BLACKLISTING IN RUSSIAN PUBLIC PROCUREMENT: HOW IT DOESN'T WORK[1]

Elena Podkolzina[2], *Tatiana Voytova*[3]

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Abstract

The main goal of the reform of public procurement in Russia, initiated in 2005, was to prevent corrupt deals between suppliers and procurers. That is why the public procurement law favors formal mechanisms to govern most of the stages of procurement: the procurer is not allowed to take into account the reputation of the supplier when he announces call for bids and selects the supplier, and he is prescribed to use the legal system (courts) if he is not satisfied with the contract performance. As the efficiency of formal institutions is not very high, these mechanisms are complemented with a «formalized informal instrument» - blacklisting opportunistic suppliers, which is believed to substitute for reputation mechanisms to support formal mechanisms when they are weak. In the paper we show how and why the institutional environment in Russia makes the blacklisting of opportunistic suppliers irrelevant. We explore how the percentage of contract breaches out of the total number of signed contracts depends on corruption and transparency measures for Russian regions. We also argue that such factors as measurement costs, verification costs, length of contract and lawsuit amount influence the probability to win the legal action on breached contract.

Key words: public procurement, blacklist, corruption, measurement costs, courts decisions
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[1] The study was implemented in the framework of the Basic Research Program of the Higher School of Economics in 2011.
[2] Senior Researcher, International Laboratory for Institutional Analysis of Economic Reforms, Center for Institutional Studies, NRU HSE, e-mail: pea.work@gmail.com
[3] Research Fellow, International Laboratory for Institutional Analysis of Economic Reforms, Center for Institutional Studies, NRU HSE, e-mail: ti.voytova@gmail.com

Introduction

In public procurement, governments struggle to choose a fair supplier and insure contractual hazards. Information asymmetry is widespread in contractual relations. Usually, the supplier knows better whether he is going to deliver high quality goods on time or take the money and disappear. One powerful tool to solve such situations is reputation. One of the first papers about the role of reputation in economic transactions is by Klein and Leffler (1981). They show under which conditions the market mechanism could be used as an enforcement mechanism in infinitely repeated transactions. The basic idea of the reputation mechanism is that the value of potential future transactions forces parties not to deviate their present obligations. The reputation mechanism is one of the cheapest tools to enforce contractual obligations.

Greif (1993, 1994) treats reputation as a history of interactions in his famous works about Maghribis and Genoese traders. Reputation works only if all members of community are willing to punish deviators. Each member expects that a trader wouldn't make a deal with an unfair agent: this increases the cost of business for the unfair agent, which stimulates them not to deviate. The maghribis based their behavior on collectivist strategy and widely used histories of interactions as an informal reputational mechanism. Blacklisting is a formalized informal institution. It is an analogue of interaction history in the medieval trade. The only difference is that traders were interested by themselves in history formation, while public buyers are forced to put information on the blacklist by law. It is common practice to make blacklists open to the public. This allows customers to share quickly information about unfair firms. Nevertheless, there are some open questions about blacklisting: who can enter the list and what are the reasons? Blacklisting is an official mechanism and it could highly influence firm's performance. So on one hand, the state is interested in easy processes to put unfair firms onto the list, but on the other hand it should provide safeguards to firms. It is worth to confirm that there was opportunistic behavior. So to confirm firm's guilt public procurer would need decision of the court. That's why blacklisting is highly depend on court system and its effectiveness. According to Williams, "the effectiveness of blacklisting is also limited in many ways, depending on how much effort and expense a country is willing to put into the blacklisting process and whether the blacklisting depends on a conviction or not". (Sope Williams, 2010, p.148)

What is going on in Russia? Russian public procurement law (FL-94) relies on the state regulation and the judicial system. In order to evaluate the effectiveness of these mechanisms, we used indicator calculated by the World Bank. The indices are constructed so that when index values are higher, the corresponding institutions work better in the considered country. The maximum value of each indicator is 100. As we have seen (see Appendix 1, Figure 1.1) between 1996 and 2009 the indicators of the Russian institutional environment do not show satisfactory values. Moreover, Russia has failed to rise above 50 points in any of the indicators. Particular attention should be paid to the value of the indicator "Rule of Law." The system of federal public procurement requires extensive use of the legislative sphere, which, according to international observers, is poorly developed in Russia.

Unfortunately, we have to state that in Russia, according to World Bank data, there are serious problems in the judiciary, and state regulation. This means that many of the mechanisms offered by the FL-94 for the suppliers and customers do not always work well in practice, and their use may be associated with a number of problems. The reluctance of participants of the public procurement system to bring a suit to court is evidence of the inefficiency of the judicial system is, even when their rights have been violated. Perhaps this is one of the reasons that the majority of breached contracts are terminated with a voluntary agreement between the parties (see Table 2).

The existing Russian procurement law (94 FL) was introduced in 2005. According to it, public buyers may choose among open tenders, open auctions, sealed bid auctions (price quotations), or negotiations. The choice of public procurement procedure depends primarily on the maximum price of the procurement. The negotiations can be chosen only for small purchases (less than one hundred thousand of rubles), and only once in three months for similar purchases, so as not to create

incentives to split large procurements into smaller contracts. Though the recent trend indicates a growing number of contracts awarded through negotiations, it is not regulated by 94FL. The rules for the first three procedures are set in 94 FL, including the requirements for publishing information on the regional web sites. The requirements for open tenders and open auctions are quite similar, but the rules for sealed bid auctions are less strict. The crucial point is the priority of open auctions. The government recommends all authorities to use an open auction to purchase goods and services. Current auction procedures do not allow the procurer to take into account characteristics of potential suppliers: the choice should be based only on price.

The only formal reputational mechanism that is provided to the participants of public procurement is the blacklist. If a firm is listed there, customers have the right to exclude her from bidding. Participants of the procurement procedures have two opportunities to use a third party to enforce fulfillment of commitments. Suppliers could complaint to the Federal Antimonopoly Agency (FAS) if the procedure was organized with violations. Even if the FAS satisfies the complaint violator is not placed on the blacklist. The buyer could go to court if contract obligations are not fulfilled. A supplier is only placed on the blacklist if the court decision finds a contract was breached.

How blacklist works by law in Russia. The principles of the registry of unscrupulous suppliers are enshrined in the "Statute of maintenance the register of unscrupulous suppliers and the requirements for engineering, software, linguistic, legal and organizational means to ensure maintenance of a register of unscrupulous suppliers" (approved by RF Government Decree of 15 May 2007 N 292). We will call it the blacklist. According to this Statute, the blacklist is managed by the Federal Antimonopoly Service (FAS), based on data submitted by state customers. Customers should report to the FAS about inappropriate implementation of obligations by suppliers. Register is maintained in electronic form (http://rnp.fas.gov.ru/) and the FAS gives free and open access to everyone.

Who is placed on the blacklist? There are two reasons why the supplier enters the blacklist: the supplier has refused to sign the contract for bidding won by them, or the supplier has performed the contract with "material breach". "The concept of definition "material breach" is set forth in paragraph 2 clause 2 article 450 of the Civil Code of Russian Federation: A violation of a contract by one party, which leads to the other party to such damage, it is largely deprived of what was entitled to expect at the conclusion of the agreement. "(Definition taken from legal information and educational portal "Everything about Law" http://www.allpravo.ru/library/doc2264p0/instrum4904/item4911.html)

In order to add an unfair supplier to the blacklist, a customer must provide the FAS a package of documents containing information about the supplier and confirmation that the violation of the law took place. It is time-consuming for the customer to collect all documents. There are also few incentives for customers to provide information on unscrupulous suppliers. The customer in public procurement system does not receive residual rights, so it would be worthwhile to have an enforcement system.

The supplier may enters the black list many times if additional contract are breached, he is located on the list for 2 years from the date of inclusion.

However, the length of the update period allows unscrupulous firms to get high rents from the misconduct. The Statute notes, that information must be submitted no later than 3 days from the date of termination of the contract, and FAS should include this information into the list within 3 days. Accordingly, a maximum of 7 days must elapse from the date of termination.

Here we sum up some facts about the blacklist:

1) Some amount of breached contracts that haven't been included in the list. This number could be quite large due to low popularity of judicial system as a resolution mechanism and due to the condition of material breach of contract.

2) The average period of inclusion unfair suppliers into the list is higher than the period recommended by the law. By the law it should took less than 7 days to include unfair supplier into the list, but in practice average period is 84 days. This allows unscrupulous firms to cheat several customers.

3) The list is maintained inaccurately and contains errors that could mislead its users.

4) The majority of entries in the list are situations when the supplier refused to sign a contract, and among the breached contracts the majority of entries are situations when customer cannot avoid going to court (the contract is concluded, but the goods are not delivered or are only supplied in part).

5) The information presented in various official sources (blacklist from FAS, the general statistical information according to the Federal Statistics Service, the regional government procurement sites) does not match.

First, in this paper we explain how this institution works in different regions. Are there any differences in the demand for this institution? How we could explain this. We suppose that usage of blacklist should be correlated with the transparency of information in the region. In the highly transparent regional procurement system the demand for blacklist will be higher. Transparency leads to increase in number of potential suppliers, raises competition. Hence, the number of potential "bad" supplies could rise, consequently, this increase the probability to breach a contract. We speak later about details.

Second, in this paper we deal with inner problems of this institution. We look at the factors which determine the probability to win a case in court with minimal costs. The courts could base their decisions only on formal contracts. With a more detailed contract it is easier to prove your reasons to file for breach. The ability to write down a complete contract depends on the type of good. There are no complete contracts in the real world, but we can identify three types of good following Nelson (1970), Darby and Karny (1973) associated with three levels of difficulty to specify all details in the contract. They are search, experience and credence goods (see more detailed description in section Empirical results). The idea was that goods differ in ability to identify the quality. This is correlated with ability to specify quality in the contract. It is easy to specify details for search good and very hard for credence goods. Serious problems usually occur with credence goods and with the questions of quality. For goods and services with high measurement costs of quality demand on special resolution mechanisms is higher compare with simple standardized goods. According to Russian procurement system, blacklisting is supposed to be such a mechanism. But we showe that for the credence goods, the use of blacklist based on court decisions is too expensive because it is difficult to win a case associated with quality problems when the contract is incomplete.

Transparency and blacklisting

Hypothesis 1: We argue that corruption, transparency and gross regional product influence the share of breached contracts. Increase in corruption and transparency has positive impact on the percentage of breached contracts, and the size of the regional economy has negative impact.

Data set

We now turn to the characteristics of the database. The data was downloaded from the site (http://rnp.fas.gov.ru/) in July 15, 2011, respectively, it contains the data since July 15, 2009. But we use the data of 2010 year to look on share of breached contracts because the transparency index was measured in 2010.

Also we use available regional statistical information on public procurement from The Federal State Statistical Service (www.gks.ru): numbers of the procurement procedures conducted in one year and the amount of gross regional product. This source is built on self-reporting basis.

We took corruption perception index from the report of the Ministry for Economic Development of Russian Federation "Situation with everyday corruption in the Russian Federation" http://www.economy.gov.ru/minec/activity/sections/anticorruptpolicy/doc20110614_027. It measured corruption perception in Russian region in 2010 year.

What do we mean when say transparent? The amount and accessibility of information in Russian public procurement system is differing among the regions. Though the FL №94 introduced some

measures to increase the transparency of information on public procurement the structure of the designated web sites, functions available for users, such as search options, the standard forms for the documents and protocols are not regulated by the law and are decided at the regional level. The law lists only the names of documents (calls for bids, the auction protocols, etc) that must be uploaded to the web site, and the basic information they must contain (starting price of the auction, date of the procedure etc.). Balsevich et al. (2011) estimated the index of transparency of information on public procurement in the end of 2010 on the basis of the data on the structure of a regional site of public procurement, information, and functions that are available. Their check list includes four groups of parameters that are important from the information transparency perspective: (1) current procurements, (2) completed procurements, (3) search functions, and (4) additional features. They build four indicators that summarize the availability of information and functions for each group of parameters. The resulting index of the information transparency is a weighted sum of the four main indicators described above. Each of the first two indicators (current procurements and completed procurements) give 35% of the resulting index, the indicator of search functions gives 25%, while additional features give 5%. The weights assigned to each indicator reflect our estimation of importance of the information of a certain type for the functioning of the public procurement system. The low weight assigned to the additional features indicator also reflects the fact that the variation in this indicator is rather low (see below). The maximum possible value of resulting index is 100.

To address the question of usability of the information available for the formation of strategic behavior of the potential bidders in the region it is constructed an alternative index of information transparency which accounts for the relative quality of search related to the amount of information available. The second index is represented by the sum of the first two indicators multiplied by the relative measure of search quality.

How is transparency connected with blacklist? A procurer might also appeal to the transparent information on his or her procurement procedures while bringing a case of a breached contract to court. The level of information transparency might affect the number of cases that had to be brought to court by the procurer in two ways. A procurer who runs a nontransparent system might be more corrupt and hence have “better knowledge” of his or her suppliers and less incentives to bring a case to court. A more transparent system might also attract more opportunistic suppliers to a given procedure increasing the chance of breach. On the other hand a transparent system combined with a well functioning courts system might create the incentives to fulfill the contract obligations and keep a “good reputation” for the suppliers. The results of the OLS regressions considering the effect of information transparency on the percentage of contracts canceled by court in a given year (information provided by FAS, http://www.fas.gov.ru, and by Russian Bureau of Statistics, http://www.gks.ru) are presented in Table 1. The availability of well structured information on the calls for bids has a significant positive impact on this measure, implying that an “excessive” transparency might attract opportunistic bidders to the public procurement procedures. The availability of unstructured information, on the other hand, has a negative impact on the percentage of breached contracts.

Table 1. Transparency and percentage of contracts canceled by court

VARIABLES	(1) Canceled contracts	(2) Canceled contracts	(3) Canceled contracts	(4) Canceled contracts	(5) Canceled contracts	(6) Canceled contracts
LGRP	-0.00352**	-0.00389***	-0.00380***	-0.00391***	-0.00363**	-0.00393***
	(0.00141)	(0.00139)	(0.00140)	(0.00139)	(0.00141)	(0.00138)
Corruption 2010	0.0152*	0.0174**	0.0167**	0.0180**	0.0152*	0.0170**
	(0.00828)	(0.00813)	(0.00820)	(0.00819)	(0.00818)	(0.00803)
Court appeals rate	-0.00130	-0.00116	-0.00118	-0.00121	-0.00119	-0.00106
	(0.00102)	(0.00100)	(0.00101)	(0.000998)	(0.00103)	(0.00101)
Index1	0.000178					
	(0.000136)					
Search		0.00151**				
		(0.000711)				
Index2			0.000139*			
			(7.61e-05)			
ExAnte information * Search				0.000326**		
				(0.000151)		
ExPost information * Search					0.000214	
					(0.000148)	
Index1 - Index2						-0.000333**
						(0.000152)
Constant	0.0377**	0.0445***	0.0456***	0.0453***	0.0456***	0.0595***
	(0.0169)	(0.0159)	(0.0161)	(0.0159)	(0.0163)	(0.0174)
Observations	67	67	67	67	67	67
R-squared	0.164	0.198	0.184	0.200	0.168	0.202

Standard errors in parentheses
*** p<0.01, ** p<0.05, * p<0.1

Courts decisions and contract characteristics: empirical evidence

Hypothesis 2: The probability to win the lawsuit with minimum costs depends on the value of measurement costs and on the reason of contract breach. Low measurement costs and clear reason raise the probability to win the lawsuit.

Data set

We consider 280 judicial decisions on cancelled contracts that were entered the Blacklist from 1st of April to 15th of July, 2011. We use information related to public procurement procedures and features of contract that are reserve price, contract dates and term of a contract.

We collect all judicial decisions related to the cancelled contracts in order to rise additional information on the level of budget of the contract, the reasons of contracts cancellation, the pecuniary claims of plaintiffs, the results of cases considerations and about the initiator of judicial recourse.

Below we describe the factors and the indicators which have been used in our analysis. The list of variables is given in the appendix (see Table 2).

The probability to win a case in court. It is a dependent variable. It is equal to 1 if the claim was satisfied at first instance and 0 if the claim was partially satisfied or rejected. In general judicial decisions could be the following: the claim could be satisfied, partially satisfied or rejected. If the claim was partially satisfied or rejected the initiator had the opportunity to appeal from a judgment. Lawsuit is a costly process. Parties should pay lawyers; firms could lose their reputation and so on. When lawsuit moves to another instance costs rise sufficiently. All parties face minimal cost if they agree on court's decision at first instance.

The measurement costs. We divide all contract subjects into three groups following the goods classification by Darby, Karny and Nelson (Nelson (1970), Darby and Karny (1973)). The first group includes goods the quality of which can be checked on the view of the good or in the process of performing works and rendering of services. This group is named search goods. The second group included goods the quality of which can be checked during the application of the good or right after completion of works and rendering of service. This group is named experience goods. And the last group included goods, works and services the quality of which can't be checked or it is too difficult to do this. This group is named credence goods. Therefore if the contract subject is referred to the search group it was equal 1, if it is referred to the experience group it was equal 2 and for credence goods the indicator was equal 3. When this variable equals 3 the measurement costs are maximal.

The reason to sue. We use the classification of reasons on the ground of their evidence that is how easy the claim can be supported and disputed. We divide all reasons into five groups according to evidence. These are claims of the quality, the out of time deliveries, a mismatch to documents standards, the delivery size and the absence of the delivery. The most evident reason is absence of the delivery. Claims of the delivery size are less evident because an additional inspection is needed to check how considerable the breach of the contract was. It is usual for Russian procurement practice when in the time of the delivery procurers discover that it is not exactly the same good he expected to get. Mismatch to documents standards is even less evident because it is not only needed the check but sometimes it is difficult to prove. Next step is out of time deliveries when the purchased good delivered after the expected date. It should be proved that out of time delivery is significant reason to cancel the contract. Claims of the quality are the least evident because in most cases there is no objective test of quality and if the procurer deals with an experimental or a credible good it could be too difficult to estimate the quality and to proof that it doesn't meet the specified quality. This reason to sue is hardly could be proved in court. When the indicator equals 1 the reason to sue is hardly could be proved in court.

The length of the contract is a range in days between the day when contract was signed and the day of its expiration according to the contract. The minimal length is 0 days and the maximal is 950 days.

The amount of pecuniary claims. The amount of pecuniary claims was used as a control variable. To calculate it we separated all possible amounts of pecuniary claims in five intervals. The indicator

took on a value from 0 for the lowest sums to 5 to the highest. The minimal value of the amount is 0 rub and the maximal is 302878493,6 rub. The standard deviation is 23403084,54.

The reserve price is numeral variable too. Value distribution of prices was separated in four intervals. As the threshold values we used the median, the first quartile and the third quartile. The indicator took on a value from 1 to 4 subject to the interval that included the respective value of price. The minimal value of the price is 3081.55 rub and the maximal is 700000070 rub. The standard deviation is 58115065,26.

The type of procurement procedure. Each type of procedures relates to the number from 1 to 5: (1) quoted price request, (2) auction, (3) e-auction, (4) tenders, (5) single procurer. Transaction costs theory tells us that there is a link between ex ante and ex post costs. If procurer decided not to spent much efforts ex ante to choose a right supplier than he faces troubles ex post with contract fulfillment. This factor allows us to fix ex ante unefficiency of one of the procedures (for example, one type of the procedures frequently doesn't allow the procurer to choose better supplier, and hence he faces problems during the contract).

The budget level. The procurements could be municipal, regional or federal. To encode this indicator we assigned a value from 1 to 3 to each type respectively. All types of procurement are regulated by FL-94, but there are different incentives in state agencies of different levels. Usually, federal agencies face more strict rules and greater control.

The initiator of judicial recourse. This indicator is equal to 0 if the initiator was a procurer and 1 if the initiator was supplier.

The summary of the descriptive statistics is present in the Table 2.

Table 2. Descriptive statistics

Variable	Obs	Mean	Std. Dev.	Min	Max
Win the case	280	0,5642857	0,496738	0	1
SEC	280	2,339286	0,6413691	1	3
Experience goods	280	0,475	0,5002687	0	1
Credence goods	280	0,4321429	0,496261	0	1
The reason to sue	280	3,085714	1,132674	1	5
Good/work/service	280	1,617857	0,6776269	1	3
The length of contract	280	174,1	184,9605	0	1089
The amount of pecuniary claims	280	1,610714	1,847761	0	5
Auction	280	0,5535714	0,4980119	0	1
Initiator of judicial recourse	280	0,9714286	0,1668969	0	1
The presence of the defendant in court	280	0,2857143	0,4525628	0	1
Transparency index	261	8060,718	16290,43	0	41058
Court appeal rate	261	469,1379	107,9832	194	879
The size of the regional budget	261	2,41E+08	3,45E+08	1,32E+07	9,32E+08
Number of bids	261	119016,1	119968	6610	352566
Share of changed contracts	241	0,026833	0,0319473	0,0011183	0,256169
Careful administrators	261	0,9837137	0,0360099	0,8035714	1

To check the hypothesis we tested the statistically significant relationship between the probability to win the lawsuit at first instance and two indicators that are the type of procurement according to the quality measurement costs and the type of cancellation reasons. Thus we run Probit-regressions with the probability to win the lawsuit at first instance as a dependent variable and another two indicators

mentioned above as well as control variables being the regressors. The results are presented in tables 3 and 4.

Table 3. Quality measurement costs, cancellation reasons and probability of case satisfied

VARIABLES	(1) win	(2) win	(3) win	(4) win	(5) win
sec	**-0.199***** (0.0568)				
exp		**0.268***** (0.0636)			
cred			**-0.315***** (0.0681)		
evidence				**0.147***** (0.0307)	
gws					**0.0992*** (0.0518)
duration	**0.000539***** (0.000203)	**0.000560***** (0.000204)	**0.000639***** (0.000213)	**0.000496**** (0.000197)	0.000225 (0.000193)
claims	**-0.0791***** (0.0179)	**-0.0816***** (0.0180)	**-0.0786***** (0.0181)	**-0.105***** (0.0185)	**-0.0893***** (0.0179)
auctions	-0.0778 (0.0700)	-0.109 (0.0689)	-0.0804 (0.0703)	-0.0751 (0.0702)	-0.108 (0.0679)
budget level	**0.121*** (0.0660)	**0.141**** (0.0648)	0.108 (0.0663)	**0.109*** (0.0656)	**0.178***** (0.0632)
initiator	0.0795 (0.199)	0.122 (0.204)	0.105 (0.205)	0.0451 (0.186)	0.0669 (0.190)
presence	-0.0918 (0.0726)	-0.118 (0.0728)	-0.105 (0.0732)	-0.0672 (0.0729)	-0.113 (0.0718)
Observations	280	280	280	280	280

Standard errors in parentheses
*** p<0.01, ** p<0.05, * p<0.1

Table 4. Quality measurement costs, cancellation reasons and probability of case satisfied with fixed regional effects

VARIABLES	(1) win	(2) win	(3) win	(4) win	(5) win
sec	**-0.161** (0.0700)				
exp		**0.225** (0.0789)			
cred			**-0.254** (0.0843)		
evidence				**0.0953** (0.0376)	
gws					0.0397 (0.0647)
duration	**0.000577** (0.000255)	**0.000637** (0.000260)	**0.000658** (0.000264)	**0.000544** (0.000249)	**0.000428** (0.000247)
claims	**-0.125** (0.0223)	**-0.126** (0.0223)	**-0.123** (0.0224)	**-0.139** (0.0219)	**-0.136** (0.0221)
auction	0.0495 (0.0861)	0.0321 (0.0856)	0.0482 (0.0864)	0.0332 (0.0850)	0.0282 (0.0843)
ownership	0.0785 (0.0936)	0.106 (0.0926)	0.0803 (0.0937)	0.0614 (0.0945)	0.114 (0.0911)
initiator	0.280 (0.233)	0.327 (0.228)	0.313 (0.229)	0.242 (0.227)	0.256 (0.234)
presence	**-0.173** (0.0907)	**-0.216** (0.0905)	**-0.187** (0.0909)	**-0.153** (0.0909)	**-0.201** (0.0890)
index	**-1.54e-05** (2.88e-06)	**-1.50e-05** (2.89e-06)	**-1.49e-05** (2.91e-06)	**-1.39e-05** (2.96e-06)	**-1.60e-05** (2.83e-06)
courtrate	1.05e-05 (0.000384)	8.71e-05 (0.000388)	7.96e-05 (0.000388)	-0.000175 (0.000387)	-9.45e-05 (0.000382)
budget	**-1.57e-09** (7.56e-10)	**-1.60e-09** (7.55e-10)	**-1.49e-09** (7.62e-10)	**-1.89e-09** (7.41e-10)	**-1.82e-09** (7.34e-10)
bids	**4.75e-06** (2.18e-06)	**4.68e-06** (2.18e-06)	**4.47e-06** (2.20e-06)	**5.65e-06** (2.14e-06)	**5.37e-06** (2.12e-06)
changesrate	-1.768 (1.319)	-1.116 (1.334)	-1.627 (1.326)	-1.179 (1.296)	-1.231 (1.301)
carefuladm	**-2.875** (1.525)	**-2.747** (1.542)	**-2.713** (1.545)	-2.100 (1.519)	**-2.990** (1.534)
Observations	241	241	241	241	241

Standard errors in parentheses
*** p<0.01, ** p<0.05, * p<0.1

We concluded that the more measurement costs the less probability of the case satisfied with minimal costs. If it is rather difficult to measure the quality of the good the measurement costs can exceed the benefits after contract cancellation. Much information is needed not only to check the quality but also to prove in court that quality is low. For example some suppliers had to involve the third party for estimation the result of the performed works. Indeed there were some types of goods

when the quality couldn't be checked at all that there were no objective parameters of the quality. So the contract is characterized as incomplete. This idea was described by Posner (1986), Tirole (1999) and Battigalli and Maggi (2002). They consider that parties sometimes don't write some details in the contract because the costs of writing them can exceed the benefits of being writing for example because of a low probability of unfavorable outcome.

This relationship is connected with the influence of the cancellation reason on the probability the probability to win the lawsuit at first instance. By results of the regression analysis the more evident the reason of cancellation the higher the probability to win the lawsuit. It is easier to win the case if the cancellation reason is not connected with the quality of the good or pace of work performance because it is not necessary to prove them and it is too little grounds to dispute such claims. But if the supplier has a claims of characteristics they needed considerable more efforts, information and time and consequently the means to prove it.

Besides the relationships that we aimed to check we obtained two more statistically significant relationships. The first is the more the amount of pecuniary claims the less the probability of the case satisfied. This result was unexpected because there were not subjective pecuniary claims like reparation of moral damage that can be considerably overestimated. All pecuniary claims that are penalty, debt or interests on debt were calculated with reference to legislation so they can influence the probability of case satisfaction only if the legal system is not sufficiently effective. In addition the information about characteristics and terms of contract that related to it can be unobservable or not verifiable by the third party. So the contract is characterized as incomplete and it is impossible to prove the violation of terms in the court. The same idea was described by Shavell (1984) and Schwartz (1992). The possible explanation could be as follows. If defendant estimates the probability to change court's decision at the second instance as high enough, then he definitely appeal from judgment. This argument also demonstrates some inefficiency of judicial system. Judicial system should provide incentives for contract parties to fulfill all their obligations in time when contract is signed. it is hard to provide such incentives if parties suppose that the decision could be different in different courts.

The second relationship is the more the length of the contract the more the probability of the case satisfied. We explained it by the fact that the contract breach is found in the early stages of the contract performance when the claims are not so considerable yet. As a rule if the contract is violated unfairly it becomes clear in the early stage.

There was the reserve price in the preliminary specification of the model. We excluded this indicator from the regression because it was significantly correlated with "Pecuniary claims" and "Length of contract" but not correlated with the dependant variable.

Conclusion

The main point of this paper is to analyze how the blacklisting as an institution functions in Russia. We look on factors that influence on the demand on this institution in different Russian regions and analyze the factors that influence the ability to use this institution. We point out and show two relations between outlined factors. First, we argue that corruption, transparency and gross regional product influence the share of breached contracts. Corruption and transparency have positive impact on the share, and the size of the regional economy has negative impact. Second, we show that the probability to win the lawsuit with minimum costs depends on the value of measurement costs and on the reason of contract breach. The lower are measurement costs and the clearly is the reason the higher is probability to win. Additionally we find out that there is an influence of length of contract on probability to win with minimal costs. Our data shows that the probability to win is higher in longer contracts. One of the possible explanations, that the buyer goes to court in the first stage of contract, and it is easier to show that nothing has been done and to cancel the contract in court.

One more interesting outcome is the link between probability to win and the expected amount of financial compensation asked by the plaintiff. The more he wants the lower is probability to win with minimal costs. One of the possible explanations the more plaintiff wants the higher is the probability that defendant will disagree with court's decision. This brings us to the question about efficiency of court system in Russia.

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Appendix

Picture 1. Six indicators of the quality of the institutional environment in Russia

The picture is made based on the site of the World Bank (http://www.worldbank.org/wbi/governance/)

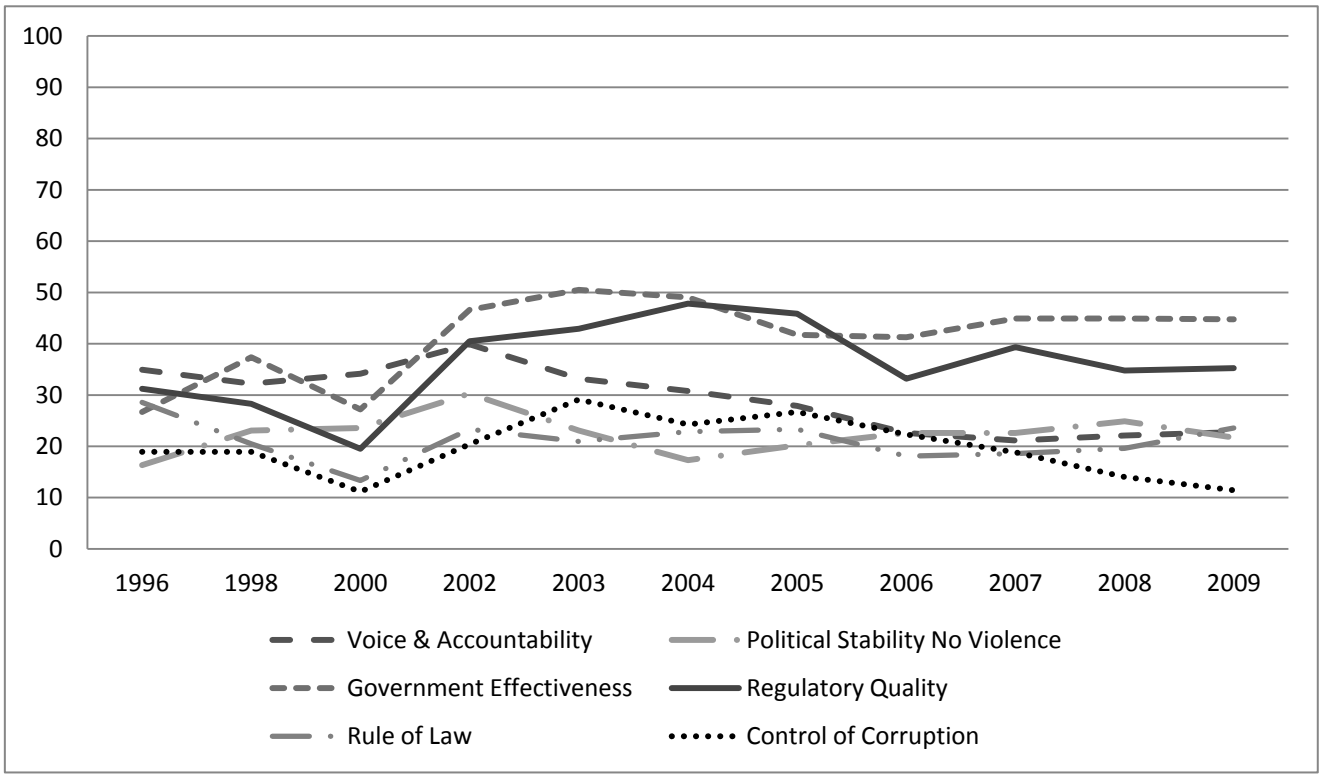

Table 1. Statistics on tenders and problem situations

	January – December 2008	January – December 2009	January – December 2010	January – June 2011
Number of all tenders	9338807	10832241	11717996	5110787
Number of signed contracts	9320410	10851866	11684517	5086651
Number of additional agreements to signed contracts		97346	102163	20419
Number of canceled contracts, including:	11793	25963	29880	9976
Mutual Agreement	11644	25741	29425	9735
Court decision	149	222	455	241
Number of invalid tenders, including:	1164	1611	1291	722
Court decision	125	72	-	-
Decision of the control authority	1039	1539	-	-

The table is made based on the information from the site of the Federal Statistics Agency (www.gks.ru/metod/torg.html).

Table 2. Description of variables

Variable	Label	Description
Win the case	win	**1** - if the procurer wins the case at first instance, **0** - if the procurer wins the case at further instances or part of the claims is not satisfied
SEC	sec	If the contract subject refers to **1** – search goods, **2** – experience goods, **3** – credence good
Experience goods	exp	**1** - if the contract subject refers to experience goods, **0** - to other types of goods
Credence goods	cred	**1** - if the contract subject refers to credence good, **0** – to other types of goods
The reason to sue	evidence	**4** - if the reason of judgment is absence of supply, **3** - if the reason is not full supply or failure to meet a date of supply, **2** - if the reason is the contradiction of supply with the requirements specification, **1** - if the reason is bad quality of supply
Good/work/service	gws	**1** - if the supply is a good, **2** - if the supply is a work, **3** - if the supply is a service
The length of contract	duration	Duration of contract (number of days)
The amount of pecuniary claims	claims	**0** – if the claim is in interval from 0 to 5000 rub. **1** – from 5000 to 50000 rub. **2** – from 50000 to 100000 rub. **3** – from 100000 to 500000 rub. **4** – from 500000 to 1000000 rub. **5** – over 1000000 rub.
Auction	auction	**1** - if the procurement procedure is an auction, **0** - if other
Initiator of judicial recourse	initiator	**1** - if the initiator of the case is procurer, **0** - if supplier
The budget level	budget level	1 – municipal procurements, 2 – regional procurements, 3 – federal procurements.
The presence of the defendant in court	presence	**1** - if the defendant is present in the court, **0** - if the defendent is absent in the court
Transparency index	index	An indicator reflects the transparency of public procurement system in the region on basis of the availability of information from web sites (http://www.hse.ru/sci/publications/36818432.html)
Court appeal rate	courtrate	the rate of appeals returned to the court by inter-regional authorities. High index means law position of the court in the rating. (The index is constructed by the portal Pravo.ru)
The size of the regional budget	budget	The size of the regional budget in million of rubles
Number of bids	bids	Average number of bids in region
Share of changed contracts	changesrate	The share of number of contracts changes in whole number of signed contracts
Share of careful administrators	carefuladm	The share of number of administrators in region who gives the information about procurement activities in total number of administrators in region

Contact:

Elena Podkolzina
Ph.D. in economics, Senior Researcher of Center for Institutional Studies, Higher School of Economics
e-mail: pea.work@gmail.com