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CENTRAL INTELLIGENCE AGENCY

Office of Congressional Affairs

Washington, D.C. 20505

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24 MAR 1989

TO: Mr. Louis Dupart
Permanent Select Committee on Intelligence
House of Representatives
Washington, D. C. 20515

Dear Louis:

[redacted] asked me to respond to your note of 8 March. Rather than raise the issue of the Soviet private sector at our next briefing, we have enclosed a memo which hopefully answers Mr. Livingston's questions.

If you have any additional questions do not hesitate to give me a call.



House Affairs

Enclosure

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23 March 1989

USSR: The Private Sector and Organized Crime

Private enterprise had existed illegally in the USSR on a large-scale for many years to compensate for the inadequate performance of state-run enterprises, particularly in providing personal services. In 1987, the Gorbachev regime confronted long-standing ideological prohibitions and legalized a wide range of private sector activity in order to satisfy consumer demand without expensive capital investment and to gain potentially sizeable income tax revenue. Many orthodox leaders and reformers alike had become convinced that the prevalent theft and diversion of resources from state-run stores and enterprises to the illegal private sector served only to line the pockets of underground entrepreneurs and the corrupt officials who assisted them. Legalization of private businesses coincided with attempts to crackdown on official corruption and other forms of so-called "unearned income."

Legal private sector activity comes in two forms: individual labor activity--cottage industries run by an individual at home--and cooperatives, which are partnerships of three or more individuals where profits are shared. The legal private sector has grown from about 100,000 self-employed in the mid-1980s to about 2 million individuals at present. Despite this growth, the underground private sector remains large, even assuming that some of its 17-18 million people who Soviet economists estimated operated at least part-time in the mid-1980s have moved over to the legal sector.

Because they operate in conditions of scarce supplies and limited competition, and they often provide higher quality goods and services, the new, legal cooperatives charge prices that are usually two-five times higher than official state prices. This breeds resentment that high coop incomes are being earned on the backs of the working class. The average Soviet worker's salary was 216 rubles/month in 1988, while coop workers

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regularly make 500-1500 rubles per month, and many workers foresee the development of a caste of millionaires. Moscow, having told its populus for years that private businessmen are by nature selfish and exploitative, faces the difficult task of reversing popular psychology and convincing workers that, in the words of the former deputy mayor of Moscow, "there is nothing wrong with honest wealth." [redacted]

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These same conditions--scarce supplies, limited competition, and high profits--make cooperatives a natural target for organized crime. During 1988, the Soviet press exposed increasing links between what it now calls the "Mafia" and cooperatives. The difficulties in getting supplies and raw materials often drive cooperatives to illegal suppliers. One coop tailor, for example, told the Soviet press that he got about half of his supplies on the black market. Several Soviet papers have also reported incidents of threats and violence by organized crime against cooperatives that refuse demands for protection money. In the fall of 1988, one Moscow cooperative cafe had to close after being severely damaged by a bomb apparently planted by the local mob. Mafia infiltration into cooperatives also appears to be increasing. The Mafia is reportedly lending money to cooperatives, charging high interest, and demanding seats on their ruling boards and shares of the profits. As one police official told a Soviet weekly, cooperatives have provided crime organizations "the possibility to legalize their capital. In their slang, to launder it." [redacted]

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The Mafia-cooperative link is only the newest form of organized crime and corruption, phenomena that flourished during the 18-year rule of former General Secretary Brezhnev. [redacted] organized criminal activity has existed in the USSR for more than a quarter-century, especially in areas such as the black market and foreign goods. [redacted]

[redacted]
Soviet press accounts accompanying Andropov's, and more recently Gorbachev's,

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anticorruption campaigns have exposed several huge Mafia-style networks. These involved government and party officials, and they created "thousands" of "underground millionaires." A sampling of these cases illustrate the breath and depth of corruption in the Soviet elite and society:

- o The 24-year rule of Uzbek party boss and candidate Politburo member Sharif Rashidov has been blamed for widespread corruption that involved party, economic, and law enforcement officials. The Gorbachev regime punished over 2,600 Uzbek officials in 1986, including sentencing the head of the Cotton Processing Industry to death. Rashidov's successor and the former Uzbek president are currently under arrest awaiting trial for corruption.
- o In 1984, the head of the main Moscow food store was executed for his involvement in the "Moscow food trade crime ring"--a corruption network that controlled retail trade in the city for over 20 years. Several other members were also sentenced for crimes such as bribe-taking, abuse of office, and embezzlement to terms ranging from 8 to 15 years.
- o The trial of Brezhnev's son-in-law, Yuriy Churbanov, and several other police officials for taking bribes amounting to over a million rubles ended late last year when the USSR Supreme Court sentenced Churbanov to 12 years imprisonment and six other republic-level officials to terms ranging from 8 to 10 years. Using the trial to lambast the Brezhnev era in general, the Soviet press carried several articles that detailed Churbanov's abuses and discussed the "degeneration" that took place during the Brezhnev years when officials would sell the country's highest honor, the Order of Lenin, or the job of regional party secretary for the right price.

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Gorbachev's campaign in the press and on the streets to broaden legal private sector activity while strengthening punishment for those who violate the law is part of

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the regime's broader reform that includes efforts to reverse the popular conception that bribery, stealing from the state, and party protectionism are effective ways of "working the system." The press reports about the Mafia, cooperatives, and official corruption--though shocking as subjects of the Soviet media--are not surprising to Soviet citizens who are used to the fact that corruption envelopes society from top to bottom. While mass corruption cannot be measured precisely, the evidence suggests that most ordinary citizens find themselves unable to avoid theft and bribery at one time or another. For some, these illegal activities are needed in procuring even basic necessities, such as food, housing, education and medical care. [redacted]

[redacted] the list of situations in which the Soviet citizen is forced to resort to bribery "is as inexhaustible as life itself, from a bed in a maternity ward to a cemetery plot." [redacted]

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