

Capitalism sharpens corruption in Russia

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For the State Journal

The introduction of capitalism to Russia has drastically redefined the relationship between business organizations and government. As such, it has also changed the nature of corruption.

In particular, the American version of corruption (tax evasion) has been added to the Russian version (bribes to government officials for special services rendered).

Under communism, the primary form of corruption was bribing well-connected government officials for their services. The higher the bribe the sooner you received the service you needed.

This common type of bribe almost disappeared by definition under capitalism. What was once a bribe is now legally a "service fee." Nonetheless, government officials still control a variety of important business activities — such as licensing, real estate contracts and registering new companies — so bribes still serve a useful purpose.

Another area of corruption under communism related to black market activities. A black market enterprise producing and selling furniture without the government's permission relied upon well-placed bribes to obtain necessary goods. Now, these former black market enterprises have legal permission to produce and sell wood products.

Nonetheless, with the shortage of resources, bribes are paid to government officials who have inside information on the product you need, such as who is producing it

and at what price. For the right price, the government official, who is already known by producers, will serve as your middleman.

Rather than reducing bribes, the introduction of capitalism and democracy have increased the intensity of corrupt activities, because government officials, due to the unpredictable nature of Russian politics, are uncertain of their job future. As such, they take advantage of their current positions and offer special licenses to businesses in exchange for part ownership of the business, jobs for family member or a percentage of the profits.

Capitalism has also introduced a major new area of corruption — tax evasion. Under communism, the government collected and redistributed all profits generated from state-owned enterprises. Now it relies on business people to report their profits. To minimize their tax burdens, business people lie about

their total sales and profits.

Most commonly, companies are able to hide a significant portion of their profits from government because they demand cash or goods for their products. To reduce the likelihood of a government audit, the business deposits some of the cash in banks, reporting it to government authorities. The rest is hidden from the authorities, and used to buy personal goods, such as a new car, clothes, a computer or vacation.

Due to inflation, it makes more sense to spend the hidden profits immediately before the price of goods increases. If one wants to save money for the future, the best way to avoid inflation is to exchange rubles for American dollars or German marks on the black market.

Another option is to purchase goods and then resell them on the open market when cash is needed. Lastly, some of the hidden profits are used to pay employees off the books.

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Wisconsin State Journal

Sunday, June 13, 1993

Russians have also adopted the primary U.S. form of individual corruption, hiding wages. Many Russian employers verbally negotiate with their employees, who want just enough reported so that the government doesn't get suspicious and audit them. The employers want to report a slightly higher amount for the very same reason.

Like employers, most employees want to use the unreported income to buy goods for immediate personal use. Some use the wages to purchase goods that will not be used for several years, such as buying clothes that fit a 10-year-old girl when your child is only 3.

Those who want to save money for future expenditures either exchange rubles for dollars and

marks on the black market or purchase durable goods, such as television sets, that can easily be resold on the open market at higher, inflationary prices.

The government is trying to catch up with some of the illegal activities. Russians, like Americans, shy away from activities that are criminalized, particularly those the government is likely to investigate. So, tax evasion has been made a criminal offense, and the number of tax service agents has increased.

The government has also implemented a new budget distribution scheme where tax service units get to keep 10 percent of the illegal profits and wages they recover. The money can be used to increase budgets, wages and number of employees.

Another new policy is tax reduction. In 1993, the value-added tax was significantly reduced and the maximum personal tax was reduced from 60 percent to 40 percent. The hope is that citizens, believing these lower taxes are more reasonable, will be less likely to hide profits and wages.

Tax laws, like Russian society, are in flux and being worked out.

CAPITALISM IN RUSSIA

This is the last of a three-part series analyzing capitalism in Russia after the dissolution of the Soviet Union.

The series was written by Svetlana Kuznetsova, a lawyer in Moscow, who recently studied at UW-Madison's Graduate School of Business, and Denis Collins, an assistant professor of business ethics at the School of Business.