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The Changing Contours of Corruption in Russia: Informal Intermediaries in State- Business Relations

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Abstract

Despite extensive academic and media discussion about corruption in Russia, there has been little analysis of how the corruption process works and what makes it so deeply entrenched. One reason is that the notion of corruption is often used as an umbrella term to cover a variety of fundamentally different phenomena that have one formal feature in common – using an official position to gain private profit. Often overlooked in the discussion is the fact that the corruption market is constantly changing, not only in terms of the scale and volume of corruption (which is almost impossible to measure), but, more importantly, in terms of substantial changes in its forms, mechanisms and content, and the emergence of new informal actors and even institutions. There are constantly emerging new forms of informal interactions, along with new actors – *informal intermediaries* – which facilitate a variety of informal relationships in the business sphere. This paper provides an empirically-based sociological analysis of the phenomenon of informal intermediaries and of the “intermediaries’ boom” – an explosive growth of intermediaries recently transforming the Russian business environment using data from a study of small and medium business in St. Petersburg. The emergence and

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institutionalization of informal mediating is considered a new stage in the evolution of corruption in state-business relations in Russia.

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Introduction

According to the annual monitoring conducted by Transparency International Russia constantly occupies one of the lowest positions in the CPI rating. Extensive discussion on corruption in Russia in the media and in academic publications provides little analysis of how the corruption process works and what makes it so deeply entrenched. The very notion of corruption is often used as an umbrella term to cover a variety of fundamentally different phenomena, with only one formal feature in common i.e.– using an official position to gain private profit. In order to undertake an exploration of the origins and the nature of corruption it is important that corruption is not seen as a holistic and homogeneous phenomenon but as a multifaceted bricolage of “corruptions” distinguished from each other in their forms, origins, and motives of participants of the corruption deal and even in the nature of the corrupt interaction. In this way a more effective strategy for the study of corruption is the analytical description of various “corruptions”, focusing on micro practices, including the cultural norms they imply, and combining insights gained from these studies with the analysis of institutional structures.

The study that provided empirical data for this paper was focused on small and medium-sized business in St. Petersburg. Informal relations with authorities in small and medium business have some specific features concerning either the level of bureaucracy involved in the interactions or the content of the problems to be solved. For small business in Russia, the problems of overregulation and impracticability of formal rules remain the main obstacles for doing business.. This is better expressed in the words of one of the informants of our study: *“If you had not been violating the rules... If you had been playing fair, then it would have been better not to be working at all!”* As a rule, corruption in small business is provoked by the impossibility to obey formal regulations without considerable losses for business. That is why it does not appear as some competitive strategy or deviating behavior but rather as an attribute of everyday economic routine, which is aimed not at improving the situation but at not worsening it. The phenomenon of corruption in small business can be labelled *“routine”* or *“everyday”* corruption, a defensive reaction of business to the state’s pressure, and in this sense it is principally different from the traditional

understanding of corruption as an aggressive business strategy (see Olimpieva, 2007). This sort of corruption can be better referred to as “weapons of the weak” (Scott, 1985) that James Scott considers in the wider context of silent resistance typical for subordinated, powerless groups in society.

Also overlooked in the literature is the fact that corruption is a flexible, constantly changing phenomenon, reflecting the evolution of the economy and society. This is particularly true for the transforming economies in which the general context is fundamentally modified almost every year. Corruption is changing, not only in terms of its volume (which is almost impossible to measure), but, more importantly, in terms of substantial changes in its forms, mechanisms and content, and in the emergence of new informal actors and even institutions. There are constantly new forms of informal interactions emerging, along with new actors, who facilitate a variety of informal relationships in the business sphere. While informality remains a dominant feature of the Russian business environment, it is taking on a more organized and systematized shape. This paper provides an empirically-based analysis of the phenomenon of informal intermediaries facilitating relationships between business and authorities which is seen as a new step in the evolution of corruption in Russia. Although our studies were focused on the St Petersburg municipality alone, the outcomes are not specific to St Petersburg and could be extrapolated to the phenomena of informal mediating throughout the Russian business sphere, particularly involving small and medium sized business.

The phenomenon of economic mediation does not appear as something new in the economy. It has been attracting the attention of many scholars for a long time. Various economic models presented in economic literature explain the essence of mediating in the trade sphere with different kinds of agents (“middlemen,” “dealers,” “market makers”) facilitating interactions between producers and consumers and between sellers and buyers of commodities and assets (see, e.g., Rust and Hall, 2002). There are also a number of works focused on bureaucratic intermediaries that assist businessmen in passing through various administrative procedures, in getting necessary information. (see, e.g., Bray, 2005; Hasker and Okten, 2008; Lamsdorff, 2002; Polishchuk 2003, and others). The peculiarities of the institute of bureaucratic mediation in the developing countries are also the subject of study of some economists (see, e.g., Andvig et al., 2000; Oldenburg, 1987). However, to date, the market of bureaucratic services in Russia has not received much attention by researchers, with only a few works that consider the phenomenon of bureaucratic mediation in Russia (see e.g., Migin et al, 2005, Olimpieva et al, 2004, Olimpieva et al, 2007, Polishchuk, 2003; Polishchuk, 2004).

Unlike the economic research approach that dominates studies of intermediaries this paper presents a sociological analysis of this phenomenon. Empirical data for this analysis was gained from the two studies of corruption in small and medium business in St. Petersburg conducted by the St. Petersburg Center for Independent Social Research in 2003-2005.² Both projects used the micro-approach perspective and qualitative research methodology. Unlike quantitative methods, the qualitative sociology does not aim at measuring the scale of the researched phenomenon, but rather seeks to answer the question concerning why it exists, what are its forms and features, and which conditions predetermine its existence. Among the main research instruments of qualitative methodology are interviews, observations, and case studies.³ Another feature of qualitative methodology is that the researched phenomenon or process is considered from the perspective of participants, that is people who are directly involved in the researched process.

The first study of corruption in small and medium business in St. Petersburg included about 30 in-depth interviews with business representatives - top managers and key persons in different kinds of business organizations – regarding various informal aspects of their relationships with officials. The second study was focused on informal mediating services in cross-border cargo transportation. Two cases of intermediary services were chosen: customs brokers serving small and medium business doing customs clearance and tourist firms that act as mediators for shuttle traders in their relationships with customs on the Russian-Finnish border. About 20 interviews were conducted with brokers, businessmen, customs officials, shuttle traders, tourist guides and other people involved in cross-border cargo transportation. We also used participant observation in shuttle buses going from St. Petersburg to different towns in Finland.

² The project “Prospects for Fighting Corruption in Post Socialist Countries: Cases of Russia and Hungary” was carried out in 2003-2004 within the frame of “Think Tank Partnership Program” supported by USAID, IRIS and KPMG Consulting Barents Group. Another project “Intermediaries’ Boom and Informal Relationships in the Business Sphere and Everyday life” was conducted by CISR researchers in 2005 with the support of the Jefferson Institute.

³ Analytical considerations and conclusions are illustrated by quotations from the interviews. After each quotation in brackets, characteristics of the informants are indicated. Although the content of the quotations has not been edited, the text of some quotations was slightly modified for the convenience of the reader by introducing words explicitly implied but missed by the informant (these words are enclosed in brackets []), and by removing redundant phrases that do not influence the general sense (the removed phrases are marked by (...)). Some quotations include not only the answers of informants but also the questions of interviewers.

The paper starts with an analysis of the difference between formal and informal mediating. We will consider the “intermediaries boom” - an explosive growth of mediating structures recently transforming the Russian business environment and the difference between Russian intermediaries and their counterparts in western economies. The essence of informal bureaucratic mediation is explained using the case of mediating services provided by different agents-intermediaries at customs. The paper then looks at different types of informal intermediaries using data from interviews with businessmen in different business sectors. The next part of the paper illustrates the development of the phenomenon of informal mediating into a sustainable informal institution. We then consider the economic essence of informal mediating with regard to particularities of the general context of the Russian business environment. Finally, informal mediating will be considered as a new stage in evolution of corruption in Russia.

The Difference between Formal and Informal Mediating

In recent years there has been an explosive growth in the market for *bureaucratic services intermediaries* that facilitate informal relations between businesses and state authorities. Numerous intermediary firms have appeared in different segments of administrative markets. Interviews with business people have demonstrated that almost all of our informants using informal ways of ‘solving problems’ resort to informal services provided by intermediaries (organizations or individuals), who assist them in obtaining documents necessary for doing business, passing through registration procedures or gaining access to bureaucratic bodies. Corrupt officials do not enter the bureaucratic market personally any more, rather they rely on a variety of intermediary structures. We call this phenomenon the ‘intermediaries boom’, and the agents providing informal mediating services – ‘informal (corrupt) bureaucratic intermediaries’.

There is, of course, nothing unique about the Russian economy having intermediary services. In established capitalist economies, the role of intermediaries has been legitimized and routinized, to a large degree, with many transactions depending on the involvement of brokers, attorneys, agents, and other individuals specialized in complex rules and bureaucratic procedures. It is possible to regard the emergence of such mediating services as evidence of functional specialization and hence as a normal development of the market. However, our study demonstrates a crucial difference between the mediating system in established capitalist economies and in Russia. While the main purpose of intermediaries in the West is to assist in meeting the requirements

imposed by bureaucratic procedures, which are too complicated for non-specialists and requiring the mastery of obscure details, mediating services in Russia often serve as a screen, functioning as a hidden form of rewarding officials for accelerating bureaucratic procedures or for “closing their eyes” to discrepancies between the formal rules and real practices. One of the key differences involves the role of informality in their activities. Our empirical data indicates that the informal component of mediating functions, through which informal access to official bodies is maintained, plays a crucial role in the effectiveness of mediating process. Thus, by “informal mediation” we refer only to the informal component of mediation functions. Specifically, we refer to mediation services that are based on informal access to a bureaucratic structure (or to an individual bureaucrat).

The difference between formal and informal mediation will become more evident through consideration of the case of custom brokers– a mediating institution present in western countries and in Russia. The complex nature and intricate character of customs rules are inherent to every country, and therefore cargo carriers everywhere resort to the help of intermediaries – customs brokers. However, the task of customs brokers in Russia is not just to assist businessmen in going through customs formalities, but to help manipulate and reduce cargo cost, accelerating the process via informal channels.

A special market of informal custom services has emerged during the last decade in Russia offering a wide spectrum of customs clearance schemes - from “white or light-grey” to “fast black.” (see e.g., Barsukova, 2002; Radaev, 2003).⁴ “Grey schemas” constitute those schemes which infringe upon legal rules or norms while making up customs declaration to reduce the overall “customs expenses” paid by the cargo owner or to speed up the process of customs clearance. The coloration of grey schemas can be lighter or darker depending on the degree of the violation of legal norms. The same color spectrum is used to mark the legal status of customs brokers – white or grey. The term “grey brokers” is used to indicate some specialized firms (or individuals) that do not have any license for customs brokerage activities, however they do all the work of customs clearance on behalf of cargo owners. Very often (but not exclusively) the role of grey brokers is played by transportation firms that fill in and submit customs declarations and solve problems with customs on behalf of their clients.

⁴ The detailed ethnographic description of informal relations at customs also see in Olimpieva, I., Pachenkov, O., Ejova, L., and Gordy, E. (2007)

“We can be labeled as grey brokers. The real broker is some juridical person (organization) that possesses a license to represent the interests of some third person in the customs. Specifically for this purpose! ... And this firm is eligible to conclude a special agreement with a third person – a brokerage agreement. This is an official agreement, according to which it can do registration of cargo on behalf of the third person. Correspondingly, the cargo customs declaration (CCD) – which is the main document at customs -- is signed by this juridical person, not by the client. ... All this we call a real brokerage. Now imagine that we do all the same things. That means we have the same package of documents, the same CCD, but we bring all these documents to ...say... the top manager of our client firm and he signs it because he trusts us. So the CCD is sealed and signed by the client but we do all the real work [of customs clearance]”

(Director of a transportation firm)

A “white” or “grey” status for a custom broker does not necessarily explain the degree of involvement in informal mediation. Our study shows that “white” brokers use “grey” schemes as often as “grey” brokers do. The essence of informal mediating at customs is the informal relationships of trust with customs officials that provide a pivotal point in the customs clearance procedure. This is true not only for “grey brokers” or the implementation of “grey schemes,” but for any kind of customs clearance operations. To capture the informal component of customs brokers’ mediation it is necessary to consider relationships between customs brokers and customs officials. Interviews with businesspeople revealed that informal relationships of trust with customs officials are a key point in customs clearance procedure. This informal role is explicitly described by one respondent:

“Actually there is no real need for the assistance of a so-called customs broker or declarant⁵. You can easily fill in the declaration especially if you constantly convey one particular type of cargo and are not doing it for the first time. But his [broker’s] main role (why he is really needed) begins after you fill in the declaration. He is like a messenger of God on the earth. In other words, he is the person who goes to customs with your documents, and the customs would decide whether to let your cargo through or not. And, then, imagine that you come to customs and bring your documents yourself. A custom official wonders – who is this stranger? Where did he come from?” ... And it is quite a different situation if a declarant comes and says:

⁵ The term “declarant” refers to one who helps in filling out the Customs Cargo Declaration

“everything is fine, the inspection is done, we can go.” It is clear that your payment – agreed payment – is shared between them. Because if the declarant didn’t pay then he would be sent to the same circle as I was sent. And they [officials] wouldn’t take money directly from me – it would be a bribe in this case”.

(Director of firm, cargo owner)

Strangers are not allowed to breach the customs-broker relationship. Customs officials working in different departments are well acquainted with “their” brokers, who act as their “bread-winners.” The amount of informal “agreed” payments depends on the status of the customs official and the scale of the deal. Regular inspectors’ “rates” are typically around \$100-300 per deal (but for a large-scale operation the amount of payments could reach thousands of dollars, especially if top level officials were involved). The higher the level of the involved bureaucratic official, the larger the informal payment and more reliable and profitable the deal⁶.

As it follows from the quotation informal relationships between custom brokers and clients also refer to “agreed payments” that are negotiated between the customs broker and cargo owner. This is why informal mediation can be considered as a form of bribery. However, even for those involved in these informal relationships it is difficult to separate corruption (pure bribery) from various informal interactions with officials:

“OK, as for customs ... they solve the problem in another way. They do not have...how to say...these direct relationships like “bribe-decision”. Everything is rather covert there, and, they have, say, nearby customs structures that guide all operations with your cargo and solve the problems with customs officials. Is this bribe or not?”

(Director of construction firm)

The scale of informal mediation provided by “grey” customs brokers can be indirectly estimated from the following figures. According to official statistics only 30% of cargo goes through “white” customs brokers, while 70% is reported directly by cargo owners ([www. custom-house.ru](http://www.custom-house.ru)). Since using “grey schemes” implies informal participation of customs officials the scale of informal mediation at customs can be partially assessed according to the scale

⁶ It should be mentioned here that in cases that were reported by our informants the level of involved officials was not as high because of the small size of the businesses and, correspondingly, consignments of goods involved.

of “grey schemes”. According to the estimates of some experts, only 5-20% of cargo passes customs clearance through “white” schema, while the rest crosses the border using “grey” schemes of various kinds (Barsukova, 2002). The fact that there were no businessmen among our informants who did not use informal payments to customs officials can serve as additional evidence of the spread of informal mediation at customs.

The case of custom brokers demonstrates just one form of corrupt mediating. Interviews collected during the study have revealed a wide spectrum of mediating bureaucratic services provided by various kinds of firms and individuals. In the next part of the paper we will try to describe the variety of informal intermediaries using examples from interviews with businesspeople.

The Types of Informal Intermediaries

While the qualitative character of the study does not allow us to develop a comprehensive classification of informal intermediaries, we can, however, determine at least three dimensions that can be used for the analysis of this phenomenon.

1. Direct or indirect mediating

Intermediary firms that fully replace official bodies in contacts with businesspeople can be considered *direct* intermediaries. To get permission from a bureaucratic body, a businessperson appeals to an intermediary firm instead of going to the responsible bureaucratic body and from this firm he or she finally receives the desired document. The best example of this type of structure is seen in intermediaries’ dealings with licensing and certification. For our informants it is clear that in order to obtain a license or certificate it is better to avoid direct contact with licensing and certification centers which “complicate the procedure deliberately”, and rather work through an intermediary firm, which will issue the same papers on the basis of the same documents, but for a different price:

Naturally, I have never seen anybody, but everything goes to a firm. We pay the firm, and they do everything. They collect all the necessary documents, which are simply bought, because nobody has that much time to collect all this – it would take me half a year! In reality, nobody does anything, but the documents are here. They are on official paper and look nice, from institutes and training center, in which somebody attended

courses, passed the exams, accepted commission, etc...It turns out that this pyramid is specially built on an empty place, and these firms, they are created around those officials who deal with issuing licenses. There are about a dozen people involved, you know...If they bring this paper, it will be accepted [by the officials]. If not– well, it won't. It's amazing!

(Director of construction firm)

The study provides numerous examples demonstrating the same situation with a range of bureaucratic bodies -- state monopolies for gas, electricity, water, and other utilities. According to our informants, the procedure of obtaining permissions from these structures directly can take several months (if not years). However, if a businessperson uses the services of an intermediary firm the problem can be solved in a few days – though for a different price.

Indirect mediation refers to the case in which a mediating firm is not involved directly in the interaction between businessmen and officials, but caters for these relationships. Indirect mediation is often provided by organizations operating around inspection agencies. These firms are not involved directly in the inspection process; however they provide services that become a condition for passing certain inspections (or for avoiding additional inspections). The best examples here can be found in the sphere of fire protection and sanitary inspection:

“There are a lot of firms selling fire protection alarm systems with all necessary norms and rules. But we were told at the very beginning that: “you know, guys, even if you find a cheaper fire alarm system and install it following all formal requirements, it wouldn't be accepted by the fire inspectors. Because we have a monopoly in this district. Such and such firm is selling alarm systems here, and the owner of this firm is a chief policeman of the district. That's it”

(Director of a sewing shop)

In this case a shop selling fire protection alarm systems serves as an indirect intermediary for getting approval from fire inspectors. In the case of sanitary inspections, the role of intermediary is played by a clinic providing medical examination services:

“Accordingly, in the very beginning sanitary inspection conducted raids upon us, well, say – flying visits with insinuations⁷ [...] then we begin to interact according to an informal agreement – we send our employees for medical examinations to a certain clinic which the inspectors indicate to us – for us it doesn’t matter to whom we pay this money. And I do not know what kind of connections they have got there. “

(Director of a café)

2. Specially created for mediating services or combining mediating functions with the main business

Mediating services can be provided by firms *specially created* for these purposes or by the firms that *combine* mediation services with their main business. Thus, the licensing and certification intermediary firm in the above-mentioned example is specially created for mediating purposes. There is also another set of firms specialized in different services and at the same time able to fulfill informal mediating functions. Some real estate firms serve as intermediaries between businesses and the Department of State Property, distributing state-owned premises for rent at reduced prices. According the Program for the Support of the Development of Small Business in St. Petersburg, renting state-owned premises is cheaper or sometimes even free for some small and medium sized enterprises. Access to these premises is limited. But real estate companies connected to the local administration can help in finding an appropriate state-owned premise for a low rental price. The condition is that a business will make additional monthly payments to this firm in “black cash.” Not only real estate firms mediate these relationships (as seen from the following quotation).

Q: Did you have any problems with officials in opening your shop?

A: Oh, horrible! There was a law firm at the district administration that offered us very good premises. But then it turned out... Well, we said in the very beginning that everything was official and we completed a cashless transfer. Nonetheless, we were told that “You need to bring \$300 every month in cash anyway” [...]. And it was impossible to reject, because this

⁷ “Flying visits” is a direct translation from the Russian, referring to unannounced visits by inspectors with a high probability, whether justified or not, of finding violations likely to lead to a loss of certification.

firm is at the administration and we were told: We will simply not allow you to work in this district!

(Director of the shop)

The number of intermediaries that specialize exclusively in informally mediating bureaucratic extortion is not as large as the number of firms that focus on “cutting the red tape.” The peculiarity of informal mediation is that it can be performed by legal firms specializing in various kinds of services. Intermediaries often combine *overt functions* and *hidden or shadow functions* in their activities. Based on documents and official reports these firms appear as ordinary business organizations, which run “normal” businesses – consulting, selling equipment, dealing in real estate, etc. At the same time, intermediaries fulfill shadow or hidden functions by facilitating informal relations between businesses and the state. Therefore, the main problem is to separate the strictly legal functions of intermediaries from the informal ones.

3. “Top-down” or “bottom-up” initiative

The intermediary structures described above have one important feature in common – all serve the process of undisguised bureaucratic extortion. The initiative to create such firms comes “from above” or has “*top-down*” direction. Officials prefer dealing with intermediary firms because they do not have to enter a rather risky corruption market personally. The use of “independent” organizations and firms changes the appearance of the interaction, reshaping it from a corrupt deal to an official procedure. It also narrows the circle of people communicating with an official directly and creates a protective barrier from undesirable “outsiders”.

Another type of intermediaries can be seen as a result of the “*bottom-up*” process, allowing businesspeople to avoid excessively demanding formal rules and requirements. This does not mean that officials are not at all involved in the process. As with any kind of informal mediation this service becomes possible exclusively due to the “good will” of officials, their readiness to “close their eyes” to some infringements of formal norms and procedures, and their informal personal relationships with intermediaries. However, informal intermediaries of this type act “on the side of businesses” rather than “on the side of officials,” and this is what distinguishes them from intermediaries facilitating bureaucratic extortion. The aforementioned customs brokers, and specifically the “grey brokers” that fill in and submit customs declarations and communicate with customs on behalf of their clients represent one of the examples of this kind of informal intermediary.

Another example of informal mediation as a “bottom-up” process can be found in the sphere of shuttle trading. Since shuttle traders regularly break custom rules regarding the weight and the amount of goods that can be brought across the border, they always need some mediating structure or person to solve the problems that arise between them and custom officials. In the case of shuttle-traders, the role of mediation is performed by tourist firms, or, to be more precise, by tourist guides who organize the trip.

Institutionalization of Informal Mediation

It could be stated that informal mediation in relationships between businesspeople and authorities is currently going through a process of *institutionalization*. In this part of the paper we will demonstrate that the phenomenon of informal mediation has developed during the past years into a sustainable informal institution that has come to occupy a stable position in the Russian economic environment.

According to Peter Berger and Thomas Luckmann (Berger & Luckmann, 1996) the essence of institutionalization is the reduction of uncertainty in the external environment, making it more predictable for people (Berger & Luckmann, 1996: 54). We consider institutionalization of informal mediation through the processes of habituation, typification, objectivation and legitimation of interactions between businesspeople and informal intermediaries.

The emergence and formation of the institution of informal mediation is preceded by the *habituation* of informal economic practices in the Russian business environment, where infringement upon (or avoidance of) formal rules and regulations has become a generally accepted norm of economic activity. The process of “deformalization” of rules taking place in the Russian business environment (Radaev, 1998) implies the incorporation of informal rules into formal institutions, and the replacement of formal regulations with informal ones. The prevalence of informal relations in vertical interactions – between businesspeople and officials – is predetermined by the imperfection of the bureaucratic system, and by the impracticability of formal regulations. It is widely acknowledged that the legislative environment in Russia does not facilitate business development, particularly for small and medium sized business. As it follows from our study, “informal stimulation” of officials of different ranks in order to overcome bureaucratic barriers has become a routine practice in everyday economic activities.

As informal practices become habituated, the most effective of them become crystallized, with their further transformation into typical patterns of behavior.

Our study provides empirical evidence that using intermediaries for informal interactions with officials has become a regular pattern for Russian businesspeople. The following are the reasons for using the services of informal intermediaries:

a) Businesspeople prefer to deal with intermediaries because it is simpler (intermediaries know all the details and hidden dangers of this process) and faster (as it saves time and, therefore, - money).

Ok, in order to register the agreement for all these premises for rent, I went to officials...one, two...- oh, this will be the eighth visit. In June I started my visits to these officials, spent overall 16 hours. Today it is already October – five months have passed! And no result so far... It is better to do it through the agency, formerly we paid them \$1000 and they did everything in one month. ...

(Director of a trading firm)

In fact there are two ways for businesspeople to solve “bureaucratic” problems. The most direct way is to apply to the official body trying to fulfill all formal legal requirements. This method can take an extremely long time and the result is not guaranteed. Another means is more indirect (operating through intermediary structures), yet is faster and less time-consuming. As a result, one can see the two-sided strategy that businesspeople often use in their relationships with officials: if the problem is urgent and vitally important for a firm, they choose the more expensive but faster and more “reliable” indirect method. In cases of less urgency, they choose the longer method of navigating one’s own way through bureaucratic procedures.

b) Using intermediaries makes it possible to avoid emotional strain, which is usually a painful part of the interpersonal communication between businesspeople and officials, and not only in cases where it is necessary to solve the problem using informal means:

“I want to say that every official - depending on his upbringing, his intellect and I don’t know what else to a greater or lesser degree - would necessarily smear you on the table. If he is a cad, then he will be actively doing this. If he is a well-brought-up, then he will be doing this by his indifference. None of them care about you!”

(Director of a dressmaking establishment)

When a businessperson goes to an intermediary, the situation is different – it takes the shape of a formal service and businesspeople in this case feel like

customers. It can thus be stated that, by using intermediary services, businesspeople reduce the “emotional costs” of informal interactions with officials.

c) A reason of no lesser importance, the use of informal intermediaries reduces the uncertainty of the situation and increases its predictability. According to our respondents, intermediaries make the whole system of interactions between business and authorities “*more clear.*” Of course, this does not imply that the procedures of the bureaucratic body are more transparent, but rather that intermediaries are uniquely positioned to offer a better understanding of the steps that businesspeople need to undertake in order to effectively achieve their goals in interacting with state institutions.

Our study also provides empirical evidence of the *objectivation* of informal mediation. In some spheres the set of informal-mediation institutions has a sort of coercive power over individual behavior. Using the services provided by intermediaries has become, if not obligatory, then vitally necessary for businesspeople if they want to run a business without trouble. This can be seen from the number of failed attempts to avoid using intermediary services. One of the most vivid examples is shown in the case of businesspeople trying to arrange custom clearance directly through customs bodies avoiding the services of intermediaries:

The way through customs – it is just horrible! We were doing everything by ‘a white scheme’. The system works as follows – we try to do everything fairly, paying all customs duties and so on. But the customs rules and customs laws are very complicated, they can object to anything, and won’t let a commodity through. But it can be done very easily ... We tried once to go through customs procedures using a ‘grey’ scheme. And it turned out to be much easier and much cheaper. And now we are thinking: what for? Why have we suffered so much for five years?

(Director of a shop)

The above quotation explicitly demonstrates how “white” business is being converted into the grey zone under the pressure of institutionalized informal relationships in the business environment.

Institutions require *legitimation*, that is, “ways by which they can be explained and justified” (Berger & Luckmann, 1996: 61). Our informants are deeply convinced that officials specially create intermediary firms (those of the “top-down” variety) in order to get additional “informal” payments. Some of our informants are sure that people who work in these structures are in close

kinship or friendship relations with officials. In general, businesspeople perceive intermediaries as an “objective necessity” of the business environment and accept them as such. Justification of “bottom-up” informal intermediaries is based on their convenience for businesspeople. Even with the high price of mediation services, they provide businesspeople the real possibility of solving problems and economizing on other expenses.

Economic Essence of Informal Mediation

One of the main peculiarities of the institute of bureaucratic intermediaries is its dual character. On the one hand, bureaucratic intermediaries might be able to provide for legal interactions between businesspeople and bureaucratic bodies acting as “regular” business. On the other hand, they may facilitate corruption deals. However, both legal and corrupt forms of mediation share a common basis. The economic essence of the institution of intermediaries can be seen as assisting businesspeople to reduce transaction costs related to complying with formal bureaucratic rules and regulations. In the case of legal mediation, reduction of transaction costs is achieved through the functional specialization of an intermediary firm, while in the case of informal (corrupt) mediating, reduction of costs occurs through the mechanism of trust based on informal contacts with the authorities.

Transaction costs, caused by the necessity to overcome administrative barriers and requiring involvement of intermediaries, exist in any economy. This is predetermined by at least two factors:

1. Formal rules never correspond completely with economic reality; there is always a discrepancy between the economic ideology standing behind formal rules that are developed by the state, and the economic interests of certain groups of economic actors, expected to comply with formal rules. This is the role of expert consultants that seek to optimize economic behavior to fit formal requirements.
2. The character of formal rules is too intricate in practice; therefore expert knowledge is needed to interpret the formal rules and provide assistance in fitting formal requirements.

While it is certainly true that formal rules never correspond completely to business reality, in Russia the gap between the former and the latter is even more essential. It is possible to identify some peculiarities of the Russian socio-economic context that ensure a wider gap between formal rules and real practices and make the role of intermediaries different.

First, the processes of the development of formal economic institutions. common view of the process of formalization as a subsequent step towards institutionalization with the purpose of legitimating rules and practices that developed over the course of institutionalization (see North, 1997) seems to not be applicable in the case of Russia. In Russia, we can see the opposite process at work in the development and implementation of formal institutions – change does not develop organically, but is imposed “from above.” The development of new economic laws in Russia is very often primarily predetermined by the goal of reproducing western patterns and models of the market economy, and does not recognize the link between legal regulation and the real economic situation. This is aggravated by the lack of professional and expert knowledge in developing laws and regulations appropriate to the transforming economy.

Second, organizational embodiment of formal institutions is poor: lack of financial resources provided by the state for the organizational implementation of formal regulations and lack of highly qualified specialists, among other factors. This is why even “good” laws fail at the stage of implementation. The inefficiency of the organizational embodiment of formal institutions results in a situation in which the deficit of bureaucratic services paves the way for corruption and informal mediation.

The third important feature is the character of relationships between business and the state in Russia, and, in particular, the lack of effective civic mechanisms of “feedback” allowing business to affect the business environment. Generally there are two options for businesses to cope with an uncertain and generally unfavorable business environment. One, which can be labeled “civic activism”, implies self-organization of business, formation of business associations and cooperation with third sector organizations in lobbying group interests to influence state legislative policy to improve the legislative and economic environment. Another is the “informal way” of establishing informal relationships with authoritative bodies and officials in order to “solve the problems”. Business associations (BAs) are supposed to play a crucial role in “vertical” state-business relations by providing businesses with mediating assistance to lobby business interests at different official levels. However as we learned conducting anti-corruption field research in 2004-2005, very few business associations in St. Petersburg can actually serve as “vertical” intermediaries, transmitting business interests to state agencies. Neither can they serve as “representative” structures to which authorities delegate some of their regulatory and monitoring functions. Most BAs perform as horizontal networks, supporting businessmen in their everyday business activities (see Pachenkov, Olimpieva, 2007; Olimpieva, Pachenkov, 2008). The domination of informal rules and the weakness of civil society institutions have led to a

situation in which businessmen avoid resorting to civic mediators – that is, organizations of civil society in the business sphere, and consider ‘informal’ ways of solving problems as more effective and more practical than ‘civic’ ways.

The informal character of the economic environment is another factor that accounts for the growth of informal intermediaries. The practice of concealment of profits and economic operations provides businesspeople with “black cash” resources, which in turn facilitates informal interactions with intermediaries.

Informal Intermediaries: a New Stage in the Evolution of Corruption?

It is almost impossible to estimate the scale of the informal intermediaries market in Russia. The problem of the dual character of bureaucratic mediating services is the main obstacle for its quantitative measurement. It is also almost impossible to separate legal and informal (corrupt) functions, which intermediary firms often combine in their activities. The qualitative character of our study does not allow an assessment of the scale of the emerging market of informal mediation. The focus on routine corruption in small and medium business also limits our ability to generalize the research findings. The types of informal intermediaries revealed in small business do not necessarily exist in big business, where informal relations with authorities and informal mediation could take different shape. However, we can assume that informal mediation can be considered the next stage in the evolution of corruption in Russia.

The growing scale of informal mediating in Russia can be assessed indirectly through the outcomes of the study of the intermediary market conducted by the National Institute of the System Research of the Problems of Entrepreneurship (Migin et al, 2005). The study considers *legal* intermediary firms formally assisting businesspeople in their interactions with bureaucratic structures in firm registration, licensing and certification, registration of land and other bureaucratic procedures. The study has revealed a considerable growth in the market of intermediary bureaucratic services in recent years. This is manifested in the increasing amount of intermediary firms operating in the market, an increase in employment in the sector of mediating services and in high profitability of this sector (Migin et al, 2005:190). As emphasized in the research such an excessive market of intermediaries could emerge only around particularly complicated and sophisticated bureaucratic procedures, through which navigating without assistance might lead to considerable costs for businessmen (ibid. : 14). The exorbitant number of mediating structures in Russia can be considered therefore as evidence of the excessively high

bureaucratic barriers and consequently, the high potential for corruption of the system. From this point of view, the very existence of the growing and flourishing market of intermediaries can be considered as evidence of the similar growth and flourishing of informal mediating.

It follows from studies of intermediaries in the developing countries, that the same intermediary structures that operate legally in advanced capitalist economies serve for corrupt mediating in the developing countries (see, e.g., Andvig et al., 2000; Oldenburg, 1987). Some economic institutions in western economies begin to mutate after being transferred to the socio-economic environment of transforming societies and they accumulate informal functions not intrinsic to their counterparts in advanced capitalist systems. The institution of informal intermediaries in Russia provides a similar example of the “mutation.”

The emergence and dissemination of informal intermediaries in Russian business environment shows that corruption is a flexible, and “alive” phenomenon which is constantly evolving with the changes in the legislative, economic and social context. The evolution of corruption in Russia can be traced from the first wave of entrepreneurship at the beginning of 1990’s. During the period of the initiation of economic reforms and the formation of a new business environment, corruption in business-state relationships existed in the form of unconcealed bribery. In 1998, Russian researchers pointed out that classical bribery “in the envelopes” had already become a thing of the past, having been replaced by more respectable institute of “friendships and mutual support” (Radaev, 1998). The role of informal contacts with officials was (and still is) even more important with the existence of the informal institute of “selective enforcement of the formal law” (Paneyakh, 2008). In this context, the institute of informal mediating has emerged as the next step in the development of informal relationships with bureaucracy. Alongside the evolution of corruption we can trace the development of the institution of intermediaries: from rudimentary cases to organized routines, from pure informal underground enterprises to legalized firms combining formal and informal functions. Although the majority of our informants were convinced that mediating structures are specially created around officials, we would argue that this phenomenon has already developed into a more organized and impersonal institution.

The institution of informal mediating has become an essential factor influencing further development of the system of state-business relations in Russia. The informal bureaucratic intermediaries described in the paper reflect the particularities of corruption in small and medium business that can be described as ‘business capture’ rather than ‘state capture’ (which is more

typical for big business). The 'routine' or 'everyday' corruption that prevails in small business is aimed not at improving the situation, but at preventing it from becoming worse. For small and medium businesses, informal intermediaries appear either as an instrument for bureaucratic extortion or as a form of latent resistance by business to the impracticability of formal rules and regulations. That is why they often serve not to adjust economic practices to formal rules, as they do in western economies, but rather to create a false impression of a link between the former and the latter. The principal resource they use for this purpose is informal access to various bureaucratic bodies.

As already mentioned in the paper intermediary firms often combine hidden and overt functions. This ratio between informal and legal functions may vary according to many reasons. One the most important amongst them is the character of the legislation environment in terms of its overregulation and practicability of formal rules. It is likely that with the institutionalization of informal (corrupt) mediation any further toughening of the legislative environment would not lead to the desired regulation of bureaucratic market but to even more corrupt mediating.

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