of notional defined contributions (NDC). Four other Western European countries—Denmark, the Netherlands, Switzerland, and the UK—also adopted reforms that moved away from a solely PAYG system (Holzmann et al. 2003: 9; James and Brooks 2001). Also see: European Commission. 2006. “Social protection in the Member States of the European Union, of the European Economic Area and in Switzerland,” Koln, Germany: European Communities.
Because post-communist EU candidate countries desired to send signals about their commitment to market-oriented reforms, we would expect them to be more likely to consider the adoption of pension privatization as a signal to the EU of their commitment to market-oriented reforms.

Finally, in the post-communist countries statist stakeholders in the form of powerful bureaucracies have been noted to play central roles how and whether welfare policies were able to be reformed (Cook 2007; Müller 1999, 2003; Nelson 2001). Ministries of Finance seeking to rein in government spending were often pitted against Ministries of Welfare seeking to maintain their own spheres of influence. In Russia, the Ministry of Social Development & Healthcare actively opposed any privatization measures as did the Pension Fund which managed the tens of billions of dollars in Russians’ retirement savings, while the Ministry of Finance and the Ministry of Economic Development and Trade pushed for market-oriented policies in the sphere of welfare. These ministries defined the scope of the debate although, as I will argue in the case study chapters, they did not determine the ultimate policy outcomes adopted. In Poland, a new Labor Minister had to be appointed in order to end the bureaucratic deadlock and overcome opposition to pension privatization in the Ministry of Welfare (Hausner 2001, 215; Müller 2003). These accounts suggest that any consideration of pension reform should address the ability of these major bureaucracies to shape the policy alternatives that were considered to be feasible.
1.2 The Financial Sector as an Interest Group in Pension Reform

1.2.1 The Political Importance of the Financial Sector in Pension Reform

Existing explanations have not directly addressed the role played by the private financial sector—which may function as a powerful stakeholder in future reforms—or how the financial sector interacts with the political and socioeconomic context in which privatization is more likely to occur. As I will show in this dissertation, a closer examination of the financial sector reveals that they did play an important role as potential stakeholders in reform and that their influence was critically mediated by the nature of the political regimes and economic conditions like market capitalization.

Pension privatization is a useful empirical lens through which to view the lobbying power of private businesses. First, in the post-communist countries, pension reform activated a wide range of groups with competing preferences ranging from citizens, to politicians, to bureaucratic interests. There was little consensus regarding the priorities for reform or the means with which to address the demographic crisis. Second, pension privatization is an area in which the private financial sector had a vested material interest in a specific policy outcome. Privatization provided the opportunity for the financial sector to profit from being allowed to potentially invest billions of dollars in mandatory retirement savings. Additionally, to a certain extent the issue of pension reform was present in all of the post-communist countries around the same time period. All faced varying degrees of the aging population problem and reform was on most public agendas. Indeed, many of the post-communist countries are among the most rapidly aging populations in the world creating pressure to consider various ways to restructure pension systems (Chawla et al. 2007). Accordingly, the politics of post-
communist pension reform provides insight into broader questions about the political roles played by private businesses—there was some possibility of structural pension reform in all of the post-communist countries during this era.\(^\text{14}\)

The private financial sector had a large interest in the course of reforms and was potentially a very powerful stakeholder. A structural reform that established a more market-oriented system would allow private pension funds and investment companies to profit from being able to invest mandatory retirement contributions. Vittas (2000) concludes that for pension privatization,

Recognizing that workers are the last group to reap the benefits from the reform is not a cynical admission of some important weakness of the new systems but rather a pragmatic and realistic assessment of the allocation of benefits of any reform program. Moreover, such an allocation is not uncommon. For instance, in the case of any type of infrastructure project (an airport, a new road, an electric utility), the first beneficiaries would be the consultants who prepare the feasibility studies, followed by the engineers who draw the blueprint and then the construction companies that build the project. But the long-term beneficiaries are the residents and workers of the country who reap the long-term benefits from the services offered by the new project (19).

For instance, the construction companies who build schools, hospitals, or roads will profit before the average citizens makes use of these resources. Likewise with pension reform, only in the long-term will citizens see the benefits of the reform; the manager of a pension fund aptly noted that, “pension reform has nothing to do with pensioners, it has to do with future pensioners” (interview PF 3-102507). Private pension funds and investment companies will profit before the average citizen sees any improvement in the stability of the pension system or any increase in the amount of benefits.

\(^\text{14}\)To be clear, I do not intend to imply that the likelihood of structural pension reform was equal in all of the post-communist countries during this era. My comments refer to the possibility, not the probability, of reform.
In many of the post-communist countries private pension funds had been allowed to invest voluntary retirement savings regardless of whether pension privatization measures were adopted. Sixteen of the post-communist countries have allowed private pension funds to invest voluntary savings either before introducing a private tier or without privatizing pensions at all.\textsuperscript{15} In other words, the businesses who would profit from pension privatization existed prior to reform debates and were aware of the money that could be made. Indeed, when Russia’s pension system was adopted, it was commonly framed in terms of, “paving the way for an injection of fresh funds into the capital market”.\textsuperscript{16}

The experiences of several post-communist countries revealed how much money the financial sector could make from pension privatization. Hungary introduced a three tier private pension system in 1998. By 2001, the assets of private pension funds in Hungary constituted 3.9 percent of GDP, reaching a high of 10.9 percent of GDP in 2007 (about 6.8 billion dollars). Contributions to private pension in funds in Hungary were 1.4 percent of GDP by 2008 which was about .9 billion dollars. Slovakia passed legislation to privatize pensions in 2003; the assets of its private pension funds went from zero to 4.7 percent of GDP by 2008 (about 2 billion dollars) with almost all of these assets coming from individual contributions.\textsuperscript{17} Finally, the stakes of reform were also high because the government did not have to adopt the largest degree of pension privatization for firms in the financial sector to see substantial profits. Even being able to access a small

\textsuperscript{15} Countries that allowed private pension funds to operate in the voluntary sector before or without privatizing included the following: Bulgaria, Estonia, Hungary, Latvia, Lithuania, Poland, Russia, Slovakia, Albania, Armenia, Czech Republic, Georgia, Kyrgyzstan, Slovenia, Tajikistan, and Turkmenistan.


\textsuperscript{17} Data on the development of private pension funds is available from the OECD for Hungary, the Czech Republic, and Slovakia from 2001 to 2008. Data are available on Poland from 1999 to 2008. The figures in dollars given here are calculated using constant 2000 US dollars.
percentage of the billions of dollars in total mandatory contributions had the potential to provide significant profits for the financial sector and particularly the nascent private pension fund industry.

Private pension funds and investment companies that would manage retirement savings would benefit the most directly, but experts have also posited broader long-term benefits to the financial sector as a whole. Walker and Lefort (2002) cite extensive cross-national analysis indicating that fully funded private pension systems promote capital market development and innovation in financial market. Vittas (2000) points out several such advantages. One of these is that institutional investors and pension funds in particular have been argued to spur financial innovation, citing examples like Chile and Argentina as empirical evidence. Specifically, he argues that structural pension reform led to the advance of asset-backed securities, structured finance and derivative products, index-tracking funds, and other financial tools designed to insulate risk from market fluctuations. He further argues that institutional investor like pension funds have been responsible for pushing for the development of means for more efficient trading (including bloc trading, an elimination of minimum limits on commissions, and automated trading facilities). For these reasons, Vittas notes that private pension funds can aid in the growth of domestic financial institutions and domestic sources of finance. Such long-term benefits provide an impetus for the government to pursue pension privatization—in the hopes of developing its domestic financial market—and also provide a reason for a broad range of financial intermediaries and businesses operating in the capital market to lobby in favor pension privatization.

The financial sector in the post-communist countries was more developed than
outsiders often realize. Capital markets, to which Vittas refers above, were quickly operating in these newly capitalist countries. In Hungary, for instance, market capitalization soared from 1.5 percent of GDP in 1991 to nearly 30 percent in 1998. In Poland, market capitalization went from .19 percent in 1991 to nearly 18 percent in 1998. The Central Asian countries (Kazakhstan, Kyrgyzstan, Tajikistan, Turkmenistan, and Uzbekistan) saw very limited growth of businesses in the capital market. However, other post-Soviet countries—like Latvia, Lithuania, and Estonia—did see significant capital market growth. In short, the types of financial interests which would lobby in favor of pension privatization were present to varying degrees in the post-communist countries.

1.2.2 Studying Lobbying Influence on Policy Choices

In understanding who governs, the question we ultimately want to answer is who influences major policy outcomes. My focus is on understanding the influence of the private financial sector on pension policy outcomes and, as such, I conceptualize influence as being the ability to alter the chances of a specific policy outcome. In this context, this means the financial sectors’ ability to change the a priori chances of privatization.

Many studies of lobbying influence, however, have avoided studying lobbying influence on policy outcomes as its impact is difficult to quantify. Mahoney (2007) writes that,

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18 Data are taken from the World Development Indicators (WDI), 2008.
19 March (1955) considered influence to be the ability to induce change, noting that, “Influence is to the study of decision-making what force is to the study of motion—a generic explanation for the basic observable phenomena” (432). Hart (1976) considers power to be control over resources, actors, or outcomes. For interest group lobbying, the most relevant indication of power would be control over outcomes (as the purpose of lobbying is to obtain particular outcomes).
The aim of lobbying, or advocacy, is to influence public policy; thus it is natural that political scientists study lobbyists’ ability to achieve influence. As natural as it may seem, however, group scholars have not, by and large studied lobbying influence. Instead they have avoided it at all costs, troubling as it is to measure the concept quantitatively. In both the United States and the European Union (EU), scholars have focused on a whole host of lobbying-related phenomena—formation, organization, access, activity—but not influence (35).

Interest group studies that focus on when groups organize, have access to the government, or self-report influence are informative and insightful. However, the questions remain about the extent to which groups like private businesses ultimately shape policy outcomes. Even groups that claim to be influential may not actually accomplish many of their policy goals.

In discussing measures of interest group influence, De Bièvre and Dür (2007) conclude that:

Despite these limitations, we consider the control over outcomes approach to be the epistemologically most sound and empirically most pragmatic route towards assessing interest group influence…[precisely because]…this conceptualization of influence does not attempt to measure and abstract, unobservable object, ‘power,’ but focuses on its empirically observable effects in actual public policy, as if actors were really powerful(3).

Given political scientists’ enduring interest in understanding who governs, a contribution of this research is that it directly examines how lobbying influences policy outcomes. To the extent that empirical evidence reveals that the private financial sector does alter the likelihood of pension privatization, it provides a concrete, measureable way in which to understand both business lobbying influence and pension reform.

1.3 Organization of the Dissertation

The dissertation is organized as follows. In Chapter 2, I review existing explanations of
business lobbying. Although existing explanations of business lobbying offer important insight, they fail to fully consider how lobbying efforts are mediated by regime type and economic conditions. Moreover, we lack an explanation of why businesses might be influential on the adoption of reforms but not their subsequent regulation. Building on existing explanations, I present a theory of conditional influence. At the stage of adopting new policies, private businesses will be less influential in more democratic systems. In more democratic systems, businesses face more competition with other groups trying to influence the government as well as electoral pressures. Democratic governments are also less likely to risk undertaking reform proposals which may not provide popular short-term gains that help politicians win elections. However, private businesses that have been influential on the adoption of a policy may not be influential on its regulation. If private businesses in non-democratic systems do not continue to retain their economic and political utility to the government, they are unlikely to be successful in shaping subsequent regulatory policy.

To test my theory, I rely on quantitative research to reveal general cross-national trends complemented by case studies which reveal in greater depth how lobbying worked as a causal mechanism in pension politics. I examine three distinct time periods in Russian politics during which the level of democracy varies. The Russian case demonstrates why the private financial sector would be more influential in less democratic system and reveals the role that demographic crisis plays in getting pension reform on the agenda.

Chapter 3 presents cross-national evidence that confirms one important empirical implication of my theory. Specifically, I show that there is an interactive effect between
regime type and the size of the capital market as my theory of lobbying would predict. A larger capital market increases the likelihood of pension privatization in non-democratic countries, but does not in democratic countries. In non-democratic countries, lobbying claims from the private financial sector are enhanced by a larger capital market. In contrast, in democratic regimes, financial sector lobbying has to compete with popular pressures against pension privatization. As such, the size of the capital market has less impact because business lobbying is not as influential in the most democratic regimes. I do not wish to argue that business lobbying is not influential in more democratic regimes, but rather that its influence is less because of populist pressure. Moreover, accounts of the pension politic dynamics in the post-communist countries is consistent with the larger trends identified in the statistical analysis.

Building on and complementing the cross-national evidence, I present a case study of Russian pension politics in which I leverage changes in the level of democracy over three distinct periods. Chapter 4 focuses on the Yeltsin era from 1990 to 1999 during which Russia was the most democratic and during which there was no major overhaul of the pension system. The private pension funds were allowed to manage and invest voluntary retirement savings in the early 1990s. Although the pension funds lobbied extensively for the introduction of a system in which they would have access to mandatory retirement savings, their efforts were unsuccessful. Democratic politics meant that the Duma during this time period was controlled by factions that were not receptive to Yeltsin’s economic reform plans in general and market-oriented pension reforms in particular. Moreover, because Yeltsin relied on the oligarchs to stay in power, the private pension funds offered little political or economic utility to the presidential administration.

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Chapter 5 covers the period from 2000 to 2001 when Putin came to power and Russian democracy is on the decline. The changing nature of the Russian regime during this time period provided an opening for the private pension funds and investment companies to influence key bureaucracies and the presidential administration. In 2001, Russia’s major pension reforms were adopted. The nature of these reforms was more market-oriented than it would have been absent the influence of the private pension sector. Specifically, private pension funds and investment companies gained access to citizens’ mandatory retirement savings thereby constituting a substantial shift from the Communist-era PAYG system.

Chapter 6 examines the period from 2002 to the end of 2009 in which major legislative battles concerning pension policy have continued to be raised. Because political power was so effectively consolidated within the Russian state, the private pension funds no longer held any political or economic utility for the Putin administration. As such, the private pension sector has largely failed to influence the regulatory policy governing Russia’s new pension system.

In the conclusion chapter, I summarize the main findings, assess their generalizability, and identify questions for future research.
Charles Lindblom (1977) famously referred to the “privileged position” of business in politics—indeed, scholars have long maintained that business exercises significant sway in the political realm (e.g., Dahl 1961; Epstein 1969; Polsby 1963; Przeworski and Wallerstein 1988; Rose 1967; Truman 1951). Not only does money buy power, but governments concerned with economic growth may cater to the preferences of businesses even when their goals are unarticulated and firms unorganized. However, scholars have questioned the extent to which businesses are actually able to monopolize democratic politics (Block 1977; Vogel 1983). What follows from this, therefore, are two related questions of perennial interest: how and when can businesses influence policy outcomes, and does the type of political regime alter the political power of money? These questions are particularly relevant to the post-communist countries as they sought to simultaneously establish democracies and markets.

Post-communist pension reform is an especially useful and interesting empirical context in which to examine business influence on policy. Pension reform was on the agenda to varying degrees for all of the post-communist countries, and was contested by a myriad of groups with competing preferences; these included citizens, governments, current retirees, and bureaucracies. One group that has not received much attention in the
story of pension politics is that of private businesses, and specifically, the pension funds and investment companies which would profit from pension privatization.

A notable exception is Arce (2005) who provides compelling evidence of the role of private business lobbying in Peruvian pension reform debates. Arce’s research offers a basis on which to expect that businesses in the financial sector do recognize the profitability of pension privatization and will lobby the government in favor of it. Arce focuses on broader patterns of political response to market-oriented reforms and “feedback effects” of societal responses which can strengthen or weaken reforms. In contrast, my research focuses specifically on the role of private businesses in pushing for particular solutions to pension reform. Specifically, I seek to determine the conditions under which businesses in the private financial sector were able to sway post-communist governments to privatize their pension systems.

In this chapter, I present a theoretical basis for how and why the financial sector affected pension outcomes. The model I present is one of business pressure which accounts for when the financial sector is of political, economic, or informational utility to the government. In democracies, businesses in the financial sector had little influence on the decision about whether to privatize, but played a central role in regulatory design once privatization measures were adopted. Businesses are of less political utility in democracies because leaders are subject to electoral pressures; research grounded in the post-communist context has shown that welfare state politics were dictated by popular pressures more than was previously assumed (Roberts 2001). However, democratic leaders are likely to engage in policymaking which seeks information all of the major players involved. Because of electoral pressures, democratic leaders have incentives to
be more inclusive in policymaking forums and to operate on a more consensus-based model. Therefore, the domestic financial sector was of informational utility in setting regulatory policy in large part because of the important role it would play in a private pension system.

In non-democracies, lobbying efforts by businesses in the financial sector made pension privatization more likely, but did not ensure such measures would be regulated in a market-oriented manner. At the adoption stage, it was easier for the private financial sector to buy influence in non-democratic systems. Successfully pushing the adoption of privatization measures, however, does not secure influence on regulation. In regimes which have privatized pensions but in which power has subsequently been fully consolidated, the financial sector is unlikely to influence regulatory policy.

My theory offers a new contribution by emphasizing how the political regime affects a group’s lobbying ability differently at two distinct stages of policy influence—adoption and regulation. Moreover, my theory also counters welfare state research in which demography is thought to be destiny according to which aging populations dictate the scope of possible policy choices. Although demographic forces are thought to constrain governments and make options like privatization prohibitively expensive, I argue that aging populations also create an opening for the financial sector to lobby for market-oriented solutions like privatization. Lobbying success, in turn, will be determined by regime type which affects the access interest groups have to the government.

Finally, I argue for the importance of understanding regulation of newly privatized systems. Pension privatization is a policy phenomenon that has spread around
the world and redefined the nature of social protection. One of the key questions is how these new systems will operate in practice which is, in turn, shaped heavily by regulatory policy. The domestic financial sector would prefer that the new system be regulated in the most market-friendly manner, while certain powerful government bureaucracies will prefer to maintain a more state-controlled system. Therefore, whether or not the private financial sector is influential on the regulatory structure can have important implications for how the new system functions and, specifically, whether it functions in a manner that is more or less pro-market.

This chapter is organized as follows. In Section 2.1, I explain the overlooked role of private business lobbying in pension reform accounts and why including them is a crucial part of the story. In Section 2.2, I review existing work on interest groups and the political power of capital, noting their contributions and shortcomings with respect to the goal of understanding the role of the financial sector lobbying on pension reform. In Sections 2.3, I present my theory of conditional influence and consider its broader implications. In Section 2.4, I lay out the research design of the dissertation.

2.1 The Overlooked Role of the Private Financial Sector in Pension Reform

Despite the private financial sector’s clear vested interest in the establishment of private pension systems, existing explanations have largely overlooked the role of parts of the private financial sector in the design and adoption of the reforms from which it stands to benefit. However, the private financial sector has not figured prominently into accounts of pension reform. The presence of stakeholders in reform (i.e., the beneficiaries) who have a vested interested in lobbying for particular policies and
maintaining them once in place should increase the likelihood that reforms are passed and are not reversed (Graham 1998). Kornai (1992: 433) also notes the importance of the development of the private sector in securing market reforms.

Building on existing explanations, we can better understand the influence of the financial sector on pension reform. Studying the role of the private financial sector in pension reforms is more than simply adding another variable to the list of factors influencing pension privatization. Considering the role of the private financial sector is important because while the increasing maturity and cost of PAYG systems make privatization prohibitively expensive, I argue that aging populations also create an opportunity for the private financial sector to lobby policymakers. Examining the part played by the private sector is also significant because it counters prevalent notions about how demographic pressures influence welfare state reform. For pension reform, scholars have often framed demography as destiny. The age of the population determines whether the government has an incentive to change retirement benefits and whether the government can afford such measures (Myles and Pierson 2001; Pierson 1996). As populations age, the cost of pension systems rises, but they simultaneously become more costly to reform. Brooks (2009) notes that there is a non-linear relationship between the age of a population and the likelihood of pension privatization such that there is a window of opportunity during which the government faces pressure to reform and can afford to do so. In the very oldest populations, pension privatization is simply too expensive.

However, aging populations also provide an opening for business pressure by providing an opening which these businesses could use to lobby for their preferred
solution to the old-age crisis. This lobbying pressure means that demographic pressures do not lock-in systems to a particular outcome, contrary to prior research, but rather produce a political battle sparked by policymakers seeking solutions and businesses offering them. Pension privatization in particular was also hailed as a means of increasing domestic savings and improving macroeconomic performance (World Bank 1994), so that the financial sector could link the financial strains of aging populations on governments with a solution that promised additional economic boons.

The extent of the crisis should not necessarily translate into a greater depth of reform. Evidence from around the world indicates that countries with the oldest populations are not necessarily those which adopt the most privatized pension systems. While it is clear that aging populations initiate political debates about pension reform, the interpretation of these objective measures of the age of a population do not directly translate into specific policy solutions. Additionally, an older population should not translate into a greater opportunity with which the financial sector could pressure the government. It is sufficient that an aging population has been linked to increased fiscal strain to create a lobbying opportunity for the private financial sector.

Scholars have noted the importance of private actors in driving the transformation of economic policies including social policies. Charlton et al. (1998) note that private businesses were the main impetus behind private sector development in areas like education and healthcare. Likewise, they observe that state pension systems only shrunk in countries with a growing private pension sector. Despite a clear financial motive of the financial sector to lobby in favor of pension privatization and accounts indicating that they were involved in negotiations, most accounts of pension reform do not consider the
role of the financial sector including private pension funds in any depth. Research based on the post-communist context indicates that financial sector did play a role, but these accounts do not fully explicate their influence. Müller (2003, 85) notes that the financial sector backed reforms, but does not give them much credit as a causal force. Nelson (2001) further notes the inclusion of the financial sector in negotiations over Hungarian pension reform, but does not explore their role beyond this. Based on an in-depth consideration of Hungary, Poland, and Kazakhstan, Orenstein (2000) notes that financial firms were often influential on the regulatory structure even when they were excluded from negotiations regarding the adoption of pension privatization.

Cook (2007) offers an authoritative account of the development of post-communist welfare politics. She notes that the early Putin administration began instituting corporatist measures of integrating business lobbies, like the Russian Union of Industrialists and Entrepreneurs (RUIE) into decision-making. She notes that the final major struggle was over the investment mechanism which would be used and that, under lobbying pressure from financial groups, the final plan adopted was a compromise (p. 171-172). Although she indicates that financial interests lobbied heavily, her central explanation for the pace and nature of welfare state reforms across countries focuses on the role of statist stakeholders—undoubtedly important players—as the agents of change. Thus, Cook’s account—like other accounts of post-communist pension privatization—suggest that there were instance in which the financial interests played an important role, but does not fully explore how or why this was the case.

Research on pension reform in other parts of the world has also largely overlooked the role of private businesses in lobbying for change, as in Müller (2003) and
Nelson (2001) where they receive only minimal attention. A notable exception to this is Arce (2005) whose research indicates the importance of studying the role of the private pension industry based on the case of Peru. Arce notes that privatization produced a clear gain for a specific group—the pension industry (which is a subset of the larger financial sector). Part of the reason that pension privatization reforms succeeded in Peru was precisely because the private pension industry constituted a well-organized group of winners in contrast to the poorly organized and disperse group of “losers,” i.e. the citizens. The business sector was the one group advocating on behalf of a private pension system to the government and citizens (p. 90). Given Arce’s research, we should be surprised if the private financial sector is not involved in the reform process. The preference of the financial sector is clear and they have shown a willingness to lobby in favor of a privatized pension system which is most profitable to them.

Observing Financial Sector Influence. If businesses in the financial sector are important stakeholders to consider in the politics of pension reform, then we should consider how we know when they are influential. The decision to privatize alone is not evidence that business pressure made the government do it. Instead, we can identify financial sector influence on pension reform in two more concrete ways. First, we can look for a statistically significant and positive relationship between factors that should enhance lobbying efforts and the likelihood of pension privatization while controlling for additional causal factors. As I will explain in greater depth below, a larger capital market should be expected to enhance the lobbying claims of private pension funds. Therefore, a larger capital market should make pension privatization more likely if the lobbying explanation is correct.
Second, if the domestic financial sector was influential, then we should observe their inclusion in policy deliberations. Additionally, we should see changes in draft legislation so that the final legislative outcome is more market-oriented than initial proposals. Businesses in the financial sector can, of course, be influential outside of official policy deliberations and evidence of informal consultation is important to consider as well. Taken together, this evidence makes a plausible case that the domestic financial sector did indeed play an important role.

A critical point is to distinguish whether governments were swayed by the pressure of international financial institutions like the World Bank or that of the domestic financial sector. Orenstein (2008, 91-92) describes how initially in the policy process, the World Bank focused on provided technical advice within governments considering pension reform. The World Bank would try to assist in building public support and took an active part in revising pension reforms and implementing them. Although the World Bank played a role in getting pension reform on the agenda and offering technical advice, its advocacy was not as unified as some have characterized it to be. Critics noted that pension privatization was not well suited to all countries and that other reforms would be better in some cases (Orszag and Stiglitz 1999). In response, the World Bank modified its stance to advocate the option of a notional defined contribution (NDC) scheme in some cases. The result was that the World Bank did not consistently promote pension privatization and applied more pressure to some countries than others. In contrast, businesses in the financial sector preferred a private pension scheme over any other possible reforms.
Moreover, cross-national statistical analysis can examine whether the size of the financial sector increases the likelihood of pension privatization while accounting for whether the effect of World Bank involvement. In the event that business in the financial sector participated in deliberations and there is a link factors that enhance lobbying and pension privatization, then the most plausible explanation is that the financial sector was able to pressure the government into adopting its preferred policy solution.

Finally, the timing of the decision to privatize and the involvement of representatives of the financial sector is important to consider in looking for evidence of their influence. The World Bank played a significant role in getting the pension privatization option on the agenda and in providing technical assistance to possible supporters within the government. However, after initial proposals were made about how to reform pensions, then domestic interest groups—like businesses in the financial sector—came more into play. By tracing the timing of political debates over pension reform, we can further distinguish between the role played by international actors like the World Bank versus private pension funds.

2.2 Existing Explanations of Business Lobbying

Existing literature identifies three important utilities of business to the government—political, economic, and informational. First, research grounded in the American context points to money as an important determinant of political power (Gordon and Hafer 2005; Grossman and Helpman 1994, 2001; Langbein 1986; Wright 1989). Overall, they predict that groups that are resource-rich are more likely to influence policy outcomes. Plotke (1992) found that the best predictor of whether or not
corporations became politically active in the 1970s was not related to any rise or decline in profits or other sector-specific characteristics, but the size of the business itself. Even broadly-defined resources like proximity or access to government—which are identified as important by Wright (1990)—can be bought with money.

Aside from their ability to buy political influence, businesses interests have a unique economic utility that lends them additional leverage with the government. Lindblom (1977) notes the privileged position of business in politics and the enormous advantages that money can buy in lobbying activity and influence on the government. Money enables groups to engage in the whole gamut of activities that a group can use to persuade the government to adopt particular policies from mobilizing citizens to act to making direct political contributions. Moneyed interests are uniquely powerful in their ability to pressure the government to adopt policies that are economically beneficial. For instance, important leverage can be exerted by convincing decision-makers that a policy is expected to influence important economic outcomes (Linblom 1982). The financial sector could use its capital (i.e., money) to engage in traditional lobbying activities, but can also make claims regarding which policies will allow their sector to grow and in turn promote economic growth just as Lindblom might have predicted.

The economic utility of businesses, therefore, is enhanced by the resources it commands even when explicit lobbying does not occur. For instance, Gehlbach (2008) finds that the government should favor businesses that are most economically valuable, in this case those that will most reliably pay their taxes, regardless of their degree of organization. In cases like Russia in which tax revenue was politically significant and sectors varied widely in their taxability, the state would favor the development of those
sectors from which it was easier to collect revenue by their nature. Gehlbach’s findings are consistent with political economy literature which finds that capital need not be organized to influence policy decisions. While the financial sector did explicitly lobby the government, this suggests that they did not have to in order to have the government adopt their policy preferences.

Arguments about the structural dependence of the state on capital suggest that formal organization is less important in shaping policy outcomes. In the case of businesses, bargaining power emanating from their structural position in the economy is a powerful resource (Frieden and Rogowski 1996; Bernhagen and Bräuninger 2005). Theories of the structural dependence of the state on capital argue that even when explicit lobbying does not occur, the state is reliant on capitalists for tax revenue and economic growth thereby lending them a great deal of influence (Block 1977; Lindblom 1977; Poulantzas 1973; Przeworski and Wallerstein 1988). Lindblom (1982) went so far as to characterize the market as a prison in which a preoccupation of the state with meeting business interests constrains democratic policymaking. In assessing structural dependency theories, Przeworski (2008) concludes that,

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\text{[S]tructural dependence need not imply that partisan and institutional differences are irrelevant…But a science of politics that ignores economic constraints on popular sovereignty misses what all democracies have in common, namely, that they exist in societies where the future of all depends on the decision of some, those who control productive resources. Popular sovereignty is constrained by private ownership of collective resources (16).}
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This conclusion about the implicit power of businesses is echoed in the terms of exit, voice, and loyalty game in which the powerful do not always need to exercise voice to be influential (Hirschman 1970). Most importantly, these arguments suggest that in many
cases, capital does not even have to organize to be an influential pressure on the government. In lobbying, therefore, businesses are likely to be particularly persuasive when they can argue that a particular policy will hurt or harm the larger economic conditions in a country.

The utility of businesses to politicians in their potential to contribute to economic growth was especially true in relation to arguments for pension privatization and the private businesses which would benefit from it. The economic leverage of businesses in the financial sector was enhanced by their exit option that provided them with an implicit lobbying tool. Scholars have noted that businesses’ mobile assets provide an exit option that translates into leverage with the state to obtain specific policy options (Hirschman 1970; Bates & Lien 1985; Frieden 1989). Moreover, the larger the financial sector the greater the implications of corporations taking their business elsewhere.

Finally, informational expertise can be a crucial lobbying resource, particularly when the adoption of a new policy with which policymakers have limited experience is being considered. In a classic work on lobbying influence—Who Governs? Democracy and Power in an American City—Dahl (1961) explains that resources can be broadly defined to include anything that can influence policy outcomes including resources like information. Thus, while money lends groups political power, information can be equally beneficial in persuading politicians to take action. For instance, using in-depth cases studies of environmental and educational policy, Esterling (2004) shows that the information possessed by groups shapes how effectively they lobby. He offers evidence that when groups can persuade the government that they have useful expertise, the government should be more receptive to their policy preferences.
The interest group literature provides a basis on which to understand the lobbying influence of the financial sector. While these theories inform what factors contribute to business influence, they ultimately give us an incomplete explanation for the conditions under which businesses will successfully lobby the government in general and, in particular, the conditions under which the financial sector would influence post-communist pension privatization.

Additionally, existing explanations have failed to make a sufficient distinction between business influence on the adoption versus the regulation of policies. In the study of pension reform, much more attention has been paid to explaining the politics behind the adoption of pension privatization measures rather than its regulation or operation in practice (see Chlon-Dominczak and Gora 2003 for one example). However, it is theoretically and empirically important to consider regulatory policy over newly privatized systems. According to Orenstein (2000), the implementation of pension privatization entails a number of important regulatory decisions regarding the funds. Specifically, it entails the establishment of private pension funds, appointing a government agency to oversee these accounts, the creation of an individual account for each contributing citizens, and finally the transfer of mandatory contributions to the private accounts. Orenstein (2000) notes that a consideration of the policy decisions at this stage have major consequences. He writes that,

Numerous issues arise in the early implementation stages that were not resolved in the reform legislation and cry out for further regulation or legislation. Deliberation at this stage tends to accentuate the role of business organizations involved in implementation, and interest groups aggrieved by some aspect of the reform. Wholly new actors often enter the process, in some cases created by implementation. Amendments and changes during the implementation stage often
result. The implementation stage never properly ends, but deliberation within it is likely to be particularly intense in the first few years (15).

Thus, we should expect business actors like the financial sector who will—by design of the system adopted—be important players in a new private pension system, to be actively involved in negotiations over how that system is regulated.

Influencing the regulation of the new private pension system is also an opportunity to fight for alterations to the original reform regarding points with which they are dissatisfied. Empirically, the preferences of the financial sector include setting up individual accounts to which mandatory savings can be contributed and minimizing the number of government agencies with which they must work (Orenstein 2000). These were all issues that had to be resolved regarding the regulatory structure.

Among the post-communist countries adopting pension privatization measures, often legislation allowed for significant latitude in how those measures would be regulated. For instance, governments could make private investment of mandatory pension contributions the default option rather than state management. Alternatively, the government may choose to restrict the ease with which citizens can opt to transfer their contributions into private management.

When the financial sector has more influence on regulation, we are more likely to observe that the legislation passed is enacted in a more market-oriented manner than it would be otherwise. For instance, in Croatia the government actively facilitated the establishment of private pension funds. Specifically, the government ensured registration of most of the pension funds within a 3 month period at the end of which it immediately began transferring mandatory contributions into the private accounts. The capital market
in Croatia did not allow for a diverse set of investment options and the government expanded its debt instruments for the pension funds and offered them special discounts. The result was that in the first 4 months of 2002, the return on government bonds for the pension funds was described as an “exceptional” 15 percent which, when taking into account the rise in consumer prices, meant a real rate of return of about 8.9 percent (Anusic et al. 2003, 59-62). It was partially in the interest of elected politicians to insure that the private pension funds would have high initial rates of return. However, there were costs associated with making government bonds available at discount to the private pension funds. Anusic et al. (2003, 62) comment that, “it is unlikely that such a level of generosity at the expense of the taxpayers was equally desired.” Such a measure strongly indicates an action by leaders in the government which was uniquely favorable for the private pension funds, potentially even at the expense of popular support (Anusic et al. 2003, 59-61).

In Kazakhstan, the financial sector had little sway in the regulation of what was the most radical pension privatization scheme adopted amongst the post-communist countries. The pension funds in Kazakhstan have been restricted in their ability to invest in private companies. For instance, the pension funds were supposed to be allowed to invest in approved Kazakh companies which were due to be privatized as part of the “Blue Chip” program. However, the privatization scheme was delayed and then scaled back limiting their options. Additionally, the government required that more than 50 percent of investments be in government securities to which pension funds have objected (Andrews 2001, 38). The Kazakh government has also not offered the same kinds of discounts on government bonds as were seen in Croatia so that this requirement is a
hindrance not a help. The Croatian government also did not require that more than 50 percent of investments be in government securities. Rather, it offered more government bonds with special discounts, arguably at the expense of current taxpayers, to boost initial pension fund returns. Andrews (2001) notes that Kazakh investment restrictions contrast with the Chilean system, on which Kazakh pension reforms were modeled, where investments like mortgage bonds played an important role.

Existing explanations offer important insight into the utility of businesses—political, economic, or informational—to the government. However, important questions remain as to how the businesses in the private financial sector would be able to utilize these resources to influence pension privatization in different political regimes and at different stages of the policy process. I now turn to a theoretical explanation of when the financial sector will be able to influence the adoption and regulation of pension policy.

2.3 A Theory of Conditional Influence

Building on these existing explanations, I lay out a model of business pressure in which the leverage of the domestic financial is determined by its utility—political, economic, or informational—to the government. I consider financial sector influence on the adoption and subsequent regulation of private pension systems in democracies versus authoritarian regimes.
2.3.1 Adoption of Pension Privatization

Among the post-communist countries, the most democratic countries were also the most market-oriented.\textsuperscript{20} This correlation suggests that the most democratic countries might be the most receptive to policy proposals from private businesses as they were ideologically more market-oriented regimes. In particular, private businesses with proposals for conducting further reforms should be more likely to have access to governments which were ideologically prone to support a market-oriented agenda.

Survey evidence of businesses from the late 1990s indicates that in countries like Poland the regulatory and legal system were much friendlier to business than in other countries like Russia which have ultimately proven to be much less democratic (Frye and Shleifer 1997). In the Polish case—which Frye and Shleifer characterize as adhering most closely to the invisible hand model—we might think that the government would be more receptive to the proposals of private businesses regarding the best policies to adopt because the government was ideologically more market-oriented and less predatory.

However, there are several reasons that we should expect democratic institutions to have hindered the ability of the financial sector to influence the adoption of pension privatization. First, the financial sector held less political utility for democratic leaders over non-democratic ones as elected officials rely more on popular support to stay in power. Moreover, where there is democratic competition amongst a wide variety of groups aiming to influence the government, the financial sector should be less useful than in would be in a non-democratic system. Research on the post-communist cases has

\textsuperscript{20} For a description of the relationship between democratic and economic reforms in the post-communist countries, see the 1999 transition report from the European Bank for Reconstructions and Development (EBRD). EBRD experts identified several political factors which contribute to more radical market-oriented reform including the extent of organized political competition.
indicated that special business interests are indeed more constrained by democracy (Hellman 1998; Hellman and Schankerman 2000). In less democratic systems, the influence of powerful rent-maximizing business interests is less constrained, if at all, thereby resulting in reforms that are damaging to overall economic growth. In more democratic systems, however, the sway of powerful business interests is restricted because politicians are concerned with creating policy outcomes that help them secure popular support.

The point is not that business interests will not be influential in democratic systems, but rather that their influence is less when leaders are under democratic pressures. Lindblom (1968) notes that all democracies have restrictions on the use of money in politics specifically to help prevent special business interests from dominating the system. Other research supports this argument, finding that pluralist interest group systems prevent concentrated interests from monopolizing the policy process (Sheingate 2001). While non-democratic systems are not entirely free from popular pressures, public support should dictate policy choices much less. Accordingly, money may buy power but less so in democratic regimes.

Second, the financial sector should be of less informational utility when democratic governments were deciding whether to adopt pension privatization measures. For a market-oriented government considering pension reform, there were many sources of information besides the financial sector. The World Bank heavily promoted pension privatization in the 1980s and 1990s although it has since somewhat modified its stance. Governments could also obtain information from other countries which had privatized pensions. Domestic economic advisors were yet another source of information.
Given the wide range of actors available to provide information about pension privatization, even governments which were ideologically prone to be more market-oriented would not necessarily turn to the financial sector as a source of expertise on whether to adopt a private pension system. Furthermore, the government could choose to adopt a pension system in which private financial sector would play no role so that their expertise would not be useful in deliberations. Only once the government had decided to adopt a private pension system in which the financial sector would play a role would those businesses arguably have unique expertise to offer. When debating over which pension reforms to adopt—be they parametric or structural—the financial sector would also be a biased source of information in choosing amongst alternative reform plans. Due to the competing pressures democratic politicians were attempting to meet, the policy expertise of the financial sector did not help it to be influential as an interest group (i.e., its informational utility was low).

Finally, it is important to consider the financial sector’s economic utility in relation to pension privatization for democracies versus non-democracies. The promise of economic growth through the development of the financial sector should be more directly influential in non-democratic regimes. Although all regimes care about economic growth, democracies cannot concern themselves with economic growth alone because of electoral pressures and greater pluralism in interest group competition. Rather, politicians in democracies must consider a myriad of competing preferences including short-term demands for welfare benefits like pensions.

Politicians in democracies also operate under shorter time frames, namely the period until their next election. Leaders in non-democracies can afford to concern
themselves with longer timeframes because they do not rely on elections to stay in power. Such leaders can also accept a higher degree of uncertainty about whether and when pension privatization will foster the development of the financial sector and improve economic growth. If they are wrong, then they do not run the same degree of risk of losing office. Therefore, the willingness of leaders to adopt pension privatization for economic reasons should be higher in non-democratic regimes.

In summary, regarding leaders’ decision about whether to privatize pensions, the informational, political, and economic utility of the financial sector should be much higher in non-democracies than in democracies meaning the financial sector should be more influential in non-democratic regimes. Although I have framed this terms of democracies versus non-democracies, this can also be conceptualized continuously. As the level of democracy declines, there is a decline in the utility of the financial sector to elected officials in deciding whether to privatize.

2.3.2 Regulation of Pension Privatization

As with political battles over the adoption of pension privatization, the influence of the financial sector on regulatory policy will vary depending on whether the regime is democratic or not. Influence on the adoption of pension privatization does not ensure that businesses in the financial sector will have sway over regulatory policy.

Democracies & Regulation. If a democratic government adopts pension privatization measures, there are a couple of reasons we would expect the financial sector to be influential on the regulatory structure governing the system. First, the desire for well-functioning policies, in turn, leads to a policymaking strategy in which the
government seeks outs more sources of advice including the domestic financial sector. Leaders in a democratic state should want to implement a system that functions well producing a fiscally sustainable system, one which provides adequate retirement savings, does not overburden the current working population with high contributions, and promotes long-term economic growth at the same time. In other words, leaders in a democratic government should be concerned with establishing a system that, at a minimum, citizens perceive as functioning well and ideally which does offer returns to citizens which help politicians get re-elected. There are leaders who do not prioritize putting into place a good, well-functioning reform, at least not in the same sense that democratic leaders do. In authoritarian regimes, leaders do care about putting policies in places that accomplish their goals (cutting long-term pension obligations, for instance) but care much less, if at all, about goals that serve the average citizen (a transparent system, adequate retirements savings, and contributions that are not burdensome).

Following from this, democracies have an incentive to learn and innovate that non-democracies do not. The reason is that democratic leaders care about certain policy outcomes more than non-democratic leaders. Promoting policy outcomes that are good for the average citizen like adequate pension benefits with sustainable financing are harder than accomplishing goals like cutting spending or generating more revenue. Additionally, the cost of policy failures for elected leaders in democracies is higher in the short-term (i.e., they may lose elections), while authoritarian leaders can afford a longer timeframe in which to see whether reforms pay off. Because democratic leaders are concerned with electoral timeframes, they should be less willing to wait and see if a policy works and more likely to seek out policy advice and change direction if a policy is
not producing the desired outcome. For instance, in the short-term privatizing pension systems produce high rates of returns to savings and operate transparently to citizens. If this does not occur, democratic leaders may choose to reverse privatization measures.

Empirically, we observe that the democratic post-communist governments were more likely to engage in policy innovation. For instance, Orenstein (2001) details the uncertainty surrounding market-oriented reforms in the post-communist countries and the learning processes on which they relied including policy alternations in order to select the best methods. Innovation is characterized by this willingness to try different policy instruments to make a particular type of policy work; we can observe innovation in the willingness of governments to adopt different strategies to accomplish the same goals. According to Orenstein, democratic governments were more likely to rely more on policy adjustments and innovation.

For democratic regimes, there are several areas in which the financial sector can arguably offer useful expertise regarding regulatory policy over private pension systems. The specific type of information to which financial sector could, at least arguably, offer insight include how domestic financial markets operate, setting up and managing individual accounts, and yet to be specified parameters such as administrative fees and the acceptable degree of investment risk. Leaders in democratic countries certainly had other sources of information on which to draw including the World Bank and other countries.21 Prior to the adoption stage, however, it was not clear that the private pension funds would play any important role and therefore their policy expertise was less useful

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21 Leaders in non-democratic countries had access to other sources of information as well and in non-democratic regimes there was no the same tendency to rely on policy adjustments or innovation after the policy was passed.
and potentially biased towards what may not have been the preferred solution. However, once a democratic government had chosen to privatize its pension system, the private pension funds would be important actors in the new system. As such, lobbying regarding regulation is a way in which the private financial sector could offer practical advice and voice concerns about how the system was designed to operate. Even if leaders drew on other sources of information, for democratic leaders spearheading pension privatization, it would be more surprising if they did not consult with private pension funds.

The financial sector could also offer important insight into how the market would react to pension privatization measures including the likely economic consequences of taking such measures. In this case, the informational and economic utilities of businesses in the financial sector overlap. This is consistent with arguments about the structural dependence of the state on capital. If the state wants to use pension privatization to promote an increase in domestic savings and overall economic growth, then it should be concerned with how businesses in the financial sector will react to pension privatization even if such businesses fail to articulate preferences. Business in the financial sector did, in fact, express preferences about how pension privatization was pursued. Because of concerns about how pension privatization would affect the economy and how businesses might react to these policies, knowledge of the preferences of financial sector interests was important to policymakers.

Specifically, policymakers would want information on what types of private pension funds would emerge and how quickly. Information on how businesses in the private pension industry would react to regulations would be important as well. The government was also likely to want to keep a close watch on the early activities of
businesses in the private pension sector which would be easier to do if it worked closely with them. Information on the reaction and operations of the private pension market would vary by country, so that the utility of the World Bank and other countries’ experiences would be less useful in this regard.

This theoretical expectation is consistent with the example of regulatory policy in Croatia versus Kazakhstan used above. The regulation of the new private pension system was more market-oriented in Croatia than in Kazakhstan. This is consistent with the explanation that businesses in the financial sector—and specifically those in the private pension sector—were more influential in Croatia because it is more democratic. In Croatia, initial rates of return were a major priority (which is unsurprising for elected officials concerned with maintaining popular support) while in Kazakhstan the priority appears to have been cutting government spending (in which popular pressures were less pressing given President Nazarbayev’s consolidation of political power). Policy outcomes alone, however, are not definitive evidence of business influence. Rather, in systematically considering whether private businesses were more influential, we should also observe their inclusion in policymaking forums, a task I undertake in the empirical case study chapters.

Additionally, the extent to which the financial sector can portray themselves as having a useful expertise that provides valuable information to the government will depend on how developed the sector is. A larger financial sector should be able to more convincingly claim that they have policy expertise. The government may also be more concerned about the economic response if the sector is larger. This means that we should expect there to be an interactive effect between lobbying and the level of democracy in
determining financial sector influence on the regulatory structure of the new private pension system. In countries where the financial sector is very underdeveloped, they should have a less credible claim to information that is useful in deciding how and at what pace to enact a policy. In countries where the financial sector is more developed, their informational utility should be higher. Therefore, it is both the extent of democracy and group characteristics which interact to determine whether the financial sector will be influential on the regulatory structure.

Finally, I do not mean to imply that the involvement of the financial sector allows for objectively better policy outcomes for citizens or the government. It is not the case that more business influence means the system will run better than if businesses were excluded. Rather, the incentive of democratic government to pursue policy innovation and to learn about new policies—particularly from actors who will play a central role in the new system—suggests the government would be receptive to including the financial sector in discussion of regulatory policy. Democratic leaders should be cautious before adopting new major policy initiatives and, in turn, be innovative in making adjustments to ensure that these policies will work well. This provides an opening with which the financial sector can then push its own agenda.

*Non-Democracies & Regulation.* In non-democratic countries the financial sector is not guaranteed to maintain their influence over regulatory policy just because they were influential in the decision to adopt private pension systems. First, in non-democracies, the informational utility of the financial sector for political leaders deliberating over regulatory policy is much lower. Authoritarian leaders care much less about implementing policies in a way that is good for the majority of citizens and
prioritize accomplishing goals like cutting the state’s long-term pension obligations and, possibly, promoting economic growth. This means that authoritarian leaders care less about policy innovation or learning as they do not run the risk of electoral consequences associated with citizens’ perceptions that the policy is functioning poorly. Therefore, we should not expect leaders in non-democratic countries to typically employ tactics like policy roundtables which bring together major policy actors in setting regulatory policy. As such, the expertise of the financial sector is not valued by non-democratic leaders implementing pension privatization. Again, this is not because business sector involvement would necessarily produce better policy outcomes, but because there is less incentive for non-democratic leaders to seek out additional policy information from interest groups.

Moreover, authoritarian leaders can accomplish goals like cutting pension spending through privatization without information from the financial sector. This means that the economic leverage of the financial sector is much lower because authoritarian regimes are less concerned with promoting broad economic growth in the short-term. My point is not that the financial sector does not in principle have useful information for non-democracies implementing private pension systems, but rather that leaders in non-democratic countries do not have an incentive to solicit advice from interested third-parties solely for informational purposes.

Second, for non-democracies, the financial sector would be influential on adoption but not regulation if, after adoption, there is a shift in the political system
resulting in a consolidation of political power within the state apparatus.\textsuperscript{22} In such cases a single leader or a single party will have effectively monopolized control over elections including national and local politics. Private businesses in the financial sector would lack political utility in such systems for reasons that are especially evident in the least democratic post-communist countries. Examples include Belarus, Kazakhstan, and Russia. These regimes maintain power through control over the state apparatus and—in the case of Russia and Kazakhstan—in controlling and profiting from the country’s natural resources. In such systems, leaders do not rely on monetary contributions from businesses in the financial sector in order to win elections. Nor are monetary contributions from the financial sector an important source of revenue. Such a dynamic in which power has been so thoroughly consolidated only exists in the very least democratic systems.

I do not mean to overstate my claim by arguing that the financial sector will never influence regulatory policy in non-democratic systems, but rather argue that they are less likely to influence regulatory policy in such cases.

\textit{2.3.3 Lobbying, the Capital Market, and Pension Privatization}

One way in which to observe the influence of financial sector lobbying on pension privatization is by considering the role of the capital market. Experts have pointed to the size of a country’s domestic capital market—which encompasses all publicly tradable companies and is measured as the number of stock multiplied by the

\textsuperscript{22} The influence of the financial sector could also be expected to wane if the system became much more democratic. If the system becomes much more democratic, then the financial sector will not be able to use its money to buy influence as easily (although democratic systems should value the informational utility of the financial sector more at the implementation level, as argued above.
price of the stock—as one of the possible factors influencing the decision on whether or not to privatized pensions. Vittas notes that, “The link between pension reform and capital market development has become a perennial question that is raised every time the potential benefits and preconditions of pension reform are discussed” (2000, 1). There is not agreement, however, on the effect that the capital market will have.

There are two predominant explanations of the connection between the capital market and the likelihood of pension privatization. Figure 1 depicts different theories about the link between market capitalization and the likelihood of pension privatization. One existing explanation is that the capital market must be sufficiently developed before pension privatization is feasible; this is labeled Theory #1 in Figure 1. The other explanation is that, because pension privatization is advocated on the grounds of expanding the capital market, as the capital market grows, governments have less of an incentive to privatize pensions; this is Theory #2 in Figure 2.1.
Neither of the existing arguments regarding the capital market is theoretically persuasive nor is there compelling empirical analysis for either. Several scholars have persuasively argued that these technical prerequisites have been overstated (Vittas 2000; Walker and Lefort 1999 in Walker and Lefort 2002). For the system to work well, the government should show a commitment to financial stability, should encourage the development of well-functioning banks and insurance companies, and should establish the necessary regulatory agency (Vittas 2000: 7). Pension fund assets accumulate gradually giving the government plenty of time to adopt such measures. A developed capital market, therefore, is not necessarily a prerequisite to providing the basis of a system in which pension privatization can be implemented.
Another theory (labeled Theory #2 in Figure 1) is that where the capital market is very small, the government will pursue pension privatization in order to increase the size of the domestic capital market. The converse of this is that in countries with very developed capital markets, governments do not see any need to privatize pension systems. This argument is not persuasive in large part because pension funds are only one way for the government to encourage the development of the domestic capital market. If the government’s goal is a larger capital market, there are a number of ways to accomplish this other than pension privatization which is an option that entails substantial transitional costs. While pension privatization might in part be an effort by the government to develop the capital market, we should not expect the presence of an underdeveloped capital market alone to prompt pension privatization.

Theory #1 and #2 are not exclusive and can be combined so that the predicated relationship between market capitalization and pension privatization looks like an inverted U-shape. In this case, there is some minimum level of capital market development that is necessary for reforms to be feasible, but when the capital market is already quite large the government will have little incentive to privatize pensions.

I offer an alternative explanation of the role of the capital market in pension privatization, one which is linked to business lobbying and regime type. Taking into account how developments in the capital market would affect the ability of businesses in the financial sector to lobby the government produces a distinct prediction from either of the two existing explanations. As the capital market grows, investors’ arguments about the feasibility and benefits of pension privatization should be more credible. In countries in which large capital markets are already operating, policymakers are more likely to
recognize the benefits of securing future investment to maintain this market. There should also be a greater fear of capital flight in countries with large capital markets so that policymakers should take actions that are perceived to retain future investments. Lobbying by businesses in the financial sector serves the function of articulating the concern to policymakers that a failure to privatize pensions would have negative consequences for an important part of the economy, i.e. the capital market. Where capital markets are small, however, the claim that a lack of privatization hurts an important market is unpersuasive because capital markets are already small and therefore capital flight has much lower consequences for the general economy.

We must also take into account regime type, as argued above. The lobbying of businesses in the financial sector for the adoption of pension privatization is more likely to be successful in non-democratic regimes. Moreover, the size of the capital market is more likely to enhance the claims of the financial sector in non-democratic systems where they enjoy better access to those in power and leaders are less concerned with popular pressures like maintain current benefits. Conversely, in democratic regimes, the size of the capital market is much less likely to enhance the claims of businesses in the financial sector whose lobbying efforts are hampered by other popular pressures. Therefore, because of the nature of lobbying, we are likely to observe that larger capital market in non-democratic countries makes pension privatization more likely, but that the size of the capital market does not affect the likelihood of pension privatization in non-democratic regimes.
### 2.3.4 Summary of Argument

My argument is summarized in Table 2.1 below. For democracies, the financial sector will not influence the decision about whether to adopt pension privatization but will influence regulation if such measures are taken. For non-democracies, the financial sector will influence the decision to adopt pension privatization but will not influence regulation if political power is further consolidated within the state apparatus. Additionally, because lobbying should be influential on the adoption of pension privatization in non-democracies but not in democracies, the size of the capital market will affect lobbying efforts in the former but not the latter.

### Table 2.1: Expectation regarding Regime Type & Policy Stage

<table>
<thead>
<tr>
<th></th>
<th>Adoption</th>
<th>Regulation</th>
</tr>
</thead>
<tbody>
<tr>
<td><strong>Democracies</strong></td>
<td>Private Financial Sector Not Influential</td>
<td>Private Financial Sector Influential</td>
</tr>
<tr>
<td></td>
<td><em>Lobbying efforts unaffected by the size of the capital market</em></td>
<td></td>
</tr>
<tr>
<td><strong>Non-Democracies</strong></td>
<td>Private Financial Sector Influential</td>
<td>Private Financial Sector Not Influential</td>
</tr>
<tr>
<td></td>
<td><em>Lobbying efforts enhanced by a larger capital market</em></td>
<td></td>
</tr>
</tbody>
</table>
For simplicity’s sake, I have discussed my theoretical expectations in binary terms, i.e. democracies versus non-democracies. However, the effect of democracy can accurately be considered to be continuous so that as a country becomes more democratic, the dynamic described for democracies applies and as a country becomes less democratic, the corresponding dynamic is relevant. The key point is that the market operates as a source of pressure whose influence is mediated by the level of democracy.

My three central hypotheses are the following:

*Hypothesis 1: Influencing Adoption.* If the system is more democratic, financial sector lobbying will be less influential on the adoption of pension privatization. Conversely, if the system is less democratic, financial sector lobbying will be more influential on the adoption of pension privatization.

*Hypothesis 2: Size of Capital Market & Lobbying.* A larger capital market should enhance the lobbying efforts of the financial sector in non-democracies, but should not influence lobbying efforts in democracies. Therefore, we should observe an interactive effect between regime type and the size of the capital market because of how each affects lobbying by businesses in the financial sector.

*Hypothesis 3: Influencing Regulation.* If the system is democratic, financial sector lobbying will be more influential on regulation (which can be observed in the extent to which regulation is market-oriented). If the system is not democratic, the financial sector lobbying will only be influential on regulation if the financial sector provides key political support for the regime.

These hypotheses posit that there is an interactive effect between economic factors like market capitalization and the level of democracy on pension policy because of how changes in the regime affect lobbying. Critically, the influence of the private financial sector—here, the private pension funds—is altered by the degree of democracy. We also should see the influence of the private financial sector change depending on whether it is the adoption or regulation of pension privatization that is at stake. The key point is that policymaking differs in democratic and non-democratic regimes.
2.4 Research Design of the Dissertation

The choice of research design for this dissertation is motivated by the comparative nature of the question and the hypotheses generated by the theory presented above. The theory was generated by considering existing explanations of business lobbying and literature on post-communist economic reform rather than being based on the experiences of a single country. I utilize both large-N statistical analysis and small-N qualitative cases to answer the question of when the private financial sector will influence policy outcomes.

My research design follows the nested-analysis approach advocated by Lieberman (2005). One of the primary advantages of the nested-analysis approach is that we utilize multiple types of evidence to answer a question. According to Lieberman, one should begin with a large-N analysis. If the results of the large-N analysis are robust and satisfactory, then a case should be selected which is “on the line” and the researcher should assess whether the case(s) fit the original theoretical model (Lieberman 2005, 437). I use the cross-national statistical analysis to test my hypothesis that a larger capital market will only make pension privatization more likely in less democratic systems thereby providing important insight into one aspect of cross-national trends. This analysis further identifies several variables which were and were not influential on the decision of the post-communist countries to privatize pensions. Because the results of the statistical analysis do indicate a cross-national trend and highlight that democracy and the capital market have an interactive effect, I then further explore my hypotheses in the context of case studies.
The large-N statistical analysis looks for determinants of pension privatization across the post-communist countries over time. Geddes (2003, 138) notes that it is preferable to look at the influence of an interest group (or groups) in one policy area across countries, rather than trying to look at the influence of an interest group on different policies—which have different costs and benefits—within the same country. In addition to a consideration of the interactive effect of democracy and market capitalization, the statistical analysis provides a test of several of the other variables that the literature hypothesizes will affect the decision to privatize pensions. I use a binary dependent variable capturing whether or not pensions were privatized in a given country and year. The level of democracy is one of the main independent variables of interest. I choose to use the Freedom House measure of democracy rather than Polity (Beck et al. 2001) or the binary measure developed by Przeworski et al. (2000). For the post-communist countries, the Freedom House measure best reflects qualitative assessments of levels of democracy by regional experts including the Russian case. Scholars have also identified problems with the concept validity of the Polity measures (Gleditsch and Ward 1997; Herrera and Kapur 2007).

The case studies are selected on variation on one of the key independent variables of interest—the level of democracy—within a single country over time. Russia is a particularly useful case study because there are three distinct eras of Russian politics which offer useful leverage on the democracy variable while holding country-specific factors largely, if not entirely, constant. The statistical analysis tells us little about the causal mechanism of lobbying or how different regime types channel lobbying efforts. I use the Russian case studies to more explicitly evaluate the claims about how changes in
the level of democracy will affect the ability of the private financial sector to successfully lobby the government. Because the case studies examine developments in a single country over time, this is akin to the “most similar” case design in which we examine how changes in one key variable (here, democracy) affect outcomes while other factors stay (roughly) constant (Mill 1843).

One advantage of my case study approach is that I avoid selecting on the dependent variable. Geddes (2003) notes the importance of not selecting on the dependent variable for several reasons. First, we want to avoid drawing conclusions only from cases in which the event of interest actually occurred. Second, choosing based on the outcome risks hand-picking cases which confirm the theory instead of truly evaluating hypotheses. When selecting these cases I was, of course, aware of the policy outcome during each of these three periods; however, by organizing the analysis around changes in one independent variable, my goal is to make a more persuasive argument for why the level of democracy has a causal effect.

Another advantage of my case study approach is that it allows me to examine primarily the effect of one variable (democracy) on how lobbying affects pension policy outcomes in three different cases in which the other explanatory factors are held roughly constant. By doing so, I seek to avoid the problem of too many variables with too few cases, a common challenge with qualitative comparative research that was articulated by Lijphart (1971). This approach is in keeping with George and McKeown’s (1985) recommendation to use structured focused comparisons in which the researcher looks at the same possible causes and effects for each observation, or case. King, Keohane, and Verba (1994, 45-46) further advocate employing structured focused comparisons for case
studies, emphasizing the need to systematically collect the same information across cases. By focusing on the changes in one variable in three different cases, I am able to draw more meaningful conclusions about the impact of democracy on lobbying efforts.

All else is not strictly equal as we examine the effect of the changing level of democracy in Russia, but the comparison across time periods provides one that is much more comparable than a comparison across countries. For instance, the nature and organization of communist regimes varied widely (Linz and Stepan 1996). Comparisons across countries would need to take into account differing economic and welfare reforms in the late communist era and divergent political legacies. By examining a single country, we can hold constant the ideological and policy legacies of the communist era. Furthermore, the lobbying efforts of the private pension funds in Russia were well-organized and consistent from the mid-1990s onwards providing a somewhat comparable degree of lobbying pressure over the three time periods. I will also point to evidence that the timing of the shift in the level of democracy suggests that legislative proposals from the private pension sector become influential because of a change in regime type, not because of changes in the size or organization of the sector.
<table>
<thead>
<tr>
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<tbody>
<tr>
<td>Electoral support</td>
<td>Oligarchs (in oil and gas industry): In particular, the oligarchs help finance Yeltsin’s re-election campaign in 1996</td>
<td>Non-oligarchic business interests (Yakovlev 2006)</td>
<td>“Economic statism” (Fish 2005): The state re-nationalizes large parts of the oil and gas industry.</td>
</tr>
<tr>
<td>Liberal parties (such as Yabloko)</td>
<td></td>
<td>Center-right parties including Unity which wins in the 1999 parliamentary elections</td>
<td>United Russia (party of power) which controls much of the state apparatus</td>
</tr>
<tr>
<td>Yeltsin successfully gets passed a constitution in 1993 that sets up a super-presidential system. Ultimately, this means that power is disproportionately in the hands of the president and that control over the state apparatus will become the key source of support.</td>
<td>Parts of the state apparatus: In 2000, the media is still independent and the oil and gas industry are not under state control.</td>
<td>Majority of the state apparatus: This includes the Federal bureaucracy and the national security, defense, and law enforcement agencies (Yakovlev 2006). This also includes sub-national leaders, regional governors and mayors of major cities. Regional governors are now appointed by the president. The upper house, the Federation Council, is no longer directly elected. The state largely controls the media.</td>
<td></td>
</tr>
</tbody>
</table>

| Sources of Opposition to the Presidential Administration | | | |
|----------------------------------------------------------|-----------------|-----------------|
| Oligarchs (in oil and gas industry); businesspeople like Khodorkovsky fund political parties opposed to Putin and show interest in running for office themselves | Small presence of opposition parties in Duma (Communists, Nationalists); right-wing parties including the Union of Right Forces | Limited opposition from Communist Party and right-wing parties including the Union of Right Forces |
| Opposition parties in Duma (Communists, Nationalists) | | |
| Independent media is critical of Yeltsin including in regards to actions in Chechnya | As of 2000, the media is still independent and free to be critical of the presidential administration. | |

Sources: Aslund 2007 (p. 278); Fish 2005; Stoner-Weiss 2002; Konitzer and Wegren 2006; Yakovlev 2006
The case studies center on the following three time periods, respectively: 1) the Yeltsin era from 1990 to 1999 during which politics is the most democratic and competitive, 2) the first two years of the Putin administration from 2000 to 2001 during which democracy markedly declines and, 3) the second part of the Putin administration from 2002 to 2008 during which political power has been consolidated in the state apparatus.

Table 4.1 on the previous page provides a summary of the major sources of political support for the presidential administrations in each of these three eras. Russia was most democratic from 1990 to 1999, then the level of democracy begins to decline from 2000 to 2001, and the system becomes undemocratic by 2002 when Putin has consolidated his power.\(^23\) The legislation that Putin used to consolidate political power—through measures including changes in the electoral system and ending the direct election of regional governors—are presented as legislative bills by 2002. By 2002, Putin had also succeeded in consolidating media power as well. Most importantly, most Russian experts no longer considered the course of Russian politics to be uncertain but rather characterized Russia as being governed according to non-democratic politics. For instance, Konitzer and Wegren (2006, 504) point to the consolidation of recentralization efforts as of 2002. Stoner-Weiss (2002) concludes that Russia had failed to develop a party system which could serve as the basis of a truly democratic system. By 2002, the nature of Russian politics had changed to be much more authoritarian.

Although democratic systems vary widely in their organization of business-state relations, interference by the state which hampers property rights and the free

\(^{23}\) By Freedom House standards, Russia was a partially democratic system throughout the 1990s, showing a decline in 1998, another decline when Putin comes to power in 2000, and then a decline again in 2005 after Putin had officially consolidated the political power of the president.
organization of business associations is associated with a decline in democracy. The Freedom House rankings—which are the measure of democracy used in Chapter 3—include some criteria that are related to business-state relations, but do not directly capture the lobbying environment nor businesses access to the government. For instance, according to Freedom House, democratic countries should allow trade unions and business associations to freely organize. The rule of law is taken into account; there should be an independent judiciary and fair trials. Finally, property rights are considered and specifically whether the government exercises undue influence over private businesses. However, the Freedom House scores do not include any measure of the political access enjoyed by businesses. Furthermore, being more or less democratic by Freedom House standards does not dictate that private businesses will or will not be influential. Rather, whether or not the level of democracy is related to successful business lobbying remains an issue for empirical investigation.

Each of these three time periods provides crucial insight into why the financial sector was or was not influential at different junctures. Chapter 4 covers the period of 1990 to 1999 during which Russian politics was the most democratic. This allows me to evaluate my hypothesis that financial sector lobbying should be inhibited by more democratic regimes.

Chapter 5 examines the period of 2000 to 2001 which are Putin’s first two years in power and a period that shows a marked decline in the level of democracy. This decline in the level of democracy allows me to assess my theoretical expectation that less democratic regimes should be more responsive to financial sector lobbying.
Chapter 6 addresses the period of 2002 to the present. This is the most authoritarian period of Russian politics during which Putin consolidated political power within the state apparatus. The 2001 reforms were being put into place during this period including key decisions about the regulation of the new pension system. The dependent variable in Chapter 6 is still conceptualized as policy influence, but the specific policy outcome of interest here is regulation rather than the adoption of pension privatization. Critically, Chapter 6 allows me to examine the third hypothesis regarding the on-going policy influence of the private financial sector. This is especially important because the cross-national evidence only addresses policy influence on the adoption of pension privatization and not subsequent influence over policy outcomes.

In developing these case studies, I draw on interviews, official government commentaries and documents, news reports, and primary and secondary sources. All interviews were conducted in Russian and any translations from Russian language sources and interviews are my own. I conducted 45 interviews during my field research on multiple trips between 2006 and 2008 in which I met with a wide range of public and private actors including high-level executives working in Russia’s private pension funds, investment companies, employers, and business associations representing these interests. Academic experts were also a useful source of information. The research was enhanced by meetings with representatives of several of the most influential private pension funds and investment companies, the major relevant business associations, the

24 In Russian language literature, the term for the private pension funds would be literally translated, word-for-word, as “non-state pension funds”. Some English language secondary sources will also refer to the “non-state pension funds”. I use the term “private pension funds” to avoid undue confusion except when citing specific Russian legislation in which I will refer to legislation such as the bill, “On Non-State Pension Funds”. “Private pension fund” is synonymous with “non-state pension fund”.
primary bureaucracies involved in the policymaking process, and representatives of political parties.

To date there has been little systematic consideration of the role of private businesses in shaping the reform of pensions in the post-communist countries making these interviews a unique source of information about a major policy political battle in Russia. To my knowledge, no survey or interview data has inquired about the activities in which these particular businesses have engaged in order to lobby the government on pension policy. A summary of the groups with which I conducted interviews can be seen in Appendix B. I do not report the names of most of my interviewees to preserve their confidentiality and anonymity; however, throughout the next three chapters I cite my personal interviews according to an interview label which consists of an abbreviation of the type of interviewee’s organization, an interview number I assign, and the date.25

Although both the cross-national statistical analysis and the case studies have limitations, taken together a consideration of the cross-national trends and pension reform in Russia over three distinct eras allows me to address some of the challenges often facing research in comparative politics. Geddes (2003, 220) emphasizes that given the low quality of data and measurement often plaguing comparative politics, several flawed tests are often more persuasive than trying to obtain one perfect test. The cross-national analysis allows me to address trends over 25 countries over 18 years thereby identifying cross-national trend. Furthermore, the cross-national analysis allows me to at least partially respond to concerns about over-fitting the theory to a single post-communist case by identifying its broader applicability. In turn, the three case studies confirm the

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25 I follow the format in which I write “Organization type, #-mmdyy”. For instance, for interview number 1 with an official in the Ministry of Health on July 1, 2008, I would write “Ministry of Health, interview 1-070108”.
findings of the cross-national analysis and clarify how democracy affects the causal mechanism of lobbying in practice. Thus, only by combing both quantitative and qualitative approaches can I more effectively address some of the challenges inherent to comparative research.
Chapter 3  
Cross-National Evidence of How Lobbying Mediates  
Economic & Political Pressures to Reform

My prediction regarding the effect of the size of the domestic capital market offers an empirical observation unique to my theory (reference Figure 2.1 in Chapter 2). Existing theories predict either that there is a minimum threshold of capital market development necessary for pension privatization, or that countries with very large capital markets have little economic incentive to privatize in order to attract more investment. Unlike these explanations, I expect that a larger capital market will make pension privatization more likely, but only in non-democratic regimes and will have little if any influence in democratic countries. The reason we should observe this is lobbying.

Lobbying by financial intermediaries—i.e., banks, mutual funds, investment companies, and private pension funds—is the mechanism that explains why we should observe my hypothesized relationship between the level of democracy, the size of the domestic capital market, and pension privatization. Existing theories have overlooked how domestic political battles will mediate the influence of economic conditions, in this case market capitalization. This is hypothesis 2 presented in Chapter 2 which is as follows:

*Hypothesis 2: Size of Capital Market & Lobbying.* A larger capital market should enhance the lobbying efforts of the financial sector in non-democracies, but should not influence lobbying efforts in democracies. Therefore, we should
observe an interactive effect between regime type and the size of the capital market because of how each affects lobbying by businesses in the financial sector.

The lobbying efforts of financial intermediaries should be greater in non-democratic regimes. In turn, a larger capital market should bolster the claims of the financial intermediaries that a private pension system will secure domestic investment and prevent capital flight. Pension privatization was touted as a means of sending a positive signal to international investors regarding the government’s commitment to pro-market policies. I argue that these economic claims—highlighted by lobbying efforts—should be particularly persuasive when the government is less concerned with short-term electoral pressures, i.e. when the country is less democratic. Finally, where the capital market is larger, the fear of capital flight should be greater than when the capital market is underdeveloped; when you don’t have money, you’re less worried about losing it. The way in which lobbying is affected by political and economic considerations, therefore, should mean that market capitalization increases the chances of pension privatization in non-democratic countries but not in democratic ones.

The causal mechanism posited here is lobbying by the financial sector and private pension funds. However, there is no consistent cross-national measure of lobbying by financial intermediaries in general or private pension funds in particular. Moreover, much of lobbying is informal and indirect which means that crude approximations—like the size of the banking sector—offer little insight into the magnitude of lobbying activity and could produce misleading results. Indeed, a major challenge of studying lobbying is in quantifying its occurrence. Fortunately, my argument about how financial sector lobbying changes the effect of democracy and the capital market on pension privatization provides an empirical prediction unique to my theory. The evidence that I present in this
chapter indicates that the size of the capital market increases the likelihood of pension privatization in non-democratic regimes but not democratic ones. I can think of no equally plausible alternative explanation to lobbying for why the state of the capital market would matter in one kind of regime over another.

This chapter is organized as follows. In Section 3.2, I present statistical evidence which reveals that a larger capital market increases the risk of pension privatization in non-democratic countries, but not in democratic ones. I also find that in the most democratic systems, a larger market actually has a negative effect on the risk of privatization. The change in the effect of the capital market under different regimes is consistent with my expectations and the business lobbying explanation of pension reform. In Section 3.3, I conclude and identify remaining questions to be addressed in the case study chapters.

3.1 Empirical Test: Determinants of Pension Privatization

3.1.1 Choice of Cox Models

I conduct a cross-national empirical analysis including the 25 post-communist countries of East Europe, Russia, and Central Asia from 1990 to 2007. I choose to limit the analysis to these post-communist countries because the theory is grounded in the specific international, political, and economic context of market-oriented reforms in these countries. Countries enter the dataset in the year in which communism collapses (here meaning the first year in which there are competitive elections which include non-Communist political parties) and exit the dataset in the year in which a private pension system is introduced.
I am interested in the probability of the timing of pension privatization in relation to domestic factors including the size of the capital market. Because I am interested in the timing of reform, event history analysis is the most appropriate statistical test. As I do not have a theoretical basis on which to make an argument about whether pension privatization becomes more likely over time or not, I estimate Cox models in which there is no assumption about the functional form of the variables over time.26

3.1.2 Variables

Appendix A includes tables summarizing the variables used in the analysis and their summary statistics. I use a binary dependent variable—pensions—which captures whether a country has privatized pensions or not. Table 3.1 on the following page shows which countries have and have not privatized pensions and includes information on the level of democracy and market capitalization in each country.

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26 An alternative to using the Cox model is to use a probit or logit model which I estimate as a robustness check. Liao (1994) writes that, “[g]iven the similarities between the two types of models, either model will give identical substantive conclusions in most applications. In fact, one can go from one set of estimates to the other. If one multiplies a probit estimate by a factor, one gets an approximate value of the corresponding logit estimate,” (pages 24-25). Logit models would be preferable when there are a very large number of cases with a large concentration of the observations in the tails (Liao 1994, 24). Because I have a relatively small N with around 140 observations (depending on the specification), I estimate a probit model. The interaction between market capitalization and democracy is significant and has the same effect as in the Cox proportional hazard models. The results of the probit model and an interpretation of the resulting interaction term can be found in Appendix A.
### Table 3.1: Privatization Across the Post-Communist Countries

<table>
<thead>
<tr>
<th>Privatized Pensions</th>
<th>Year of Privatization</th>
<th>Freedom House Classification</th>
<th>Market Capitalization Average (Standard Dev.)</th>
<th>Market Capitalization in year of Privatization</th>
</tr>
</thead>
<tbody>
<tr>
<td>Bulgaria+</td>
<td>2000</td>
<td>Free</td>
<td>3.1 (3.4)</td>
<td>14.9</td>
</tr>
<tr>
<td>Croatia</td>
<td>1999</td>
<td>Part Free</td>
<td>11.7 (7.09)</td>
<td>12.98</td>
</tr>
<tr>
<td>Estonia +</td>
<td>2001</td>
<td>Free</td>
<td>24.5 (9.8)</td>
<td>24.8</td>
</tr>
<tr>
<td>Hungary +</td>
<td>1998</td>
<td>Free</td>
<td>11.07 (13)</td>
<td>29.8</td>
</tr>
<tr>
<td>Kazakhstan</td>
<td>1998</td>
<td>Not Free</td>
<td>7.2 (1.6)</td>
<td>8.3</td>
</tr>
<tr>
<td>Latvia +</td>
<td>2001</td>
<td>Free</td>
<td>5.04 (2.8)</td>
<td>8.4</td>
</tr>
<tr>
<td>Lithuania +</td>
<td>2002</td>
<td>Free</td>
<td>10.5 (4.2)</td>
<td>10.4</td>
</tr>
<tr>
<td>Poland +</td>
<td>1999</td>
<td>Free</td>
<td>5.9 (5.9)</td>
<td>18</td>
</tr>
<tr>
<td>Romania</td>
<td>2004</td>
<td>Part Free</td>
<td>4.7 (5.2)</td>
<td>16.1</td>
</tr>
<tr>
<td>Russia +</td>
<td>2001</td>
<td>Part Free</td>
<td>11.8 (13.6)</td>
<td>24.9</td>
</tr>
<tr>
<td>Slovakia +</td>
<td>2003</td>
<td>Free</td>
<td>7.2 (1.8)</td>
<td>8.5</td>
</tr>
<tr>
<td>Ukraine</td>
<td>2003</td>
<td>Part Free</td>
<td>5.4 (2.6)</td>
<td>8.6</td>
</tr>
<tr>
<td>Uzbekistan</td>
<td>2004</td>
<td>Not Free</td>
<td>.72 (1.03)</td>
<td>.04</td>
</tr>
<tr>
<td>No Pension Privatization</td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Albania+</td>
<td>Part Free</td>
<td>NA</td>
<td></td>
<td></td>
</tr>
<tr>
<td>Armenia+</td>
<td>Part Free</td>
<td>.71 (.37)</td>
<td></td>
<td></td>
</tr>
<tr>
<td>Azerbaijan</td>
<td>Not Free</td>
<td>.08 (.01)</td>
<td></td>
<td></td>
</tr>
<tr>
<td>Belarus</td>
<td>Not Free</td>
<td>NA</td>
<td></td>
<td></td>
</tr>
<tr>
<td>Czech Republic+</td>
<td>Free</td>
<td>24.6 (8.1)</td>
<td></td>
<td></td>
</tr>
<tr>
<td>Georgia+</td>
<td>Part Free</td>
<td>5.4 (4.04)</td>
<td></td>
<td></td>
</tr>
<tr>
<td>Kyrgyzstan+</td>
<td>Not Free</td>
<td>1.4 (1.3)</td>
<td></td>
<td></td>
</tr>
<tr>
<td>Moldova</td>
<td>Part Free</td>
<td>15.4 (11.8)</td>
<td></td>
<td></td>
</tr>
<tr>
<td>Slovenia+</td>
<td>Free</td>
<td>19 (16.8)</td>
<td></td>
<td></td>
</tr>
<tr>
<td>Tajikistan+</td>
<td>Not Free</td>
<td>NA</td>
<td></td>
<td></td>
</tr>
<tr>
<td>Turkmenistan+</td>
<td>Not Free</td>
<td>NA</td>
<td></td>
<td></td>
</tr>
</tbody>
</table>

+ Indicates a country in which private pension funds operated in a voluntary third tier of pensions prior to the adoption of a second tier

*Market capitalization is a percentage of GDP

**Freedom House classifications are for the year in which pension privatization occurred or the most recent year of data.

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27 In the Cox models presented in this chapter, there is not sufficient data for Kazakhstan to be included in the analysis (specifically, there is no data in the necessary years for government fractionalization for Kazakhstan). In addition, Macedonia privatized its pension system in 2002 but does not have sufficient data on market capitalization to be included in the analysis.
The dataset captures changed over time, so that a country receives a “0” in each year in which it did not privatized and a “1” in the year it privatized its pension system. A country is coded as privatizing pensions if it adopted any degree of privatization. Russia, for instance, adopted a system in 2001 based on notional defined contributions (NDC) with a private component meaning that a specified portion of mandatory savings can be privately managed and invested. A country enters the dataset in the first year in which there were competitive elections including non-Communist parties and drops out of the dataset once it has privatized pensions as it no longer constitutes a meaningful observation. This means that the data account for different starting points. There have been no reversals of pension privatization measures once adopted, although there have been notable revisions to certain parameters of the new private systems in some cases.

The two main covariates of interest are Democracy and Market Capitalization. Democracy is measured using the Freedom House measure of political rights and ranges from 1 to 7; I have rescaled the original index so that “7” represents the highest level of democracy and “1” represents the lowest level of democracy. I use the Freedom House Political rights scores rather than the Polity scores, as scholars have pointed to the latter as suffering from serious concerns regarding concept validity (Gleditsch and Ward 1997; Herrera and Kapur 2007). Additional measures of democracy are binary (Przeworski et al. 2001) while a continuous measure provides more information.

Market capitalization (also known as market value) captures the size of the capital market. It is the share price times the number of shares outstanding for companies listed on the domestic stock exchange.
Other covariates included in the analysis account for factors identified in the literature as making pension privatization more or less likely (see Chapter 1 for a full review of these). The existing explanations suggest the following hypotheses regarding pension privatization:

1. Aging populations get pension reform on the agenda and increase the likelihood of pension privatization up to a point, but the most mature pension systems will be too costly to reform.

2. The higher a government’s debt the less able it is to afford the substantial transitional costs of pension privatization.

3. Globalization creates incentives to privatize, but also makes it harder for countries to afford the risk of privatizing, particularly the risk of capital flight.

4. Diffusion to neighboring countries increases the likelihood of pension privatization especially when the reform entails large sunk costs.

5. Partisanship matters, but how it matters is contingent on the context. In some circumstances, large left-wing coalitions increase the likelihood of pension privatization.

6. Pressure from international organizations will increase the likelihood of pension privatization. World Bank pressure to reform should increase the likelihood of pension privatization. As such, in countries with larger amounts of World Bank loans, we should be more likely to observe privatization. EU candidate countries will be more likely to pursue pension privatization in order to cut government deficits (in the long term) and as a signal of their commitment to market-oriented reform.

The variables included to account for these hypotheses include: **Age Dependency Ratio**, **Debt**, **Trade**, **Partisanship**, **World Bank loans**, and the **EU**. The age dependency ratio—an important indicator of the burden of the PAYG system—is the ratio of the working age population to dependents. Partisanship is a binary variable in which a country is coded with a “1” if it is a left-wing administration and a “0” otherwise. Trade captures the effect of globalization and is measures as a percentage of GDP. World Bank loans
are measured as a percentage of GDP. Finally, the EU variable is binary so that countries receive a “1” if they are EU members.

In addition to the variables included to account for alternate explanations of pension privatization, I also use the variable *Government Fractionalization* taken from the Database of Political Indicators (DPI) (Beck et al. 2001). A highly fractionalized government has been thought to hinder the likelihood that a government adopts any kind of reform because an increase in the number of veto players (Tsebelis 2005). Recent research, however, has found that fractionalization makes economic reform more likely by undercutting the power of special interests (Gehlbach and Malesky 2010).

3.1.3 Results of Analysis

The results of the Cox models are presented in Table 3.2 below.
Table 3.2: Determinants of Pension Privatization  
Dependent Variable—Privatized Pensions (1) or Not (0)

<table>
<thead>
<tr>
<th>Independent Variables</th>
<th>Model 1: Baseline</th>
<th>Model 2: Interaction</th>
</tr>
</thead>
<tbody>
<tr>
<td>Market Capitalization</td>
<td>.96 (.05)</td>
<td>1.65 (.34)*</td>
</tr>
<tr>
<td>Democracy</td>
<td>.83 (.49)</td>
<td>2.65 (1.01)**</td>
</tr>
<tr>
<td>Mark Cap*Democracy</td>
<td>------</td>
<td>.92 (.03)***</td>
</tr>
<tr>
<td>Gov’t Fractionalization</td>
<td>.10 (.15)</td>
<td>.05 (.09)</td>
</tr>
<tr>
<td>Partisanship</td>
<td>.23 (.19)*</td>
<td>.45 (.43)</td>
</tr>
<tr>
<td>Trade</td>
<td>1 (.04)</td>
<td>1.02 (.03)</td>
</tr>
<tr>
<td>Debt</td>
<td>1.04 (.03)</td>
<td>1.02 (.03)</td>
</tr>
<tr>
<td>Age Dependency Ratio</td>
<td>2.32 (28.4)</td>
<td>1.67e+11 (1.93e+12)**</td>
</tr>
<tr>
<td>World Bank Loans</td>
<td>1.59e-16 (3.76e-15)</td>
<td>3.38e-22 (5.02e-21)***</td>
</tr>
<tr>
<td>EU</td>
<td>1.75 (4.17)</td>
<td>.48 (.74)</td>
</tr>
</tbody>
</table>

| N                             | 136               | 136                  |
| No. Failures                  | 12                | 12                   |
| Prob > χ²                     | .000              | .000                 |
| Log pseudolikelihood          | -36.07            | -31.45               |
| AIC                           | 90.14             | 82.9                 |

Estimates are clustered by country and use the Breslow method for ties  
Significance: * p < .1,  ** p < .05,  *** p < .01
Model 1 is the baseline model without any interactions. Model 2 includes the interaction between democracy and market capitalization. Comparing the log pseudo-likelihood and the Akaike Information Criteria (AIC) provide a relative indicators of goodness-of-fit across models with lower scores on both indicating a better fit. Model 2—which includes the interaction term—is the better fit with a log pseudo-likelihood of -31 (compared to -36 for Model 1) and a AIC of 83 (compared to 90 for Model 1).

The Cox models presented here rely on the proportional hazards assumption which assumes that the influence of any covariate proportional and constant and does not depend on when in the period of analysis the value of the covariate changes (Box-Steffensmeier and Jones 2004, 131-132). I estimate a test of the proportional hazards assumption based on the Schoenfeld residuals. Model 2 receives a p-score of .097 for the global test, just within the conventional bounds of statistical significance thereby indicating that the assumption has been violated. The full results of the test for violations of the proportional hazards assumption are reported in the data appendix.

Two additional robustness checks, reported in Appendix A, indicate that the results of Model 1 are reliable and that the possible violation of the proportional hazards assumption here is not problematic for interpreting the effect of the interaction term. First, I interact the offending variables with time and re-estimate the model as recommended by Box-Steffensmeier and Jones (2004). With this fix, the model no longer violates the proportional hazards assumption and the interaction term is still significant. Second, Kazakhstan—which privatizes pensions in 1998—has been omitted from the analysis in Model 2 because of a lack of data for the government fractionalization variable from 1996 to 1998. If we omit the government fractionalization
variable from the analysis, the Kazakh case can be included. In the resulting estimate, the model passes the global test for the proportional hazards assumption and the interaction term is significant and has the same sign and effect as in Model 2 presented above.

3.1.4 Interaction of Market Capitalization and Democracy

In Model 2, the partisanship of the administration, trade, debt, and the EU are not statistically significant predictors of pension privatization suggesting that several of the usual suspects did not play as important a role in the post-communist countries. Rather, regime type and socioeconomic factors like the age dependency ratio appear to have been the important determinants of the decision to privatize or not.

In Model 1, neither democracy nor market capitalization are statistically significant. In Model 2, however, the interaction between the two is highly significant. This suggests that although democracy and market capitalization do not have a direct influence on the likelihood of pension privatization, they do have a strong interactive effect. As hypothesized, the interaction between democracy and market capitalization is statistically significant. Figure 3.1 presents hazard functions—calculated from the regression results in Model 2—in which the level of democracy is held constant while the level of market capitalization varies.
Figure 3.1: Hazard Functions Showing the Effect of Market Capitalization at Different Levels of Democracy (based on Model 2)
Figure 1 shows the hazard functions at four different levels of democracy ranging from the least democratic to the most democratic systems (for which higher scores indicate more democratic regimes). For these functions, I have specified that countries are EU candidate or member countries with right-wing administrations. The partisanship and EU variables are not statistically significant in the models and changing their value for the calculation of the hazard functions does not alter the results. All other covariates are held at their mean values. For each level of democracy, the hazard functions are calculated at three levels of market capitalization—the minimum (0 percent of GDP), the mean (11 percent of GDP), and one standard deviation above the mean (22 percent of GDP).

As hypothesized, market capitalization has a positive effect on the risk of pension privatization in non-democratic countries, but has less impact as the level of democracy increases. In the least democratic countries, an increase from the minimum level of market capitalization (0 percent of GDP) to the mean (11 percent of GDP) increases the risk of pension privatization by nearly 20 percent over time. Indeed, when market capitalization is at the minimum, the risk of privatization does not increase at all over time at lower levels of democracy. Going from a mean value of market capitalization to one standard deviation above the mean increases the risk of pension privatization by nearly an additional 60 percent. This very high increase in the risk of pension privatization in going from the mean market capitalization to one standard deviation above is likely an artifact of the small dataset. In fact, among the least democratic countries, only two—Russia and Moldova—have a market capitalization that is one standard deviation above the mean. Russia privatized its pension system in 2001, while
Moldova has not. Because there are just two non-democratic cases with high levels of market capitalization, one of which privatizes, the estimated increase in the hazard of privatization that results from the model is quite large.

As democracy rises, higher levels of market capitalization have less of an effect on the risk of privatization. In partially democratic systems (in which democracy is scored at three), an increase from the mean to one standard deviation above the mean increases the risk of pension privatization 20 times less than in the least democratic systems. At the higher end of the partially democratic spectrum (in which democracy is scored at five), going from the minimum value of market capitalization to the maximum only increases the risk of pension privatization by about 20 percent.

The effect of market capitalization changes markedly even when just going from a partially democratic system to a highly democratic system. In fact, the interpretation of the interaction term shows that in the most democratic countries, a larger capital market actually decreases the risk of pension privatization. The risk of privatization is 20 percent lower when market capitalization is at the mean instead of the minimum. This offers partial support for the hypothesis that the presence of a larger capital market convinces policymakers that pension privatization is unnecessary for economic growth. However, the negative effect of market capitalization is only in the most democratic countries. This may be because democratic countries are only willing to undertake what are perceived to be more radical options like pension privatization when the capital market is very small. Conversely, non-democratic leaders can let the capital market do badly with lower risk of political repercussions.
The difference across regime types supports my hypothesis that the size of the capital market has a significant impact on lobbying claims by the private financial sector. Because the size of the capital market only enhances lobbying claims in less democratic systems, market capitalization does not have a positive effect in the most democratic countries. Critically, differences in the effect of market capitalization across regime types suggest that the influence of economic conditions on policy decisions is mediated by the level of democracy.

Because the effect of market capitalization changes under different regimes, these results have important implications for the risk of pension privatization in different sets of the post-communist countries. In countries that were the least democratic, the size of the capital market is a determining factor in whether privatization measures will be adopted. Ukraine and Romania are among the less democratic post-communist countries, have larger capital markets, and have privatized pensions. Russia is another less democratic country with a large capital market which privatized its pension system in 2001.

The Ukrainian case provides a good example of broader trends reflected in Model 2. The Ukrainian government became particularly concerned with market-oriented reforms in the early 2000s (Åslund 2009). The role of financial sector lobbying appears to have provided the necessary push for the government to pursue pension privatization. In a report prepared for the Ukrainian government, one expert noted, “It is possible to reform the pension system without using financial markets. However, using them can accelerate both the pension reform itself, as well as other reforms and changes going on in other parts of the state” (Gora 2008). The World Bank further emphasized that the
structural pension reforms adopted by Ukraine could help to address its fiscal problems which arose in 2000 (World Bank 2005). Because Ukraine was not fully democratic, the government had some insulation from public pressures which might have deterred it from taking on potentially high transitional costs. This is precisely the type of case in which my theory predicts that the financial sector should be able to insert itself into the policy system and more successfully promote its preferred solution to the pension crisis. Indeed, the Ukrainian government passed pension privatization measures in 2003.

In contrast to a case like Ukraine are the countries which were less democratic but had very small capital markets. In less democratic countries like Uzbekistan, Bulgaria, and Kyrgyzstan in which the capital market is very small, we are unlikely to observe pension privatization unless the capital market grows significantly, all else equal. The results of Model 2 indicate that if a country like Uzbekistan went from its highest level market capitalization of 3 percent of GDP (in 1997) to 11 percent of GDP (the mean of market capitalization across all countries in the dataset), its chances of pension privatization would increase by nearly 40 percent.

The results of Model 2 also suggest that in the most democratic countries business lobbying will not affect the likelihood of adopting pension privatization. In the case of the most democratic post-communist countries, existing accounts indicate that domestic political and economic factors were the most important factors in determining whether market-oriented pension reform measures would pass. Fultz and Ruck (2001) offer several examples of how political contestation in democratic systems delayed or modified the course of pension reform. For instance, in Hungary, the alternation in power between liberal Fidesz party and the socialist MZSP party led to modifications in the pension
Latvia’s pension legislation was amended 9 times before being put up for a national referendum in 1999. This dynamic by which alternations in power are prevalent in countries in which the financial sector appears to be less influential is consistent with Hellman’s “winners take all” argument (Hellman 1998). The regular alternations in power appears to have empowered popular forces and prevented the financial sector, arguably short-term winners in Hellman’s terminology, from having the opportunity to insert themselves as successfully into political debates.

Another good example of a highly democratic country in which the financial sector is unlikely to successfully lobby is the Czech Republic. The Czech Republic is unlikely to privatize pensions although it has a relatively large capital market (at over 40 percent of GDP) along with a sufficiently developed financial sector to support private pension operations. The Czech case is particularly interesting in comparison to that of Russia. The size of the financial sector as a share of GDP in the Czech Republic was nearly the same as in Russia in the early 2000s. The crucial difference between the two countries is that Russia was only partially democratic while the Czech Republic was a highly democratic country. As in Russia, the Czech Republic had also allowed the operation of private pension funds in the voluntary market early on in the transition to a market economy. The Czech government passed the Supplementary Pension Insurance Act in 1994 allowing for the creation of voluntary pension funds. As of 2003, approximately 50 percent of the labor force was participating in this voluntary third tier of pension savings, although the system has been heavily supported by state subsidies (Lisicky 2003). However, concerns about the high transitional costs associated with privatization reforms, including those observed in Poland, discouraged the Czech
government from further considering privatization measures (Fultz and Ruck 2001). In other words, concerns with democratic and electoral pressures meant that the large capital market does little to enhance lobbying claims from the financial sector.

Like the Czech Republic, Slovenia—which has the highest level of market capitalization of any country in the dataset at 63.7 percent of GDP—is unlikely to privatize pensions. The Slovenian government was only able to secure the passage of pension reforms after dropping a proposal to establish a second tier. Instead of structural reforms, Slovenia has made parametric cuts to its PAYG system including raising the retirement age and cuts in the area of special pension privileges such as subsidized transportation. Legislation was also passed to change pension accrual rates for each year of work and relying on a larger number of years to calculate average wages (Fultz and Ruck 2001, 12). These reforms resulted in a strong link between lifetime earnings and benefits, but Slovenia has not shown any inclination to adopt more market-oriented reforms of its pension system. Legislation was adopted to allow for the creation of a voluntary third-tier of pensions and by 2004 approximately 43 percent of the workforce had enrolled (Stanovnik 2004). The voluntary sector, however, is rather small with only 5 mutual funds, 4 pension funds, and 2 insurance companies licensed to operate in the third tier (IOPS 2007).

Plans for establishing a second-tier for pensions were abandoned in 1998 after opposition was mobilized by the Free Trade Unions of Slovenia (FTUS) and the then opposition party, the United List of Social Democrats (ZLSD). In March of 1998 the FTUS and ZLSD organized one of the largest protests in Slovenian history promoting the position that a second tier would undercut solidarity and lead to pensioners’ poverty.
Thus, in Slovenia we can see that democratic pressures made the possibility of the financial sector inserting itself into the policy debate and pushing the privatization solution much less likely than in less democratic countries. Guardianich (2004) concludes that Poland passed radical reforms while Slovenia did not because the latter had a much stronger “civil society—party system interaction” as evidenced by the influence of FTUS. As such, Slovenia’s experience fits well with my explanation that the financial sector should be the least likely to be influential in the most democratic systems.

The statistical results provide evidence consistent with the explanation of how lobbying is affected by regime type and market capitalization. All regimes want economic growth, but democratic regimes like the Czech Republic and Slovenia are more subject to popular pressures including the uncertainty associated with the adoption of privatization measures. In contrast, the less democratic countries like Russia and Ukraine were more likely to be influenced by lobbying from the financial sector. Therefore, we can see that the statistical analysis is consistent with lobbying as the causal mechanism which determines the effect that regime type and market capitalization have on policy outcomes.

3.1.5 Other Significant Predictors of Pension Privatization

Figure 2 presents the effect of several other variables in Model 2 that are statistically significant predictors of pension privatization. The government fractionalization variable nearly passes the conventional threshold to be considered statistically significant with a p-value of .101. I include an interpretation of its effect here. A decline in government fractionalization from the minimum to one standard
deviation above the mean increase the risk of pension privatization by about 20 percent. This supports the expectation that a more fractionalized government will impede any kind of policy reform.

A higher age dependency ratio also increases the risk of pension privatization which is consistent with existing theoretical explanations. There is a more than 20 percent greater risk of pension privatization when the age dependency ratio is at the mean rather than the minimum. An increase from the minimum level of the age dependency ratio to one standard deviation above the mean increases the risk by about 80 percent. Such a large increase in risk is may be an artifact of the relatively small number of observations in the analysis, but is nonetheless indicative of the positive relationship between the age dependency ratio and pension privatization.
Figure 3.2: Hazard Function of Pension Privatization at Different Levels of Covariates (based on Model 2)
The presence of more World Bank loans—measured as a percentage of GDP—makes privatization less likely. Going from no World Bank loans to one standard deviation above the mean decreases the risk of privatization by nearly 50 percent; an increase from the minimum to mean decreases the risk by about 40 percent. One possible explanation for the negative impact of World Bank loans on pension privatization is that the World Bank actively loans more money to countries which are the least likely to privatize pensions in order to encourage them to do so.

Notably, neither government fractionalization nor World Bank loans have the size of the effect that market capitalization does in less democratic systems. A higher age dependency ratio appears to have quite a large effect which is not surprising given its direct relationship with the cost of current pension systems. In addition to the effect of the age dependency ratio, in less democratic systems market capitalization has quite a large impact on the timing of pension privatization.

3.2. Conclusion

The above analysis provides evidence consistent with my expectation that a larger capital market should increase the likelihood of pension privatization in non-democratic regimes, where lobbying is more likely to be persuasive, but not in democratic regimes, where politicians will be more concerned with popular, electoral pressures over the lobbying of the financial sector.

An important limitation of the analysis in this chapter is that it does not offer direct insight into how lobbying by the financial sector influenced the decision of policymakers to privatized pensions. In the following chapters, I complement this cross-
national statistical analysis by examining the causal mechanism posited by my theory—
financial sector lobbying—in Russian pension reform as it varies over three distinct
periods which vary on the levels of democracy.
Chapter 4
Russian Pension Policymaking in an Era of Democratic Contestation, 1990-1999

In the next three chapters, I leverage changes in the level of Russian democracy over three distinct political eras to examine how differences in regime type altered the lobbying success of financial intermediaries including private pension funds. These case studies reveal that for the Russian financial intermediaries lobbying was necessary but not sufficient to influence pension policy. Lobbying was necessary to articulate policy preferences and highlight the utility of financial intermediaries to the government. However, their lobbying efforts were not successful in all three eras due to differences in the regime in each era. Financial intermediaries had a harder time influencing policymakers in the bureaucracy and the presidential administration when politics were more democratic from 1990 to 1999. Conversely, lobbying by the financial sector was more successful when the system became less democratic in the early 2000s. During the least democratic period from 2002 onwards, however, the Russian financial sector was not influential on pension policymaking.

4.1 Trajectory of Russian Pension Reform in the Yeltsin Era

Demographic and fiscal pressures got the issue of pension reform on the agenda. However, pension privatization was only one of several possible ways in which to
address the pension problem. A combination of macroeconomic, policy, and political factors affected the likelihood that Russian politicians and policymakers would opt for privatization as a solution. The trajectory of Russian pension reform in this era made a structural overhaul of the system unlikely and lobbying by the financial sector, specifically private pension funds, did this. Financial intermediaries failed to even influence the proposals of those advocating market-oriented pension reforms such as the Yeltsin administration and the Ministry of Economic Development and Trade.

4.1.1 Demographic & Fiscal Pressures

The increasing burdens of the pension system for the state were evident in the 1980s and came onto the political agenda with the Gorbachev era beginning in 1985. Soviet policymakers were well aware that demographic trends made the current system unsustainable. In a 1988 budget speech, Gorbachev openly acknowledged that the country was experiencing financial strain (Chandler 2004). Adding to state pressures regarding pensions, Gorbachev ushered in glasnost—a period of political opening and liberalization—that allowed for a number of complaints to be voiced about low pensions and special pension benefits (for instance, the favoritism enjoyed by those with exemplary service to the Communist Party). Discontent surfaced about the inadequacy of pensions for covering daily living costs. Despite the fiscal incentives to cut costs (from the state’s perspective), the pressure of financial constraints was trumped by demands for

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28 The challenge of sustaining a relatively generous pension system was evident long before the collapse of communism. From 1927 to 1932, pension expenditures tripled so that in 1931 pension arrears became a problem. Some anecdotal evidence indicates that individuals fell through the cracks during this period and were denied pensions for petty disputes over the documentation of their working years, suggesting the government may have been looking for ways to avoid making payments when possible. The Soviet pension system was also plagued by intergovernmental disputes about financing reflecting a struggle by the national and regional governments to cover their obligations (Chandler 2004).
higher pensions for workers even though the increases often provided only slight improvements. In November of 1990 one pensioner wrote a letter to the local newspaper sarcastically thanking those responsible for the minimal increase in her pension writing that,

Today, at the savings bank [after the pension reform], I found out that my pension has been increased...by a whole 80 kopecks! I do not know who initiated this improvement in my material well-being, but I would like to thank, through your newspaper, all those who had a hand in this act - the LenSoviet, the Social Security Board, and I even dare say—the Supreme Soviet [Parliaments] of the Union and the Russian Federation, and personally comrade Polozkov [head of the Communist Party of the Russian Federation] (Russian Press Digest 1990).

Such blatant criticism by pensioners of the meager increases in their benefits was indicative of a significant shift in politics and a new pressure on politicians faced with trying to please retirees while simultaneously realizing the need to provide for a sustainable pension system. This political shift marked the increasing importance of public pressure as a restraining influence on the government’s actions. The irony of the late Soviet pension situation is that despite complaints about low benefits, the financial burden on the state was still quite substantial given the large number of pensioners.

Some attempts were made to establish earmarked sources for financing pensions that did not come from general budget revenue. Towards the very end of the Soviet period, preparations were being developed to modify the pension system indicating that the government recognized the system’s unsustainability (Chandler 2004). In 1990, before the collapse of the Soviet Union, a Russian Pension Fund was established. In 1991, the Supreme Soviet also established an Insurance Pension Fund for the Sciences. The first private pension fund was established in November of 1991 and shortly
thereafter, in December of the same year, the government began preparation on a law entitled, "On Non-State Pension Funds". 29

The first attempt at pension reform in the late Soviet era was on January 1, 1989 with the introduction of the law, "On Measures for Improving Pension Provision and Social Protection of the Population" which established a minimum pension that was 100 percent of the minimum wage. The result was a 6.5 billion ruble increase in pension expenditures (Degtyarev 2001). By raising pension benefits, this legislation exacerbated the problem of high pension costs. In November of 1989, the government published the legislative project on pension reform for the purpose of public discussion. The result was 10,000 letters of complains. Only a month later, the Russian statistical agency conducted a social survey to ask whether citizens agreed with the proposed pension reform. Some noted that these attempts to solicit public feedback only created more unresolved problems in pleasing the public, rather than offering constructive advice (Degtyarev 2001).

The 1990 Soviet pension law was the basis for some changes made immediately after the collapse of communism, although it focused on increasing pension benefits over limiting state expenditures. The goals of this law included increasing pensions in keeping with the rising cost of living, providing more benefits for war veterans, and introducing social pensions for those without sufficient workforce years. The law had initially been intended to create a self-financing autonomous pension fund although this ultimately was not included. A Soviet law passed in May of 1990 committed the USSR to the world’s highest percentage of pension spending as a percentage of GDP (Chandler 2004). The

29 "Non-state pension fund" is synonymous with "private pension fund". The literal, word-for-word translation from the Russian is "non-state pension fund". To avoid undue confusion, I use "private pension fund" except when referencing specific pieces of legislation.
law ultimately adopted by the Russian Federation in the early transition included many
similar measures but differed in that it explicitly resolved to create an independent fund
to finance a new pension system as the government’s interest in limiting state
expenditures had resurfaced.

The measures taken by the Soviet and early Russian government make their goals
evident. The government wanted to limit expenditures while still covering pensioners
well enough to avoid backlash and social unrest. Because of the new exposure to public
pressure, politicians were hesitant to seriously undertake any unpopular cuts in benefits
even though deficits in the government’s budget were rising. At this stage, introducing a
funded pension tier was not discussed, but the government was increasingly confronted
with growing pension expenditures and financial deficits.

The pressure to reform pension systems in the late 1980s and 1990s mounted as
aging populations exacerbated pressure on the Russian government and the ability of the
Pension Fund to finance pension payments. Russia’s population was steadily aging.
Projections of the ability of the Pension Fund to cover future benefits became
increasingly grim throughout the 1990s and into the early 2000s. The extent to which
demographic factors provide an objective basis on which to reform is unclear as experts
have argued that in many cases parametric reforms could have averted crisis. However,
aging populations were used as a pretext for the consideration and adoption of reforms
(Augusztinovics 1999, 102). The population was simultaneously rapidly aging and
shrinking simultaneously. Of the post-communist East European countries, Russia is one
of the starkest examples of population decline. Between 1990 and 2005, the Russian
population fell from 149 to 143 million and is further projected to decline to 111 million

101
by 2050 (Chawla et al. 2007, 45). The percentage of the population at retirement age will increase from 20 to 30 percent (Hauner 2008). Finally, from 1990 to 2008 the old age dependency ratio has risen from 15 to 18 (WDI 2009). In Russia, the financial status of the national Pension Fund declined despite large budgetary transfers. Russia managed this problem by incurring huge pension arrears in the mid-1990s (de Castello Branco 1998, 20-21). Costs were rising and Russia’s Pension Fund increasingly could not cover benefit payments. From 1992 to 1997, pension costs rose from 4.7 to 6.7 percent of GDP and the Pension Fund’s surplus of 1.6 percent in 1992 shifted to a deficit of 1.1 percent by 1997 (Denisova et al. 1999, 21). Projections indicated that the Pension Fund’s fiscal resources would be increasingly strained due to an aging population, poor tax collection, and a falling GDP. 

4.1.2 Macroeconomic, Policy, and Political Pressures to Privatize

Although an aging population and rising government deficits raised the issue of pension reform for bureaucrats and politicians, there were many possible solutions of which privatization was only one. Options included a variety of parametric reforms, establishing an NDC system, privatizing pensions, or some combination thereof. Nor did debate over pension problems mean that any policy would be adopted in response as one

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30 Life expectancy, particularly for males, dropped in the early 1990s. The drop in male life expectancy in the early 1990s was not part of a long-term trend, and life expectancy began to rise in the 2000s. Between 1950 and 2000, the average life expectancy for Russian men only declined from 60 to 1959 (Chawla et al. 1007, 52). In 2009, average male life expectancy increased to nearly 62 years of age. This combination of an aging and shrinking population meant that the burden of a higher age dependency ratio strained the ability of the government to cover current pension benefits. Only in 2008 was there a slight move in the other direction with old age dependency rates dropping from 19 to 8 and in 2007 the overall age dependency ratio dropping from 40 to 39 (WDI 2009).

31 The pension crisis in 1995 that led to widespread arrears in benefits payments was blamed in part of a fall in government revenue resulting from tax breaks and amnesties granted by Yeltsin prior to the 1996 presidential elections (Jensen 2001).
option was to stay with the status quo. Therefore, it is important to first consider the pressures for and against privatization as a solution before considering lobbying by the financial sector. In other words, we should consider Russia’s trajectory for pension reform before considering whether business lobbying altered its course. These include a consideration of the factors discussed in Chapter 1 as applied to the Russian case.

First, there were macroeconomic pressures and influence from the World Bank and policy diffusion. Russia was an increasingly globalized economy in the 1990s with pressure to adopt market-oriented reforms. Globalization creates a double-bind for countries in creating incentives to privatize but also in raising the risk of privatization (i.e., the risk of capital flight due to high government deficits which fund transitional costs). The privatization of state enterprises and liberalization of the economy were the priorities for economic reform in the early transition (Åslund 1995). The issue of structural pension reform was taken up during the second Yeltsin administration. During the second Yeltsin administration, Russia had an increasingly globalized economy (with trade constituting 48 percent of GDP in 1996 when Yeltsin was re-elected).³²

Russia’s aging population and increasing old-age dependency ratio meant that the pension systems was a growing burden on the government’s finances (Karasyov and Lublin 2001). In 1997 on average there were 60 pensioners for every 100 working citizens (Cichon 1999). Mikhail Dmitriev—a senior official in the Ministry of Economic Development and Trade and one of the most influential bureaucratic proponents of pension privatization—promoted the economic benefits of promoting savings and argued that any transitional costs could be covered without raising deficits. He argued that the

³² Trade statistics taken from the World Development Indicators (WDI).
PAYG system could be financed by increasing contributions to the system and by making parametric reforms to the system such as raising the retirement age (Dmitriev 2000). Dmitriev specifically linked pension privatization to a way in which Russia could recover from its 1998 financial crisis, noting that other countries had successfully used this tactic. Other experts expressed doubt that Dmitriev’s projections were accurate, arguing that higher deficits would be necessary to finance the PAYG benefits and that the administrative costs of a private system would be up to 20 times higher (Denisova et al. 1999). These experts argued that increased foreign debt to finance pension privatization would only postpone the problem rather than solve it. Thus in Russia, we see evidence of the double-bind created by macroeconomic pressures in which potential benefits were weighed against the cost and risk of pension privatization.

The diffusion of pension reforms to other post-communist countries influenced Russia’s decision as well, albeit indirectly. Hungary and Kazakhstan privatized in 1998 providing early models of how pension privatization might be conducted. Other countries like Poland and Slovakia provided notable demonstrations of major structural pension reform for the other post-communist countries that had opted only for parametric reforms (Lisicky 2003). Although the spread of privatization might promote its merits, it also highlighted the costs. Some countries like the Czech Republic and Slovenia only adopted parametric reforms. Poland adopted a mixed NDC-FDC system which provided another, less radical option for reform. The Swiss and Polish examples were particularly influential on the Yeltsin administration’s reforms and directly shaped its 1997 pension reform concept (Maleva and Sinyavskaya 2005, 19). However, difficulties with
implementation in Poland revealed potential problems with pursuing this strategy including public discontent (Chłoń-Domińczak and Gora 2003).

Pressure from the World Bank was an important consideration. The World Bank highlighted the coming “old-age crisis” and the need to establish three tier systems in which the second tier was based on mandatory contributions that would be privately invested (World Bank 1994). Jose Piñera, the former Chilean Minister of Labor and the architect of its pension privatization measures adopted in 1980, traveled to Russia to offer his advice advocating the Chilean model of radical neo-liberal economic reform (Piñera 2000). He identified four top-priority areas of reform in order to promote growth in Russia, top among which was pension privatization.33 Piñera expected that pension reform would be “wildly popular” in Russia both growing the value of benefits and prompting Russian citizens to become stakeholders in the new system. This was also an area in which Russia could beat the US in the “pension reform race” (Piñera 2000: 68). Russian experts confirmed that the Chilean model and other international experiences with pension reforms were indeed discussed during the 1990s (interview IC 9-091707).

In 1998, the World Bank offered Russia a Social Protection Adjustment Loan in the amount of $800 million in order to pursue pension reform. Because of this, some scholars have argued that the World Bank significantly influenced Russia’s choice of pension reforms (Williamson, Howling, and Maroto 2006). However, the terms of reform were not specified in the loan agreement meaning that there was no binding agreement to pass a particular reform. Additionally, the Russian government made it a point to exclude the World Bank from the most important discussions including the

33 The other three reforms recommended were tax deregulation, radical decentralization, and replacing the ruble with the euro (a highly unlikely measure for Russia to take).
National Pension Council established in 2000. Personal interviews with top-level bureaucrats in the Ministry of Economic Trade and Development and the Ministry of Health and Social Welfare also confirmed that the World Bank was almost completely excluded from discussions about the reform of pensions, particularly in the early 2000s (interview 1-10020, interview 5-101607, interview 1-070108).

The influence of the World Bank on the consideration of pension reform in Russia mirrors that of other countries. Nelson (2001) notes that while the World Bank was partially responsible for pension privatization being on the political agenda, the exact content of reforms was determined by domestic actors. The International Labor Organization (ILO) and the International Social Security Administration (ISSA) were potential sources of information who did not promote pension privatization, but they lacked the resources of the World Bank (Orenstein 2009).

In addition to these international pressures, bureaucratic battles were also indicative of the lack of consensus on the right course of action (Cook 2007; Müller 2003, 2002a, 2002b). Important ministries include the Pension Fund, the Ministry of Social Protection and Healthcare, the Ministry of Finance, the Ministry of Economic Development and Trade and the Ministry of Labor and Social Development. These major bureaucracies involved disagreed on the proper way to reform pensions. Importantly, in debates within the Russian government amongst competing bureaucracies, the issue of capital flight or the potential cost of pension privatization (which would drive up deficits thus resulting in higher deficits) was not the main issue. Rather, bureaucrats invoked the goals of providing social goods to citizens or promoting economic growth. At the root of the issue was also which bureaucracies would play a
central role in the pension system and whether the Pension Fund would retain its enormous power.

The Pension Fund favored maintaining the power to invest the retirement savings of Russian citizens, amounting to tens of billions of dollars. The Pension Fund was a powerful bureaucracy from the beginning; Åslund (1997) and McFaul (1999) both note that there was a major political struggle between Yeltsin and the legislature over control of the Pension Fund in the early transitional period. Accusations of corruption suggested that bureaucrats in the Pension Fund reaped significant financial gain from maintaining this power. The Ministry of Social Protection and Healthcare also opposed privatization measures which ran the risk of decreasing its sphere of influence and ran counter to the bureaucracy’s primary purpose in administering an expansive welfare state.

In contrast, the Ministry of Finance and the Ministry of Economic Development and Trade favored privatization measures. The Ministry of Finance came from the perspective of reigning in unsustainable government expenditures. The Ministry of Economic Development and Trade (MEDT) was the bureaucratic vanguard of market-oriented reforms. The head of the Ministry of Economic Development from 2000 to 2007, German Gref, strongly supported pension privatization measures. The Ministry of Labor and Social Development was another source of support for market-oriented reforms and was partially responsible for helping produce official government pension reform concepts.

Bureaucratic battles, however, are only one part of the larger story. The importance of bureaucratic stances is dependent on the larger political battles within which they operate. In Poland, for instance, the head of the Ministry of Welfare was
replaced after he refused to cooperate with market-oriented pension reform measures (Müller 2003). Bureaucracies are a source of proposals, but they are not the ultimate sources of power and, even when head ministers have policy discretion, they can be replaced. The preferences of these bureaucratic actors signal the starting point for proposals about how to reform. Interest groups, like the private pension funds, could play a crucial role in modifying the policy stances laid out by these two actors. In short, bureaucratic battles do not answer the question of why the government settles on a specific policy solution.

In addition to bureaucratic in-fighting, there was political gridlock between the Yeltsin administration and the Duma—in which the Communist party had significant sway up until the 1999 parliamentary elections—that precluded the adoption of any major pension privatization. The platform of the Communist Party of the Russian Federation (CPRF), unsurprisingly, supported full state responsibility for providing social welfare, including pensions. They opposed any market-oriented welfare reforms and did not support any parametric cuts to the system. The CPRF ran on an agenda calling for the state to provide a host of social services as a basic right, including pensions; thus, the Party’s official line was to argue in favor of the Soviet-era welfare state (Cook 2007, 113). The Communists called for increasing current pension benefits saying that benefits should be double or even tripled with the financing to come from a nationalization of Russia’s natural resources. Gennadi Zyuganov regularly emphasized the need for a minimum pension benefit.\footnote{See: BBC Monitoring of the Former Soviet Union, Radio Russia (Moscow), “Russian Communist leader outlines his programme, attacks Russian Public TV,” 9 February, 2000.}
Russia’s nationalist party—the Liberal Democratic Party of Russia—did not take consistent ideological stances that would allowed it be definitively classified as being on the political right or left, but it did not support pension privatization measures. Specifically, the head of the LDPR, Vladimir Zhirinovsky, criticized the Yeltsin administration for being unable to address pension arrears. The focus of the LDPR was not offering any pension reform proposals, but rather calling for the payment of pensions.

There was a Pensioner Party during the Yeltsin era which advocated on behalf of retirees, although it never won any seats in the Duma. The Pensioner Party has since been dissolved with the formed head of the party joining a new center-left party, A Just Russia. An interview with the former head of the Pensioner Party revealed that they lobbied for the protection of pensioners’ benefits rather than offering proposals for any reform of the system as a whole (former head of the Pensioner Party 1-120507). Other policy experts indicated that the Pensioner Party did not play a serious role in reform debates (interview TE 4-090506).

The Communists and the nationalist Liberal Democratic Party of Russia (LDPR) enjoyed significant representation in the Duma during the 1990s which posed a hurdle for Yeltsin’s presidential agenda, particularly in regards to pensions. In 1993, the Communists controlled about 10 percent of the seats and the LDPR got about 14 percent of the seats. Democratic factions which were receptive to Yeltsin’s agenda received only about 38 percent of the seats. In 1995, the Communists got 35 percent of the seats and the LDPR got about 11 percent of the seats. The Agrarian Party, a small Communist Party, got another 4 percent of the seats, so that nearly 50 percent of the seats in the

Duma were controlled by the Communists and Nationalists who did not support the Yeltsin administration’s proposals for market-oriented reforms including pensions.

As a result of the success of the Communists and the LDPR, executive-legislative gridlock blocked agreement on any pension reform during the 1990s. Cook (2007) cites this standoff between the Duma and Yeltsin as one of the primary reasons that the 1990s is characterized by “contested liberalization” in the area of welfare reform more broadly. Contested liberalization meant that, although the Yeltsin administration was successful in transforming some areas of social policy, in other areas like pensions the Soviet system stayed largely in place. This strength of the Communists and Nationalists in the Duma only declined at the very end of the Yeltsin era. More centrist right-wing forces did not come to power until the 1999 legislative elections, less than 2 months before Yeltsin resigned and Putin became acting president.

Table 4.2 below summarizes the competing pressures for and against market-oriented pension reform during the Yeltsin era. Macroeconomic and policy pressures created incentives to reform but the pressures of globalization and experiences of other countries also highlighted the potential costs of doing so. Bureaucratic disagreements were indicative of competing preferences within the government about the proper course of action. Moreover, gridlock between the Yeltsin administration and the Duma blocked agreement on what to do.
# Table 4.1: Competing Pressures for and against Market-Oriented Pension Reform during the Yeltsin era

<table>
<thead>
<tr>
<th>Domestic Political Actors</th>
<th>In favor of Market-Oriented Pension Reform (which could include NDC or pension privatization)</th>
<th>Opposed to Market-Oriented Pension Reform (including pension privatization)</th>
</tr>
</thead>
<tbody>
<tr>
<td>Yeltsin administration</td>
<td></td>
<td>Communist Party Nationalist Party (LDPR)</td>
</tr>
<tr>
<td>Ministry of Economic Development &amp; Trade</td>
<td></td>
<td>Ministry of Healthcare &amp; Social Protection Pension Fund</td>
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<td>Ministry of Finance</td>
<td></td>
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<tr>
<th>Macroeconomic Pressures</th>
<th></th>
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<tbody>
<tr>
<td>Growing implicit pension debt (due to aging population)</td>
<td></td>
<td>High transitional cost</td>
</tr>
<tr>
<td>High Pension Fund deficit</td>
<td></td>
<td>High transitional costs could result in higher deficits which could spur capital flight</td>
</tr>
<tr>
<td>Privatization was argued to increase higher domestic savings &amp; economic growth</td>
<td></td>
<td></td>
</tr>
<tr>
<td>Privatization linked with recovery from the 1998 financial crisis</td>
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<tr>
<th>International Financial Institutions’ Pressures</th>
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<tbody>
<tr>
<td>World Bank provided loans &amp; technical assistance in favor of pension privatization</td>
<td></td>
<td>International Labor Organization promoted non-structural options (but was much less influential than the World Bank)</td>
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</tbody>
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<th>Diffusion Pressures</th>
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<tbody>
<tr>
<td>Examples of options &amp; ways to reform (including, but not limited to, the Swiss, Polish, Hungarian, and Chilean reforms)</td>
<td></td>
<td>Highlighted the costs and risks of reform</td>
</tr>
</tbody>
</table>

**Policy Trajectory during the Yeltsin era:**

*No major structural pension reform*
The result of these competing pressures was that the trajectory of pension policy was a lack of any major structural reform. Amidst this context, businesses in the financial sector lobbied and attempted to sway the government in favor of the privatization solution. I turn now to the development of financial intermediaries and private pension funds and their lobbying efforts.

4.2 Democratic Contestation Prevents Financial Lobbyists from being Influential

In lobbying politicians and policymakers, financial intermediaries including private pension funds had to situate themselves amongst the pressure to privatize versus pressures to favor alternatives like a NDC system or parametric reforms. The lobbying efforts of the financial sector during this period were necessary but not sufficient for them to be influential on pension policy. Lobbying had to occur within a less democratic setting to be more effectual. Democratic contestation during this period meant that the financial sector did not have political, informational, or economic utility for the Yeltsin administration.

4.2.1 Emergence of Financial Market and Private Pension Funds

Legislation early in the transition allowed private pension funds to operate. In addition, a financial sector was rapidly developing in Russia. The significance of this is that as the Yeltsin administration faced pressure to reform pensions and competing preferences about how to do so, a private sector with a preference for the privatization option was emerging. As the capital market expanded and financial intermediaries and
private pension funds emerged, business associations formed and lobbied in favor of legislation favorable to their members including privatization.

One of the earliest pension reforms was legislation permitting the existence of private pension funds to manage voluntary pension savings. The initial structural changes in the Russian pension system involved creating a two tier system under which the government permitted the investment of voluntary savings. The 1992 presidential decree “On Private Pension Provision” officially marked the beginning of market-oriented pension reform in the Russian Federation (Karasyov and Lublin 2001). The law provided for the creation of private pension funds which would operate independently from the state system and be allowed to invest voluntary pension savings. These funds did not have the right to conduct other commercial business and would be overseen by the Ministry of Social Protection of the Population which would be responsible for registering and licensing funds. Pension benefits paid from these funds would supplement state financed pensions (Orlov-Karba 2005). Significantly, the presidential decree indicated that the government’s goals for pension reform as it indicated that the government was looking for ways to shift the burden of pensions away from the government to private sources, if only to a limited degree at this time.

Around 400 new pension funds were created by September of 1994 (Alekhin et al. 1994). Due to a delay in legislation establishing the regulation of these funds, the oversight body—the Inspectorate of Private Pension Funds was not created until 1994 and licensed the first 10 private pension funds in October of 1995. By the end of 1995, there were 26 licensed funds which grew to 255 funds by the end of 1996. Figure 4.3
shows the number of private pension funds from 1995 to 2008. Figure 4.4 shows the number of individuals with money invested in private pension funds from 1999 to 2009.

Figure 4.1: Number of Private Pension Funds, 1995-2008

Source: Ministry of Labor of the Russian Federation, Inspectorate of Private Pension Funds
The number of licensed pension funds stayed between 200 and 270 between 1996 and 2008. While there was some turnover with pension funds losing previously granted licenses, turnover was minimal overall. The sector underwent a quick learning curve, rapidly gaining experience in managing and investing voluntary pension savings. Most notably, we see three years—1999, 2000, and 2001—prior to the adoption of Russia’s major pension reform (in December of 2001) in which the private pension fund sector was growing.

Figure 4.5 shows the growth of the private pension funds from 1999 to 2009 during which time they continued to expand.
From 1998 to 2002, the net worth of the private pension funds increased six-fold going from 8.2 to 50.5 million and pension reserves increased nine-fold going from 4.2 to 39.6 million. The number of citizens with money invested in private pension funds increased as well. From 1998 to 2002, the number of individuals with money in private pension funds more than doubled, going from 1.8 to 4.1 million people in just five years (Mudrakov et al. 2002: 39).

While the number of licensed pension funds grew dramatically in 1996, the wealth was very concentrated in this sector. As of 2004, the three largest private pension funds (by net worth)—GAZFOND, LUKOIL-Garant, and Suruneftegaz (Mudrakov 2002: 52-55)—controlled 65 percent of pension reserves, 95 percent of investments, and managed the funds of 68 percent of individuals privately investing their retirement...
savings (Orlov-Karba 2005: 155). The surge in the number of private pension funds suggests an interest group that should increasingly be able to influence the government. The concentration of wealth amongst a handful of the most powerful pension funds suggests that organization should be less of a challenge (in keeping with Olson’s expectation that larger groups would have more difficulty in organizing themselves).\textsuperscript{36} The resources of the pension funds should have given it an advantage in being able to organize itself and make proposals. An increase in the capital in this sector should also lend it more leverage with the Russian government, particularly since the issue of economic development was so salient during this period.

The ownership of private pension funds ranged a broad spectrum of companies. As of 2002, many of private pension fund founders (46 percent) were industrial businesses including gas and oil companies such as Lukoil and Gazprom. Credit organizations, insurers, and investment companies constituted about 20 percent of the founders of private pension funds. Even government bureaucracies established some private pension funds, although they were only about 5 percent of all founders. Social and religious organizations founded about 7 percent of the private pension funds (Mudrakov et al. 2002: 23, 52-55). The wide range of founders of private pension funds also suggests that the stakeholders in pension privatization were widespread across sectors. About 50 percent of the funds were located in Moscow and St. Petersburg which provided many representatives of the sector easier access to the government (Mudrakov et al. 2002: 19).

\textsuperscript{36} See: Mancur Olson, \textit{The Logic of Collective Action}, 1965 (Harvard University Press)
Although the private pension funds were linked with oligarchic business interests rooted in natural resources, the oligarchs had a distinct economic and political identity from the financial intermediaries and private pension funds. The oligarchs were the businessmen who owned the major corporations, primarily those in natural resources like oil and natural gas, which constituted about 75 percent of the Russian economy. Yeltsin gained electoral and financial backing from the oligarchs by offering them a number of concessions, particularly during the privatization of the early 1990s (Kapstein and Milanovic 2000). These large corporate business interests were particularly useful in funding Yeltsin’s expensive campaigning costs for his 1996 re-election (Åslund 2007; Hellman 1998; Shleifer and Treisman 2000). For instance, in return for their political backing in Yeltsin’s 1996 presidential campaign, the director of Oneksimbank, Vladimir Potanin, was appointed as a deputy prime minister (Jensen 2001, 54-55).

The Russian Union of Industrialists and Entrepreneurs (RUIE) was the lobbying arm of the oligarchs and, to this day, is the most powerful organized lobbying group in Russia (interview TE 9-071108). The RUIE was founded in 1990 (as the Scientific-Industrial Union, taking on its current name in 1992) and while initially opposed to major economic restructuring as its founding members were mostly state enterprises, it later came to champion market-oriented reforms as the managers of formerly-owned state enterprises started to profit from the new capitalist system. Today, it cites as its primary activity the introduction of new bills and the improvement of existing legislation and numerous committees on specific areas of policy reform (RUIE 2010).37 The RUIE’s official statement on pension reform indicates that its position favored market-oriented

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structural pension reform, meaning privatization, and pension reforms that would be conducive to allowing the development of corporate pension benefits that were competitive with other advanced economies (RUIE Pension Reform Statement). The RUIE has also sought opt-out exemptions from making mandatory payroll contributions in favor of using those contributions to finance private corporate benefit systems (interview TE 2-092707). The official preference of the oligarchs’ lobbying organization, therefore, was clear. However, pensions were not at the top of the RUIE’s agenda even if their pension funds that were held by some of its member companies could have profited from it. Particularly beginning in 1998 when several of the major oligarchs began backing the RUIE, the organization focused on securing industrial business interests including favorable tax legislation and subsidies from the government (Hanson and Teague 2005, 661).38

The lack of political access for business associations formed by the private pension funds—discussed in the next section—is striking in comparison to the access enjoyed by the oligarchs and the RUIE during this period. This difference in influence between the RUIE and the pension funds is evidence that certain business interests like the pension funds were of little utility to the government during this period and therefore enjoyed little sway on policy outcomes.

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38 Hanson and Teague (2005) characterize the RUIE as a “frequently-shaken kaleidoscope” rather than a typical economic interest group (p. 664) in large part because of transition from an organization of state enterprises to a political tool of the oligarchs. It has been, nonetheless, the voice of big business in Russian since 1998.
4.2.2 Lobbying by the Private Pension Funds

The private pension funds were poised to provide advice to the government about how reforms should progress and were organized into a national association called the League of Private Pension Funds. The League was created in September of 1994 with the purpose of coordinating businesses working in the private pension provision sector (League of Private Pension Funds ND). As a professional league, it considers itself to be one of the most influential and active organizations in the area of Russian pension provision (interview PPF 1-101907). As of 2007, the League included about 40 percent of all private pension funds whose holdings made up the retirement savings of about 1.5 million people.

The League engaged in typical activities for a professional organization lobbying on behalf of its sector’s interests. As of 1997, the League was a member of the European Federation for Retirement Provision and was also a member of the Russian government’s Trade and Industry Association suggesting that it had at least some access to the government. Through journals like Pension Funds and Investments and later Pension Money, the League regularly published material on questions related to private pension funds and, critically, pension reform (League of Private Pension Funds ND).

In the spring of 2001, just prior to the formal consideration of the legislation that would overhaul Russia’s pension system, the League announced that it had a new concept of its organization and purpose. It would now consider itself to be a club for the leaders of the private pension funds with the goal of promoting the basic development of private pension funds in Russia (League of Private Pension Funds ND). These stated goals made it sound like the League would be taking a more direct advisory role in advocating for the
development of the sector and that this was not the role that it had previously envisioned for itself.

The National Association of Pension Funds (NAPF) was created in 2001 explicitly as an organization that would take initiatives to push for favorable legislation regarding voluntary pension savings and also in the debate over pension reform initiated by Putin with his National Pension Council in 2001. One expert who worked in the private pension sector since its inception and now works as a consultant for the National Association of Pension Funds indicated that the private pension funds did have some access to the government during this period (interview PPF 1-101907) and businesses were an important source of proposals for pension reform (interview IC 5-091407). While NAPF presents itself as having provided technical advice to the government rather than as lobbying per se, its interests clearly lie in securing favorable legislation.

The League, and later NAPF, engaged in concerted efforts to sway the government regarding pension legislation but with only moderate success during this time period. The chronology of major events in Russian pension reform in Appendix C lays out many of the major events in the development of the private pension funds during this period. In the first few years of their operation, the focus was on pushing the government to adopt the necessary legal framework and regulatory structure for the funds to do business which took several years to accomplish.

Those working in the Russian pension sector indicated that they did regularly consult with government bureaucrats (interview PPF 2-102507, interview PPF 3-102507, interview PPF 5-062308). 39 Those in government bureaucracies confirmed that they had

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39 One interviewee indicated that in all of her close encounters with bureaucrats and many years working in the sector, she had never engaged in what she would consider lobbying (interview IC 5-091407). This
regular communications with businesses in matters relating to the private pension funds (interview MEDT 5-101607, interview PF 2-071008). Despite the developing ties between the private pension funds and some government bureaucrats, the ability of the private pension funds to introduce proposals for structural pension overhauls was extremely limited. The private pension funds attempted to introduce proposals, but government officials were not receptive. The Ministry of Economic Development and Trade indicated that business did not shape the reform proposals they produced (interview MEDT 1-100207). Additionally, private pension funds were not invited by the government to participate in official policymaking circles. Of the several official pension reform concepts announced by the Yeltsin administration in the 1990s, none were drafted with the inclusion of the financial sector. Thus, the lobbying of private pension funds were unsuccessful.

The legislation to allow private pension funds to operate was passed in 1992, but an Inspectorate to monitor the private pension funds (at the time under the Ministry of Labor) was not formed until 1994. The first licenses for private pension funds were only issued in 1995. After private pension funds began their operations, in January of 1996 the Inspectorate held its first forum related to business in the sector with the top three private pension funds. After this forum, the government subsequently adopted several pieces of legislation clarifying how the private pension funds would operate in Russia.

The private pension funds regularly expressed their concerns about the formation of the sector, particularly about the development of appropriate regulations. In response can almost certainly be attributed to the fact that the term “lobbying” has negative connotations in Russian politics. When pressed as to what activities actors engaged in, accounts suggest that the activities typically considered lobbying did in fact occur on a regular basis.
September of 1993, the Association for the Development of Private Pension Funds brought together more than 150 private pension funds and investment companies in order to establish their professional interest to the state organs of power. Another similar conference was held in February of 1994 and in September of 1994. In the “Declaration of the Basic Principles of Private Pension Fund Business,” the sector expressed several specific policy concerns regarding necessary legislation (Alekhin et al. 1994). One of the major contentions of the sector expressed at this conference was that private pension sector still lacked a legal basis for its operations.

The establishment of the Inspectorate in 1994 had been long-awaited and took two full years since the original legislation, but several remaining major policy issues were raised in the 1994 Declaration (Alekhin et al. 1994). First, the private pension funds agreed that they should be considered non-commercial organizations as evidenced by a 1993 declaration regarding business standards in the voluntary retirement sector. However, they noted the lack of any Federal legislation on the status of non-commercial organizations including their legal status, operating rules, and even basic issues like tax requirements and accounting standards. Without any of these in place, the private pension funds indicated that it would be extremely difficult for them to operate even several years after legislation allowed them to operate and several hundred funds were attempting to enter the market.

There were additional concerns about property rights for those investing their money in the private pension funds and the ability to transfer retirement savings from one fund to another in order to allow for “healthy competition” in the market. On a larger scale, the pension funds called for a “civilized” financial market and an organized system
of protection against incompetent fund managers (Alekhin et al. 1994). Finally, the funds emphasized that they did not want to be grouped together with investment companies in their regulation and oversight but should be considered to be independent and legally distinct and should not be licensed or overseen by the same government agency. Being distinct from the investment companies was significant as the regulations would be quite different for non-commercial pension funds. Likely, the pension funds did not wish to be grouped in the public mind with higher risk investment companies, but rather wanted to emphasize their concern with social well-being. This is evidenced in a 1993 declaration in which the funds declare that they would adhere to the best market practices, have a higher degree of commitment to those investing their funds with them, and compliance with principles of diversification to decrease risk.40

Many of the basic regulatory issues were resolved by the end of 1996 although some additional legislation did continue to be adopted in later years. Aside from these regulatory issues was the larger question of structural pension reforms. Since their inception, the private pension funds recognized the potential for their sector in the establishment of an option by which citizens could transfer their mandatory state-collected contributions from the state Pension Fund to private pension companies. Furthermore, they made these suggestions known in official publications like the “Ideological Concept of Private Pension Funds” (Yakushev 1994). The report indicates that this idea of allowing the possibility of private management of mandatory savings is very popular among several of the industry’s leaders and pension funds. The report also notes, however, that there is limited support in the government for this more market-

40 “Deklaratsia Ychastnikov R’nka Dopolnitel’nogo Pensionogo Obespechenia,” Adopted at the First All-Russian Meeting of Leaders of Non-State Pension Funds, 23 September (copy available upon request).
oriented plan at present and suggests that the young pension funds should be more concerned with the basic development of their market first.

While a preoccupation with getting basic regulatory systems in place may have been the primary concern from 1992 to 1996, after 1996 structural pension reforms were soon part of Yeltsin’s agenda again (as evidence by the 1997 and 1998 pension reform concepts discussed below). Most importantly, it is clear that even from the sector’s origins they were aware in favor of advocating for pension policies in which they would play a role in the mandatory pension system.

The lobbying efforts of financial intermediaries and private pension funds—although sustained—were not poised to successfully persuade the Yelstín administration or key bureaucracies like the Ministry of Economic Development and Trade. Lobbying efforts alone were not sufficient for financial intermediaries to alter policy outcomes. Democratic politics during the Yeltsin era made it more difficult for the financial intermediaries to convince the government of their informational, political, or economic utility for several reasons: there were many sources of information regarding reform, the Yeltsin administration relied on the oligarchs for political support, government infighting made compromise unlikely, and the economic benefits of privatization were countered by their potential costs.

First, any policy expertise of the private pension funds did not provide a high informational utility to the government. The Yeltsin administration and the Ministry of Economic Development and Trade could look to information provided by the World Bank, other post-communist countries (and countries outside the region which had privatized), and their own economists and experts (interview MEDT 1-100207,
Furthermore, the Yeltsin administration and the Duma had not yet agreed to pursue privatization so that the private financial sector was not definitely going to play a central role in the new system and therefore could not promote itself as an actor whose advice or consultation would be critical.

One possibility would have been for the pension funds to lobby the key bureaucracies in favor of market-oriented reforms—the Ministry of Economic Development and Trade and the Ministry of Finance. The Ministry of Economic Development and Trade in particular was responsible for producing reform proposals to the Yeltsin administration. However, this Ministry had its own economic experts and had access to information from the World Bank and neighboring countries. A senior official at the Ministry of Economic Development and Trade indicated that the pension funds were not directly involved in the formation of its proposals in the 1990s (interview MEDT 1-100207). Those working in the private pension industry further indicated that demographic, socioeconomic, and fiscal pressures motivated reform debates rather than policy proposals from pension funds (interview IC 9-092607). There was no incentive for these bureaucrats to consult with pension funds regarding proposals, particularly at the stage in which the government was deciding on whether to privatize rather than how to privatize.

Furthermore, financial intermediaries and private pension funds were not able to insert themselves as important players into political or bureaucratic debates as a means of advancing their proposals during this era (interview IC 6-092507). One interview in particular noted that the bureaucracy of the pension system was very opaque and that the Pension Fund was like a “black box” whose operations they could not decipher
(interview TE 4-090406). In the executive-legislative standoff, financial intermediaries did not have the possibility of backing a faction which would be receptive to their preference for pension privatization. The Yeltsin administration backed market-oriented reforms, but the oligarchs provided the most valuable source of financial support. Opposition factions in the Duma—including the Communist Party and the nationalist LDPR—would not support pension privatization, but rather distinguished themselves politically, in part, by promoting an increase in pensioners’ benefits. In this context of democratic contestation, the private pension funds in particular had no political utility to any of the major political factions.

Finally, we must consider the potential economic utility of the government being responsive to the lobbying efforts of the private pension funds. The financial sector, while growing, was underdeveloped during the Yeltsin era. Even Dmitriev (2000), one of the most influential proponents of market-oriented pension reform, acknowledged that the single largest hindrance to reform success was an underdeveloped market. Although he argued that the financial sector could and should be modernized in order handle a private pension system, this meant that claims that the sector could handle privatization measures were less credible to policymakers during this time period, including proponents of reform.

In summary, lobbying efforts by the private pension funds were a necessary was not sufficient to change the trajectory of pension reform. The informational, political, and economic utility of the sector to the government was limited for the reasons described above. Political gridlock and competing macroeconomic pressures already
meant that a major overhaul of the pension system was unlikely in the Yeltsin era; lobbying by financial intermediaries and private pension funds did not alter this.

4.2.3 Policy Outcome in the Yeltsin Era

The lack of influence of the financial intermediaries and pension fund during the Yeltsin era are evident in their lack of inclusion in policy deliberations and, notably, in their lack of influence of the official pension reform proposals advanced by the Yeltsin administration. Even the proponents of market-oriented pension reforms during this period did not include explicit recommendations for private pension funds to be allowed to manage and invest mandatory retirement savings.

The lack of influence by financial intermediaries is particularly reflected in the evolution of the official pension reform concepts issued by the Yeltsin administration. These reform concepts were not legislation, but rather declarations of intent by the administration. Throughout the 1990s, the government adopted official reform plans which reflect a gradual change in the pension agenda. All of these agendas were initiated by the government and the private pension funds had no official input in their formulation. While the plans became more explicit in their intention to pursue more market-based structural pension reforms, none included the option of mandatory retirement contributions being privately invested. These reform agendas came from Yeltsin and his administration and were declarations of intent, rather than legislation. A summary of these reform plans can be seen in Table 4.3 on the following page. The four plans reveal that structural pension was on the agenda, but that privatization as a component part of the system was not included until 1998.
<table>
<thead>
<tr>
<th>Year</th>
<th>Reform Concept</th>
<th>Key Characteristics</th>
</tr>
</thead>
<tbody>
<tr>
<td>1992 Pension Reform Concept</td>
<td><strong>Short-term goals</strong> included introduction of pension indexation, pension determined by work history and age, minimum pension set at a subsistence level, and higher pensions to be financed by mandatory insurance payments</td>
<td><strong>Mid-term goals</strong> included gradual increase in size of pensions, decreasing number of pensioners in special work categories, introduction of individual pension accounts, development of automatic systems for departments of social protection, and introduction of private supplementary pension savings</td>
</tr>
<tr>
<td>1995 Pension Reform Concept</td>
<td>1st Tier: Base pension for everyone, determined by the degree of disability</td>
<td>2nd Tier: Labor pension, financed on a redistributive basis, preserves the right to special pension benefits (such as free transportation)</td>
</tr>
<tr>
<td>1997 Pension Reform Concept</td>
<td>1st Tier: Social pension determined by need, depending on the amount that cannot be covered by the second tier</td>
<td>2nd Tier: Labor pension, financed exclusively by defined contributions; Mandatory contributions from professional pension instead of special pension benefits</td>
</tr>
<tr>
<td>1998 Pension Reform Concept</td>
<td>1st Tier: Social pension determined by need, depending on the amount that cannot be covered by the second tier</td>
<td>2nd Tier: Labor pension from two sources: notional defined account and individual accumulated account</td>
</tr>
</tbody>
</table>

Source: Adapted from Degtyarev 2001 (regarding the 1992 reform concept); Maleva and Sinyavskaya 2005, p. 30 (regarding 1995, 1997, and 1998 reform concepts)
The 1992 reform plan laid out short and medium-term goals which involved parametric reforms to the existing pay-as-you-go system. Specifically, the government expressed an intention to cut back on special categories of workers and to introduce a system of supplementary pension payments. There was discussion of developing a three-tier system, but the details were not settled and this was considered to be a long-term goal to the revision of the system.

Building on the goals expressed in 1992, Yeltsin’s government under Prime Minister Chernomyrdin took the initiative to create a comprehensive reform plan, albeit not a very radical one. The primary purpose of this 1995 plan was to acknowledge the problem of pension reform and to signal intent to tackle the issue. The timing of this document suggests that its purpose was political, hoping to signal Yeltsin’s recognition and commitment to solving the pension problem before facing re-election in spring 1996.

The 1995 plan introduced the concept of a three tier pension system, although not one based on the principle of a second tier with individual, privately managed accounts. The first tier would provide a base on pension support. The second tier would provide a labor pension that was redistributive and maintained special benefits. Finally, the third tier allowed for voluntary private investment of pension savings (Karasyov and Lublin 2001; Maleva and Sinyavskaya 2005). Most notably, the 1995 reform concept did not include provisions for a private pension system based on individual accounts.

Yeltsin pulled off a remarkable turn-around from single digit approval ratings in early January of 1996 to enjoy a resounding victory in the presidential election in June 1996 with 54 percent of the popular vote. He accomplished this largely by spending vast amounts of money, often to the dismay of his advisors who had stressed fiscal austerity.
Yeltsin’s spending was strategically targeted to particular regions and for social policies designed to compensate those hurt most by the shock therapy of the early 1990s (Treisman 1996). Treisman explains that part of this strategy included decrees to make short-term increases in pension benefits prior to the election. Evidence of this can be found in Appendix D which lists all of the major pension legislation during the period, with laws pertaining to indexation and increases in benefits highlighted. In 1995, there were five laws enacted to raise the minimum level of pensions, in part to try to keep pace with the rate of inflation. In late May of 1996, just a few days before the election, a law was passed to raise the minimum pension benefit (see Appendix D).

After the election, spending was curtailed and there was not another law passed to raise the minimum pensions again until September of 1997. In the meantime, Yeltsin’s government under Prime Minister Chernomyrdin and new reformist deputy prime ministers Anatoly Chubais and Boris Nemtsov produced another Pension Reform Concept. In a marked shift from 1995, the 1997 plan introduced defined contributions as the sole source of labor pensions in the second tier of pension reform. While the 1995 plan had maintained a second tier based on redistributing benefits, this second iteration of a reform plan shifted in a more market-based direction.

The 1997 plan, however, did not include provision for the private management of mandatory savings. Mikhail Dmitriev, a deputy minister at the Ministry of Economic Development and Trade in 1997, advocated a funded second tier in which mandatory savings would be privately invested. In 1996 Mikhail Dmitriev wrote Alternative Scenarios for Pension Reform in Russia laying out the case for a market-based pension reform. Dmitriev’s ideas were incorporated into the 1998 plan but, critically, did not
specify that individual accounts would be privately invested and confined the role of the
private pension funds to the voluntary sphere. This version of the government’s official
pension reform agenda was produced by a group of experts including bureaucrats at the
Ministry of Economic Development and Trade, a group of experts from the Center of
Macroeconomic Research, the Institute of Sociology, Economics and Law, and the
Moscow Carnegie Center (under the direction of the World Bank). The concept was
heavily influenced, and largely written, by Mikhail Dmitriev, the first deputy Minister of
Labor and Social Development (Degtyarev 2001: 22). Notably absent from this list of
contributors to the new reform concept were any of the private pension funds which had
been operating since the early 1990s.

The 1998 plan modified the goal of establishing a second tier based entirely on
defined contributions to one in which the second tier would be based on a combination of
notional defined contributions (NDC) and individual accumulated accounts. This was the
most market-oriented reform plan the Russian government had yet advanced. Critically,
however, the 1998 concept preserved the dominant role of the national Pension Fund and
did not provide for money in the individual accumulated accounts to be privately
invested. This concept also did not establish any organization or financial mechanism to
create a private savings element. The plan declared the intent to develop voluntary
pension savings, but specified no other role for the private pension funds. Maleva and
Sinyavskaya (2005) note that,

The program of pension reform in 1998… preserved the monopoly of the Pension
Fund as the state financial actor controlling the entire national pension
system…The possibility of increasing the role of private actors was not
considered (p. 21).41

41 Author’s translation from the original Russian
The final official pension reform plan at the end of the Yeltsin era was one in which financial intermediaries had failed to secure any role in managing and investing mandatory retirement savings. Private pension funds were confined to the realm of voluntary savings.

Had the financial intermediaries and private pension funds been more influential, then we would have seen one of two policy outcomes. First, the official reform proposals announced by the Yeltsin administration would likely have included a role for the private pension funds. For instance, the 1998 reform concept would have included a specific provision for the private pension funds to be allowed to invest mandatory retirement savings. Second, if business lobbying had been especially successful then not only would a role for private investment have been included in proposals, but it might have passed in the Duma. Even in the presence of an influential financial lobbying effort, the latter was unlikely due to the executive-legislative gridlock. However, the first scenario—in which political and bureaucratic advocates of market-oriented reforms would take up business proposals—would be a plausible outcome to expect. The policy outcome that did occur during this time period, however, clearly points to a lack of influence, consistent with my theoretical expectations.

If Russia had been less democratic during the Yeltsin era, there would have been a greater possibility for businesses in the financial sector—specifically those operating in the capital market, financial intermediaries, and private pension funds—being more influential on the policy process. In this scenario, Yeltsin could have consolidated his control over the major bureaucracies and the Duma would be controlled by a single party which favored the presidential agenda. There would be less concern with electoral
demands. Yeltsin could have replaced the head of dissenting bureaucracies and considered more radical measures of structural pension reform. Had Yeltsin consolidated his control over the state apparatus, then he might have made an effort to reduce the power of the oligarchs who posed a potential political threat, an initiative which Putin did undertake. In short, had the Yeltsin era looked more like what the Putin era would be, then the private pension funds would have had an easier time inserting themselves into policy deliberations as their political and economic utility to the presidential administration would have been greater.

4.3 Conclusion

The lobbying of the private pension funds in favor of Russian pension privatization served the function of articulating their policy preferences and highlighting their possible informational, political, or economic utility the government. In this way, lobbying was not sufficient for the financial intermediaries to be influential; ultimately, financial intermediaries had to convince the government of their utility to change policy outcomes. Despite lobbying by the private pension funds, they did not change the course of Russian pension reform during the Yeltsin era. Actors in the state ultimately held the power to determine the course of pension reform and financial intermediaries were unable to sway its trajectory during the Yeltsin era. In short, democratic politics blocked the influence of financial intermediaries regarding the adoption of pension privatization.

Although they failed to be influential during the Yeltsin era, the private pension funds played a significant role during the first two years of the Putin administration. Chapter 5 examines how changes in the political regime altered the utility of the private
pension funds thereby allowing them to influence the course of pension reform in 2001.

Once political power had been consolidated by Putin, the private pension funds had a much easier time convincing the government of their utility and the advantages of incorporating privatization into structural reforms.
As of January 2000 when Putin became acting president, the Pension Fund continued to pose a major hurdle to the adoption of any pension privatization measures. Lobbying by private pension funds, however, altered the course of reforms and resulted in the adoption of a partially privatized system. Unlike during the Yeltsin era, the private pension funds had greater access to and influence on key bureaucrats and those in the presidential administration. This was directly due to a decline in the level of democracy associated with Putin’s consolidation of power. The government’s concerns about the recovery of the capital market after the 1998 crash further enhanced the claims by the private pension funds that pension privatization was part of the path to renewed economic growth. Thus, an important part of the reason the change in regime type and pressures related to the 1998 financial crisis resulted in a partially privatized pension system was because of lobbying by the private pension funds. The end result was that the pension funds successfully won the right to invest mandatory retirement savings thereby fundamentally changing Russia’s pension system to be more market-oriented than it would otherwise be.

The evidence of the shift in the influence of the pension funds in the Putin era can be seen in their inclusion in official policy deliberations and accounts of those involved in pension reform in 2000 and 2001. These accounts indicate that the private pension funds
were able to align themselves with key bureaucracies and work through the RUIE successfully to promote their proposals. Moreover, a consistent story emerges from representatives of the major actors involved in policy deliberations including representatives of political parties, the state Pension Fund, the Ministry of Economic Development and Trade, the Ministry of Healthcare and Social Protection, and private pension funds. Finally, the timing at which compromises were made—between the first and second version of bills proposed in the Duma—provides compelling evidence that policymakers were specifically responding to the lobbying of the private pension funds.

Some scholars have characterized the 2001 pension reforms as constituting only a minor change to the system. Åslund (2007) quips that, “In the end, little changed” (220). In contrast to such assessments, this chapter provides evidence that a great deal changed in the nature and design of Russia’s pension system, although—as will be discussed in Chapter 6—the regulation of the new system prevented the major overhaul for which market-oriented reformers had hoped. The compromise that the Putin administration struck between the state Pension Fund and that of the private pension funds made the pension system more private than it would otherwise have been. The private funds gained access to a significant portion of mandatory savings. By 2009, about 5 percent of those eligible transferred their funds into private management and the private funds grew significantly gaining about $5 billion in net worth in a 5 year period (see Figure 4.3 in Chapter 4).

The findings of this chapter are theoretically interesting because they show that the effects of regime type and economic factors like market capitalization are mediated by lobbying efforts. First, scholars have long been skeptical of the extent to which
regime type along predicts policy choice, arguing that the nature of the regime is only a starting point (Remmer 190). Specifically, regime type affects the utility and access that interest groups will have to those in power. Once businesses have access, their claims about economic policy will be helped or hindered by larger economic concerns. In short, changes in regime type explain why private pension fund lobbying efforts were not influential under Yeltsin but were under Putin. Second, the evidence in this chapter counters arguments based on the structural dependence of the state on capital according to which the state should pander to valuable economic sectors regardless of regime type (Block 1977; Lindblom 1977; Poulantzas 1973; Przeworski and Wallerstein 1988). In fact, the change in the nature of the Russian regime under Putin—specifically, becoming less democratic—allowed the private pension funds to effectively link pension privatization and broader macroeconomic consequences in the minds of policymakers.

I use the term corporatism in keeping with the definition provided by Schmitter (1974) who writes that,

> Corporatism can be defined as a system of interest representation in which the constituent units are organized into a limited number of singular, compulsory, noncompetitive, hierarchically ordered and functionally differentiated categories, recognized or licensed (if not created) by the state and granted a deliberate representational monopoly within their respective categories in exchange for observing certain controls on their selection of leaders and articulation of demands and supports (93-94).

This accurately describes the model of business-state relations which the Putin administration actively worked to create as part of his strategy to consolidate political power. Although a corporatist model of business-state relations is not inherently more or less democratic, in this case it was Putin’s use of a corporatism as part of a larger strategy to decrease the extent to which those in power were subject to conventional democratic
pressures (like public criticism, free and fair elections, and a more competitive lobbying environment) which ultimately provided an opening for the private pension funds to effectively lobby.

This chapter is organized as follows. First, in Section 5.1, I describe the trajectory of pension reforms as of January 2000 and emphasize the extent to which the Pension Fund’s position on reform constituted a significant hurdle to any privatization. In Section 5.2, I examine the changing political and economic climate under the Putin administration and why the lobbying efforts of the private pension funds were more successful under these conditions. The result was a compromise on pension policy between the positions of the state Pension Fund and the private pension funds which produces a more market-oriented reform than we would have otherwise seen. I conclude the chapter in Section 5.3.

5.1 Trajectory of Pension Reform in 2000

In part because Putin was Yeltsin’s hand-picked successor, adopting the 1998 reform concept would have been an expected and politically viable step. Doing so would mean the adoption of an NDC system in which the state Pension Fund preserved its role as the sole proprietor of the national pension system. There was no provision in this plan for private pension funds to play a role in managing and investing mandatory retirement savings. Because of the bureaucratic standoff regarding pension reform—in which MEDT and the Ministry of Finance favored market-oriented structural reforms versus the Pension Fund and Ministry of Healthcare and Social Development who opposed them—the 1998 concept was a politically feasible compromise between the bureaucracies. It
allowed for a market-oriented reform—a NDC system—but not privatization and the Pension Fund would retain its monopoly.

During this period, the Pension Fund was one of the most powerful bureaucracies in the government in large part because of its sizeable fiscal resources which it commanded as one of the largest extra (or off) budgetary funds. From 1993 to 1998, its expenditures averaged about 6.1 percent of GDP annually with revenue at an average 6.3 percent of GDP annually. Deficits began to emerge in 1998 which necessitated larger transfers from the federal budget (Orlov-Karba 2005, 71). Despite needing federal support, the Pension Fund still directly controlled a significant amount of money. Because Pension Fund revenue is “off-budget,” its resources are not under the purview of other government agencies and there is a significant source of tax revenue removed from the general budget. For the private pension funds, access to even a small portion of the state Pension Fund’s revenue stream (which amounted to an average of $15 billion annually—in constant 2000 USD—from 1993-1997) would be a huge windfall.

The Pension Fund’s resources also lent it political power. Cook (2007) describes social fund administrators like the Pension Fund as a “second set of veto actors against liberalization” who worked with representatives in the Duma to produce legislation that would preclude reform (p. 131). The operations of the Pension Fund in managing and paying out benefits were also important for the presidential administration to maintain support among pensioners, who might oppose politicians who would be blamed if benefits were not paid in full and on time. The operations of the pension system could

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42 Data are from the Russian Ministry of Finance as reported in Denisova et al. (1999), p. 12.
43 The Pension Fund publishes its annual budget online at www.pfrf.ru.
also being linked to larger economic performance which gave the state Pension Fund leverage with politicians who needed their cooperation.

Putin further strengthened the powers of the Pension Fund, suggesting that he was not initially inclined to challenge this bureaucratic power. As part of his initiative to address pension arrears from the Yeltsin era, in September of 2000 he transferred all responsibility for paying pension from the regional level to the state Pension Fund thereby giving an already powerful bureaucracy even more control.\textsuperscript{44} In October of 2001, the Pension Fund was further granted the authority to directly collect part of the Unified Social Tax.\textsuperscript{45} The powers of the Pension Fund were, therefore, growing during Putin’s early time in office.

The Pension Fund vehemently opposed any privatization measures which would have diminished its influence. The Yeltsin administration’s 1998 reform concept was already more market-oriented than what the Pension Fund had proposed. Therefore, the likelihood of the Russian government adopting an even more market-based plan in which some privatization was allowed was particularly unlikely. In 2000, Zurabov, then the head of Pension Fund, announced that the solution was to delink the connection between wages and pensions, instead determining benefits on the basis of the minimum subsistence level.\textsuperscript{46}

In the official commentary of the system that was ultimately adopted in 2001, Zurabov—at the time the head of the Pension Fund—emphasized the need for a more

\textsuperscript{44} RIA News Agency (Moscow), “Russia’s Putin orders centralization of pension funds,” 28 September, 2000.
effective system of collecting contributions to the pension system and paying adequate benefits, not the benefits of a market-based system. Zurabov stated that,

The pension system that existed on the eve of reforms had practically exhausted its resources. It was characterized by a low level of pension provision for 38.5 million pensioners. The average pension size in the Russian Federation (the social and state labor pension together) provided for a minimum subsistence wage for pensioners. The differences between the minimum and maximum pension was not more than 25-30%. The pension system could not be considered a system in which there was any connection between wages, salaries, and pensions. It was an equalizing system which in essence paid social benefits. This ineffective pension system for the working population resulted in the pension system receiving extremely limited revenue and, as a result, the redistribution [of resources] among pensioners was trivial (Ministry of Healthcare and Social Development of the Russian Federation and the Pension Fund of the Russian Federation official commentary 2007, p. 7).47

Although Zurabov implies the need for some connection between wages and pensions, even in a publication that is intended to explicate the rationale behind the 2001 reforms that were ultimately a NDC system with partial privatization, his focus is on the amount of benefits received by pensioners and revenue for the pension system. He notably omits any discussion of the advantages of introducing elements of private investment into the system such as increasing domestic savings or growing the capital market.

Because of the resources and influence commanded by the Pension Fund, the 1998 reform concept allowed for some structural reform while minimizing backlash from this bureaucratic power (what Cook refers to as a “statist stakeholder”). Even if the Putin administration had the political backing in the Duma to pass a market-oriented reform that the Pension Fund opposed, the Pension Fund could exercise a great deal of leverage on the administration by being uncooperative in implementing a new reform. In fact, after the 2001 reforms were passed, the Pension Fund initially refused to transfer money

47 Author’s translation from the original Russian
into individual accounts. In 2007, the Pension Fund called for some individual accounts to be liquidated and the funds transferred back to the Pension Fund.\textsuperscript{48} Putin’s political goals would be better served by working with, rather than against, the state Pension Fund and this meant that overcoming Pension Fund opposition to privatization was a significant hurdle for the private funds. Any compromise to allow private pension funds to play a role would be a major success on the part of private business.

Finally, it is important to consider the role of public debates over reform during this time period. Pension privatization is a reform that has enormous implications for the nature of citizen-state relations and whether the state or the market will be responsible for supporting individuals in old-age (Brooks 2009). Roberts (2003) has shown the importance of public opinion in shaping post-communist social policy in housing and pensions in Hungary, Poland, and the Czech Republic. In particular, the point in the electoral cycle at which policies were introduced suggests that politicians were taking into account popular demands. Chłoń-Domińczak (2004) has also described the campaign to market Poland’s NDC system to citizens among whom surveys showed some support for a new system.

There is no evidence in the Russian case that public opinion in 2000 and 2001 was a serious consideration. No opinion polls were commissioned by the government and the public had very little information or understanding of the reform. Even Russia’s pensioner party had little concern with the new policy changes but was focused on advocating for benefits for current pensioners (interview 1-120507). Policy experts confirmed that the pensioner groups have not made useful recommendations in the

deliberation process, but simply demanded larger current benefits (interview TE 3-090406). Even the National Pension Council, ostensibly created to promote the image of public deliberations, was a hand-picked group of advisors who met all of three times and outside the sight of the media (Cashu 2001). Additionally, Cashu (2001) writes that participants in the National Pension Council indicated that suggestions were only given a token acknowledgment without ever being incorporated into actual drafts. Rather, the forum was used to inform participants of the government’s plans and garner their support, or more cynically, to create the appearance of consensus support.⁴⁹

One director of a private pension fund succinctly summed up the situation saying that, “You have to understand: Pension reform has nothing to do with pensioners…it has everything to do with future pensioners” (interview PPF 3-102507). This statement reflects in part the fact that pension reforms are almost always phased in so as not to affect current retirees. There were no mass protests against structural pension reforms, however, nor was there a civil society organization attempting to organize them. On the day on which the first version of Russian pension reform was initially passed by the Duma in July 2001, reports indicated that there were a mere 100 people outside the Duma protesting its adoption.⁵⁰ Although structural pension reform is more of a young person’s problem, younger workers who would be most affected by Russia’s reforms were largely unaware of the changes.

⁴⁹ Based on interviews with those involved, Cashu (2001) notes that no other figures except those from the major bureaucracies were allowed so that there would at least be the appearance of agreement.
5.2 Lobbying by the Private Financial Sector, 2000-2001

Private pension funds continued their lobbying efforts begun under the Yeltsin administration, but with much greater success in 2000-2001. I first address the shift in political and economic conditions in the Putin years. I then turn to a discussion of why private pension fund lobbying was more influential during this time period due to these political and economic changes.

5.2.1 Shift in Political and Economic Conditions, 2000-2001

The Yeltsin era was characterized by chronic pension arrears. At the height of Russia’s pension arrears in 1996, 34 percent of pensioners reported not receiving their benefits (Jensen and Richter 2003, 214). The issue of pension payments continued to be an important one for Putin. As acting president in January of 2000, Putin oversaw allocation of federal funds to assist the regions in disbursing pension payments which were still in arrears from the Yeltsin era. Zurabov, then the head of the Pension Fund, presented Yeltsin with his pensioners’ card in a public ceremony, with the promise that Yeltsin would always receive his pension on time and in full, a thinly veiled criticism of the pension arrears under the first Russian president. In October of 2000, Putin raised pensions again, as he had done previously that year, announcing that the total increase in pensions for the year would be 60 percent (the real value of the increase, accounting for

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51 Survey evidence is reported from the Russian Longitudinal Monitoring Survey. The highest incidences of pension arrears were reported in the Northern Caucuses (where 55 percent reported not receiving their pensions) and Western Siberia (where 45 percent reported not receiving their benefits).

52 Amelia Gentleman, “Yeltsin Collects Pension On Time and with Perks,” The Guardian, 6 April, 2000, p.20
inflation, would be 40 percent).\textsuperscript{53} Putin’s moves to increase pensions directly contributed to his popularity at the end of his first term in office. The All-Russian Center for the Study of Public Opinion reported that when citizens were asked what they considered Putin’s most successful measures to be, 44 percent cited raising pensions.\textsuperscript{54}

Unlike Yeltsin, Putin adopted the strategy of combining increases in current retirement benefits with structural reforms as a means of making the latter less objectionable to citizens (Chandler 2004). Putin had begun talks with his economic advisors regarding a reform of the pension system although he was non-committal regarding what specific measures would be taken, indicating that he would be meeting with experts to discuss the issue.\textsuperscript{55} The National Pension Council was founded by Putin in February of 2001 in large part to help mediate the bureaucratic stalemate over reform (Karasyov and Lublin 2001).\textsuperscript{56} As such, the members were primarily top bureaucrats including Zurabov, the Minister of Health and Social Development, and German Gref, the Minister of Economic Development and Trade and high-level politicians including the head of the “Yabloko” political faction, Grigorii Yavlinsky, and the mayor of Moscow, Yuri Luzhkov.\textsuperscript{57} The Council was a publicity measure to sell reform to the general public. After its original founding in February of 2001, the National Pension Council only met for four days in March and a few days in May of 2001 (Orlov-Karba 2005). The Council ultimately functioned more as a symbolic forum than a true arena of

\textsuperscript{53} The Moscow Times, “Putin Signs 10% Pension Increase,” 18 October, 2000. Note that the article refers to a one-time 10 percent increase that was occurring in the fall of 2000. In addition to previous increases, this brought the annual increase in pension benefits in 2000 to 60 percent.

\textsuperscript{54} Interfax News Agency (Moscow), “Russian president’s poll rating survives Kursk Disaster Intact,” 5 December, 2000.

\textsuperscript{55} Interfax News Agency (Moscow), “Putin meets his economic advisor to discuss pension reform,” 23 October, 2000.

\textsuperscript{56} Decree No. 137 of the President of the Russian Federation, “On the National Council of the President of the Russian Federation on Pension Reform,” 8 February, 2001 (copy available upon request).

\textsuperscript{57} Ibid.
policy deliberation. Aside from only having three meetings, its sessions were closed to the public and its members were hand-picked by Putin so that it was a state-led corporatist institution not a public forum.

Reform of the pension system was one part of the larger issue of rebuilding the Russian economy and financial sector, also taken up by Putin during his early tenure. As with pension reform, Putin was somewhat vague on the specific steps that were to be taken, preferring to announce that he wanted to gather all points of view before deciding. Although Putin was unclear on details, certain moves indicated that he seemed to favor a market-oriented approach to reform. For instance, German Gref was put in charge of the Ministry of Economic Development and Trade and was a main source of pro-market reform proposals. Mikhail Dmitriev, a prominent proponent of market-oriented pension reform, was brought in as Gref’s first-deputy minister. These proposals were further backed by the Ministry of Finance and center-right politicians in the Duma who were much larger in numbers after the 1999 parliamentary election (Åslund 2007). Gref’s economic plans were often opposed by other ministries. Regarding pension reform, opposition came from the Pension Fund and the Ministry of Healthcare and Social Development. Therefore, while the Putin administration was inclined towards market-oriented reforms, there was significant internal opposition which would require compromise. Putin was vague enough in his statements to allow for some flexibility in the policies ultimately adopted rather than committing himself to a particular course of action.

Putin’s approach to pension policymaking and the economy varied from the previous presidential administration. This was because Putin had a different strategy for
ruling the country and staying in power than Yeltsin did. One part of this strategy was the successful creation of a presidential party of power (Konitzer and Wegren 2006). Establishing a party of power further facilitated the centralization of political power, a reduction of media freedoms, and a crackdown on the political power of the oligarchs. Fish (2005) explains that Putin’s early moves in this direction had mixed consequences with unclear implications. For instance, Putin’s desire to recentralize would help him consolidate power but could also potentially improve state capacity. Putin also announced his desire to create a “dictatorship of the law” which could in principle serve democratization by promoting a respect for rights. Putin’s rapid moves to bring most national media directly under the government’s control had negative consequences for democracy. Even efforts to consolidate control over the media, however, have had somewhat mixed results. For instance, Gehlbach (2010) documents how Putin consolidated his power over the major media outlets—including the three biggest national TV networks of Rossiya, Channel One, and NTV—but emphasizes that this is not comparable to Soviet-era censorship. In particular, while media coverage is heavily state-influenced there is still space for dissent in print publications like Novoye Vremya and through radio broadcasts like Ekho Moskvy.

A central part of Putin’s new strategy was an attack on the power of the oligarchs. Yakovlev (2006) notes the clear shift in business-state relations in the Yeltsin versus the Putin era. Although Putin was Yeltsin’s hand-picked successor, the political environment would change dramatically. Yakovlev (2006) writes that,

Under President Putin, the relationship between Russian business and the state swung between two extremes. From the situation in 1998-99 when both federal and regional authorities were under the control of ‘oligarchic capital’, and the relation between business and the state was characterized by the so-
called ‘privatization of the state’ (or ‘state capture’), by 2003-04 Russia had made a rapid shift to the dominance of the state over big business (1033).

The sharp change in business-state relations between 1999 and 2003 occurred in the span of just a few years during the early Putin administration. This shift in business-state relation diminished the close personal ties between the presidential administration and the major oligarchic powers. Yakovlev further writes that,

The relations between big business and the federal government were fundamentally changed. The new relationship was labeled as ‘equidistance,’ and authorities tried to avoid direct informal contacts with business tycoons. Such contacts were common in the mid-1990s, and President Putin himself first met the leading oligarchs in summer 2000 at his dacha [summer house], but all subsequent meetings took place in the Kremlin. Meanwhile, the activities of Boris Berezovsky and Vladimir Gusinsky, who had opposed this principle in the mass media under their control, were ruthlessly suppressed (1043).

Rather than relying as extensively on personal connections with the oligarchs, Putin instead favored a more corporatist model in which the government collectively bargained with the RUIE which still represented the interests of the largest corporations and businesses. For the representation of small and medium-sized businesses, the government relied on two commercial associations—Delovaya Rossia and OPORA.

Putin’s attempts to diminish the direct influence of the oligarchs provided an opening for businesses like the private pension funds, whose interests had been marginalized under Yeltsin. First, the pension funds had less competition with the major corporate interests. Second, the pension funds would be able to utilize this more corporatist interest group model to press their policy recommendations upon the new administration. In particular, those working in the private pension fund industry typically had connections with the RUIE. Under the Yeltsin administration, the pension funds were unsuccessful in presenting their proposals through the RUIE which was more
concerned with representing the interests of the oligarchs in seeking favorable tax policies and subsidies. The nature of business–state relations in the Yeltsin era also meant that personal connections with the administration were more important than negotiations with formal organizations. The pension funds as an interest group had little likelihood of being successful in the more personalistic system, but stood a much better chance of getting serious consideration when state-led mechanisms of representation were in place and the oligarchs’ personalistic power was declining.

Non-oligarchic economic interests were also useful to the presidential administration in sending the signal to investors that Putin was pro-market and that his policies were economically sound, particularly since the crackdown on the oligarchs could be perceived as an anti-market move. A Russian equity portfolio manager was quoted as saying,

Nobody knows exactly who Putin is. At the moment, people are waiting to see what Putin will do. There is local buying, and some of the hedge funds have already placed their bets, but the global emerging markets are sitting and waiting.  

Support from the financial sector, therefore, could offer legitimacy to the administration’s economic policies for investors by giving their public endorsement. This is particularly true given that financial intermediaries including private pension funds were the businesses responsible for managing and investing capital in the country and thereby could send a credible signal regarding whether a new leader was pro-market. For instance, because Putin’s statements were initially ambiguous, Russian financial intermediaries—of which pension funds were an important part—had the leeway to

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interpret these comments as reassuring or problematic for investors. At a minimum, it was important for Putin that the financial sector was not a source of vocal opposition to the new presidential administration during this initial time in power.

5.2.2 The Success of Pension Fund Lobbying, 2000-2001

In December of 1999, the League of Private Pension Funds met and formed a new organization entitled the National Association of Private Pension Funds (NAPF). NAPF’s primary stated mission was to lobby the government. This was the first step in revamping the lobbying efforts of the private pension funds. NAPF’s founders emphasized that it would contribute to the professionalization of its lobbying efforts. NAPF laid out four main sets of goals: 1) improving legal conditions for the operations of pension funds, 2) forming an effective system for voluntary pension funds, 3) educating the public about pension funds, and 4) modernizing pension fund transactions (Kalashnikov 2003, 7-8). As with the League in the 1990s, NAPF engaged in typical lobbying activities designed to promote their policy preferences during the Putin era. Regular publications from NAPF offered specific policy recommendations in response to developments in their sector. For example, a 2003 NAPF publication, Existing Problems of Private Pension Funds, documents the developments in the sector and government policies from 2000 to 2003 with three volumes and more than 750 pages of analysis, mostly from the directors of private funds. In short, NAPF was a highly organized and professional association with experienced members and a clear articulation of its goals for bureaucrats and politicians.

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59 NAPF literature does not use the term “lobbying,” likely because of the negative associations with this term in Russia. Instead, NAPS refers to advocacy on behalf of its members’ interests.
NAPF held conferences and organized working groups which brought together high-level bureaucrats and those working in the private pension sector. Sometimes Duma representatives were also included in these conferences. The first meeting of NAPF was held in February of 2000. By June of that year a working group of the NAPF Board of Directors and the Ministry of Labor formed an expert council on private pension fund provision in order to provide policy advice (interview PPF 6-120307). This collaboration between the Ministry of Labor and the newly founded NAPF represents a significant shift in relations between the pension funds and the government during the Yeltsin era. NAPF was having success that the League did not. This is precisely what we should expect to observe if the Putin administration’s incentive was to secure backing from the financial sector for its reforms. This type of formal collaboration between the private sector and the bureaucracy was also in keeping with the more corporatist lobbying model that was developing.

In addition to allying themselves with the pro-reform bureaucracies, the private pension funds also worked through the RUIE to advance their proposals. Working through the RUIE was especially useful for making claims about the economic benefits of privatization as the RUIE represented the largest business interests in Russia. The head of a private pension fund explained that,

We have good relations with the Russian Union of Industrialists and Entrepreneurs because nearly all of our proposals coincide. Because of this we have developed a corporate program, and therefore here [within the RUIE] we are better understood and we have more influence (interview PPF 1-101907). 60

The RUIE had been the lobbying arm of the oligarchs during the Yeltsin era, however, its role shifted under Putin with the emergence of a more corporatist lobbying structure.

60 Author’s translation from the original Russian
During the Putin era, the RUIE played an important influence on pension policy because representatives of pension funds worked through the organization to pressure the government. The proposals of the pension fund channeled through the RUIE may have been better heard under Putin because, unlike during the Yeltsin era, personal relations between the oligarchs and the presidential administration were less important than these formal lobbying channels.

The RUIE has a number of standing committees on policy issues whose primary purpose is to make policy recommendations to the government, one of which is specifically designated for pension reform. The RUIE’s agenda regarding pension reform was determined by its business members who were working in the pension fund industry. For instance, the current head of the board of directors of NAPF, Konstantin Ugrumov, is also the head of the RUIE’s committee on pension reform and himself the director of a private pension fund. If the pension funds were not collaborating with the RUIE, it is hard to imagine that the RUIE would have taken up pension reform as forcefully. In fact, the RUIE did not take up pension reform as key issue during the Yeltsin administration when corporate oligarchic interests dominated the RUIE.

Ugrumov explained that the RUIE and businesses like his private pension fund worked closely with the government concerning technical issues surrounding pension reform (interview with Ugrumov, PPF 5-062308).\textsuperscript{61} He indicated the Putin administration explicitly considered the proposals of the private pension funds articulated via the RUIE and accepted some, but not all, of them. He further indicated that there

\textsuperscript{61} Ugrumov explicitly denied that the RUIE was “lobbying” the government, although this is almost certainly due to the stigma attached to the term “lobbying” in Russia. In interviews, I never initiated the use of the term “lobbying”. Rather, I would inquire first about whether there were policies or regulatory issues about which a business was unhappy and what they might do to affect change on these issues. In answering these questions, interviewees would often clarify that their activities were not lobbying.
were regular collaborations between key bureaucrats and the private pension funds. This was a marked change from the Yeltsin administration. Although oligarchic interests represented by the RUIE were less influential under Putin, concessions were made on pension reform.

The official proposals from pension funds, some of which were issued by the RUIE, emphasized the macroeconomic implications of pension reform. The heightened utility of the pension funds potential role in Russia’s economic recovery made their lobbying efforts more powerful. In regards to this, the state of Russia’s capital market played an important role in helping the lobbying efforts of the private pension funds. Figure 5.1 shows market capitalization in Russia from 1991 through 2008.

Source: World Development Indicators, 2008

**Figure 5.1: Market Capitalization in Russia, 1991-2008**
The capital market began to grow steadily in the mid-1990s, took a major hit during the 1998 financial crash and recovered in 1999 only to take another hit in 2000. A mostly steady recovery began in 2001 although there is another decline in 2008 as a result of the global financial crisis. The sharp fall of market capitalization in 1998 heightened the government’s awareness of the consequences and possibility of capital flight thereby creating an opportunity for the private financial sector to offer its advice on economic recovery.

Concerns about the capital market and broader economic growth enhanced the efficacy of the lobbying efforts of private pension funds on the Putin administration and pro-market bureaucrats like those in the Ministry of Economic Development and Trade. In particular, a growing capital market raised the risk and cost of capital flight. The significant drop in market capitalization in 1998 and again in 2000 particularly highlighted the necessity of recovering to pre-crisis levels of market capitalization. Had the capital market remained small during the 1990s, then the effect of a financial crisis in 1998 might have been much lower and the decline would have not had such a high cost that spurred policymakers to consider its future growth. However, Russia had an increasingly globalized economy, had previously benefited from capital market growth, and then suddenly experienced a sharp decline. The effect of these economic changes meant that the claims of the financial intermediaries in linking pension privatization to capital market growth and larger economic development were all the more attractive to pro-market advocates. This is consistent with theories of the structural dependence of the state on capital which argue that governments will pander to sectors or markets—here the capital market—which are seen as being economically valuable. This case, however,
also indicates that it was the change in regime type in combination with lobbying which made the economic utility of the private pension sector greater.

Developments in the capital market bolstered arguments being made by the pension funds regarding the link between pension privatization and economic development. As the capital market grew, the private pension funds could better assert that the financial infrastructure of the country would be able to handle pension privatization and would therefore realize significant economic gains from it. The sharp drops in the capital market in 1998 and 2000 further meant that they could highlight the risk associated with not adopting policies conducive to capital market growth.

In May of 2001, the RUIE published an official alternative proposal for pension reform in response to the position being taken by the Pension Fund in which it stated that,

All of these questions [in relation to pension reform] can be decided today. And they cannot and should not be decided in accordance with the position of the Pension Fund. It is obvious that the Pension Fund is not interested in the competitive institutions which are the basis for an effective comparison of state and private pension systems according to their administrative resources (in part related to their absolute size and in part to dynamic changes), and according to the effective management of financial resources (RUIE 2001).\(^6^2\)

As the quote reveals, the RUIE’s official objection to the Pension Fund’s position on pension reform criticized an adherence to an outdated model of collective responsibility rather than individual contributions. They also emphasized the macroeconomic consequences of reform pointing to how the Pension Fund’s position would promote high state debt and allow pensions to be managed by a largely unchecked, inefficient state power.

\(^6^2\) Author’s translation from the original Russian
These proposals from the private pension funds via the RUIE were heard by pro-market bureaucrats in the Ministry of Economic Development and Trade, who began promoting strikingly similar proposals. An economist who served for many years as an independent consultant before joining the Ministry of Economic Development and Trade in 2007 noted the influence of the pension funds on politicians saying that,

For the market, of course, there are several possibilities [for influencing the government]. In the very large companies they have these possibilities, these small openings. In principle, if for example, let’s say there were a situation in which the Ministry of Economic Development had prepared some law, drastically worsening things for pension funds, for the majority of the very large private pension funds—these funds of very large companies like Gazprom, Lukoil, and so on. Then, probably, the funds would communicate with them and say, ‘Comrades, oh my god, this is really bad work, you’ve written a very bad law’. And these companies would encourage the deputies not to pass the law. So these large businesses do have this possibility of action in taking initiative in the Duma. This is less possible than 5 years ago, but the option still exists (interview MEDT 5-101607; emphasis added).  

At the time that the major pension reforms were passed, the private pension funds were able to make recommendations to the government regarding pension legislation. He notes, significantly, that their influence waned in the later years of the Putin administration (which is the topic of Chapter 6). However, in 2000 to 2001, the opinion of the pension funds mattered not only for key bureaucrats, but for deputies in the Duma as well. Moreover, these demands of the pension funds were articulated through trade associations like the RUIE which presented formal proposals.

Following the recommendations and reports of the pension funds, pro-market reform bureaucrats in MEDT linked an economic recovery with financial sector reforms including pension privatization. A recovery of the capital market was an important part of this. Key influential bureaucrats like Mikhail Dmitriev, a deputy minister in the

63 Author’s translation from the original Russian
Ministry of Economic Development and Trade, explicitly linked market-oriented pension reforms with an improvement in pension benefits and recovery from financial crisis based. A report initially prepared in 1999 concluded that,

[T]he program of pension reform in the Russian Federation, adopted by the Government of Russia in May of 1998, currently needs to be corrected in connection with the worsening of financial conditions of the pension system as a result of the economic crisis (Dmitriev et al. 2002, conclusion).  

Thus, economic conditions after 1998 had a direct effect on the pension proposals that these pro-market bureaucrats advocated. In a report published in 2000 entitled “Consequences of the 1998 crisis for the pension security system,” Dmitriev noted that the 1998 financial crisis was followed by a 20 percent decline in the real value of payroll contributions to the Pension Fund. As a result the state Pension Fund was unable to increase benefits to prevent a drop in the purchasing power of pensioners.

Dmitriev (2000) further indicated that pension privatization could directly contribute to the improvement of the domestic financial sector and economic recovery. He wrote that,

The majority of successful pension reforms accompanied by the introduction of savings principles, which have been implemented around the world over the past 20 years, were initiated in countries that had experienced profound financial upheavals or systemic banking crises no more than 5 years prior to the initiation of pension reform. One should also bear in mind that, as international experience demonstrates, pension reform based on savings principles in and of themselves are a powerful factor in the strengthening and stabilization of national financial markets and thereby create an environment for a gradual buildup of pension reserves over the long run (p. 7).

Although Dmitriev also acknowledged in his report the challenge posed by the weak state of the financial market for implementing pension privatization in Russia, he argued that

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64 Author’s translation from the original Russian
65 Author's translation from the original Russian
introducing a “savings principle” was linked with recovery of the financial sector. This closely mimics the language used by private pension funds in highlighting their potential role as a sector in the broader economic recovery. Critically, however, Dmitriev did not explicitly link establishing a savings principle with private investment of retirement savings. Rather, at this stage, he left open the question of whether mandatory savings should be held by the state Pension Fund or private funds.

Other policy experts were much less influential on the government, suggesting that the resources and organization of the private pension funds did indeed give their proposals privileged access to policymakers. For instance examples, Russian academics regularly published articles and recommendations about the preferred reforms, but the political influence of such scholars was extremely limited by their own account (interviews TE 3-090406, TE 4-090506, TE 5-091206, TE 6-090706). There is also no indication that such individuals had strong ties with political parties or government bureaucracies. The lack of influence of academic experts provides a useful contrast to the lobbying advantages of the pension funds. For instance, one academic expert on Russian pensions indicated that the Pension Fund was a type of “black box,” the activities of which were hidden to any outside observer (interview TE 3-090406). Such a comment stands in sharp contrast to statements from business people indicating close ties with government bureaucracies and even some ties with the Pension Fund. Private business interests are the only non-government official to have confirmed a working relationships with Pension Fund bureaucrats. A representative of the Department of Investment Organization and Regulation at the Pension Fund confirmed the account of private
businesses explaining that his office continues to work with businesses, especially investment companies, on pension investment related matters (interview PPF 2-071008).

The initial version of the pension reforms passed its first reading in the Duma in mid-July of 2001. Even just a month before the passage of the final reform package in December of 2001, however, it was unclear who would win the battle between the private pension funds and the state Pension Fund. The bill passed in the first reading reflected that the government was mostly concerned with the expansion of the state savings that were accumulated in the Pension Fund rather than allowing private investment (interview MEDT 4-101807). Chandler (2004) further notes that,

…even at this point, the pension reform program was not receiving unanimous support, even within the government. Variants were being proposed by the Ministry of Economic Development and Trade and by the Pension Fund which differed slightly—for example, in the extent to which each was willing to reduce pension benefits for working pensioners. An even more radical variant was proposed by SPS member Boris Nemtsov, who was a member of the National Council on Pension Reform (147).

One of the major issues which would have to be resolved was, if private investment was allowed, the proportion of mandatory contributions which a citizen could choose to have privately invested. There would need to be decisions, in turn, about how these investments would be regulated. A Duma deputy who served on the National Council of Pension Reform summed up the situation saying that, “Naturally, there are many who would like to get their hands on that money” (Duma deputy Valentina Pivnenko quoted in Chandler 2004, 149). Although the debate over the percentage of private investment was not the most public aspect of the reform—public debates instead focused on providing benefits for current retirees and rhetoric about creating a sustainable system—this was an

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important debate between the private pension funds and the state Pension Fund over a crucial aspect of the system’s design.

The Pension Fund maintained that if any private investment was allowed, it should be capped at 2 percent of contributions rather than the 6 percent being proposed by pension funds. The difference between 2 and 6 percent was substantial; it meant an estimated difference of up to 2.4 billion dollars a year in 2004 alone (mandatory contributions were projected to continue rising so that the amount of potential capital lost to the private pension funds would continue to grow annually). 67

The private pension funds—via the RUIE—continued to argue that allowing the existing system to continue was also detrimental to current and future pensioners, the development of the larger financial market, and the national economy. In this way, the corporatist lobbying model that had emerged under Putin allowed the private funds to counter proposals coming from the state Pension Fund by effectively linking pension privatization with broader macroeconomic consequences in the minds of policymakers. They made their case by arguing that,

Russian stock market capitalization today is around $50 billion. In the account of the Pension Fund in 2001 alone (without the introduction of a savings element) there is about 2.5 billion dollars. With the introduction of a savings element, in 5-6 years there would already be financial resources in the Pension Fund worth nearly half of the capital market. Putting these resources in the financial market would of course improve the conditions of the entire economy….adopting the model of pension reform proposed by the Pension Fund would not only hurt the quality of pension provision for current and future pensioners, it would also hurt the growth of savings in the system…and have negative consequences for the national economy (RUIE 2001, 3). 68

67 Ibid.
68 Author’s translation from the original Russian
The claims from private funds that the state Pension Fund proposal would hurt the national economy directly played to Putin’s concerns about insuring that investors saw his administration as pro-market. Given Putin’s interest in an economic recovery, it was especially important that he not take steps which were being touted by the financial sector as detrimental.

Ultimately, these claims coming from the private pension funds persuaded those in MEDT and the presidential administration to modify its proposal; in turn pro-reform Duma deputies sided with the presidential administration and adopted its proposal. Evidence of this can be seen in changes between the versions of the bill adopted in July versus December of 2001 which indicated a compromise to accommodate pro-market proposals. A senior bureaucrat in the Ministry of Economic Development and Trade explained that in the second reading,

[The changes were] very big. Especially in the second reading there were very big changes, in particular, private investment companies were influential in the second reading. And this is the version of the system that was ultimately adopted (interview MEDT 4-101807).  

Specifically, unlike previous iterations, the version passed in December 2001 allowed the private pension funds to manage and invest up to 6 percent of wages which would otherwise be handled by the state Pension Fund. Contrary to the trajectory of pension policy in January of 2000 when a purely NDC system was the most likely outcome, the Russian government adopted a mixed system combining elements of NDC and private

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69 Author’s translation from the original Russian; Another senior bureaucrat with the Ministry of Economic Development and Trade indicated that although the private pension funds had been very influential in deliberations over pension reforms, the investment companies had been less so (interview MEDT 5-101507). He said that the investment companies were less influential because they were simply not as developed in the sphere of pensions in Russia. In any case, the pension funds were the ones most actively developing legislative proposals, indicating that the adoption of proposals for market-oriented pension reforms came from the funds and the investment companies with the latter playing a less critical lobbying role.
pension investment. Furthermore, the percentage of mandatory contributions that could be privately invested was not limited to only 2 percent as the Pension Fund had wanted, but rather was set to increase to 6 percent of wages over time. Given the political and bureaucratic strength of the Pension Fund, this compromise is especially surprising. The Pension Fund, while still powerful, was no longer the sole proprietor of the nation’s pension system.

On December 17th, 2001, President Putin signed into law the three pieces of legislation which overhauled Russia’s pension system. These three pieces of legislation adopted include the following: 1) “On State Pension Provision in the Russian Federation,” 2) “On Mandatory Pension Insurance in the Russian Federation,” and 3) “On Labor Pensions in the Russian Federation”. The first piece of legislation details the pensions covered by the general budget including those for individuals with military service and other civil servants. The second two pieces of legislation—on mandatory insurance and labor pensions—embody what has been referred to as “partial privatization” given that they provide for some private management of mandatory contributions. These bills created a system of notional defined contributions (NDC) under which citizens could choose to transfer a portion of their mandatory savings to be managed by a private pension fund or investment company. A diagram of the Russian pension system can be seen in Table 5.1 on the following page.

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70 Pension legislation in 2001 moved rapidly through the Russian political system. This legislative speed is particularly unusual given that the design of Russia’s constitutional system is uniquely prone to deadlock given the strong powers granted to the president, weak legislative powers, and the fact that the government’s survival depends on support from both the president and the parliament. Remington (2000) notes that it is surprising that as many bills do pass given the hurdles they face in the legislative process. That pension reform, once on the agenda, went through so quickly is characteristic of a process that consisted primarily of elite negotiations among political and business leaders rather than a reform subject to public scrutiny.

Table 5.1: Russian Pension System Adopted in 2001

<table>
<thead>
<tr>
<th>Characteristics</th>
<th>State pension provision</th>
<th>Mandatory Pension Insurance</th>
<th>Additional Pension Insurance &amp; Provision</th>
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<tr>
<td></td>
<td>Pensions for the military and civil servants</td>
<td>Mandatory Pension Insurance</td>
<td>Additional Pension Insurance &amp; Provision</td>
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<td>Pensions granted to those affected by technological catastrophes and their families</td>
<td>Base Portion</td>
<td>Occupational Pensions</td>
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<td></td>
<td>Social pensions for state dependents</td>
<td>Insurance (NDC) and Accumulated Portion</td>
<td>Private pensions, insurance annuities</td>
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<td></td>
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<td>(Between 2-6% of mandatory contributions to this portion can be transferred to private</td>
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<td>investment)</td>
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<td>Tiers</td>
<td>Special Categories of Pensions</td>
<td>Tier 1</td>
<td>Tier 2</td>
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<tr>
<td>Financial Basis</td>
<td>Tier 3</td>
<td>Tier 3</td>
<td>Tier 3</td>
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<tr>
<td>Size of Pension</td>
<td>45-75% monetary support</td>
<td>Calculated based on pension capital and savings, calculated for the expected period of</td>
<td>Determined by the organization paying the pension</td>
</tr>
<tr>
<td>Administration</td>
<td>Fixed size</td>
<td>payments (on an actuarial basis)</td>
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<td></td>
<td>Pension Fund</td>
<td>Pension Fund, private pension funds &amp; other insurers*</td>
<td>Private pension funds &amp; other insurers</td>
</tr>
</tbody>
</table>

Source: Adapted from Afansiev (2003: 8) and Orlov-Karba (2005)

* As of January 2010, the Unified Social Tax has been eliminated and replaced with payroll taxes that are directed to three separate social insurance funds, one of which is the state Pension Fund. The base portion of the labor pension will be financed from these contributions to the social insurance funds. The intent of the reform is, in part, to raise the overall tax rate from 26 to 34 percent of wages by 2011.
As Table 5.1 on the previous page indicates, special categories of pension benefits going to groups such as the military, citizens injured in major disasters (such as nuclear accidents), or other categories of state dependents received pensions funded directly by general government revenue and were not included in the standard labor pension system.

For all other non-special categories of pensions, Russia’s new pension system could be divided into three tiers. The first and third tiers of the pension system constitute the base and voluntary portions respectively, while the second tier is the most significant for market-oriented reformers. This first tier constitutes a basic social safety net which is not connected to contributions, but rather operates on a defined benefit basis intended to establish a minimum level of benefits. The third tier of pensions consists of voluntary, supplementary pension savings which may come from personal savings or from employment-based retirement plans. Recently, the Russian government has tried to encourage higher levels of voluntary savings by offering to match individuals’ contributions (up to 12,000 rubles or about $360) to the accumulated portion of their pensions (Afanasiev 2003; Orlov-Karba 2005).

The second tier of Russian pensions is the most significant for the private pension funds and investment companies seeking to invest mandatory contributions. The second tier of Russian pensions is made up of two component parts—an insurance and an accumulated (or savings) portion. This second tier of pensions was initially financed by

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72 This base part of labor pensions was financed by a portion of the Unified Social Tax (in place from 2001 to 2009) although as of January 1, 2010 the Unified Social Tax has been replaced by contributions to social insurance funds, one of which is the pension fund. The first tier provides a set defined benefit independent of the level of contributions. Although the first tier provides some additional guaranteed security, its replacement rate has declined as increases in the base benefits have not kept pace with increases in wages. The basic pension provided by the first tier is not means tested; therefore, there is no formula for its calculation. Additional benefits may be granted for disabilities and dependents.
14 percent of the Unified Social Tax. Of the contributions going to the second tier, depending on the year in which an individual was born, the mandatory payroll contribution would be divided between the NDC insurance component and the accumulated portion of pensions. Six percent of wages goes to the funded defined contributions (FDC) (which constitute the portion which can be privately invested) and 8 percent to the notional defined contribution (NDC) portion (for a total contribution of 14 percent of wages).

The insurance portion is the part of the pension system based on the NDC concept. Under this system, citizens have individual accounts which are credited with their contributions. However, the accounts are notional in the sense that the contributions to individual accounts are used to fund current pension benefits, rather than being held aside for future generations. Future benefits from the NDC portion of pensions are calculated based on contributions over a lifetime a work and a notional rate of return.

The portion of contributions to the second tier that does not go into the NDC system is held in accumulative individual accounts which operate according to a defined contribution scheme. Depending on a citizens’ age, 0 to 6 percent is appropriated to the accumulated portion of pensions. Figure 5.2 shows the proportion of contributions to tier 2 which make up the accumulative pension.

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73 The Unified Social Tax (UST) was up to 36.3 percent of wages, but was regressive so that those earning more paid a lower rate. Fourteen percent of the UST went to finance the second tier of Russian pensions and a portion of that 14 percent would be appropriate to the accumulated portion of pensions (the size of which is determined by the year in which a citizen was born).
The amount devoted to the accumulative portion of tier 2 increased for certain age groups over time. According to the initial legislation, for men born in 1952 or earlier and women born in 1956 or earlier, none of the contributions to the second tier would be allocated to the second tier. For men born between 1953 and 1966 and women born between 1957 and 1966, the percentage was initially set at 2 percent of contributions to the second tier. However, subsequent legislation passed in 2004, excluded all of those born before 1967 from participating in the accumulative portion of pensions. The only citizens who currently contribute to the accumulative portion of pension are those born after 1967.

\[\text{Percentage of Contributions to the 2nd Tier in the Accumulative Portion of Pension}\]

Source: Orlov-Karba (2005, 108)

Figure 5.2: Size of Contributions to the Accumulated Portion of Pension (in the 2nd Tier)

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portion of pensions are those born after 1967. For these citizens born in 1967 or later, the percentage going to the accumulated portion rose from 3 percent in 2002 to 6 percent by 2007.

The percentage of pension savings to which the private financial sector now had potential access signified a substantial amount of resources, particularly for this still relatively underdeveloped sector. Ultimately, in 2007—even with only 5 percent of those eligible having transferred their savings—the private pension funds net worth quadrupled, increasing by about $5 billion (in constant 2000 USD). At the time of passage, this compromise represented a significant legislative victory and still offers a potential boon for the private financial sector depending on the course of future regulation of the system. As of 2010, about 5 percent of those eligible to transfer their savings have done so and there are about 450 million dollars of mandatory contributions that are being privately invested (in addition to voluntary savings invested with these funds).

Russian pension experts at the Ministry of Labor noted that the passage of the 2001 pension reforms gave a substantial boost to the potential development of the private pension funds. In 2002, they predicted that in three years there would be a tripling in the amount of pensioner reserves and a 68 percent increase in the number of participants. While the gains by 2005 were not quite as good as projected, it was clear that the industry saw this as a very big gain for its potential growth. Data from January 7, 2002 shows an increase in private pension fund reserves and participants less than a month after the passage of reforms and a further increase in the number of private pension funds by July

75 This is calculated based on data on the total holdings of the private pension funds presented in Figure 3 of Chapter 4. Data are from the Inspectorate of Private Pension Funds which is part of the Ministry of Labor of the Russian Federation.
of 2002 (Mudrakov et al. 2002). At this point, the private pension funds had not actually been allowed to manage mandatory contributions—the legislation was not implemented nearly so quickly—but the passage of the reform itself seems to have given the sector a positive boost.

5.3 Conclusion

The trajectory of pension reform at the beginning of the first Putin administration pointed to the adoption of a NDC system in which the state Pension Fund alone managed mandatory retirement savings. Given bureaucratic in-fighting and strong opposition from the powerful Pension Fund, the barriers to any degree of pension privatization were high. However, Putin’s strategy for consolidating his power meant that the private pension funds could serve an important political function because of the diminished role of the oligarchs and the emergence of more corporatist lobbying mechanisms. Had the pension funds not been operating in the sphere of voluntary pensions and developing proposals during the 1990s, they would have been a less identifiable and organized source of proposals in 2000. Their claims were more persuasive due to conditions in the capital market and the larger economy after the 1998 crash. As a result, the private pension funds were able to win the right to invest mandatory savings in the 2001 reforms.

The fact that market-oriented compromises were introduced after the initial draft of the reform provides compelling evidence that the government was reacting to pressure generated by the private pension funds. It is difficult to imagine an explanation for the government’s modification of its pension reform at this stage in the policy process aside from the active lobbying of the private pension funds who were working with key
bureaucrats (especially the Ministry of Economic Development and Trade) and the RUIE. Had pension funds not enjoyed better access to the political system due to changes in business-state relations and a shift to more corporatist lobbying and therefore been able to pursue policymakers and politicians of the economic utility of adopting pension privatization, the Russian government would have little incentive to allow for private management and investment of funds.

In short, the main point of this chapter is that the private pension funds had a unique impact in pushing the adoption of pension privatization measures. For instance, even the most pro-market bureaucracy, the Ministry for Economic Development and Trade, could have opted for the more market-oriented NDC system—as existed in Poland or Switzerland—without privatizing. Moreover, one of the primary authors of Russia’s pension reform, Mikhail Dmitriev, initially promoted the benefits of introducing a savings principle without explicitly stating that private investment was necessary. Allowing private investment constituted a major concession to the private sector more than a concession to pro-market bureaucrats. Thus, the political sway of the pension funds and their ability to convince policymakers of the economic benefits of privatization directly changed the nature of Russian pension reform.
Chapter 6

Financial Sector Not Influential on Regulatory Policy, 2002 and beyond

In this chapter, I examine the period beginning after the adoption of major pension reforms in December of 2001 through the end of 2009. The passage of the 2001 reforms alone was initially considered a major step towards a market-oriented system. While it would take time and additional legislation for a significant shift to private investment of mandatory retirement savings to occur, the move was extremely significant for the sector. Yakushev and Kolobaev (2002) write that,

The participation of the private pension funds in mandatory pension provision is a declaration of a real investment in pension provision and, with this step, the beginning of a real competition between state and private organizations in pension provision, even if the main business of private pension funds will remain in voluntary [supplementary] pensions. 76

In short, the legislation was a very important first step and a signal of a new organization of the pension system and, at least potentially, the basis of a new citizen-state relationship regarding pension rights. While realistic assessments from those in the sector realized that it would take time to see significant growth from investing mandatory contributions, investment companies and private pension funds welcomed the reform. Despite this legislative victory for the private pension funds, a number of regulatory issues remained to be decided. Moreover, the pension funds did not get everything they

76 Author’s translation from the original Russian
wanted in the 2001 reform. The decision to transfer savings into private management is voluntary and the default location is the state-run Vneshekonombank (VEB) which manages the Pension Fund’s holdings. Additionally, all contributions to the second tier are handled through the Pension Fund and citizens wishing to transfer their funds into private management must complete paperwork handled by the Pension Fund. The Pension Fund, therefore, continues to act as the gatekeeper in the new system. In this chapter, I examine why the private pension funds were not able to maintain their influence on the regulation of the new system. Some of those working in the sector even argue that a true reform of Russia’s pension system has yet to begin (interviews IF 2-092507; IF 3-092607), going as far as to refer to the 2001 reforms as “botched”.77

A great deal of additional legislation and regulatory policies were left to be put in place. These issues were significant because they would affect the extent to which Russia’s pension system would operate as one that was run by the market or the state. In this way, the 2001 reforms should be seen as a continuation of pension policy negotiations rather than their culmination. For instance, writing in 2003, the program director of the International Confederation of Public Consumers, Polina Kruchkova, wrote of the large amount of additional legislation, decrees and decisions necessary to implement the new system. She notes that,

These documents will be adopted quietly without discussion with the interested parties…If the population does not received the current necessary information,

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77 Ben Aris, “What’s Really Wrong with Russia,” business new europe (bne), 24 March, 2010
they will not be able to exercise their right of choice….In this situation, without a
doubt, the Pension Fund wins…the resources will stay in the state Pension Fund.\footnote{Polina Kruchkova, “Pensionnaya reforma: Grazhdane Opyat Proigrali Gosudarstvu,” \textit{Vedomosti}, Febrary 26, 2003; author’s translation from the original Russian}

In the early period after reforms were adopted, critics complained that while the rights of
citizens to choose where their pension savings would be invested had been declared by
the government, there was no actual mechanism in place for citizens to exercise this right.
Until 2003, there was literally no process set up for citizens to elect to transfer their
savings to private management even if they had wanted to. The government had not set
up any individual accounts or delegated any bureaucratic offices to be in charge of
processing any request to have mandatory contributions privately invested. The vice
president of the Russian Union of Industrialists and Entrepreneurs (RUIE) declared,
“How the government’s conducted pension reform is shocking!” in regards to the slow
pace with which the 2001 plan had been put into action.\footnote{Konstantin Smirnov, “Shok Reformatorov: RSPP Predlagaet Perestroit Pravistel’stvo,” \textit{Kommersant}, 17 April, 2003; author’s translation from the original Russian}

Even as late as 2005—several years after the passage of the initial pension reform
package—the legal and legislative basis for the new system had not really been
formulated at all (Orlov-Karba 2005: 9). This was especially surprising given the
influence of the private pension funds in obtaining access to mandatory retirement
savings in the 2001 reform. The areas in which legislation still needed to be passed, even
three years after the adoption of the major reforms, included the following: insurance
payment contributions, pension payments, regulations about the investment of
accumulated pensions, the responsibilities and obligations of actors in the new pension
system, and control and oversight of the accumulated portion of pensions. The additional
legislation necessary to make the pension system functional would also greatly influence
the ultimate goals it would accomplish. For instance, Orlov-Karba (2005) notes an improved prognosis for reducing the Pension Fund’s deficit depended on whether additional reforms were adopted. By 2050, he estimated that the balance of the Pension Fund budget under the new pension system with additional reforms compared to a system without additional revisions would change from being a surplus of 500 billion rubles to a deficit of 6000 billion rubles. In addition to dramatically altering the prognosis for the Pension Fund deficit, the follow-up legislation would determine whether the private investment companies and pension funds would actually profit from the new system.

Two main conclusions emerge from this time period. First, while the pension funds enjoyed some legislative success in the 2001 reforms, the implications of that success depended on the regulatory structure of the new system. Three of the major pension policy areas with which Russia had to deal were the accessibility of information about the new retirement scheme, the scope of investments allowed, and continuing debates over the design of the new system. These were critical measures because they defined whether and how the system would work in practice. The pension funds and investment companies so far have failed to see much benefit from the measures adopted in 2001 because the way in which the reforms were implemented limited the profitability for the private financial sector. Second, politicians and bureaucrats were no longer turning to the pension funds and investment companies for policy advice. The private financial sector is of less political utility during this period because Putin had effectively consolidated his political power within the state apparatus. This meant that the system became more centralized and hierarchical so that a great deal of decision-making power was held by the president. As the democratic nature of Russian politics has declined,
politics was increasingly dominated by a small circle of political elites, rather than the group of business and state elites and corporatist policymaking of the early Putin era. These elites primarily consisted of the presidential administration and the heads of major bureaucracies. Thus, this is a period of business capture in which state power is controlled by a few.

This chapter is organized as follows. First, in Section 6.1 I address how the decline in democracy in Russia after 2003 affected the ability of those working in the financial sector, including, the private pension funds to influence the government. I then trace this lack of influence to the failure of the private pension funds to gain concessions in three specific policy areas. In section 6.2, I conclude the chapter.

6.1 How a Decline in Democracy Hampered Private Pension Sector Influence

6.1.1 Changing Political Regime under Putin

As Putin continued consolidating his political power within a single political party and within the state apparatus, the climate of Russian politics changed dramatically. I will first discuss the ways in which democracy declined in Putin’s early tenure. Next, I will link these changes to why private pension funds have been unable to influence the regulation of Russia’s partially private pension system.

The 2000 to 2001 period was part of a short-term, transitional period and by 2003 Russia was governed by one-party authoritarian-style politics. The monopolization of power by United Russia as a party of power significantly diminished political competition. Yeltsin had never formally allied himself with a single political party, but rather had relied on his individual personal popularity. Towards the end of Yeltsin’s time
in office, there were several nascent political parties competing to become the next party of power. Fatherland-All Russia had its base of support in the mayor of Moscow, Yuri Luzhkov, the heads of major republics within Russia (including the president of the republic of Tatarstan), and some oligarchs. Another aspiring party of power—Unity—had its basis of support in the ruling Kremlin powers ultimately including Vladimir Putin.

During his early time in office, Putin was looking for a way to consolidate his power by weakening the power of the oligarchs, particularly those who had already backed another political party or might do so in the future. Unity, which ultimately became United Russia, proved a useful way to do this and was the predecessor to Russia’s first presidential party of power. In 2000, after Unity’s electoral success, United Russia was created through a merger of Unity and Fatherland-All Russia (Smyth 2000). Alongside the establishment of this pro-presidential party, Putin began recentralizing political power in Russia through a series of steps that favored presidential power and helped ensure greater success for United Russia. Ultimately, United Russia was a key organizational tool for Putin to use in establishing his power over regional government, controlling financial resources, and building presidential support in rural areas (Konitzer and Wegren 2006). However, it is telling that both times Putin ran for president, he ran as an independent candidate rather than formally joining what had come to be considered his personal party of power (Hale 2006). In other words, United Russia was a tool to consolidate Putin’s power rather than an indication of the development of a competitive party system. The consolidation of United Russia’s power meant that beginning with the 2003 legislative elections the Russian political system was making a clear move to a one-party system with limited opposition. In 2003, United Russia won 221 out of the 450
seats being contested. The party receiving the second largest number of seats was the Communist Party with a mere 52 seats. United Russia was subsequently able to form a coalition with the Communists which allowed them to control the Duma.

Putin’s crackdown on the oligarchs eliminated another source of possible political opposition. Putin pushed for a “dictatorship of law” and a fight against corruption which was targeted, in part, at the oligarchs. Some oligarchs—such as Vladimir Gusinsky and Boris Berezovsky—chose to leave Russia after being harassed by the new presidential administration and, in some cases, having state-owned entities appropriate some of their holdings. Gusinsky formerly owned the Media Most holdings including the popular NTV television channel on which reports critical of the government’s actions in Chechnya had been aired. In 2001, NTV was sold to the state-run Gazprom. Gusinsky subsequently left the country. A similar story can be seen with Berezovsky. Boris Berezovsky owned a network, at the time called ORT, and Putin allegedly told Berezovsky, “I am going to run ORT. I personally am going to run ORT” (Hoffman 2001, 487). Berezovsky chose to sell his shares in ORT and immigrated to the United Kingdom (Gehlbach 2010, 80-81).

One particular high-profile case caught the attention of the international media as evidence that Putin was going after the oligarchs, although the Kremlin denied its involvement and refuted that the prosecutions were politically motivated. Mikhail Khodorkovsky, formerly the richest man in Russia and the CEO of Yukos, had given money to political parties that opposed the Kremlin and had made some indications that he might consider running for office himself. In 2003, Khodorkovsky and his associate Platon Lebedev were arrested and convicted of charges related to illegal activity in
regards to privatization deals in 1994 and tax evasion.\textsuperscript{80} After Khodorkovsky’s incarceration, Yukos was auctioned off to a new, mystery bidder and only three days later had its production units largely take over by state-owned Rosneft.\textsuperscript{81} Khodorkovsky’s conviction, therefore, removed a source of political opposition and allowed the government to nationalize one of the country’s biggest companies. In 2009, while still serving his initial sentence, Khodorkovsky was brought up on new charges of embezzlement and laundering of stolen property. The on-going trial has prompted renewed discussions about the rule of law in Russia.\textsuperscript{82}

By 2007, there was little serious opposition to the new party of power. United Russia swept the 2007 legislative elections with 315 of the 450 seats. Unlike in 2003, where the non-United Russia votes were spread across several minor political parties, in 2007 only 3 additional parties are represented. The Communist Party and the nationalist Liberal Democratic Russia Party (LDPR) maintained small, but notable, support bases winning 57 and 40 seats respectively. A new party combining several smaller left-wing parties has created the center-left party, A Just Russia. However, the liberal right-wing parties have been entirely marginalized. In 2003, the Union of Right Forces had won a paltry 3 seats in the Duma but won no representation in the 2007 legislative elections.

Several other major changes during the Putin era are indicative of Russia’s declining democracy. First, media freedom was markedly restricted as the government appropriated media outlets, some of which had previously been run by oligarchs like Gusinsky and Berezovsky. The Russian government has come to own all of the major

\textsuperscript{82} The Economist, “A New Moscow Show Trail; the Khodorkovsky Case,” 4 April, 2009.
media outlets, so there is only very limited independent media today. Journalists continue to be jailed and killed amidst a climate which—while not as repressive as the Soviet system—is nonetheless highly restrictive and far from being free or pluralist (Becker 2004; Egorov et al. 2009; Gehlbach 2010). In 2009, Reporters sans Frontières ranked Russia 153 out of 175 countries for media freedoms. Russia’s three main television stations—Rossiya, Channel One, and NTV—are owned directly by the state or by the state-owned company, Gazprom (Lipman and McFaul 2004). Second, in 2004 Putin decreed that regional governors would no longer be directly elected, but rather would be appointed by the president. This was in addition to the creation of the position of presidential representatives in each region. Finally, whereas Russia previously had a mixed electoral system combining single-member districts with proportional representation, in 2005 Putin proposed a bill, which was ultimately passed, to change the electoral system to be based entirely on proportional representation (Moraski 2007). This was a move that favored United Russia and hurt independent candidates with regional bases of support who could win in a first-past-the-post contest but would not clear the threshold to win under proportional representation.

Furthermore, the minimum threshold is set at 7 percent, somewhat higher than the typical
thresholds of 3-5 percent, so that smaller parties do not benefit as much as they could from the switch to proportional representation.

A variety of explanations have been offered regarding why Russia has been on a steady path of declining democracy since 1990. Åslund (2007) blames the lack of clear advice to Yeltsin during the early 1990s which prevented him from taking advantage of the “revolutionary window of opportunity”. Other scholars point to structural issues in explaining why Russia has become less democratic. Fish (2005) notes the presence of a natural resource curse in Russia in addition to a lack of sufficient economic liberalization and a weak national legislature resulting from Russia’s hyper-presidential system. Stoner-Weiss (2006) examines regional level politics, pointing to the ability of local businesspeople to conspire with regional governors to limit market reforms and create a system that is neither free nor transparent. Hale (2006) argues that the combination of Russian institutions of federalism and a hyper-presidential system in combination with the power of the oligarchs precluded the development of a functioning party system thereby hampering democracy.

Regardless of the reasons for Russia’s democratic decline, it is within this authoritarian climate that businesses now lobby the state. Yakovlev (2006) notes that the current climate has shifted from one of business capture to state capture. Rather than oligarchic business interests controlling the state, it is clear that the state is controlling businesses in the post-2003 political era. The change in regime hampered the influence of the private pension sector on major bureaucracies and the presidential administration. First, there was little need for the government to court the support of any potential stakeholders in reforms—like the private pension funds or investment companies—as it
had an incentive to do in 2000 and 2001. Having consolidated power—so that there was “business capture” as Yakovlev calls it—Putin no longer needed to make an effort to accommodate the views of the private pension sector. The model of business lobbying in 2000-2001 morphed into an even more state-directed system in which lobbying was dictated by presidential discretion. Although the private pension sector could formally participate in some policymaking forums, its proposals were largely ignored, evidence of which will be provided below.

Second, the consolidation of power within United Russia meant that there were fewer opportunities through which to introduce proposals opposed to the position of Putin’s administration. During the Yeltsin era, the presence of competing factions in the Duma provided an opportunity for bureaucracies like the Pension Fund or the Ministry of Economic Development and Trade (MEDT) to work with deputies to provide drafts of different legislative proposals. Private pension funds could, in turn, influence the proposals of MEDT and in this way introduce alternatives. With United Russia in power, there was less competition and therefore less opportunity for input from the major bureaucracies. United Russia could solicit the proposals it wanted and ignore others. The power shifted, therefore, from bureaucracies and interest groups like the private pension funds to the new party of power. As a consequence, the private pension funds were of less political and informational utility.

Finally, arguments about the importance of the development of a private pension system being important for larger macroeconomic recovery no longer appeared to be persuasive to the presidential administration. Instead the presidential administration favored increases to current benefits over promoting the development of the private
pension tier. One reason for this is that the presidential administration arguably did not need the help of private businesses to reassure investors it was pro-market. Unlike the Yeltsin administration, Putin exercised significant control over the media. This meant that the Putin administration had a much greater ability to control how its measures were presented in the news, at least domestically. Of course, international investors might still form their own opinions, but the key point is that the Putin administration would not need to worry as much about the negative consequences of open dissent from those working in the financial sector, including the private pension funds.

The hesitance of the private pension funds to criticize the government during the Putin era was apparent in talking to those working in the private pension sector including Konstantin Ugrumov, the president of NAPF and the head of the RUIE committee on pension reform. When I inquired about the issues over which the administration and the pension funds had disagreed prior to the passage of the 2001 reform, Ugrumov simply smiled and said he had already forgotten what any of the disagreements were (interview with Ugrumov, PPF 5-062308). If anyone had knowledge of the disagreements between the government and the private pension funds—about which the Russian media openly reported at the time—it would be someone like Ugrumov who had been involved in daily negotiations over design issues. His response was indicative of a norm of not acknowledging disagreement between those in power and the private sector. Although anecdotal, this is suggestive of closed system in which the government need not fear as much open criticism by those in the market. The economic leverage of the private pension funds could be expected to be lower in the authoritarian system in which the
government controlled the media than in the more pluralist system of the Yeltsin era where the media was freer.

Despite a heavily restricted media, the private financial sector did voice unhappiness about the state of pension reforms in certain venues, even if its opinions were largely absent from the government-controlled media. From the perspective of the private pension sector, the government’s reticence to implement the system is a significant hurdle to the development of the private pension market. The directors of investment companies complained that the government was intentionally dragging its feet in implementing the reform, speculating that the government did not wish to lose any revenue from mandatory contributions. In January of 2003, investment company directors, frustrated by the slow pace of reform, pointed out that the returns to pensions savings being managed by the state-run bank, Vneshekonombank (VEB), were receiving returns of only 6 to 8 percent compared to a 10 percent inflation rate. 87 Those in the industry estimated that because of the government’s hesitance to implement the reforms, 64 billion rubles that could be in private investment were not. 88 It is significant to note that this latter estimate was published in Vedomosti, one of the limited outlets in which we still observe articles that regularlry criticize the policies of the Russian government. 89

The broader international investment community has also criticized Russia’s lack of pension reform, particularly the government’s focus on increasing current benefits through valorization. As a result of valorization, years of work during Soviet times have come to be of increasing importance in determining benefits. In the summer of 2009,

88 Boris Grozovskii, “PFR chitaet zaranee i ni uspevaet zachislist na lichnii pensioni sheta 64 mldr rub.,” Vedomosti, 21 April, 2003.
89 Gehlbach (2010) notes that publications like Vedomosti and the radio program Ekho Moskvy continue to be outlets in which government policy is still regularly criticized.
Bank of America/ Merrill Lynch published a report on Russia’s “looming pension crisis” indicating concerns about the rising deficit of the Russian government. The report indicated that,

The heavy pension burden confirms our view that the budget deficit is likely to remain chronic in the coming decade… We also believe that the shift in budget focus from the investment and economic growth stimulation typical in 2005-08 toward social expenditure and social patronage represents a step change in policy that is likely to be sustained in the mid-term. We do not believe that the government has the financial resources at hand to deliver on its previous ambitious infrastructure investment plans in full (Tsepliaeva and Bokhmat 2009).

International investors expressed particular concern that the sovereign debt-to-GDP ratio could grow from a mere 5.7 percent of GDP in 2008 to 45 percent of GDP in 2010-2020 and that up to 30 percent of government revenue would have to be spent on pensions and debt. One commentator concluded that,

… the Kremlin's botched pension reform must be fixed. The Kremlin has just hiked pensions by 50%. However, there is a hole in the pension fund that already accounts for a quarter of this year's deficit. As the demographic window closes, caused by the aging population, the pension system must be made to pay for itself or this problem will only get worse.90

This strongly negative assessment from the business community reflects concerns that the system will not be fully implemented, that reversals will be made, and that the government’s focus is on increasing the base pension rather than making the funded tier work well. To make the system more sustainable, the financial community is calling for raising the pension age, hiking the relatively low flat tax rate of 13 percent, and increasing the share of accumulated pension savings (Tsepliaeva and Bokhmat 2009). Unlike during the Yeltsin administration, however, business’ claims about how the

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90 Ben Aris, “What’s Really Wrong with Russia,” *business new europe (bne)*, 24 March, 2010

184
failures of the pension system will hurt the larger economy do not appear to have had the same sway on the government’s policy positions.

6.1.2 Diminished Influence of Private Pension Funds

Orenstein (2000) notes that a number of important policy decisions, many of them regulatory, remained to be made in the post-communist countries after the adoption of market-oriented pension reforms. Although the private pension funds continued to lobby the government, changes in the political regime hindered their lobbying efforts compared to powerful government agencies, like the state Pension Fund. For Russia, these issues included three major areas:

1. Restrictions on investment options
2. Accessibility of information about the new pension system
3. Continuing debates over the design of the system

For all of the actors involved in pension reform—citizens, elected politicians, the private sector, statist stakeholders—the stakes of these policy decisions in these three areas were high because they would determine the extent to which investment companies and private pension funds would actually manage and invest mandatory retirement savings in practice. Political battles over these issues, therefore, would determine the consequences of the 2001 legislation.

In this section, I will examine the evidence that the investment companies and private pension funds preferred an outcome in which information about the new pension system to be government-sponsored and easily accessible and would prefer to be able to disseminate information directly. The evidence to be presented below indicates that the private pension funds have pushed for a wider scope of investment tools outside of
government securities, transparent and looser regulation and their activities, and advocated that some portion of mandatory savings go directly into private management by default. The Pension Fund in particular—still a powerful statist stakeholder—used its bureaucratic powers to make information about the new system less accessible, criticize the investment strategies of private companies, limit the role played by investment companies, and advocated diminishing the role of private investment in the new system. It is clear from these continuing political debates that the 2001 reform was a continuation rather than the culmination of pension reform efforts.

I address each of these three specific policy areas—restrictions on investment options, accessibility of information, and continuing debates over policy design—in turn and the unsuccessful efforts of the private financial sector in pushing for reform.

1. Restrictions on Investment Options. The initial pension reform legislation did not specify any regulations for the investment of the privatization pension funds, but such regulations had to be in place before the private pension sector could begin operating under the new system. For policymakers in the government, the concern was regulating the degree of risk that could be taken on by the private pension funds and investment companies. Specifically, some experts argued that a more pro-market system with few restrictions was critical for pension privatization to positively affect the capital market and that more restrictive regimes would undermine the positive economic benefits (Roldos 2004). Some advocated a more self-regulatory framework restricted only broadly by a provision that the investment portfolio be “prudent” as exists in some Western countries (OECD 2002). For instance, in some OECD countries, there are no specific restrictions on where pension savings may be invested (World Pension
Association 2002). Likewise, the IMF argued that loosening government restrictions would improve competition.\textsuperscript{91} Given the highly contentious nature of debates over the design of the system, battles over regulatory policy were a major part of post-2001 pension politics and were at the crux of how Russia’s new pension system would operate in practice.

We should not assume that a more lenient regulatory structure would produce qualitatively better pension policy outcomes. The restrictions of private pension investment may be a prudent measure on the part of the government to minimize risk in the private component of pensions. Tighter restrictions could also address concerns about the consequences of introducing a private pension system in an underdeveloped financial market. The point that I want to make here, however, is that such a regulatory structure is certainly at odds with the type of system that the private pension sector would have liked to see. Countries in Latin America and Eastern Europe which have adopted new pension systems typically have more restrictive regulations on investments than the OECD countries (Rozinka and Tapia 2010). This suggests that in countries in which pensions are recently privatized the private pension sector has had difficulty obtaining what they consider a more favorable regulatory structure.

A more pro-market system would be more akin to what exists in Ireland or Luxembourg, just two examples of where private pension funds face only very minimal restrictions on their investments.\textsuperscript{92} Instead, private pension funds in Russia face a


\textsuperscript{92} In Luxembourg, private pension operate under a “prudent person” restriction but have no specific constraints on their investments. In Ireland, in principle private pension funds are subject to legislation governing the insurance industry broadly, although in practice these rules do not apply to pension funds.
number of constraints on their investment strategies. The first legislation to regulate private pension fund investments was passed on July 24, 2002 (Federal Law 111, “On the investment of resources for financing the savings portion of labor pensions in the Russian Federation”). A large portion of private pension funds’ holdings are invested in short-term government treasury bonds, called GKO\(s\), on which there are no investment restrictions. In 2005, private pension funds had an average of 70 percent of their investments in GKO\(s\) (Orlov-Karba 2005: 151).\(^93\) Investments in stocks or bonds from any foreign issuers, including foreign government treasury bonds, are capped at 20 percent of investments. Investments in currencies are likewise restricted to 20 percent of all investments. Investments in securities from a single issuer are limited to 5 percent, while investments in the stocks or bonds of a single company are restricted to 10 percent. Investments were allowed in mortgage-backed securities although the government left the maximum percentage to be determined by additional legislation (Orlov-Karba 2005: 231-232).

A year after the initial regulatory legislation, in July 2003 additional restrictions on investment were passed. Investments in securities from regional governments are capped at 40 percent and municipal bonds are also limited to 40 percent. No more than 40 percent of investments are allowed to be in mortgage-backed securities (thereby filling in a gap from the regulatory legislation passed in July of 2002). Investments in agricultural collectives would be phased in with a cap of 50 percent of investments in 2004 rising to 80 percent by 2007. The restriction on investments in joint stock

For a detailed explanation of restrictions on pension investments in different countries, see: World Pension Association, “Investment Restriction on Pension Funds,” 2002.\(^93\) Orlov-Karba (2005) reports that 121 pension funds had 50 percent of their reserves in GKO\(s\), 85 funds had more than 75 percent in GKO\(s\), and 66 funds had all of their money in GKO\(s\).
companies would be allowed to be a maximum of 20 percent in 2004 rising to 65 percent by 2007. Additionally, the government instated a new restriction of investments in government bonds legislating that no more than 35 percent could be from a single type of bond (Orlov-Karba 2005, 233). The result of these restrictions is that pension funds and investment companies had limited options for diversifying their portfolios. In addition to caps on investments from single issuers and the types of stock, there were even limitations on the sources of government bonds which could be purchased.

From the perspective of private pension funds and investment companies, they were much too severely restricted in their investment options. Speaking in 2006 about the state of private pensions, Natalia Plugar, the CEO of the UralSib investment company, said that, “Investment companies today have a deficit of [investment] instruments; therefore, to build a balanced portfolio with sufficiently good profits is problematic.”94 The restrictions on the private pension funds are stricter than any other investment vehicles, including mutual funds. This has meant that although the private pension funds have the right to invest in mutual funds, in practice they have been largely unable to do so because very few of the stocks in which the private funds wished to invest meet the legal requirements. For pension funds to invest in mutual funds, the latter must meet the strict investment restrictions applied to the former which very few do. For instance, mutual funds can have up to 15 percent of their investments in a single company while pension funds are limited to only 10 percent. Additionally, for mutual funds at least 15 percent of their holdings must be kept as liquid assets while for private pension funds liquid assets must be at 50 percent. As of 2007, only 1.67% of the holdings of

94 Albert Koshkarov, “Pensionerov Dopustili k Ipotechnim Bumagum,” RBC Daily, 15 September, 2006; author’s translation from the original Russian
private pension funds were invested in mutual funds. Alexander Beskrovny, the head of the Administration on the Regulation and Control of Collective Investment, announced that there would be the creation of special pension mutual funds with the help of investment companies.\textsuperscript{95} It is difficult to see how such measures would make much of a difference, however, if the financial corporations have not previously wanted to establish mutual funds with such restrictive investment criteria.

Despite calls for more diversified investment options, additional restrictions on the investment of private pension funds have been instituted since 2002. One such restriction is on investment in real estate. Previously, the private pension funds had been allowed to invest up to 40 percent of their reserves in any type of real estate. In the summer of 2007, the government adopted legislation restricting the private pension funds to investing only in non-residential real estate and only investing up to 10 percent of their reserves. At the end of 2006 the National Association of Private Pension Funds indicated that only 5 percent of its sector’s investments were actually held in real estate. Although non-residential real estate is considered much more lucrative than residential properties, the new restriction limited their ability to expand into the real estate market.\textsuperscript{96}

The business community saw private pension funds’ assets as a potentially good source of financing for long-term investment in construction which would be beneficial for the development of national infrastructure and a safe, lucrative investment for the pension funds. Some noted, for instance, that American and European pension funds had actively invested in Russian real estate with an estimated 30 percent of foreign

\textsuperscript{95} National League of Investors, “Pensionie PIFi i Pribretenie Inostrannih Tsennie Bumag,” 16 March, 2007.
investments in Russia earning money for Western pensioners.\textsuperscript{97} Restrictions on real estate investment, therefore, are a stark example of an area in which the private pension funds have not been able to secure their desired outcome for regulatory policy. This also stands in contrast to other countries which instituted stricter regulations when they first privatized but then gradually eased restrictions; Chile is one such example (Roldos 2004; World Bank 2001). In contrast, the Russian government is tightening restrictions rather than loosening them.

Other proposals from the private pension sector would have changed the regulatory structure to allow them to invest money that currently goes directly to the state-run VEB bank. News reports indicated that one plan eagerly endorsed by investment companies was to allow for a portion of the default savings that currently go into the state-run bank VEB to instead be entrusted to investment companies.\textsuperscript{98} Despite restrictions on their investment strategies, the investment companies had received larger returns than VEB and given the rising deficits of the Pension Fund, allowing the investment companies to manage savings and get higher returns was, according to the private financial sector, a good alternative. The investment companies were particularly in favor of this option as their ability to compete with the private pension funds to obtain pension savings had been largely unsuccessful.\textsuperscript{99} Unsurprisingly, the private pension funds were less enthusiastic about handing over private pension savings to the investment companies and not them. To date, no such plan has been adopted. As a result of investment restrictions, therefore, the nature of regulatory policy over private pension fund investments in Russia is far from what the private pension sector would like to see.

\textsuperscript{97} Ibid.
\textsuperscript{99} Ibid.
2. Accessibility of Information. The accessibility of information is an important area in which the influence of private pension funds and investment companies has been thwarted. This is one of the most common complaints about government policy by those working in the sector. Due to the unfamiliarity and complexity of the pension system, extensive public education would be necessary to convince Russian citizens voluntarily to transfer their savings into private management. Survey evidence reported by VTsIOM suggests that Russian citizens are ill-informed about the new system, but that those who are informed about it are not enthusiastic.\footnote{A summary of the results of the 2007 VTsIOM survey questions on pension reform can be found at: \url{http://www.rospensia.ru/modules/php?name=pensia_news&year=2006&month=10}} In 2003, about 3 percent of eligible citizens had transferred their savings from state to private management. A mere 5 percent of eligible citizens had chosen to transfer their mandatory contributions from the state into private management. Russian citizens on average did not feel like they understood the reforms or knew how to get more information although this is typical in countries with newly privatized systems. Sixty percent of citizens had heard something about the reform, while 22 percent were hearing about it for the first time when being surveyed. Fifty-six percent of citizens mostly did not understand or completely did not understand the new pension system. Furthermore, citizens who were poorly informed were unclear about where to get more information. Seventy-four percent of respondents said that they did not know which government officials would be able to answer their questions about the reform of the pension system and 77 percent had not received any official information about the pension reforms.

Those citizens who were aware of their options were largely opposed to the new system. Forty-six percent preferred the old system, while only 28 percent preferred the
new system. Six percent thought that the pension reform would worsen the material well-being of the population. Eighty-two percent were not planning on transferring their mandatory contributions to private management. Focus groups indicated that the main reason individuals did not want to transfer contributions to private management was because they preferred the stability of a state guarantee. Seventy-five percent indicated that they were not prepared to participate actively in the process of forming their future pension although it is unclear how Russian citizens would have interpreted such questions. In any case, the hope that Russian citizens would be eager to embrace the new pension system has not been borne out, largely because many are unaware of their options.

A common complaint from private pension funds and investment companies is that the government has failed to advertise sufficiently the new program system and, as a result, few citizens have chosen to have their mandatory contributions transferred to private management. While businesses might take on the responsibility themselves for advertising the merits of private management to the public, they have placed the blame for the reforms failure to take off with the government. One general director of an investment company explained that because this is a government plan, the government should take responsibility for its design. While the logic of the government seems counter-intuitive from the perspective of the government promoting a private option, one director of the investment company argued that the government would be more credible. The director of this investment company explained that,

Currently the state is not providing any general education about this reform. There are advertisements, but nonetheless they need to explain about what future pensioners need to know about the pension the state will pay them. I’m tired of reading in newspapers and journals and so on that the size of my [future] pension
is evident. I know my salary, I know how many years I have worked, I know the amount in my individual pension account and therefore I should know what pension I will receive—but at this moment this question is even too complicated for me, much less the [average] person who comes to us and asks what pension he will receive. It’s a very complicated system…if we’re talking about reform I would propose simplifying it so it can be better understood (interview 2-092507).101

While it seems counter-intuitive to argue that the government should promote a private option, the argument that the government, as arguably a more neutral source than private businesses, would be more credible in promoting the program is plausible. As the quote above indicates, investment companies themselves are having difficulty understanding the implications of the new system for individuals suggesting that the government might be required to clarify the legislation adopted.

The RUIE made several attempts to lobby the government during this period in response to concerns about how the new system was operating. In June of 2006, the RUIE held its first public discussion of the “Concept of the Development of Pension Reform in the Russian Federation” which included representatives of the Ministry of Healthcare, the Duma, the Federation Council (Russia’s upper legislative body), and private pension funds. One of the main concerns was that the population should be more involved in the process of planning and saving for their own pension benefits. In other words, citizens should be better informed.102

A government consultant from the Ministry of Economic Development and Trade likewise concluded that the lack of public awareness was the reason that the system’s development has been stalled. He noted that,

101 Author’s translation from the original Russian

194
On the question of education [of the public about the pension system], people say that it is the investment companies who do not want to invest in the development of the market…[But] it is the task of the government and the investment companies to explain what this system involves…Unfortunately, the state thinks that it’s work is done—it built the system and passed the legislation. If someone is interested, then it’s their responsibility to find information [about it]. I think that the system will grow when the new generation enters into it. But the services [of the pension system] are unclear and it is unclear why the state cannot break up [the power of] the Pension Fund (interview MERT 4-101807).103

This reflects the changing political incentives of the state in the authoritarian context.

The state was not willing to accommodate the preferences of private businesses in the manner it did before.

Officially, the government has not taken a position on promoting the growth of the accumulated portion of pensions. The director of an investment firm noted that,

The government has taken a neutral position on this, so that if private businesses want to make money, then they should propagate pension reform and the state should not try to influence anyone in this regard. But this is not the correct position (interview IF 7-091707).104

This particular investment company director went on to explain that the government was supposed to have provided each citizen in 2003 which an official letter explaining their options between state-run versus private management. From the perspective of the financial sector, their business interests would be served by informing the public about their options. The interests of the Pension Fund were served by encouraging people to take the default option according to which individual contributions would remain under its management. In practice, due to an under-informed public people were, in effect, only offered a single choice as the default was for pension savings to remain in state control.

As such, he considered the system to have been implemented such that citizens were

103 Author’s translation from the original Russian
104 Author’s translation from the original Russian
offered “a choice without a choice” (interview IF 7-091707). Finally, while the
government is officially neutral, it has a clear conflict of interest in promoting the growth
of the second, private tier. The more citizens who transfer their mandatory savings from
state to private management, the more difficult it will be for the state to finance current
pensions. While businesses might hope that the government would more vigorously
advertise its program, there is no reason to believe this will happen.

The investment companies especially lamented the difficulty of finding ways to
market their new pension products. Some chose to work with the private pension funds
which had been investing voluntary pension savings for more than a decade. Still others
placed an emphasis on working with employers rather than engaging in large advertising
campaigns to attract clientele. In any case, the main challenge for these new private
stakeholders was making Russian citizens aware of the option of transferring their
mandatory contributions out of the Pension Fund and, further, convincing them that it
would be profitable to do so. They have yet to be successful in this task.

In some instances, government bureaucracies actively blocked the dissemination
of information relevant to the new pension system. From 2003-2005, investment
companies managing retirement savings received higher rates of return than the state-run
VEB bank which was the default location for contributions to the individual accounts.
According to a rather strange legal stipulation, however, the investment companies were
not allowed the inform citizens of the returns to their pension savings except with the
permission of the Pension Fund, which had declined to allow them to do so.

105 Elena Myazina, “Hunting for Pension Money: Investment companies look to expand through the
106 Elena Myazina, “Kak Uvelichili Pensii: Chasti Upravlaushie Opredili VEB,” Vedomosti, 2 December,
2005
The Ministry of Finance retaliated to the Pension Fund’s refusal to provide information on returns to pension savings by issuing a decree regarding the standards for information that should be provided regarding the investment of pension savings. Additionally, the Ministry of Finance obtained quarterly data on the returns to the investment of pension savings from the Federal Office of Financial Markets (which had only been created in March of 2004) and published these data on their website. While in principle this might mean that citizens could theoretically find the information about returns to their pension savings, the convoluted manner in which the information was disseminated makes it highly unlikely that even citizens who chose to transfer their mandatory contributions into private savings would become well-informed.

The actions of the Pension Fund in obstructing the availability of this information indicate that at least one part of the government was actively working against the establishment of the new pension system and against the interests of the private pension funds. The Pension Fund had no incentive to assist the new private actors in encouraging more citizens to transfer their savings. That the Ministry of Finance actively sought to subvert the Pension Fund’s attempt to prevent the information from getting out suggests that the same bureaucratic battles characterized the political struggle after the 2001 reforms. If bureaucracies could not agree how the system should work, it is unlikely that the average citizen would be able to.

While businesses blame the government for the lack of citizens transferring their savings, the government blames the businesses for their poor performance and inability to attract citizens interested in transferring their savings. The assistant head of the Duma’s

\[107\] Ibid.
Bank committee, Nikolai Bursnikin was quoted as saying that, “the weak bargaining position of the private companies does not encourage the Pension Fund to have any desire to quickly transfer resources [meaning pension savings]” and that in 2004 when citizens could begin to exercise their rights to transfer their savings, “no one is going to be interested in transferring pension savings”. As such, from Bursnikin’s publicly stated perspective, the government had rightly chosen to wait to encourage citizens to transfer their savings as the system was not ready for this shift and citizens were not interested in it anyways.  

This dynamic of the state and private businesses passing the buck between each other regarding why Russian citizens have failed to transfer their savings raises the question of why the private financial sector does not take the initiative to promote a system from which it stands to profit. It appears that there is a circular, or self-fulfilling, pattern which prevents greater progress from being made. The state refuses to invest much time in advertising the system and has at points actively prevented the distribution of accurate information about citizens’ options. In turn, the private pension funds and investment companies, perceiving this lack of state support, are not willing to accept the costs of promoting a system which could be reversed or substantially modified (as is discussed later in this chapter). In part because the state lacks a clear commitment to implementing the reforms, the private financial sector appears to want to avoid investing much time in a potentially stagnating or doomed system.

3. Continuing Debates over the Design of the New System. The investment companies in particular have been the focus of criticism by government bureaucrats who

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were opposed to allowing for the private investment of mandatory pension savings. Unlike the private pension funds who had established their credibility by managing voluntary pension savings since 1992, the investment companies have regularly been the target of bureaucratic complaints and jokes about whether grandma’s pension should be subject to stock market games (although in reality, of course, it is future grandmas’ savings who would be invested on the stock market, not current ones).¹⁰⁹ Legislative proposals from key statist stakeholders threaten the role of investment companies and the private tier of Russia’s pension system more generally. The government’s focus has been on increasing the base portion of pensions, rather than encouraging the growth of the private tier.

In 2005, the Pension Fund proposed two possible pension reforms, both of which would have cut investment companies out of managing savings in the mandatory pension system. Specifically, the Pension Fund recommended that the government either: 1) build a private pension fund system in which the state Pension Fund would act as an intermediary, or 2) the Pension Fund would become the only entity to directly receive mandatory contributions rather than having some contributions go directly to the state-run VEB bank.¹¹⁰ While neither of these measures has yet to be enacted, the limited role of the investment companies in the pension market and the general trend towards focusing on raising the minimum level of pensions suggests that the private pension funds might not survive much longer.

In early 2007, the head of the Ministry of Healthcare and Social Protection at the time, Mikhail Zurabov, began advocating that the pension savings in individual accounts

of citizens who had not chosen to transfer their contributions from the state-run VEB into private management (which constituted about 300 billion rubles or 9 billion dollars) should be used by the Pension Fund to cover its deficit.\textsuperscript{111} This suggestion would have meant a partial reversal of the 2001 reforms and may have been partially response for Zurabov’s replacement in September of 2007. The change in leadership created some cause for concern because Golikova had built her career in the Ministry of Finance, rather than having a long-term ideological interest in the goals that had been traditionally backed by the Ministry of Healthcare and Social Development (interview PPF 1-101907). However, despite the change in leadership, the direction of the Ministry of Health and Social Development has not changed significantly since Tatiana Golikova took over as Minister at the end of 2007. Upon assuming her position, Golikova promised to fix the pension problem in just a three year time period, but the focus was on improving the well-being of current pensioners rather than a concern with implementing the 2001 reform. From the perspective of the Ministry of Health and Social Development, the problem was the value of state pensions not returns to private funds. As part of this, in March of 2010, Golikova has most recently overseen the implementation of a valorization plan which recalculates pensions by giving additional weight to years of work during the Soviet era.\textsuperscript{112}

The Ministry of Healthcare and Social Protection has also advocated for a partial reversal of the legislation passed in 2001. A deputy director of the Ministry, Yuri Voronin, announced that in reforming the pension system, several measures were key: 1) taking the accumulated portion of pensions out of the mandatory system including not

\textsuperscript{111} Evgenii Belyakov, “Intervu s E.S. Gonthmakher,” Gazeta, 9 April, 2007. 
allowing investment companies to manage mandatory contributions, 2) allow the investment companies to transfer the pension savings they manage to private pension funds, 3) transfer the regulation of private pension funds, which are currently regulated as non-commercial entities, to the Ministry of Labor which deals with pension rights anyways, 4) replace the state-run VEB bank which currently manages the savings held in individual accounts of the state-run pension funds, and 5) raise pensions to 70 percent of wages.113 The central theme of Voronin’s suggestions is a dismantlement of the three tier system so that private pension funds are only allowed to operate in the voluntary system. Furthermore, the priority is raising the pension to wage ratio to 70 percent which would mean nearly double the ratio from where it stood at 38 percent in 2008.114

The Ministry of Finance, in keeping with the business community, maintains that increasing pension benefits—particularly without increasing the retirement age—will bankrupt the government. In March of 2010, it was announced that the base portion of Russian pensions would be increased by 6.3 percent in the following month prompting the head of the Ministry of Finance, Alexei Kudrin, to once again announce that the budget cannot handle such increases contrary to Prime Minister’s Putin insistence that the government can afford it. According to Kudrin, taking such steps can result in a deficit for the Pension Fund of up to $5.3 billion.115 However, the 6.3 percent increase pales in comparison to the planned 46 percent increase in pensions that Putin announced in July

114 Tsepliaeva and Bokhmat (2009) report the pension to wage ratios from 2000 to 2008 which range from a high of 38.5 percent in 2000 to a low of 38 percent in 2008.
of 2009.\textsuperscript{116} By all public indications, the government’s priority is increasing the base part of pensions rather than bolstering the private savings portion of retirement benefits.

The Ministry of Economic Development and Trade (MEDT), the bureaucracy largely responsible for the 2001 pension system, has continued to advocate a more market-oriented approach to pension reform. The head of this Ministry from 2000 to 2007 was German Gref. Alongside the replacement of the head of the Ministry of Healthcare in September of 2007, the head of the Ministry of Economic Development changed over from Gref to Elvira Nabulina. However, as with the change in leadership in the Ministry of Healthcare, the direction of Ministry of Economic Development did not substantially change with the new appointment in large part because Nabulina had worked closely with the former minister Gref (interview PPF 1-01907). Since the passage of reforms, the Ministry of Economic Development has been publicly much less vocal in the arena of pension reforms, although still advocates continuing with the market-based system adopted in 2001 rather than backtracking to a more PAYG based system (interviews MERT 1-100207; MERT 2-100207; MERT 3-100207; MERT 5-101607).

An issue of major concern to the private pension funds is gaining access to more mandatory pension contributions for private management. For the private financial sector, the biggest concession that could be won would be to change the default for mandatory contributions to be investment in private pension funds instead of being managed by the state-run VEB bank.\textsuperscript{117} Such a measure is very unlikely to happen as the interest of VEB and the Pension Fund are retaining contributions in state control. This is

\textsuperscript{116} \textit{ITAR-TASS}, “Russia to increase pensions by about 46% in 2010—Putin,” 21 July, 2009.
\textsuperscript{117} \textit{Vneshekonombank} translates as a short-hand form of “domestic economic bank”.

202
both for reasons of financial sustainability and because the Pension Fund seeks to maintain its sphere of influence. In fact, a very big part of the compromise that resulted in the 2001 reforms was that private investment of pension savings would be voluntary and that the default would be the state investment option.

In a somewhat similar proposal to allowing default contributions to be privately managed, the RUIE suggested allowing pension savings that were by default invested in the state-run VEB bank instead be invested in corporate accounts so that there would be a state-private partnership in handling the mandatory retirement savings. According to the RUIE, this was advantageous because it would allow for a more diversified investment portfolio for pension savings thereby increasing returns to the savings and bolstering future benefits.\(^{118}\) Despite these efforts, many of the steps the RUIE has advocated for after the 2001 reform have yet to be adopted or seriously considered. In an interview in June of 2008, the head of the RUIE’s committee on pension reform and himself the general director of a private pension fund, Konstantin Ugrumov, indicated that the most important legislative changes were yet to come (interview NPF 5-062308).

### 6.1.3 Lack of Influence in Official Policymaking Forums

To push for their preferences in the three policy areas discussed above, the private pension funds and investment companies relied on lobbying tactics that they had during the Yeltsin era. However, the effect of the decline in democracy on the influence of the private pension sector is revealed in their role in official policymaking forums. For instance, an economist who served for many years as an independent consultant before

joining the Ministry of Economic Development and Trade in 2007 noted that businesses had previously been able to openly criticize government initiatives to bureaucrats and in the Duma, however, he indicated that, “This is less possible than 5 years ago, but the option still exists” (interview MEDT 5-101607). At the time that the major pension reforms were passed, the most powerful private pension funds were able to successfully push their recommendations to the government regarding pension legislation, but in 2007 experts in the field were indicating that the ability of firms to successfully take such actions were much more limited.

At the beginning of 2003, the government made plans to create a consultative Public Council of Pension Reforms intended to advise the government on key issues related to the design of the new system. This was much akin to Putin’s National Pension Council which had been created in 2001 to discuss the formation of Russia’s new pension system, but dealt with regulatory issues rather than the design of the system. Proposed candidates for the Council included representatives of the National League of Investment Companies (NLU), the National Association of Private Pension Funds (NAPF), and the Association of Russian Banks. Furthermore, government bureaucrats announced their desire to have advisors who knew how to build an investment market, for which the above mentioned commercial organizations were uniquely qualified. Despite proposals for the representatives from the private pension sector, the government chose not to include any of them in the Pension Council in 2003. Instead, the government included representatives of several unions and government agencies. The explanation for this was that the government intended for the Council to be politically neutral and avoid including
any members with vested interests in the financial sector. In short, the private businesses who had just won a major concession in the government’s pension reform plan were quickly shut out from aiding in deliberations over the design of the new system.

Amidst rising public complaints about inadequate pensions, a growing Pension Fund deficit, and the increasing need for the government to make large budgetary transfers to support the Pension Fund, in November 2008 the government organized a Russian Pension Forum that was intended to become an annual forum in which to discuss pension reform issues across a broad range of actors. The Pension Forum included over 300 participants including representatives of business interests, the state, civil society, and other experts. The focus of the Forum, as announced by the Minister of Healthcare and Social Development, Tatiana Golikova, was the strengthening of the insurance principle of the pension system. Strengthening the insurance principle was directly linked with the sum of mandatory contributions to the accumulative portion of pensions in individual accounts. The Pension Fund’s deficit was an issue of concern as well.

A second Pension Forum was held in December of 2009. Prime Minister Putin participated in the forum, emphasizing the importance of pensions meeting European standards for wage replacement being at least 40 percent of wages from which social contributions were made during the preceding 30 years. A deputy head of the Ministry of Healthcare and Social Development, Yuri Voronin, commented that his three main hopes for the forum were: 1) to bolster insurance payments into the system, 2) the

121 ITAR-TASS, “Second Annual RF Pension Forum to be held in Moscow,” 25 November, 2009.
valorization of pension rights, and 3) to raise the social benefits of pensions to a livable level.\textsuperscript{122} One of the main courses of action following this Forum has been to valorize pensions in a manner that weights years of work in the Soviet era more heavily than before and involves a significant increase in benefits for older pensioners. The 2009 Forum culminated with the adoption of an official, “Conception of long-term social-economic development of the Russian Federation in the period up to 2020”.

As with the 2008 Pension Forum, while several hundred participants including representatives of the private pension funds and investment companies and their corresponding professional associations, issues pertaining to the development of the second tier and the accumulative portion of pensions which are privately invested were not addressed. Deputy Director Voronin indicated, contrary to complaints in the industry, that the private sector was growing and doing well and that the focus needed to be on providing a system of stable social insurance. In particular, he noted that the number of participants had risen slightly during the financial crisis of 2008. While it is true that the number of participants rose slightly in 2008, in 2009 the number of participants dropped back to 2006 levels (see Figure 4.2 in Chapter 4). Some of those participating in the Forum even connected the importance of raising pensions with the resolution of the financial crisis.\textsuperscript{123} Despite the inclusion of representatives of private businesses, the focus of both Forums, therefore, has been on increasing pensioners’ benefits and laying out a long-term plan for social development rather than implementing the 2001 reforms.

The power of the Pension Fund to block reform became especially apparent in the mid-2000s. In 2004, the private pension funds had been allowed to begin collecting mandatory pension savings, but problems persisted particularly in relation to cooperation from the Pension Fund in disbursing the funds of citizens who had requested to have their contributions managed privately. The Pension Fund initially refused to transfer individuals’ contributions to any private companies, claiming that it was waiting for a list of federally-insured banks and that, without such a list, it refused to transfer even a single kopek to what it considered unreliable sources. In response to problems such as this, in 2005 the National Association of Private Pension Funds published an open letter to President Putin in the Russian newspaper, Kommersant. The letter asked that the federal organs of power prepare and adopt the legislative acts necessary for the realization of the legislation, “On Private Pension Funds”. The private pension funds were referring back to the 1992 legislation which had initially allowed them to invest voluntary retirement savings, suggesting that the current delays were not only in implementing the new pension system but even in allowing them to operate in accordance with legislation passed 13 years earlier. The Pension Fund did ultimately release the funds to private companies by the end of 2005, as it was legally obligated to do. However, the lack of cooperation by the Pension Fund significantly hampered the development of the private pension fund market.

6.4 Conclusion

This chapter, in combination with the previous two case study chapters, suggests an important modification to our understanding of welfare state politics and pension reform in particular. Demographic factors have been thought to strongly dictate the options that a government can pursue in revising its pension system. However, the research here demonstrates that we should see demographic factors as creating a debate about the proper course of action and shaping the parameters of what can or will be done. Lobbying by private interests can play a determining role in which course of action is chosen.

Additionally, the case of Russian pension reforms and investors’ concerns about the high cost of Russia’s PAYG system are consistent with arguments about the double-bind that globalization creates for policymakers in pursuing pension privatization (i.e., Brooks 2009). Globalization is argued to create pressures to revise PAYG systems while simultaneously making the transitional costs of privatization too high for government’s that fear higher government debt will lead to capital flight. Although Russia passed legislation that in theory would partially privatizes its pension system, the government has done very little to facilitate the growth of private pensions and there are even discussions of significant reversals. Thus, investors express concern about the cost of the current system and the expansion of existing benefits, while the Russian government might also fear the reaction of actually taking on the transitional costs of privatizing.

The findings of this chapter are consistent with my theory of conditional influence in which I argue that policy crisis will open a window of opportunity for the private financial sector to be influential, but the sector’s ability to utilize that opportunity is
contingent on the political regime and economic conditions. In combination with the case studies presented in Chapter 4 and Chapter 5, the evidence presented from the period of 2002 to the present provides compelling evidence that the private financial sector was only able to be influential during a brief window of opportunity in the Russian political system. The private financial sector was politically beneficial during 2000 and 2001 when Putin sought potential stakeholders in the system to back, or at least not actively oppose, his regime. Once Putin had defeated the oligarchs and consolidated government power, however, there was little need to court the support of a group which, while it had capital, was not the largest or most powerful economic sector. This is very much in keeping with Russia’s transition from a system of state capture, in which businesses had captured control of the state, to business capture in which the state has captured control of businesses.

From the early 1990s, structural pension reform were explicitly part of the government’s agenda and official documents prepared by the private pension funds indicate that they saw the potential for profits in a market-based system that allowed them to invest mandatory contributions. Political conditions, however, dictated their success in pushing this agenda. In the Russian political system of the 1990s, the private financial sector simply did not constitute important political allies. A brief window of opportunity in Russia’s partially democratic era of 2000 to 2001 made it advantageous for Putin to court the support of this non-oligarchic business interests. After power was consolidated and Russia was established as an authoritarian system by 2002, the private financial sector was once again largely excluded from meaningful participation in the policymaking process. The changing influence of the private financial sector—jointly
determined by their lobbying activities, resources, and access to the government—
provides a clear indication that money alone does not buy power.
7.1 Main Findings of the Dissertation

I have sought to address the question of when and why businesses in the private financial sector would be able to successfully lobby the post-Communist governments regarding pension policy. I distinguish between influence on the adoption of pension privatization measures versus their subsequent regulation. I find that a critical determinant of lobbying success is the extent to which a regime is democratic. A larger capital market should enhance lobbying claims, but is more likely to do so in less democratic regimes in which leaders need not contend with popular pressures to the same extent as politicians who are freely and fairly elected.

The research presented here offers insight into larger questions of lobbying and business-state relations as well as the politics of economic reform and the welfare state. There are two main related findings: 1) the political power of money and arguments about economic outcomes are not sufficient to secure political influence, and 2) the extent of democracy affects business lobbying. The level of democracy and economic factors like market capitalization do not have a direct impact on policy decisions. Nor does a country’s demographic situation dictate the policies it will pursue. Rather, two countries with similar demographic situations may choose very different pension reforms due to
how differences in the nature of the political regime and the size of the capital market affect financial sector lobbying.

In Chapter 2, I present a theory of conditional influence which is based on the literature on pension politics and business lobbying. At the adoption stage, lobbying by the financial sector was more likely to be influential in less democratic regimes and vice versa. Regarding regulatory policy, however, private businesses were not guaranteed to maintain their influence even if they had successfully pushed for the passage of pension privatization. Additionally, I note that experts have disagreed about the effect that the size of the capital market should have on pension privatization. In contrast to existing explanations, I argue that a larger capital market should enhance the lobbying claims of the private financial sector which argues that pension privatization will be beneficial in securing investments in the domestic economy. A larger capital market, therefore, should make pension privatization more likely. However, because of the effect of regime type on lobbying, we should only observe this positive relationship between market capitalization and pension privatization in less democratic countries. In more democratic countries, electoral pressures and a hesitancy by politicians to take on transitional costs should mean that a larger capital market does not enhance the lobbying claims of the financial sector.

In Chapter 3, I provided cross-national empirical evidence in support of my hypothesis that the capital market would have a different impact on the likelihood of pension privatization in different regimes because financial sector lobbying would be influential in less democratic countries. The cross-national chapter provides evidence of a general trend in the post-communist countries of Eastern Europe, Russia, and Central
Asia, but does not directly evaluate the posited causal mechanism of lobbying. To address this, I complement the cross-national analysis with case studies.

In Chapters 4, 5, and 6, I undertake case studies of Russian pension politics in which I leverage changes in the level of democracy over three distinct political eras. The case studies were chosen to vary on one of the key causal variables of interest, the level of democracy. Chapter 4 covers the period of 1990-1999 when Russian politics was at its most competitive and democratic. The private pension funds were formed in the early 1990s and quickly established business associations to represent their interests. Politics during the Yeltsin era, however, allowed for disagreement between the executive and the Duma, which was dominated by representatives at odds with the presidential agenda. Democratic contestation meant that inter-government battles—including an executive-legislature standoff and bureaucratic disagreements—precluded the private pension funds from having any significant sway. As a result, the Yeltsin era produced no major structural pension reforms.

Chapter 5 covers the 2000 to 2001 period when Putin was first in power and begins to create his base of supporting in part by consolidating his control over the political system. Putin looked to non-oligarchic economic interests for backing which provided an opportunity for the private pension funds to have greater access to those in power. Additionally, in contrast to the more personalistic lobbying under Yeltsin, Putin encouraged the development of a state-led corporatist system in which certain business associations were designated to represent their sectors interests. This enabled the private pension funds to work more effectively through the Russian Union for Industrialists and Entrepreneurs (RUIE) to press their agenda. Lastly, by establishing a single dominant
party of power, United Russia, Putin effectively precluded the possibility for bureaucrats in opposition to his reforms to work with representatives in the Duma to produce alternate legislation. Thus, the decline in democracy in Russia directly contributed to the private pension funds being able to make their case that pension privatization had the potential to grow the capital market and strengthen the overall economy. The result was a compromise in which the private pension funds gained access to billions of dollars in mandatory retirement contributions in the legislation passed in December 2001.

Chapter 6 examines the most recent period from 2002 to the present during which time Russia politics is largely authoritarian. Although the private pension funds had secured a major legislative victory, their opportunity to influence the government quickly ended as Putin consolidated his power within the state apparatus. In this new political environment, the private pension funds had little if any political, economic, or informational utility to the presidential administration. The result has been that the private pension funds have not managed to influence regulatory policy over Russia’s partially privatized system. Although the private pension funds have enjoyed growth in the 2000s, only some of the benefits that they hoped to see as a result of the 2001 reforms have actually manifest.

Taken together, the cross-national analysis and the case study of the Russian case provide compelling evidence of the interplay between the nature of the regime, economic factors like the capital market, and lobbying by the private financial sector in determining whether and how countries revised their Communist-era pension systems.
7.2 Generalizability of Findings and Remaining Questions

The central contention of this dissertation—that the influence of private businesses on policy outcomes is constrained by regime type—can be tested in a wide variety of contexts thereby providing ample material for future research. The theoretical expectations presented in this dissertation are also not limited to businesses as an interest group. More broadly, we should consider how the claims of other non-commercial interest groups are affected by exogenous conditions and, in turn, whether these lobbying claims are more effective depending on the level of democracy. Other possible contexts in which to test the findings include any policy area in which private businesses will advocate a particular solution which includes almost all possible policy realms. For instance, Lowi (1964) separates policy issues into three categories—regulatory, distributive, and redistributive. He argues that different issues activate different groups so that the political battles over distinct issues will have a unique political dynamic. My theory is testable in any of these three policy areas. In keeping with Lowi’s argument, I would also argue that we should consider how the effect of regime type on business lobbying will change with the type of policies under consideration.

We can also test the influence of private businesses on how governments form other economic policies. Stabilization packages provide a specific area in which to observe whether certain businesses, like banks, are able to obtain their preferred outcome. Given the enormous economic implications of stabilization packages, this would be a good case in which to consider how the economic arguments made by a sector may (or may not) undercut democratic policymaking as Lindblom (1982) feared they would. For instance, Keefer (2007) has found that democracies intervene more quickly in financial
crises but their bailouts are 10 to 20 percent of GDP less than in non-democratic regimes. This research suggests that democracies do indeed pander less to “special” interest groups. Keefer (2007) further finds that electoral accountability only affects financial regulatory policy when a crisis emerges. This suggests that scholars should pay more attention to how financial institutions are able to lobby to secure regulatory policy which may not serve the interests of macroeconomic stability or the median voter. Questions about influence on regulatory policy are particularly relevant in light of the 2008 global economic recession, but are also topics of perennial interest to social scientists.

Environmental policy is another area in which my findings could be tested. As with pension privatization, in environmental policy certain private businesses are likely to have clear incentives to push their preferred policies. For instance, based on an examination of the US and the EU, Coen (2005) has noted that businesses have particular advantages over other groups in lobbying governments on environmental policy. Is business lobbying for more lax environmental regulations likely to be more successful in less democratic regimes? Or would the resources and organizational capacity of certain businesses and their arguments about how environmental regulation hurts economic development continue to hold sway? It would be particularly interesting to find that environmental policy is an issue in which the level of democracy did not affect business lobbying. I am assuming that these are cases in which the lobbying of specific businesses may be at odds with the median voter. This is, of course, not always the case. We could also consider the effects of regime type in cases in which businesses might try to alter policy outcomes by mobilizing public support (Kollman 1998).
Aside from testing the implications of my theory in other empirical settings, three major questions are raised by the research presented here which are important areas for future research. First, this research does not address instances in which businesses are instrumental in agenda-setting and how this would influence their ability to propose their favored solutions. In the case of pension privatization, neither the larger financial sector nor private pension funds were responsible for bringing the problem of aging populations or strained finances to the attention of the post-communist governments, policymakers, or the wider population. In contrast, there are issues like regulatory policy or a host of economic policies in which the business communist may be responsible for alerting policymakers or the public to what they perceive to be problems. This is a very different kind of influence than the one considered in this dissertation and is a topic for future research.

Second, there is the question of how businesses form their policy preferences in the first place. In some policy issues such as pension privatization, certain businesses will have a clear financial interest in particular outcomes. It is not always so clear, however, which policies will be most beneficial for which businesses. Following on the example of environmental policy above, some businesses may have good reasons to lobby in favor of stricter environmental regulations, particularly those seeking to develop and profit from renewable energy sources. Moreover, it is important not to assume that all private businesses have the same preferences. For instance, Mares (2003) provides evidence of cases in which certain types of employers would favor the expansion of government-financed social benefits in order to retain a more competitive workforce. Thus, we must be careful not to assume that all businesses share the same preferences and
should explicitly consider the incentives of some businesses over others regarding not just social policy, but other issues as well.

Finally, an issue raised by this research is the circumstances under which a group can secure its on-going influence over a particular policy sphere. In Russia, the private financial sector was able to capitalize on a brief window of opportunity. That the shift in the political system quickly closed that opening speaks to the forceful impact of political institutions on group influence. The private financial sector secured a significant legislative success but within a system in which it was quickly marginalized. The result has been that the Russia’s financial sector has failed to see many of the benefits it hoped to attain from pension privatization. In a broader context, this raises the question of how a group might influence the adoption of policies in which its future role would be more difficult to mitigate.

7.3 Conclusion

This dissertation has aimed to contribute to our understanding of when groups will be influential thereby speaking to the bigger question of who governs in different types of political systems. Although this is only one step in addressing a larger research agenda about how groups are able to successfully shape different policy outcomes under a wide variety of circumstances, the results are theoretically important. Lindblom (1977) writes that, “some of the most fundamental and pervasive features of industrial society are what they are because of the privileged position of business in government and politics.” The findings presented here, however, suggest that—even with a privileged role, resources, and organization—private businesses are constrained by how democratic a society is. In
answering the question of who governs, we should be careful not to assume that material resources and organizational ability directly translate into political influence. Indeed, a central contribution of this research is in showing that money can only buy power some of the time.
# Appendix A: Data and Additional Statistical Analysis

## Description of Variables & Sources

<table>
<thead>
<tr>
<th>Variable</th>
<th>Description</th>
<th>Source</th>
</tr>
</thead>
<tbody>
<tr>
<td>Pensions</td>
<td>Binary variable; a country receives a “0” in a year in which it did not privatize pensions and a “1” in the year in which it adopts private pension reform; a country drops out of the dataset in the year after which pension privatization was adopted</td>
<td>Coded by author</td>
</tr>
<tr>
<td>Market Capitalization</td>
<td>Reported as a percentage of GDP; WDI states that, “Market capitalization (also known as market value) is the share price times the number of shares outstanding. Listed domestic companies are the domestically incorporated companies listed on the country’s stock exchanges at the end of the year. Listed companies do not include investment companies, mutual funds, or other collective investment vehicles.”</td>
<td>WDI, 2009</td>
</tr>
<tr>
<td>Democracy</td>
<td>Freedom House Political Rights Score; I have rescaled the data so that higher values reflect more democratic countries</td>
<td>Freedom House</td>
</tr>
<tr>
<td>Age Dependency Ratio</td>
<td>Ratio of dependents—people younger than 15 or older than 64—to the working-age population—those ages 15-64</td>
<td>WDI, 2009</td>
</tr>
<tr>
<td>Debt</td>
<td>Percentage of GDP</td>
<td>WDI, 2009</td>
</tr>
<tr>
<td>Trade</td>
<td>Percentage of GDP</td>
<td>WDI, 2009</td>
</tr>
<tr>
<td>Partisanship</td>
<td>1= left-wing executive, 0= not left-wing executive</td>
<td>Coded by author</td>
</tr>
<tr>
<td>Government Fractionalization</td>
<td>Probability that two government deputies picked at random from among the government parties will be of different parties</td>
<td>DPI (Beck et al. 2001)</td>
</tr>
<tr>
<td>World Bank loans</td>
<td>World Bank loans as a percentage of GDP; I use this data as a categorical variable with 4 quartiles.</td>
<td>WDI, 2009</td>
</tr>
<tr>
<td>EU</td>
<td>“1” indicates that a country was or is an EU candidate country, “0” indicates that it was not</td>
<td>Coded by author</td>
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### Summary Statistics

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<th>Stan. Dev.</th>
<th>Min</th>
<th>Max</th>
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Test for Violation of the Proportional Hazards Assumption for Model 2 (in Chapter 3)

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<th></th>
<th>P</th>
<th>$\chi^2$</th>
<th>Degrees of Freedom</th>
<th>Prob &gt; $\chi^2$</th>
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<td>.63</td>
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Model including Time Interactions

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<th>Hazard Ratio (Stan. Error)</th>
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<td>Age Dependency Ratio</td>
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<td>World Bank Loans</td>
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<tr>
<td>EU</td>
<td>.13 (.21)</td>
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</table>

| N                          | 136                        |
| No. Failures               | 12                         |
| Prob > $\chi^2$            | .0006                      |
| Log likelihood             | -29.8                      |

Estimates are clustered by country and use the Breslow method for ties
Significance: * p < .1, ** p < .05, *** p < .01
Test for Violation of the Proportional Hazards Assumption for Model with Time Interactions

<table>
<thead>
<tr>
<th></th>
<th>P</th>
<th>$\chi^2$</th>
<th>Degrees of Freedom</th>
<th>Prob &gt; $\chi^2$</th>
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<tr>
<td>Mark Cap*Time</td>
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<td>.92</td>
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<td>Gov. Fractionalization</td>
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<td>.43</td>
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<td>.37</td>
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# Model Including the Kazakh Case, but Omitting the Government Fractionalization Variable

<table>
<thead>
<tr>
<th>Independent Variables</th>
<th>Hazard Ratio (Stan. Error)</th>
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<tbody>
<tr>
<td>Market Capitalization</td>
<td>1.58 (.27)***</td>
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<tr>
<td>Democracy</td>
<td>2.15 (1.03)</td>
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<td>Mark Cap*Democracy</td>
<td>.92 (.03) ***</td>
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<td>Trade</td>
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<td>Debt</td>
<td>1 (.02)</td>
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<td>Age Dependency Ratio</td>
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<tr>
<td>World Bank Loans</td>
<td>1.48e-17 (2.53e-16)**</td>
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<tr>
<td>EU</td>
<td>.28 (.43)</td>
</tr>
</tbody>
</table>

| N                             | 144                        |
| No. Failures                  | 13                         |
| Prob > χ²                     | .002                       |
| Log pseudolikelihood          | -37.68                     |

Estimates are clustered by country and use the Breslow method for ties
Significance: * p < .1,  ** p < .05,  *** p < .01
Test of Proportional Hazards Assumption for Model with Kazakh case (and omitting the government fractionalization variable)

<table>
<thead>
<tr>
<th>Variable</th>
<th>P</th>
<th>$\chi^2$</th>
<th>Degrees of Freedom</th>
<th>Prob &gt; $\chi^2$</th>
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<tr>
<td>Market Capitalization</td>
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<td>Democracy</td>
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<td>.52</td>
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<tr>
<td>EU</td>
<td>.14</td>
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<td>Global Test</td>
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<td>9</td>
<td>.21</td>
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**Probit Models**  
**Dependent Variable: Privatized Pensions in a Given Country Year (1), or Not (0)**

<table>
<thead>
<tr>
<th>Independent Variables</th>
<th>$\beta$ (Stan. Error)</th>
<th>Diff. in Pred. Prob. from -/+ $\frac{1}{2}$ stan. dev.</th>
<th>Marginal Effect</th>
</tr>
</thead>
<tbody>
<tr>
<td>Market Capitalization</td>
<td>.21 (.08)***</td>
<td>.02 → .03</td>
<td>.01</td>
</tr>
<tr>
<td>Democracy</td>
<td>.16 (.24)</td>
<td></td>
<td></td>
</tr>
<tr>
<td>Market Capitalization* Democracy</td>
<td>-.04 (.01)**</td>
<td></td>
<td></td>
</tr>
<tr>
<td>Gov’t Fractionalization</td>
<td>-1.09 (.70)*</td>
<td>.08 → .006</td>
<td>-.06</td>
</tr>
<tr>
<td>Partisanship (binary)</td>
<td>-.72 (.54)</td>
<td></td>
<td></td>
</tr>
<tr>
<td>Trade</td>
<td>.006 (.01)</td>
<td></td>
<td></td>
</tr>
<tr>
<td>Debt</td>
<td>.001 (.002)</td>
<td></td>
<td></td>
</tr>
<tr>
<td>Age Dep. Ratio</td>
<td>7.49 (4.47)*</td>
<td>0 → .96</td>
<td>.44</td>
</tr>
<tr>
<td>World Bank loans</td>
<td>-17.72 (6.5) ***</td>
<td>1 → 0</td>
<td>-1.05</td>
</tr>
<tr>
<td>Diffusion</td>
<td>.19 (.05)***</td>
<td>.02 → .03</td>
<td>.01</td>
</tr>
<tr>
<td>EU (binary)</td>
<td>.40 (.71)</td>
<td></td>
<td></td>
</tr>
<tr>
<td>Constant</td>
<td>-6.95 (3.25)**</td>
<td></td>
<td></td>
</tr>
<tr>
<td>N</td>
<td>136</td>
<td></td>
<td></td>
</tr>
<tr>
<td>Prob $&gt; \chi^2$</td>
<td>.000</td>
<td></td>
<td></td>
</tr>
<tr>
<td>Pseudo $R^2$</td>
<td>.29</td>
<td></td>
<td></td>
</tr>
<tr>
<td>% Correctly Predicted</td>
<td>.93</td>
<td></td>
<td></td>
</tr>
<tr>
<td>Proportional Reduction in error</td>
<td>.17</td>
<td></td>
<td></td>
</tr>
</tbody>
</table>

Note: Probit models estimated with robust standard errors and clustered by country. Significance: * $p < .1$, ** $p < .05$, *** $p < .01$

**Note:** These probit models use the same specification as the Cox proportional hazard models with the exception that I also include the “diffusion” variable here in the probit models in part to account for changes in the probability of pension privatization over time. I do not report the substantive interpretation (here, the change in predicted probability or the marginal effects) for variables which are not statistically significant. A substantive interpretation of the interaction term is offered below.
Interpretation of the Interaction Term of Democracy*Market Capitalization based on Model 2 of the Probit Model

**Effect of Market Capitalization as Democracy Changes**
Interpretation of Probit Model Results

<table>
<thead>
<tr>
<th>Mark Cap: Min to Mean</th>
<th>Mark Cap: Mean to 1 SD above Mean</th>
</tr>
</thead>
<tbody>
<tr>
<td>Dependent Variable: Pension Privatization</td>
<td>Dependent Variable: Pension Privatization</td>
</tr>
</tbody>
</table>

Note: In this graph, we see the effect of changing levels of market capitalization at different levels of democracy based on the probit models presented above. This is the Brambor, Clark, and Golder (2006) method for interpreting an interaction term in a model with a limited dependent variable. The graph shows the effect of one variable over a modifying variable. The calculations are based on simulations of the model parameters which is essentially what the CLARIFY program does (King et al. 2000; Tomz et al. 2001). Following Brambor et al. (2006), I chose 10,000 values of the model parameters using the “drawnorm” command in Stata. The values of all other variables are set at the mean for continuous variables and the mode for binary ones. The graphs above show the first difference—based on the difference between two values of market capitalization—across the observed range of democracy.
Appendix B: Summary of Interviews

<table>
<thead>
<tr>
<th>Group</th>
<th>No. Interviews</th>
</tr>
</thead>
<tbody>
<tr>
<td><strong>Private Pension Funds &amp; Investment Companies</strong></td>
<td></td>
</tr>
<tr>
<td>Including the National League of Administrative Companies, National Association of Private Pension Funds, Pervii Kapital, Aton Management, Uralsib, Alfa Bank, Agana, Trinfiko, and others</td>
<td>19</td>
</tr>
<tr>
<td><strong>Bureaucrats</strong></td>
<td>9</td>
</tr>
<tr>
<td>Including Ministry of Economic Development &amp; Trade, Ministry of Healthcare and Social Development, Ministry of Finance, and Pension Fund</td>
<td></td>
</tr>
<tr>
<td><strong>Other Experts &amp; Politicians</strong></td>
<td>17</td>
</tr>
<tr>
<td>Including former head of Russian Pensioner Party, Russian Union of Industrialists and Entrepreneurs, and Academic Experts</td>
<td></td>
</tr>
<tr>
<td><strong>TOTAL</strong></td>
<td>45</td>
</tr>
</tbody>
</table>

**Note on interviewee codes**

In creating interview codes I follow the format in which I write “interview organization type #-mmddyy”. For instance, for interview number 1 with an official in the Ministry of Health on July 1, 2008, I would write “interview MH 1-070108”.

I use the following labels to indicate the type of organization with which the interviewee:

- PPF = private pension fund
- PF = national (government) Pension Fund
- IC = investment company
- MEDT = Ministry of Economic Development and Trade
- MF = Ministry of Finance
- MH = Ministry of Health and Social Development
- NAPF = National Association of Pension Funds (private, not state, pension funds)
- TE = technical expert
Appendix C: Chronology of Events in Russian Pension Reform

1990-1999 Chapter 4: Russian Pension Policymaking in an Era of Democratic Contestation

*Empirical Outcome:* Creation of stakeholders (private pension funds) who, despite growth in their resources & organization, unsuccessfully lobby for pension privatization

*Theoretical Finding:* The demographic crisis gets pension reform on the agenda, but the influence of the private financial sector is stymied by a lack of access to the government. This confirms the hypothesis that the financial sector will be less influential in more democratic systems.

1990 Soviet law “On state pensions in the Russian Federation adopted (20 November); serves as the basis for 1992 legislation legalizing private pension investment

1991 December: Soviet Union dissolves

1992-1996 First Yeltsin Administration

1996-1999 Second Yeltsin Administration

1992 First Pension Reform Concept Adopted

1993 September: First meeting of Private Pension Funds, results in a declaration of their interests in developing the sector

1994 February: Meeting of the Private Pension Funds, declaration of their interests and concerns in developing the sector; addresses the interest of many in the sector regarding in a system in which some portion of mandatory contributions would be privately invested
29 April: Clarifying legislation (*postavlenie*) No. 408 “On the Inspectorate
of the Private Pension Funds under the Ministry of Social Protection of the Population of the Russian Federation”; this created the Inspectorate of the Private Pension Funds

May: Clarifying legislation (postavlenie) No. 474 “On the Basic Administration of Social Politics,” mentions the necessity of the possibility of the development of the private pension funds with the goal of payments into the voluntary pension accounts of employers and employees

September: Meeting of the private pension funds, results in a declaration of their interests including many specific policy recommendations

1995

7 August: Second Pension Reform Concept (as part of postavlenie No.790)

9 October: Inspectorate of Private Pension Funds under the Ministry of Social Protection issues the first 10 licenses of private pension funds

15 December: Inspectorate of the Private Pension Funds adopts temporary rules on stock investments of the private pension funds and economic laws for payments into private pension funds

1996

Surge in the number of private pension funds after legislation passed at the end of 1995 makes the licensing of private pension funds easier

18 January: Inspectorate of the Private Pension Funds holds the 1st Forum related to the business of the pension funds (with the top 3 funds)

7 February: Inspectorate of Private Pension Funds adopted temporary decree on the organization of the introduction of accounting and the responsibilities of private pension funds

10 November: Government introduces a bill into the Duma of the federal law, “On Private Pension Funds”


1997

Most major regulatory issues regarding private pension funds have been settled by the end of 1996

18 June: Duma accepts in its 3rd reading the law, “On Private Pension Funds”

7 May: Yeltsin signs the federal law “On Private Pension Funds”

20 May: Clarifying legislation No. 463 adopts the Third Pension Reform Concept

1998

Fourth Pension Reform Concept Adopted

August: Financial Crisis

December 31: Yeltsin resigns
27 May: Zurabov becomes the head of the Pension Fund (replacing Barchuk)
13 December: Clarifying legislation (postavlenie) No. 1385, “Responsibilities of the Pension System, laid out for private pension provision of the population”
16 December: General agreement between union representatives, employers, and the Russian government in which it was recommended that all sides had the possibility to work to develop the private pension sector
23 December: Clarifying legislation No.1432 related to the Responsibilities of the components and the structure of the pension reserves of private pension funds and the control of their distribution

2000-2001 Chapter 5: Russian Pension Policymaking in a Partially Democratic Era

Empirical Outcome: Pension reform on the decision agenda: businesses formally included in policymaking, and partial pension privatization is adopted in 2001

Theoretical Finding: The increasing cost of the demographic crisis keeps pension reform on the agenda. Because this is a less democratic era in which Putin does not have a stable base of support, the state has an incentive to co-opt the support of the private financial sector by including it in the policy process. This confirms the hypothesis that the financial sector will be more influential in less democratic systems.

2000-2004 First Putin administration (Putin become acting president as of 1 January, 2000 and is popularly elected in March of 2000)

2000 22 February: In Moscow, there is a meeting of the National Association of Pension Funds; participants include several of the major private pension funds (GazFond, LukOil-Garant, Sberegatelnovo Bank, Semeini, Surguneftgaz, Ugol, Elektroenergetki)

28 April: Adoption of clarifying legislation NO. 383, “On the organization of private pension fund contracts with depositors and the business of depositors with private pension funds”
2001  8 February: Presidential decree creates the National Council on Pension Reform

11 May: Government presents a package of law on pension reform to the National Council on Pension Reform for the President’s consideration

28 May: The Nation Council of Pension Reform propose 3 major law to the President for Pension Reform


2002-2009  Chapter 6: Russian Pension Policymaking under Authoritarian-Style Politics

*Empirical Outcome:* The private financial sector fails to successfully influence regulatory policy.

*Theoretical Finding:* This confirms the hypothesis that the influence of the private financial sector on regulatory policy is limited in less democratic systems.

2004-2008  Second Putin administration

2008-2012  Medvedev administration

2002  Implementation of New Pension System Begins

26 June: Duma Adopts in 1st Reading the Federal law “On Mandatory Corporate Systems in the Russian Federation”

24 July: Law No. 113-FZ “On Investing the Resources for Financing the Accumulated Part of Labor Pensions”


23 July: Presidential decree No. 827 on the Recommendation of the Public Council on the investment of the resources of pension savings

2003  9 March: Presidential decree No. 314 creating the Federal Office on the Financial Market to replace powers previously held by the Ministry of Labor and the Ministry of Healthcare and Social Development

9 March: Presidential decree No. 322: Zurabov becomes Minister of
Healthcare and Social Development (was previously the head of the Pension Fund)

9 April: Clarifying legislation (postavlenie) No. 206 “Questions related to the Federal Office of the Financial Market regarding basic functions including its control and oversight in relation to private pension funds”

30 June: Government adopts clarifying legislation (postavlenie) No. 321 about the role of the Ministry of Healthcare and Social Development in the development of state politics in the sphere of pension provision and in connection to private pension provision

2005

4 February: In Kommersant (a major Russian newspaper), the National Association of Pension Funds publishes an open letter to the Russian President in which they request that the federal organs of power quickly prepare and pass the legislative acts necessary for the realization of the Federal Law, “On Private Pension Funds”

6 January: Clarifying legislation (postavlenie) No. 2 is passed making changes to legislation No. 669 (from Nov. 2003) on changing to the organization of oversight and regulation of the business of private pension funds, mandatory pension insurance, and corporate pension insurance; specifically this clarifies that the Ministry of Healthcare and Social Development will deal with the legal relations between the private pension funds and participants and those investing their mandatory savings in private pension funds; a Federal Office on Financial Markets will regulate the private pension funds in all other areas

2006

1 February: Clarifying legislation (postavlenie) No. 63 is introduced with rules about the distribution of the resource of pension reserves to private pension funds and the control over their distribution

26 April: Putin proposes beginning state financing of voluntary pension savings; This is adopted as the “1000-for-a-1000” plan in which the government matches contributions of 1000 rubles to voluntary savings account, up to 12,000 rubles.

9 May: Law No. 574-r; Milovidov begins leadership of the Federal Office on Financial Markets

20 July: Federal law No. 70-FZ, begun in 2005, regarding the transfer of insurance payments for the formation of the accumulated part of labor pensions for persons born after 1967, rate deduction into pension system lowered from 28 to 20 percent

December: Bureaucratic overhaul - German Gref is replaced by Elvira Nabiulina as the head of the Ministry of Economic Development and Trade; Mikhail Zurabov is replaced by Tatiana Golikova as the head of the Ministry of Healthcare and Social Development
2008  30 April: Proposal of Federal Law No. 56-FZ, “On additional insurance payments to the accumulated portion of labor pensions and state support for the formation of pension savings,” and Law No. 55-FZ on insurance changes and other legislative acts
   September: Prime Minister Putin meets with the government and adopt a strategic plan for the further development of the reform of the Russian pension system
   September-October: Global financial crisis begins
   1 October: Adoption of Law 56-FZ (proposed on 30 April, 2008)
   16 December: First Pension Forum held in Moscow
   27 December: Government presents Putin with a package of proposed legislative reforms for the accumulated pension insurance system

2009  Continuation of the “1000-for-1000” plan to encourage citizens to save more in their voluntary pension accounts (government offers matching contributions in 2000 ruble increments up to 12,000 rubles)
   25 November: Second Pension Forum held in Moscow
Appendix D: Major Pension Legislation & Decrees, 1990-1999*


Resolution No. 2122-1, Questions about the Pension Fund of the Russian Federation (Russia), 27 December, 1991.


Presidential Decree on Non-State Pension Funds, Decree No. 1077, 16 September, 1992 (edited from Presidential Decree 4.12.1999, No. 456)


Resolution No. 5357-1, On Tariffs of Insurance Payments in the Pension Fund of the

* Copies of the original text of legislation and decrees in Russian were obtained from official government publications and are available upon request. The highlighted pieces of legislation are those pertaining to indexation measures intended to increase pension benefits which, as is evident here, were one of the primary measures taken by the government during this period.


Presidential Decree on Indexation of State Pensions in the Russian Federation from 1 August, 1994 and the Sources of its Financing, No. 1584, 3 August, 1994


Law on Raising the Minimum Size of Pension and the Organization of Indexation and Recalculating Pensions in accordance with the Law, “On State Pensions in Russia,” No. 30-F3 3, 1 October, 1994

Law on Raising the Minimum Size of Pensions, Organization of Indexation and Recalculating of State Pensions in the Russian Federation, No. 31-F3, 31 October, 1994


Concept of the Reform of the System of Pension Provision in the Russian Federation, issued as a directive by the government on 7 August, 1995, No. 790


Law on Improving Pension Provision for Participants in the Great Fatherland War [World War II]


Law on the Organization of the Calculation and Improvement of State Pensions, No. 113-FZ, 21 July, 1997


Law on Mandatory Social Insurance from Accidents in Industry and Work-Related


Resolution No. 117, On the Inspection of Non-State Pension Funds under the Ministry of Labor and Social Development of the Russian Federation, 5 October, 1999


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