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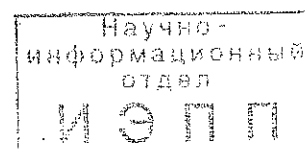
**Takis PROMETEE II**

# **KALININGRAD REGION THE DIAGNOSIS OF A CRISIS**

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This book is a diagnostic of the current situation in the Kaliningrad Region, it corresponds to the first stage of the project. The material production sphere, the international economic activity of Kaliningrad, the budget, the infrastructures and services, the institutional changes are reviewed. Besides it the social aspects are also investigated with regards to the social sphere and the living standards, moreover a sociological survey has been conducted on the population of Kaliningrad Region and social groups in crisis conditions. The conducted analyses propose some recommendations and ways of transformation. More will be proposed in a second publication referring to the second stage of the project, dealing with a long-term strategy and scenarios of development. The chapter one is an introduction to the book and is to be understood as a synthesis of the main outputs of the research and includes a rapid overview of the other chapters.

This book is dedicated to the researchers, the local and regional authorities and students dealing with the questions of the development of the Region.

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## Chapter 4. THE BUDGET OF THE KALININGRAD OBLAST

### 4.1 The revenues of regional budget and of municipalities

#### 4.1.1 Tax performance in the oblast in 1992-1997

According to IET calculations, the tax burden, that is amount of tax revenues in proportion to gross regional product (GRP), constitutes in the Kaliningrad oblast 28% concerning regional and federal tax revenues and about 16% when only tax revenues of regional budget are taken into consideration (data for 1996-1997). For the consolidated budget of the all Russia Federation the same indexes constitute respectively 21% and 12%. At the same time tax revenues per capita in the oblast are small in comparison with the average for the Federation. For instance, average tax revenue per capita is 1.95 times higher in Russia than in the Kaliningrad oblast and average regional budget tax revenue per capita in Russia exceeds the same amount for the oblast by 1.7 times (for gross product the Russia level exceeds the oblast level by 2,9 times). In other words, when the tax burden in the Kaliningrad oblast is 1.3 times higher than the average level in Russia, there are no more ways left for raising it further. The considerable increase in tax revenues of the regional budget may be possible only after the regional economic performance improves.

The quarterly dynamics of all tax revenues at all levels of the budgetary system collected on the territory of Kaliningrad oblast in 1992-1997 is presented in the Fig. 1 and Table 1. It can be seen from the presented data that from 1992 till 1995 there was a continuous fall in the figures of tax collection calculated in the constant prices of December, 1991. But a stabilisation on tax performance in 1997 and a slow growth of tax revenues in 1997 haven't yet compensated for the amount lost in 4 years. A seasonal component can also be seen from the diagram - a fall in total amount of tax revenues in the first quarter of a year - a phenomena which is characteristic of the tax collection in Russia. Despite the fact that in the first quarter of 1997 the total amount of taxes collected was lower than in the same period of 1996 and of any other year, the total amount of tax revenues of all levels of the budgetary system in 1997 exceeded the amount of 1996 (in constant prices).

In 1997 there was a visible growth in personal income tax and especially excise tax revenues. The dynamics of corporate income tax and value added tax collection was unstable to a significant extent, showing a general tendency to growth.

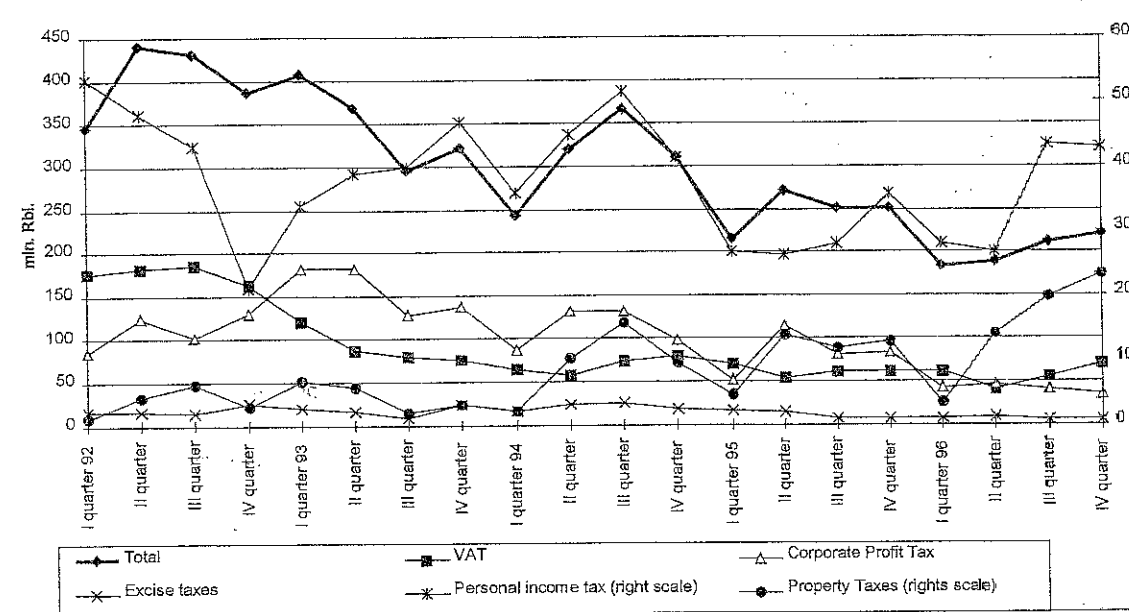


Fig. 1. The quarterly dynamics of tax revenues in the Kaliningrad oblast in 1992-1997 in prices of 1991

It is evident that among the factors that influence the tax performance and dynamics of the tax revenues collected we can mention the consequences of the free economic zone regime. But up to now it is not possible to determine the nature and the scale of this influence (it exercises direct influence only in relation to the federal budget - decrease in custom duties revenues). On the one hand, this regime looks like an incentive to manufacture added value (as goods, manufactured or assembled on the Kaliningrad oblast territory, are exempt from customs duties when imported from the oblast to the main all Russia territory), but on the other hand there is a depressing effect on the Kaliningrad manufacturers for the reason of the price advantages of the imported goods because of customs import duties exemption granted to the imported goods by the free trade regime. The uncertainty of the effects of the free trade zone regulations may also be proved by the absence of visible shifts in tax collection level and tendencies in the period of suspension of the free trade zone regime in Kaliningrad oblast which took place for 10 months in 1995 (see Tab. 1 and Fig. 1).

The structure of all tax revenues collected in the Kaliningrad oblast was unstable in 1992-1997 (see Fig. 2).

In 1997 the structure of tax revenues collected on the territory of the oblast was to a significant extent the same as in the all Russia Federation (Table 1). The particular feature of the tax revenues structure in the oblast as compared with that of the whole country lies in the fact that the proportion of personal income tax revenues in the total amount of tax revenues collected is rather high beginning from the third quarter of 1996. It cannot be explained by the high rate of collection of this tax for while real personal

income in the oblast exceeds average all-Russia personal income in real terms by 1,55 times (according to the data for January-November, 1997), the amount of personal income tax collected per capita in Russia exceeds the same in the oblast only by 1,36 times (among possible reasons for this state of affairs we can mention the high rate of military population in the oblast, who are not subject to personal income tax).

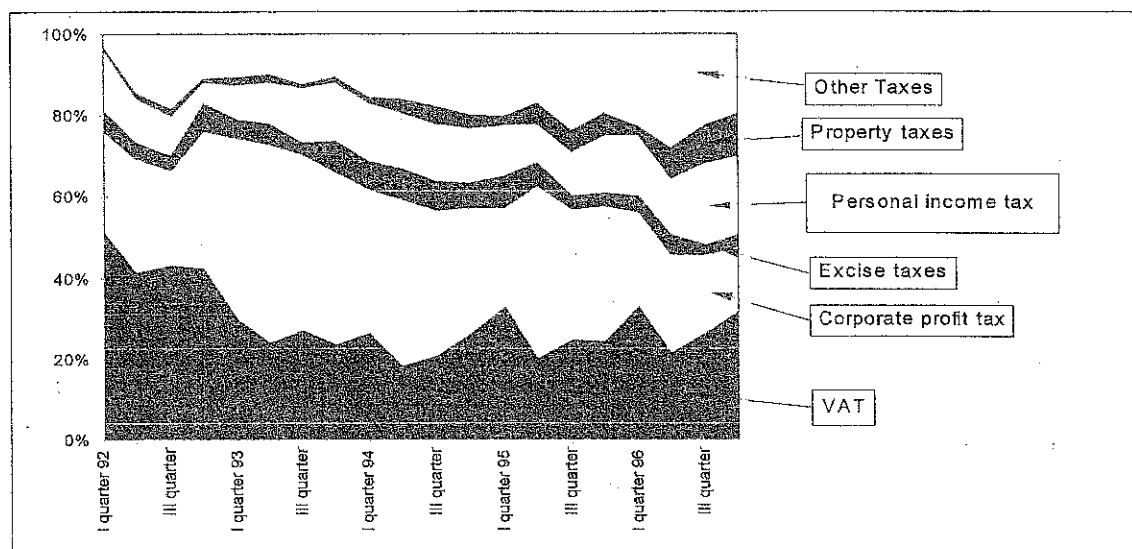


Fig. 2. The structure of tax revenues in the Kaliningrad oblast

The low proportion of corporate profit tax revenues evolves from the low rate of profit of Kaliningrad enterprises. For example, average profits of commercial enterprises in Russia exceeded average losses in 1996-1997. And as for commercial enterprises of the Kaliningrad region their average losses either were higher than profits or profits exceeded losses by a very small rate. As a result - a corporate profit tax revenues per capita for the whole Federation exceeds the same ratio for the Kaliningrad oblast by 2.3 times. (For reference: the same correlation for VAT is 1.77 times in favour of the oblast: to a certain extent it confirms our previously mentioned hypotheses on the free trade zone effect from the point of view of added value).

We have obtained the same results for the revenues from certain other taxes' in proportion to the gross product of the oblast and of the all Russia Federation. The proportion of personal income tax revenues compared with the gross product in the oblast is 1.6 times higher than in Russia, the proportion of VAT revenues is 1.2 times higher and the proportion of corporate profit tax is 1.1 lower than in the all Russia Federation.

One of the major problems for the oblast is that the forecast on the ground of which the law on the regional budget is adopted differs significantly from the actual tax revenues. It is worth mentioning that in spite of the fact that the revenues of the regional budget remained in 1997 at the level of 1996, the rate of budget revenues execution in

the first half-year of 1997 constituted less than 70% of the plan. This plan was approved by the regional Duma in the form of the regional law "On the budget of the oblast for 1997" and the total amount of tax revenues in this law fixed at the level of 370.8 bln. rbl. Actually this resembles the situation of 1996, when revenues both of the consolidated regional budget and of the oblast's budget constituted about 65% of the plan.

Table 1

**The structure of tax revenues in the Kaliningrad oblast  
and in the all Russia Federation in 1997**

	Kaliningrad oblast, mln. Rbl.	Kaliningrad oblast, % to total tax revenues	all Russia, % to total tax revenues
Total tax revenues collected	1928363	100,0	100,0
Direct taxes on profit, income, capital growth	650131	33,7	31,1
- corporate profit tax	299175	15,5	18,4
- personal income tax	350956	18,2	12,7
Taxes on goods and services	714879	37,1	40,8
- VAT	610047	31,6	29,0
- excise taxes	78678	4,1	11,1
- license and registration fees	19281	1,0	0,5
Payments for natural resources	123965	6,4	6,9
- payments for depths usage	12516	0,6	2,9
- land tax and leasing payments for land	71144	3,7	1,6
Taxes on property	156067	8,1	8,0
- personal property tax	2511	0,1	0,1
- corporate property tax	151291	7,8	7,8

Taking into consideration the fact that the adoption of a realistic expenditure program and its execution during the year depends first of all on the quality of revenues forecast, one of the main tasks for regional authorities is working on the calculations of budget revenues so that the forecast will match actual receipts.

**4.1.2 Dynamics and structure of tax arrears in the oblast in 1995-1997**

The quarterly dynamics of tax arrears in 1995-1997 is shown in Table 2 and in Figures 3-7. It can be seen from the presented data that there has been a significant growth of tax arrears both to the federal and to the consolidated regional budget. At the

same time we can see that the level of corporate profit tax arrears is rather stable throughout the two years - a tendency that led to the decrease of the share of corporate profit tax arrears in the total amount of taxpayers' indebtedness. The VAT arrears constitutes the major share of total tax arrears.

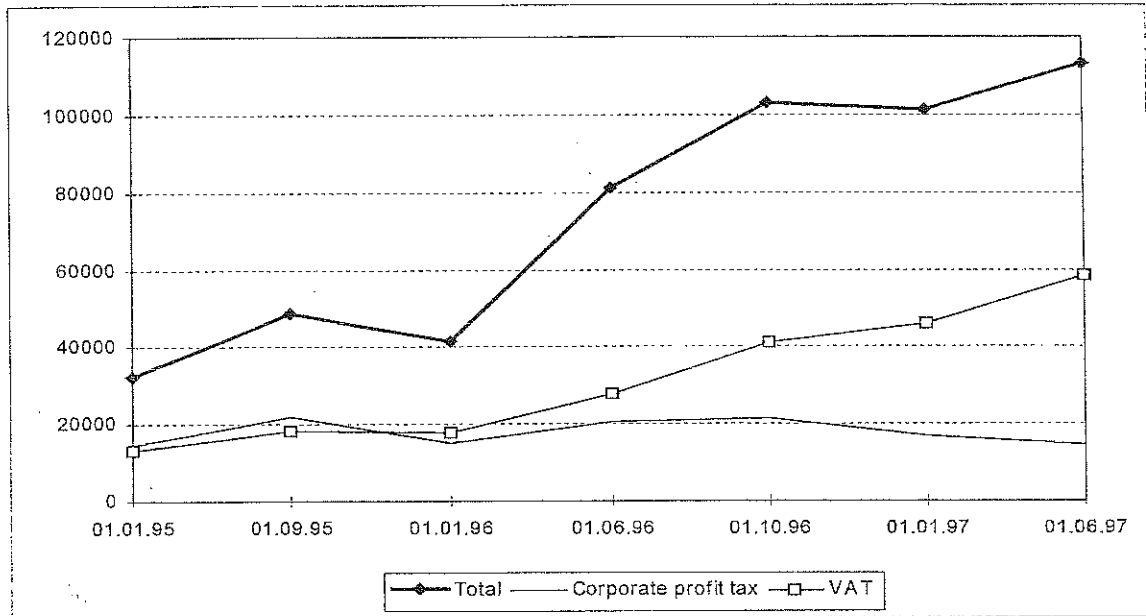


Fig. 3. The tax arrears' dynamics to all levels of budgetary system in the Kaliningrad oblast in 1995-1997 in prices of December, 1994

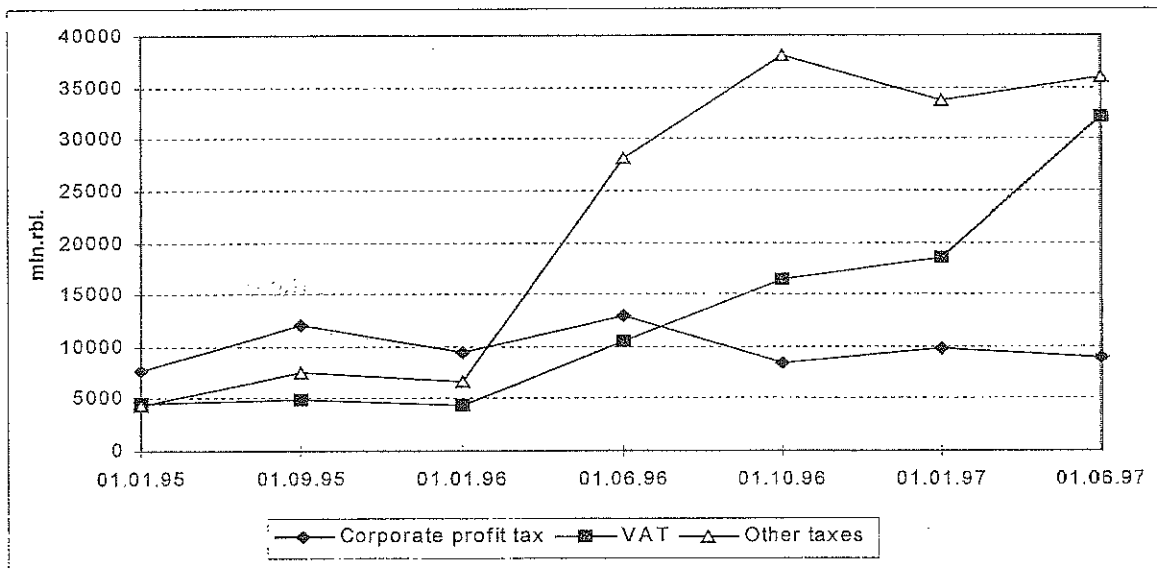


Fig. 4. The Tax Arrears' Dynamics to the Consolidated Regional Budget of the Kaliningrad oblast in 1995-1997 in prices of December, 1994

Table 2

## The dynamics and structure of tax and other payments arrears in Kaliningrad oblast, mln. Rbl.

	1.04.95	1.07.95	1.10.95	1.01.96	1.04.96	1.07.96	1.10.96	1.01.97	1.04.97	1.07.97	1.10.97	1.01.98
Total	34176	64068	106412	99783	81807	160613	221392	266464	304555	313175	353777	419528
corporate profit tax	12877	29882	45501	35966	16850	36683	48687	45074	37387	40434	44777	46019
VAT	16959	25745	42170	42527	37510	67701	83167	121281	173705	170680	171922	204497
other taxes and payments	4340	8441	18741	21290	27447	56229	89538	100109	93463	102061	137078	169012
of those:												
to the federal budget	13891	24596	53447	50747	34104	63985	83774	103409	131633	103731	114060	137456
corporate profit tax	4036	13552	21015	13451	4908	13121	20983	19375	14180	15072	16800	19433
VAT	7411	10944	28409	31895	22922	41146	49868	72735	104222	76608	77364	92024
other taxes and payments	2444	100	4023	5401	6274	9718	12923	11299	13231	12051	19896	25999
to the consolidated regional budget	20285	39472	52965	49036	47703	96628	137618	163055	172922	209444	239717	282072
corporate profit tax	8841	16330	24486	22515	11942	23562	27704	25699	23207	25362	27977	26586
VAT	9548	14801	13761	10632	14588	26555	33299	48546	69483	94072	94558	112473
other taxes and payments	1896	8341	14718	15889	21173	46511	76615	88810	80232	90010	117182	143013



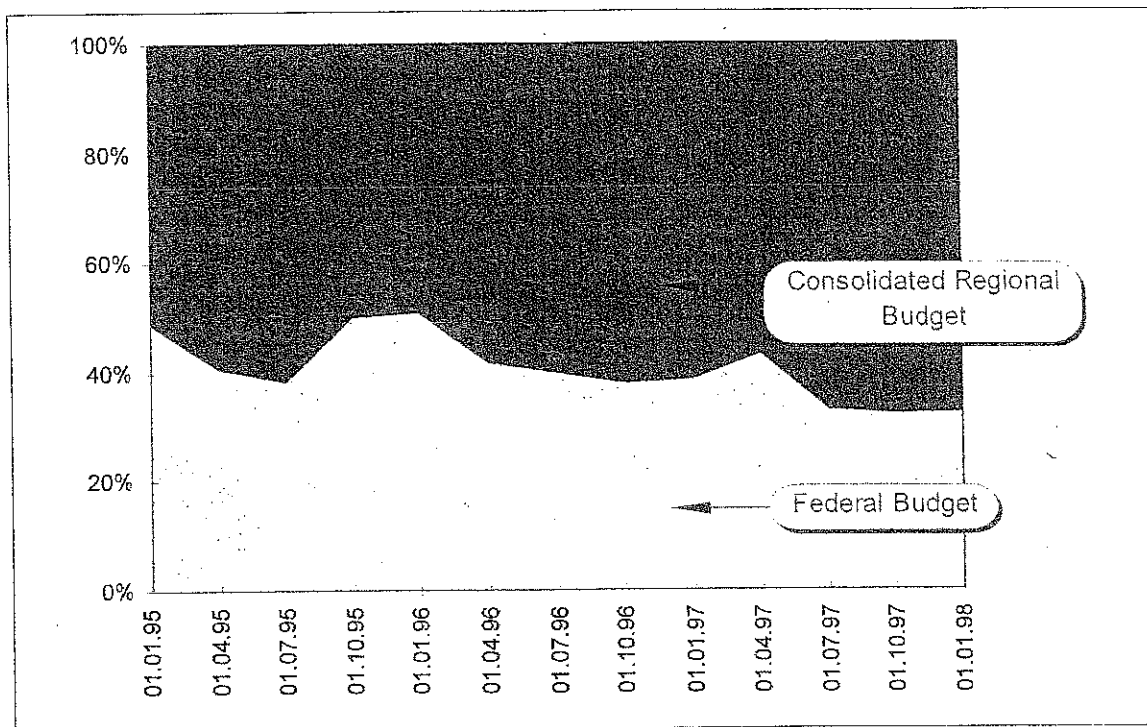


Fig. 5. The Tax arrears' structure in the Kaliningrad oblast

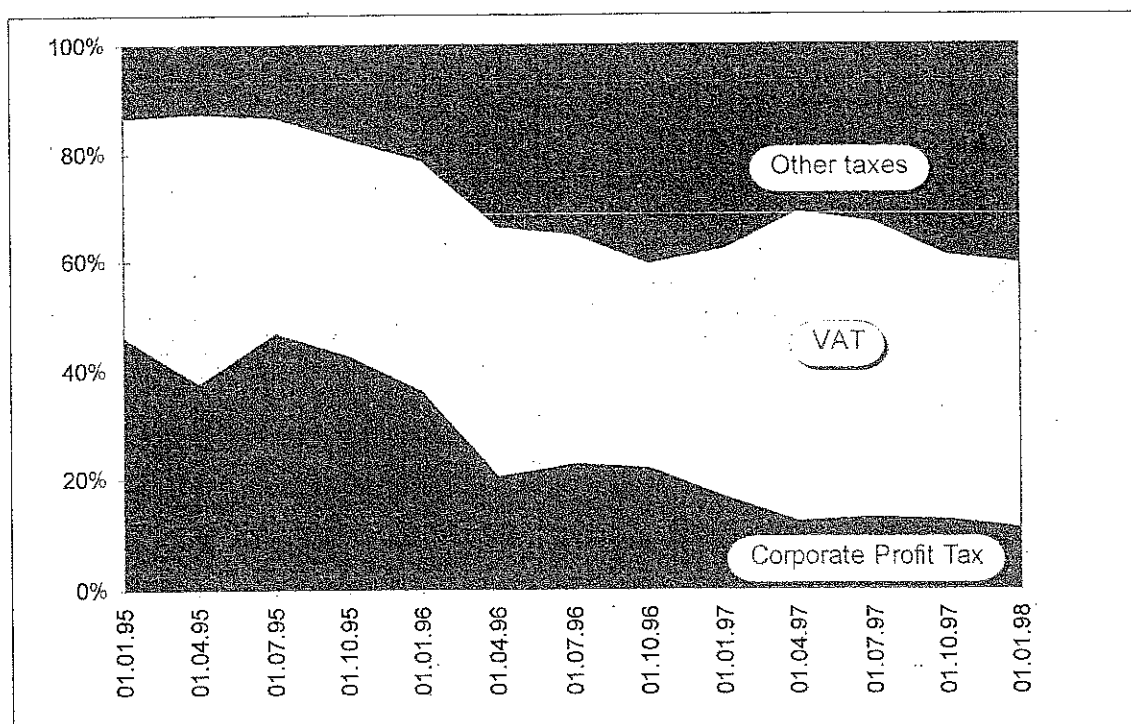


Fig. 6. The tax arrears' structure in all budgets of the Kaliningrad oblast

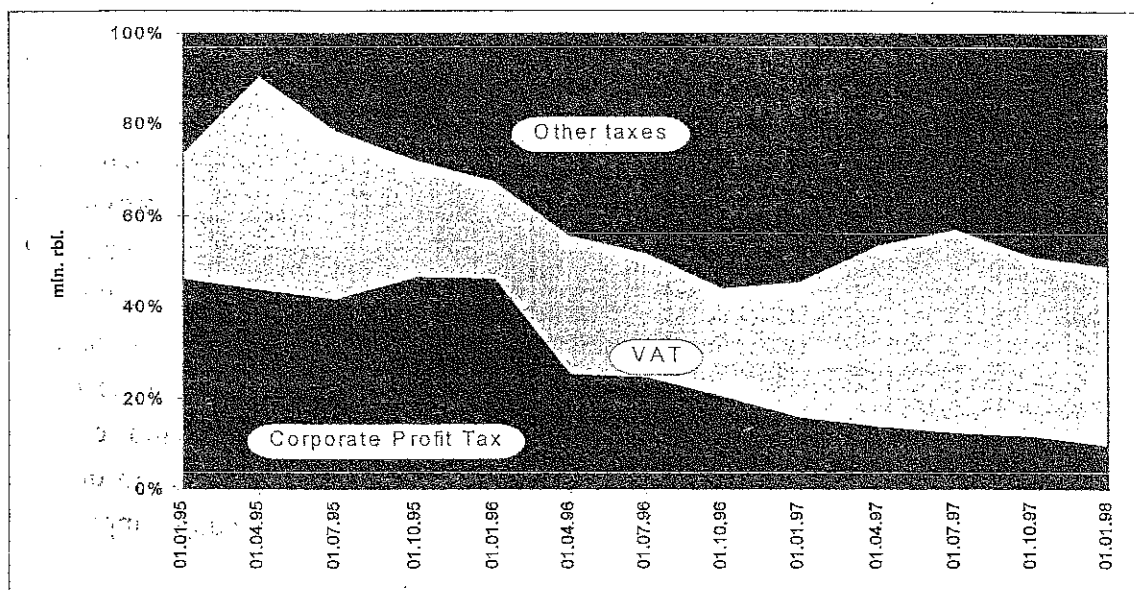


Fig. 7. The tax arrears' structure to the consolidated regional budget of the Kaliningrad oblast

The fact is that tax arrears to the consolidated regional budget exceeds tax arrears to the federal budget both in absolute terms and in relation to the total amount of tax liabilities by the end of 1997 (See Fig. 7). This situation is not usual for the majority of all-Russia regions as regional authorities always have effective measures at their disposal that make the debtor pay taxes. It will take a special piece of research to discern the reasons for such a state of affairs but according to information that we have we can assert that regional authorities do not use all opportunities to raise tax performance in the oblast.

Table 3

Tax arrears in % to the sum of tax arrears and tax revenues collected

	1995	1996	1997
<b>all Russia Federation</b>			
total	13,6	18,9	21,3
federal budget	17,4	23,1	27,3
regional budgets	10,8	15,3	16,3
<b>Kaliningrad oblast</b>			
total	6,2	14,1	17,9
federal budget	8,3	14,8	17,0
consolidated regional budget	4,9	13,8	18,3

It is evident from Table 3 that the comparison of tax arrears in relation to tax liabilities in the oblast and in the all Russia Federation could be made in favour of the

Kaliningrad oblast. But at the same time the growth rate of tax arrears against tax revenues in recent years has been higher than in all Russia Federation.

It is worth mentioning that manipulating tax rates under present circumstances and the volume of tax indebtedness is useless from the point of view of improving tax performance without taking adequate measures aimed at charging tax arrears. The present volume of tax arrears leads to asymmetric results of tax policy that results from the following mechanism: raising tax rates leads to the growth of tax arrears and reducing tax rates results in total decrease in tax revenues while the volume of tax arrears remains on the same level or even increases. The way out of this vicious circle in our opinion is to restructure indebtedness on tax and other payments - and in order to start the process regional authorities need to work out and to adopt appropriate measures.

#### *4.1.3. Econometric analysis of the factors that influence tax revenues in the Kaliningrad oblast*

In order to discern the main factors that exercise influence on the dynamics of the tax revenues collected we have made an econometric analysis where we have taken deflated monthly data on the tax revenues of the consolidated regional budget as a dependent variable. At the same time we have set as regressors monthly data on various economic indicators of the region including inflation (CPI), debit and credit indebtedness, and living standards levels of the regional population. We have chosen the following period of time for research: between January 1995 and November 1997.

To analyse the extent of dependence of tax revenues on the level of economic activity in the region we run regressions with the volume of industrial production as an independent variable. In this case we do not detect any significant influence on the tax revenues dynamics (Equation 1, Table 4). In our opinion, this could be explained by the fact that industrial production does not necessarily lead to the emergence of tax liabilities - first of all for the reason of low sales and low level of immediate payments for the shipped products.

One of the factors that exercise negative influence on the tax revenues collected is the indebtedness of enterprises to their counterparts for raw materials (debit indebtedness). To check the extent of dependence we took indicators of indebtedness of enterprises as independent variables. We also assumed that these indicators must exercise negative influence on the tax revenues collected (indebtedness of enterprises results from the lack of funds on the enterprises' accounts and hence it is impossible to redeem tax liabilities). Regression results confirmed our assumption (See Equation 2, Table 4). High t-stats of parameters of indebtedness indicate the high significance of these parameters. A Durbin-Watson statistics exceeds the upper critical level (in this

case it is equal to 1.55) and this fact enables us to put down the residuals autocorrelation hypothesis.

For the estimation of the influence of the level of living standards on the tax revenues collected we used the indicators of unemployment (the proportion of unemployed population in the total population of the oblast), together with personal income and average salary in the region as independent variables. Unfortunately, as in the case with level of industrial production, we have not found significant correlation on all variables with tax revenues (Table 4).

Table 4

The results of regressions

	1	2	3	4	5
Number of observations	35	35	35	35	35
Unemployment	...	...	-0,25	...	...
t-stat	...	...	-1,47	...	...
Real income of residents	...	...	...	-0,15	...
t-stat	...	...	...	-0,85	...
Average salary	...	...	...	...	-0,33
t-stat	...	...	...	...	-1,98
Debit indebtedness	...	-1,78	...	...	...
t-stat	...	-2,68	...	...	...
Volume of industrial production	-0,02	...	...	...	...
t-stat	-0,12	...	...	...	...
C	60683,3	75845,2	80285,1	67975,4	73041,6
t-stat	4,74	12,96	5,55	6,55	10,07
R adj	-0,03	0,21	0,03	-0,01	0,08
F-stat	0,01	5,37	2,15	0,73	3,91
DW	1,31	1,77	1,38	1,39	1,50

The absence of a significant link between indicators of living standards and tax revenues is probable for a number of reasons. Unemployment, like personal income, exercises greater influence on income taxation rather than on total amounts of tax revenues collected. The lack of the necessary number of observations concerning personal income tax revenues in the oblast does not enable us to run a full econometric analysis of the interrelationships existing between these indicators.

As far as average salary is taken into consideration, we have observed a negative influence of this factor on the dynamics of total tax revenues. Despite the fact that it explains only 8% of the dynamics of total tax revenues, the link between these two variables is quite stable (the t-statistics value enables us to reject a zero-coefficient hypothesis with 94% probability). This link in our opinion evolves from corporate profit tax evasion by raising salaries thus decreasing the tax burden on enterprises. The fact that the share of personal income tax revenues in total tax revenues collected of both the consolidated regional budget and the federal budget exceeds the share of corporate

profit tax revenues in the Kaliningrad oblast proves our assumption in indirect way as for average regional tax revenues structure the proportions are vice versa.

#### ***4.1.4 Estimation of tax revenues of the consolidated regional budget of the Kaliningrad oblast in 1996 in accordance with the main conditions of the draft Tax Code (Edition of 01.02.1998)***

This section concentrates mainly on the possible changes of tax revenues following the conditions imposed by new tax legislation which might be introduced by adoption of a Tax Code by the State Duma. We have made our calculations on the basis of 1996 statistical data for it is the latest period on which we had full data at our disposal.

In order to make an estimation of tax revenues in 1996 we use regional data (with corrections added to make the data fit the latest edition of the Tax Code), submitted by the Ministry of Finance to the State Duma, together with calculations of federal financial transfers from the Fund for Financial Support of Regions for 1998. In our research we have taken into account the following changes in tax legislation which are envisaged by the Tax Code: repeal of taxes, charged from payroll fund and companies' receipts (transport tax, duty on the needs of educational bodies, tax on housing and objects of maintenance in the socio-cultural sphere, taxes on militia support, territory improvement etc.), reduction of tax rates and changing progressive scale for personal income tax, change in rules of tax base calculation for corporate profit tax that implies introduction of accelerated amortisation, revision of expenses list that reduce corporate profit tax base, introduction of new rules of taxation for consolidated groups, introduction of a sales tax.

The corrections in the MinFin calculations was as follows:

- the VAT tax revenues were reduced on the grounds of maintaining the preferential rate of 10% on several groups of food products and on goods for children. The reduction was made in the same proportion to the actual VAT revenues collected as the estimated growth of VAT revenues to the federal budget related to the forecast of VAT revenues, calculated according to old rates (130056 mln. Rbl. instead of 135747 mln. Rbl., offered by MinFin); VAT revenues were estimated at the rate of 20% instead of the 19% that was in the draft earlier);

- corporate profit tax revenues were estimated at the rate of 19% instead of 22% (the estimated revenues decreased from 187975 mln. Rbl. to 162342 mln. Rbl.).

We have also made our own estimation of sales tax revenues in the Kaliningrad oblast, which can be seen in Table 5. If sales tax were introduced in 1996, revenues of the consolidated regional budget from its collection would have been about 175700 mln. Rbl. But one must bear in mind the fact that statistical data on retail turnover include

estimation of shadow turnover, which cannot be taxed. This may reduce the actual amount of sales tax revenues in comparison with our estimation, but calculation of the discrepancy amount is one of our tasks for the next stage of research.

Table 5

**Estimation of the sales tax revenues in the oblast**

	First half-year of 1997	1996
Retail-trade turnover, bln. Rbl.	1832	3514
Tax rate	5%	5%
Tax amount, bln. Rbl.	91.6	175.7
Tax amount, % GRP	2.9%	2.8%

The results of tax revenues estimation in 1996 is shown in Table 5. It follows from the results of our research that after the Tax Code comes into force the level of tax revenues will not change seriously. The changes in tax revenues collected will also depend on the tax arrears growth in the oblast and the proportion of tax revenues to GRP will depend mainly on its dynamics. It is possible that in the very near future regional authorities will face the problem of the decrease in tax performance in the oblast.

Table 6

**The comparison of estimated and actual tax revenues of the consolidated budget of the oblast in 1996**

	Actual of 1996		Estimates	
	mln. Rbl.	% GRP	mln. Rbl.	% GRP
Direct taxes on profit, income, capital growth including	461876	8,0%	416102	7,2%
- corporate profit tax	206651	3,6%	162342	2,8%
- personal income tax	254460	4,4%	253760	4,4%
Payroll Taxes	33003	0,6%		
Taxes on goods and services including	137539	2,4%	237890	4,1%
VAT	93931	1,6%	136901	2,4%
Excise taxes	11269	0,2%	8989	0,2%
Sales tax	0	0,0%	92000	1,6%
Taxes on property including	120472	2,1%	184991	3,2%
- personal property tax	1401	0,0%		
- corporate property tax	118933	2,1%		
Payments for natural resources	64762	1,1%	18077	0,3%
Other taxes, fees and duties	114064	2,0%	73758	1,3%
Tax on housing and socio-cultural objects	87110	1,5%		
TOTAL	931716	16,2%	930819	16,2%
GRP, mln.Rbl.	5755636			

## 4.2. Inter-budgetary relations

### 4.2.1. Inter-budgetary relations in the financial system of the oblast

The main object of inter-budgetary relations structure analysis concerning the Federation is the distribution of revenues and expenditures between levels of budgetary system. The high degree of decentralisation of tax revenues allocation is typical of the Kaliningrad oblast. For instance, if the average share of regional budgets in tax revenues of the consolidated regional budgets for the all Russia Federation in 1996 was about 48% of total tax revenues and the share of municipal budgets' share constituted 52%, the proportions of budgetary system levels in total tax revenues in the oblast was changed from 35% and 65% in 1995 to 26% and 75% in the first half-year of 1997 respectively. The process of revenue and expenditure decentralisation is dates from 1992, when municipal budgets got 50% of total revenues and bore 60% of total expenditure of consolidated regional budget, until 1996 when the proportions were 63% and 65% respectively (see Fig. 8 and 9):

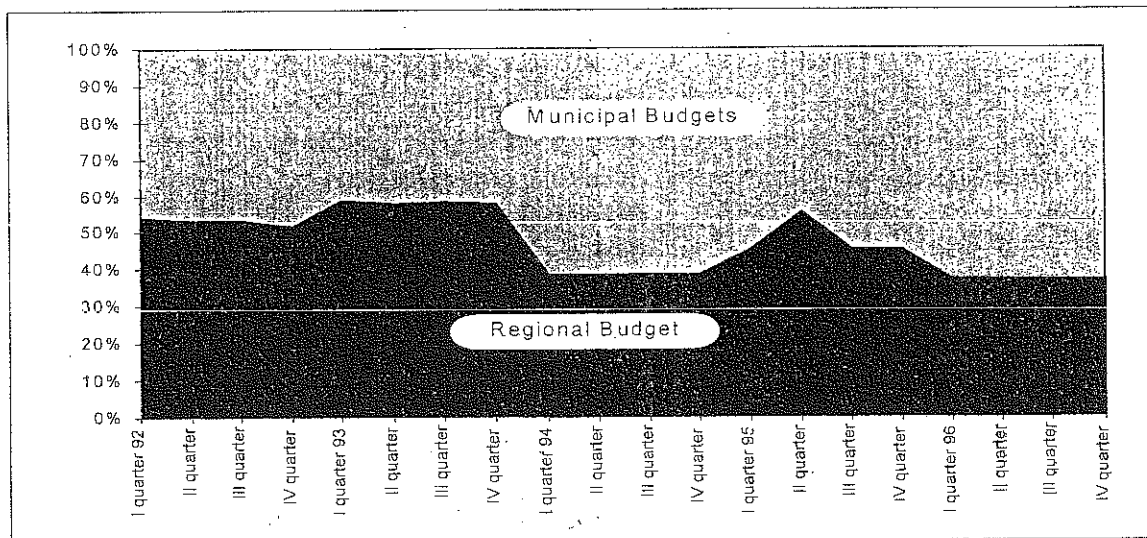


Fig. 8. Structure of consolidated regional budget's revenues in 1992-1996 (%)

The State Duma of the all Russia Federation approved on the 10<sup>th</sup> September 1996 the federal law Nr 126-FZ "On the Financial Basis for Municipal Self-Governance in all Russia Federation"; on the 25<sup>th</sup> of September the law was signed by the President. This law was aimed at making guarantees in the sphere of the municipal budgets' revenues by

setting a number of minimal proportions of federal and regional taxes revenues that must be assigned to municipal budgets. The estimation of municipal and regional tax revenues was carried out on the following minimal proportions, that are envisaged by the law:

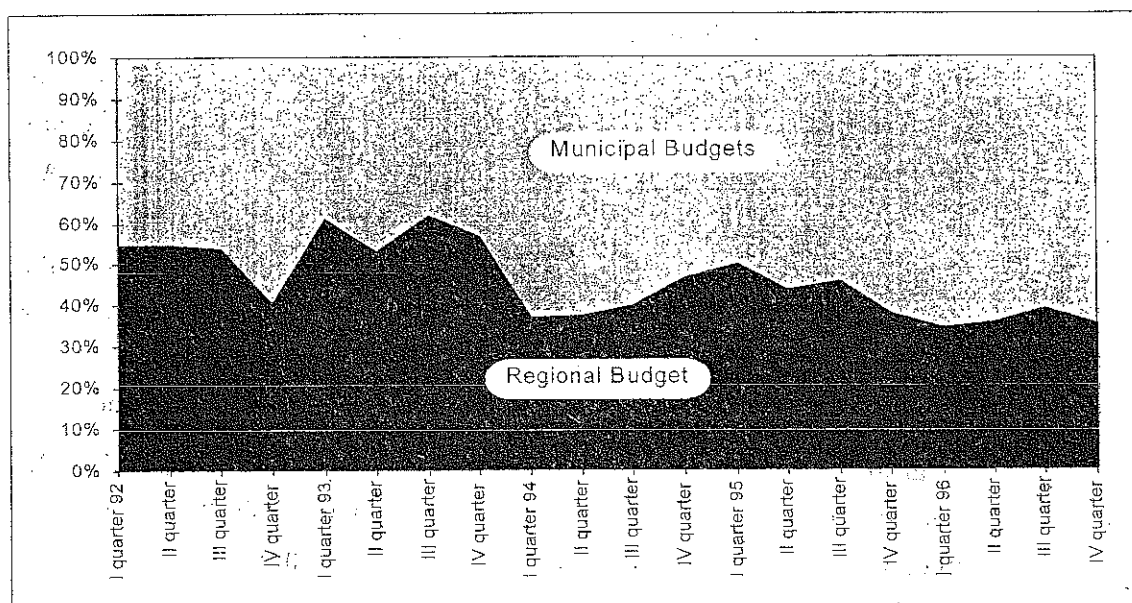


Fig. 9. Structure of consolidated regional budget's expenditures in 1992-1996 (%)

1. The proportion of the municipality in the corporate profit tax revenues is 5% compared with the share of a region (maximum regional rate is 22% or 63% of the total amount according to the law "On the tax on the profit of enterprises and organisations"). Before the adoption of the law the existing law "On the basic budget rights and rights to form and use extra-budget funds of executive and representative bodies of state power of the republics in all Russia Federation, autonomous oblast, autonomous districts, krajs, oblasts, cities Moscow and St. Petersburg, municipal self-governance authorities" did not envisage any proportion of municipalities in corporate profit tax revenues, determining that this kind of tax revenue may be assigned to these budgets in proportion of 100% or less (actual share of municipalities in 1996 on the Federation level constituted 40% of regional profit tax revenue). The law of the Kaliningrad oblast "On the budget of the oblast for 1997" does not set the proportions of municipal budgets in the total corporate profit tax revenues with reference to acting laws and regulations thus opening the way to setting this proportion by individual negotiation.

2. The minimal proportion of municipalities in personal income tax revenues is set at the level of 50% of the regional share which was 90% according to the law "On the Federal Budget for 1996". The law "On the basic budget rights..." does not also envisage any proportion of municipal budget in the revenues of this tax and the actual proportion in 1996 on the Federation level amounted to 73% of the regional share. The



law of the oblast on the regional budget for 1997 assigns 100% of the personal income tax revenues to municipal budgets.

3. The minimal proportion of municipalities in VAT revenues is set at the level of 10% of the regional share which is 25% of the total revenues according to the law "On the Federal Budget for 1996". Existing law does not regulate distribution of this tax revenue between municipal and regional governments and the actual proportion of municipalities on the Federation level in 1996 was 39% to the regional share. The law of the oblast on the regional budget for 1997 assigns 25% of the regional share of VAT revenues to municipal budgets.

4. The minimal proportion of municipalities in excise tax revenues is set at the level of 5% for excise taxes on spirits, vodka and liquor and 10% for excise taxes on other goods excluding mineral raw materials, petrol, cars and imported goods. According to the law "On the Federal Budget for 1996" the regional share in 1996 was 50% for the first group of goods and 100% for the second. The existing laws and regulations do not set any proportion of excise tax revenues distribution between regional and municipal authorities and the actual proportion of municipalities was in 1996 22% of the total amount of excise tax revenues.

5. The proportion of municipalities in corporate property tax is not less than 50% of the consolidated regional budget's total tax revenue. This proportion has not changed in comparison to the law "On the basic budget rights...". The only innovation of the new law is setting the minimum of 50%, which means prohibiting the regional authority from decreasing the proportion.

The aim of the research was to answer the question: what would be the change in the tax revenues' structure in the Kaliningrad oblast in 1996 if the schemes of sharing the regulating tax revenues were implemented valid and the assignments of tax revenues to that kind of budgets were made according to minimal rates.

Our estimation shows that in 1996 the proportions of regional and municipal tax revenues in the total tax revenues of the consolidated regional budget constituted 24% and 76% respectively and if minimal proportions of tax revenues were set in 1996 the share of the regional budget's revenues in the total tax revenues in the oblast would amount to 58%, and as for municipal budgets their proportion would be 42%. Such a result reflects the standard situation in Russia, where as has already been mentioned above, 48% of the consolidated regional budgets' tax revenues is revenues of regional authorities' budgets and 52% falls on municipal budgets. And if minimal proportions of municipal tax revenues were introduced from 1996, the actual proportion would decrease to 32% and the minimal share among all regions after setting new normative rates is estimated to be 14% (Kabardino-Balkarskaya Republic) and the maximum - 54% (Ingushskaya Republic).

In other words, adoption of the new law containing minimal normative rates of federal tax revenue assignment to municipalities does not lead to the increase in proportion of tax revenues of this level of budgetary system in the total tax revenues of the consolidated regional budget. The minimal proportion of tax revenues guaranteed by the law is 20 percentage points less than the actual data for 1996. Hence, setting new minimal proportions of tax revenue assignment both does not cause an increase in the guaranteed level of municipal budgets tax revenues and makes impossible emerging new expenditure obligations of regional authorities in relation to municipal budgets aimed at donating them up to the minimum level of tax revenues guaranteed.

The main methods of budgetary equalisation in all Russia regions are as follows: assignment of the shares of federal and regional tax revenues to municipalities, granting direct financial support (donations, transfers, subventions) to the lower level budgets, exercising mutual clearing and making budget loans to municipalities. The Kaliningrad oblast authorities use, as can be seen from the data, all kinds of financial support of districts and town except for financial transfers (from the fund for financial support of municipalities) and subventions.

Among important principles of inter-budgetary relations we can single out using plain methodology of calculating financial flows unique for all municipalities and transparency of inter-budgetary relations. We can see that the main features of regional and municipal budgets' relations are the same as for the relations of the regional and federal budgets: the proportion of financial support that is granted to the low level of budgetary system according to formal and unique for all recipients criteria is far too low to constitute 100% of all financial support. Mutual clearing and budget loans are neither formally calculated methods of financial support nor fully regulated by federal laws. Unlike normative rates of tax revenue proportions and donations granting the amounts of mutual clearing and budget loans are approved in the process of budget execution. Moreover, among the recipients of the latter forms of financial support we may find both "weak" and "strong" territories.

While organising inter-budgetary relations inside the region it is important to look at distribution of financial flows among local budgets of various levels and not only among regional budget and local budgets that are subordinate to regional budget. In other words it is interesting to look at the problem of financial flows from district budgets to the budgets that are subordinate to them (budgets of small towns, villages, etc.). According to the law "On the Financial Basis for Municipal Self-Governance in all Russia Federation" one of the instruments for financial support is financial flows from the fund for financial support of municipalities. Until 1978 there was no such a fund in the oblast.

We consider it rational to assign to the fund the amount of the federal financial transfer from the federal fund of financial support of regions and the fixed share of regional budget's tax revenues. The best variant is to form the fund on the account of the federal taxes revenues of the regional budget: 10% of the VAT and 10% of excise taxes revenues. For the more simple formula these two rates may be replaced by the equivalent - 10-15% of total tax revenues of the regional budget.

While looking at the problem of the sources of the fund for financial support of municipalities we must take into account the formal criteria in accordance of which the distribution of the fund will take place. These criteria may not include individual features of a municipality that may require additional funding. That is why it is rational in our opinion to leave a share of financial resources free as a reserve fund of regional authorities for current budgetary administration and for financial support for investment and other special purposes. This becomes more important in the case of setting the minimal proportions of municipal tax revenues for the period that exceeds 1 year and assigning fixed sum transfers for the period exceeding the duration of the budget planning cycle.

While working out methods of distribution of financial transfers to municipalities from the regional fund for financial support of municipal budgets it is important to fix the relative normative rates for the long period of time, for example, not less than three years. This requirement on the one hand will make executive and representative bodies be more responsible while setting the normative rates and on the other hand, which is more important, it will ensure local authorities of additional support from the regional budget in spite of possible growth of their revenues.

As was mentioned above, setting relative amounts of financial transfers for the period of time exceeding the budget planning cycle is one of the reasons for reserving a certain sum for special unforeseen purposes. This reserve will enable additional support to be made to municipalities. Among the possible variants of regulating the fund for financial support of municipalities allocation is one that envisages a transitional period of 1-2 years when financial transfers to municipal budgets will be fixed every year (for the experimentation of the mechanism). In future the shares of municipalities in the fund must be fixed for a period of not less than 3 years with a right given to the regional authorities to form a financial reserve aimed at financial support other than transfers from the fund.

To distribute the resources of the fund for financial support of municipalities in the Kaliningrad oblast various approaches may be used, among which we can single out one based on the principle of revenue equalisation, that implies granting financial support depending on the level of tax revenues (or total revenues) per capita and another based on expenditures-revenue equalisation of municipal budgets when a part of the fund is distributed in accordance with revenue per capita criteria and the rest — in proportion of the difference between normalised expenditure and revenue forecast.

In conclusion we can mention that the Kaliningrad oblast is open to the further development of inter-budgetary relations and the law "On the Financial Basis for Municipal Self-Governance in all Russia Federation" creates all necessary conditions for this process.

#### ***4.2.2 Financial support from the Federal Budget***

The Kaliningrad oblast is the region that receives the financial support from the federal budget and in particular from the Federal Fund for the Financial Support of Regions - Subjects of the all Russia Federation (FFSR). In 1994 the regional budget received from the FFSR for the amount of 32493 mln. Rbl. or 15% of the total budget revenues. In 1995 the amount of financial transfer was 161590 mln. Rbl. or 11.6% of the total revenues and in 1996 the regional budget received 189118 mln. Rbl. or 9.5% to total revenues (the regional share of the region in FFSR was fixed at the level of 0.8834%). The law "On the Federal Budget for 1997" envisaged the share for the Kaliningrad oblast to be 0.5026%. So, from the actual size of FFSR in 1997 that was 32658.1 bln. Rbl. and taking for granted that the financial support was distributed following fixed shares, in 1997 budget of the Kaliningrad oblast was to receive 164139.6 mln. Rbl. The law "On the Federal Budget for 1998" envisages the share of the oblast in FFSR in 1998 at the level of 0.4525%. If revenues of the federal budget constitute the planned amount this share will mean 150 - 155 bln. Rbl. in old prices.

The size of financial support in the form of transfers from FFSR has been continuously falling during the four years of the FFSR existence. The fall of the regional share in FFSR in 1998 - 0.05 percentage points in comparison with 1997 and by 2 times in comparison with 1995 - cannot be explained by objective reasons as tax performance in 1996 has not improved and the calculation of federal transfer was made on the basis of 1996 tax revenues. It is evident that the decrease of the oblast's share is the consequence of discussions of the law on the federal budget during its approval in the State Duma. This may be proved by the fact that the draft budget that was introduced by the Government to the Duma envisaged the share of the Kaliningrad oblast in the FFSR at the level of 0.63% which exceeds the same for 1997. This situation once more makes us pay attention to the main drawback of the present system of the FFSR distribution - the absence of transparency at the stage of its final approval in the State Duma. It is clear that the final approval of the regional shares in FFSR is made without taking into account the formal calculations of the MinFin that are submitted to the Duma but according to current political needs of the deputies. All regional shares in FFSR were changed after four readings of the budget law in the Duma and the majority of these shares were changed by 1.5-2 times.

The principles of FFSR distribution for 1998 are as follows. The calculations are made on the basis of actual reported data for the base year in conditions of 1996 and in prices of 1998. MinFin used normative expenditures in its calculations and if the normative rate has not yet been approved for an expenditure item, it is calculated from the payroll fund for 1993 inflated to 1996.

The calculations of regional shares in FFSR include several stages. At the first stage budget revenues per capita are replaced with average budget revenue per capita for the respective group of regions (all regions are divided into 3 groups) if the former is less than the latter. The right to financial support from FFSR is accorded to all the regions where expenditures exceed revenues. The share of the region is calculated in proportion to the estimated deficit.

At present a working group on the development of interbudgetary relations of the Commission for the Economic Reform under the Government is discussing several new approaches to FFSR distribution. The main ideas of the interbudgetary relations reform in Russia is, firstly, to make the whole process transparent and secondly, to make the amount of financial support fit the real financial needs of the regional budgets. It is worth mentioning that there are several draft concepts of inter-budgetary relations, among which we can single out two major directions: FFSR distribution in order to equalise regional budgets' revenues so that it won't be less than a normative revenue per capita and calculating financial transfers in proportion to the difference between estimated own revenues and normative expenditure of the regions.

The estimation of the results of applying of the first variant on the Federation level is now impossible for the reason of the lack of statistical information on several regions. Thus, the results of the analysis cannot be used for comparative analysis in our case. The second variant of the FFSR distribution method, the one which has a high degree of probability and which will be introduced from 1999, is the method of expenditures/revenues equalisation with additional support for depressed regions developed by IET experts.

The method includes two stages: at the first stage the part of the FFSR is allocated among depressed regions in order to maintain the maximum deficit of their budgets at the level of 50% to expenditures. At the second stage the rest of the Fund is distributed among the regions in proportion to their estimated deficits after receiving the first part of the transfer. In other words, depressed regions receive financial transfer from FFSR in two parts: first supplementing their budgets in order to make the deficit not less than 50% to expenditures and second a funding that by its nature resembles the financial transfers under the existing system of FFSR allocation.

The calculations of transfers under the existing and draft methods of FFSR allocation are as follows. Under the existing method, the oblast is to receive a transfer of

212.4 mln. Rbl. or 0.63% of the FFSR amount and according to the draft method the sum of the transfer is 1.5 times less and constitutes 154 mln. Rbl. or 0.46% to the FFSR amount. This decrease could be explained by the special approach to depressive regions, that require one-third of the Fund to support their deficit on the 50% level (the Kaliningrad blast is not included in depressed regions). But on the other hand the second result matches the share of the oblast in FFSR, approved by the budget law for 1998 (0.45%). This coincidence (and the further analysis of the full range of regional shares in FFSR) shows that the process of FFSR re-distribution in the Duma is aimed at the assignment of higher financial support to the high-deficit regions.

So, the primary analysis of relations between the Kaliningrad oblast's budget and the federal budget shows the gradual decrease in the financial transfers from central government with no ground for its raising<sup>1</sup>. That is why, while financing expenditures and making assessments for draft budgets regional authorities must account first of all on the internal resources of the oblast, thus not expecting significant financial support from the federal budget in the form of transfers from FFSR. Talking about internal resources it must be mentioned that raising additional funds cannot be performed by serious tax revenues increase, but by restructuring of regional expenditures, primarily - implementing housing reform.

### **4.3 Expenditures of regional and municipal budgets**

#### ***4.3.1 Budgets' spending execution***

The analysis of the budgetary policy in the Kaliningrad oblast aimed at the development of the set of recommendations to the regional authorities must be carried out from the positions of system approach. This implies taking into account both indicators on the consolidated regional budget, regional extra-budgetary funds, regional branches of federal extra-budgetary funds, information on federal and regional development programs in the oblast. Besides, one must consider the information on federal taxes, collected on the oblast's territory, on the tax advantages that exist in the oblast, on expenditure items that are financed from the federal budget. Such an approach

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<sup>1</sup> Raising of the amount of financial support to the oblast is impossible for several reasons: first, the planned transfer calculation on the basis of normative expenditures will lead, according to our estimations, to the fall in the oblast's deficit (first of all for the reason of the decrease in the normative expenditures on housing and communal services in comparison with actual data), second, new method of estimating future revenues will lead to the higher figures of revenues forecast in the next year (for the reason of improved tax performance in 1997), and third, a large number of regions with high deficits will extend the part of FFSR in their favor.

enables us to find drawbacks and to develop a program of optimisation of financial flows and to enable rational decisions an expenditure to be taken.

The structure of consolidated regional budget dynamics shows that in 1993-1996 the main expenditure item was expenditures in the social sphere. The share of this item in the total expenditures structure has risen from 34.9% in 1993 to 53.3% in 1996 (see Table 7). The share of expenditure on industry has fallen twice (from 50.9% to 25.4%). The draft budget of the Kaliningrad oblast envisages the opposite proportions of budget expenditures, and resembles the state of affairs in 1995. However, after comparative analysis of the two budget plans, for 1997 and for 1996, we may see that the difference in the planned expenditure structure is not very serious.

Table 7

**The expenditure structure of the consolidated regional budget in 1993-1997**

	Expenditure items	1993	1994	1995	1996(plan)	1996	1997 (plan)
	Total expenditures	100	100	100	100	100	100
1.	Economy	50,9	40,9	37,8	43,3	25,4	38,7
2.	Social sphere	34,9	40,5	49,4	47,3	53,3	48,0
3.	State authorities	2,6	3,3	4,1	3,2	4,3	3,3
4.	Other expenditures	11,6	15,3	8,7	6,1	17,0	10,0

It is worth mentioning that the approved budget plans in the oblast differ greatly from the actual budget execution. The expenditure plan of the consolidated budget of the Kaliningrad oblast for 1996 was executed only by 75% and on the financing of industry - by 48% (see Table 8). The situation is worse for the regional budget of the oblast: its execution was about 70% and on the financing of industry - 25%. We can also observe the same state of affairs in the first half-year of 1997: the budget execution constituted less than two-third and as far as industrial financing - was 13%.

Table 8

**The expenditure structure of the consolidated budget of the oblast in 1996, %**

		bln. Rbl.	%	bln. Rbl.	%	% to the plan
	Total expenditures	1977,1	100	1458,6	100	73,8
1.	Economy	858,0	43,4	474,9	32,9	55,3
2.	Social sphere	933,8	47,2	785,6	54,0	84,1
3.	State authorities	63,9	3,2	64,1	4,4	100,3
4.	Other expenditures	121,4	6,1	124,0	8,5	102,1

### 4.3.2 Social expenditures

The budgetary financing of the social sphere is in the following condition (see Table 9). During 1993-1996 the share of social expenditures in the total expenditures of the consolidated budget was growing and by now it had reached the level of 53% against 35% in 1993. The shares of expenditures on education, healthcare, social policy are growing and at the same time there is a constant redistribution of resources inside the item. The share of educational expenditure is slightly decreasing, remaining on the level of about 50% of total social expenditures. The shares of expenditures on healthcare and sport are also decreasing but more sharply. By their account the share of social police expenditure has risen more than four times.

Table 9

#### The social sphere expenditure dynamics

	1993		1994		1995		1996		1997 (draft)	
	bln. Rbl.	%	bln. Rbl.	%	bln. Rbl.	%	bln. Rbl.	%	bln. Rbl.	%
Social sphere	63,4	100,0	233,0	100,0	553,9	100,0	784,4	100,0	1144,	100,0
		34,9		40,5		49,4		53,3	8	48,0
Education	33,8	53,3	122,0	52,4	265,3	47,9	387,9	49,5	528,9	46,2
		18,6		21,2		23,7		26,4		22,2
Health-care and physical culture	24,9	39,3	79,4	34,1	179,1	32,3	240,6	30,7	406,7	35,5
		13,7		13,8		16,0		16,3		17,1
Social policy	4,5	7,1	2,5	30,9	13,3	5,4	107,9	19,5	153,6	19,6
		2,5		13,3		5,4		19,5	207,4	18,1
						9,6		10,4		8,7

The change in the tendency from the growth of the social expenditures in 1997 to the decrease is quite visible. If we look at the plan of the social expenditures for 1997 it constitutes 47.2% to the total expenditures (see Table. 10).

The adoption of an unrealistic budget law leads to the serious re-distribution of resources among various expenditure items during its execution. For instance, the share of expenditures on health-care and physical culture increased in comparison to the plan both in 1996 and in the first half-year of 1997. In the same time relative expenditures on



social policy were lower than in the plan in the regional budget and higher in the consolidated regional budget.

The analysis of social expenditures in the Kaliningrad oblast showed that its level is lower than in the regions with the same economy structure (estimated by the relation of the volume of industry production to the volume of agricultural production, see Table 11).

Table 10

**Execution of regional budget's expenditures in 1996 - first half-year of 1997 and of consolidated regional budget's social expenditures in 1996**

Item	Plan for 1st half-year (%)	Execution of 1st half-year (%)	% execution	Plan for 1996 (%)	Execution on 1996 (%)	% execution	Consolidated plan for 1996	Execution on (consolidated), 1996,%	% execution
Education	16309 (17,6 3,4)	13583 (19,9 4,5)	83,3	42127 (22,6 6,4)	23032 (16,8 5,1)	54,7	432388 (46,3 21,8)	352304 (44,8 24,3)	81,5
Culture and art	8474 (9,1 1,8)	5206 (7,6 1,7)	61,4	13747 (7,4 2,1)	15057 (11,0 3,3)	109,5	41134 (4,4 2,1)	38246 (4,9 2,6)	93,0
Health-care and physical culture	50790 (54,8 10,7)	40478 (59,4 13,5)	79,7	82581 (44,5 12,6)	76853 (56,0 16,9)	93,1	284093 (30,4 14,4)	242157 (30,8 16,7)	85,2
Social policy	17097 (18,4 3,6)	8845 (13,0 3,0)	51,7	47093 (25,4 7,2)	21996 (16,0 4,8)	46,7	176222 (18,9 8,9)	152866 (19,5 10,5)	86,7
Total social expenditures	92752 (100,0 19,6)	68112 (100,0 22,7)	73,4	185625 (100,0 28,2)	137213 (100,0 30,1)	73,9	933837 (100,0 47,2)	785573 (100,0 54,1)	84,1

This could be explained mostly by the population structure of the oblast. The average age of the oblast's residents is 33.3 for male and 39.1 for female. The predominance of this age and the relatively low share of old people and children (residents over 60 and younger than 15 constitute about one-third of total population) is the reason for the low level of social expenditures.

The important reason for the relatively low level of expenditures on education and health-care is the high concentration of population in the cities. The proportion of the urban population in 1995 exceeds the rural population of the oblast. It is evident that under such population structure the expenditures on health-care and education are

comparatively low. In spite of the present situation the regional authorities may face the problem of social expenditures growth in the following 10 years. The problems of social reform in the region can be found in the other sections of this chapter:

Table 11

**Social expenditures in the Kaliningrad oblast, in the regions with the same structure of economy and in the all Russia Federation in 1997**

	Ratio industry/agriculture	Social expenditures per head	incl. social policy expenditures per head	incl. education expenditures per head	incl. health-care expenditures per head
all Russia Federation	5,0	1079,7	180,8	484,7	337,9
Leningrad oblast	3,0	749,6	125,0	346,4	226,1
Novgorod oblast	3,1	851,9	177,2	421,3	188,8
Ivanovo oblast	3,2	747,0	148,0	303,2	261,5
Chuvash Republic	2,9	765,0	135,0	360,7	198,4
Astrakhan oblast	2,9	861,5	142,5	388,8	289,4
Republic Tatarstan	3,5	1296,5	64,0	598,3	525,8
Rostov oblast	2,9	651,0	132,9	287,3	197,3
Omsk oblast	2,9	1088,4	200,5	448,3	335,8
Republic Khakassiya	3,1	1060,8	204,7	491,3	301,6
Buryat Republic	3,0	1007,3	166,5	526,3	255,3
Kaliningrad oblast	3,2	838,4	164,2	373,9	239,3

### 4.3.3 Expenditure on the economy

The situation with the expenditures on the economy in the Kaliningrad oblast is as follows (See Table 12). In 1993 - 1996 the share of this expenditure item in the total expenditure of the consolidated regional budget fell twice from 50.9% in 1993 to 25.4% in 1996. But in the same time the expenditures on public transport, road repairs, communication and informatics have been rising in 1993-1995 and on the other items we can observe a dramatic decrease.

The re-distribution of the consolidated budget expenditures on the economy can also be observed. The share of housing expenditure has been rapidly growing and in 1996 reached the level of 75.8% of total expenditure on the economy against 52.9% in 1993. In other words compensation of housing costs absorbs all resources allocated for the development of the economy. The degree of budget law execution for expenditures on the economy is lower than for social sphere. The level of execution for this item in consolidated budget is 55.4% and in regional budget it constitutes 24.9%. In the first half-year of 1997 the financing of the item in question was 12.9% of the plan.

Table 12

## The expenditures' on economy dynamics in 1993 – 1997

Expenditures	1993		1994		1995		1996		1997 (draft)	
	bln. Rbl.	(%) *	bln. Rbl.	(%) *	bln. Rbl.	(%) *	bln. Rbl.	(%) *	bln. Rbl.	(%) *
Economy	92,6	100,0	235,6	100,0	423,4	100,0	374,0	100,0	922,3	100,0
Housing	49,4	50,9	155,0	40,9	291,3	37,8	283,5	25,4	652,3	38,7
Agriculture	26,1	27,2	38,3	26,9	65,5	26,0	31,8	19,3	172,7	27,4
Transport, roads, communication, informatics	1,9	14,4	8,1	6,7	36,4	5,8	40,6	2,2	47,7	7,2
Industry, energy, construction	(1,7)	2,1	(27,4)	3,4	(113,2)	8,6	(127,6)	10,9	47,7	5,2
		1,0		1,4		3,2		2,8		2,0
	15,2	27,3	34,2	14,5	28,8	6,8	16,3	4,4	46,6	5,1
		16,4		5,9		2,6		1,1		2,0

\*First figure is a share of the expenditure type in total expenditures on economy and the second - its share in the total budget expenditures/

Table 13

## The financing of expenditures on economy of the regional budget's in 1996 - first half-year of 1997 and of the consolidated budget - in 1996

Item	Plan for 1 <sup>st</sup> half-year (%)	Execution of 1 <sup>st</sup> half-year (%)	% execution	Plan for 1996 (%)	Execution on 1996 (%)	% execution	Consolidated plan for 1996	Execution (consolidated), 1996, %	% execution
Industry, energy, construction	3,4	13,3	50,7	5,6	23,0	102,4	3,9	3,4	48,8
Agriculture	1,3	1,0	23,8	1,3	2,0	31,1	1,7	1,1	38,7
Transport, roads, communication, informatics	36,4	67,3	128,8	35,8	44,6	28,6	9,9	6,9	72,7
Housing	13,7	5,2	0	8,4	3,8	6,6	4,3	2,3	56,3
	0,1	8,4	2,4	10,0	11,4	79,6	6,6	8,6	56,3
	0,0	0,6		2,4	1,0	2,9	2,9	2,8	
	60,1	11,0	48,6	21,0	10,8	79,6	80,1	56,3	
	22,7	0,8	11,5	1,8	34,5	26,5	26,5		
Total on economy	100,0	100,0	12,9	100,0	100,0	24,9	100,0	100,0	55,4
	37,7	7,7	23,6	8,5	43,3	32,7			

\*First figure is a share of the expenditure type in total expenditures on economy and the second - its share in the total budget expenditures/

The expenditures on the economy in the Kaliningrad oblast (the same as for social expenditures) are among the lowest in the group of regions with the same economic structure. Besides, the special feature of the oblast is the comparatively low level of expenditures on industry while it prevails in the oblast over agricultural sector - the industrial production exceeds agricultural one 3.5 times, and the number of employees - more than 2 times.

Table 14

**The expenditures on economy in the Kaliningrad oblast, in regions with the same economic structure and in the all Russia Federation in 1996**

	Expenditures on the economy	Industry and energy sector	incl. Subsidies	Agriculture	incl. Subsidies	Transport, roads, communication, informatics	incl. Subsidies	Housing	incl. Subsidies
all Russia Federation	5,9	0,5	0,3	0,7	0,3	0,7	0,5	3,9	1,9
Leningrad oblast	6,8	0,2	0,1	0,4	0,4	0,6	0,5	5,5	4,0
Novgorod oblast	8,3	0,1	0,1	1,3	1,1	0,8	0,6	6,1	5,4
Ivanovo oblast	7,3	0,1	0,0	1,5	0,7	0,7	0,6	4,9	1,6
Chuvash Republic	6,1	0,4	0,4	1,2	0,7	1,3	0,9	3,2	2,7
Astrakhan oblast	8,0	0,5	0,4	0,6	0,4	0,5	0,4	6,3	2,2
Republic Tatarstan	8,9	0,7	0,1	3,9	0,6	0,7	0,5	3,3	0,8
Rostov oblast	5,1	0,7	0,7	0,3	0,1	0,6	0,5	3,5	1,4
Omsk oblast	6,0	0,5	0,5	1,2	0,9	0,7	0,5	3,6	2,2
Republic Khakassiya	6,2	0,4	0,3	1,5	0,1	0,5	0,5	3,9	1,9
Buryat Republic	7,3	0,2	0,0	0,8	0,2	0,7	0,1	5,5	4,0
Kaliningrad oblast	5,1	0,2	0,2	0,4	0,3	0,6	0,6	3,9	3,1

Expenditures on transport and communication consists only of the subsidies and transfers. In this connection it may be important to individual compensation transfers.

#### 4.3.4 Expenditures on housing

Between 1993 - 1996 the spending on housing in the Kaliningrad oblast went down from 27.2% of the overall volume of spending to 19.3%. In 1997 it was envisaged that the spending on housing would have made up 27.4%. At the same time the situation in the housing sphere is complicated. An insufficient volume of financing, low

level of collection of payments and taxes due cause debts to the housing enterprises. At the same time one may note a non-rational, economically non-grounded use of the earmarked financial resources, an insufficient control over the use of them. The situation with the financing of this branch is subject to deterioration because of the large numbers and categories of the population who benefit from housing subsidies. This results in the fact that more than a half of citizen's occupants enjoy benefits with regard to payment for their housing. The pace of pursuance of the housing reform in the oblast needs to be thoroughly grounded, but this has not been yet done.

The main objectives of the housing reform are:

- providing the oblast population with housing standards meeting quality standards;
- diminishing production costs with regard to maintenance and refurbishment, leading to lower costs;
- the elaboration of efficient social protection mechanisms which are designated for moderating the population's transition to the non-subsidised functioning of the housing sector.

Implementation of the identified objectives is determined by a resolution of a number of priorities which must be resolved in the frame of the regional housing reform, of which the main tasks are:

- perfecting the system of management of the oblast's housing;
- promoting a competitive environment in the field of provision of housing services, providing a transition to the system of contractual relationships;
- perfecting the system of payments for housing services and social protection, regulating the system of benefits.

The perfection of the management is aimed at increasing the role of the local self-governance bodies and increasing the independence and responsibility of economic agents. One of the crucial aspects of the perfection of the housing management is the division of proxies of contractor and customer with regard to providing housing services.

The promotion of competition should encourage a reduction of the negative impact of the housing companies' monopolist position and provide the customer with an opportunity to select a contractor for necessary services and work, proceeding on from price and quality factors.

The transition to a new price-setting which is to eliminate the price gap between the housing sector and other industry branches should be implemented gradually, taking into account the whole complex of social factors. At the same time the purpose is not to mechanically increase the population's payments, but to increase their respective share in the process of creating stimuli to reduce costs for the maintenance of the housing sphere. The social protection measures comprise restrictions of a maximum share of the

population's own resources spent on housing and utilities relative to (in percentage terms) the family's total income within social norm margins.

Reform of housing is an extremely important stage of the economic reform yet because the budgetary subsidies in that sphere make up rather a significant part of public spending, the optimisation of the budgetary spending on housing must be carried out in two directions: firstly, a control over the natural monopolies' tariff policy is required and, secondly, a steady increase in the share of the population's expenses on housing maintenance is required.

The experience of a pursuance of a comprehensive evaluation of the financial and economic performance of the natural monopolies' subjects in St. Petersburg accomplished by the auditor company "Marketing Consulting Design" and the consulting company "Business" fond "Qualitet" showed that there are substantial reservations in place with regard to reducing the said subjects' current costs. At the same time, one speaks rather about inefficient use of financial and other resources than about lowering tariffs.

Whereas the housing sector is the largest consumer of the natural monopolies' services, the problems of interaction between the regional authorities and authorities controlling the subjects of natural monopolies are a core matter of the budgetary financing of this branch. In connection with this, in course of pursuing housing reform, prior attention must be paid to the following problems of formation and implementation of the regional policy in the sphere of natural monopolies:

1. A lack of a single executive body responsible for elaboration and implementation of the regional policy in the said sphere, which must perform (in addition to other duties) data collection and processing and co-ordinate other authorities' activities.

2. A lack of a strategy of regional development and elaboration of objectives (including the sphere of industry, transport, house building, etc.) which results in an uncertainty in the problem of investment required for developing the natural monopolies' subjects.

3. Normative set standards for the provision of services by the subjects (quality of services included) are to a significant extent obsolete and do not meet modern social and economic requirements.

4. The accumulating outstanding budgetary indebtedness to the natural monopolies' subjects, which needs to be restructured and separated from the current budgetary obligations.

5. Conflict of interests at the regional level:

- on the one hand, the regions is a regulator of the activities of the natural monopolies' subjects;

- on the other hand, the region is one of the largest debtors to every subject of natural monopolies;

- at the same time, the region is an owner of the property used by the majority of the subjects of natural monopolies.

The region, being a regulator of the activities of the natural monopolies' subjects, should aspire to decrease the prices for consumers while keeping the quality of services provided ( lowering respective costs with the set quality). Being the largest debtor, the region has to aspire to delay the term of payment which results in price rises and the cross- financing of different groups of consumers. As a proprietor, the region has to care for the maintenance and revenues from use of that property. In the light of this, the oblast finds it profitable to have the depreciation deductions and leasing payment rising, though that may entail either a price rise with the unchanged volume of services provided, or a growth in the volume of consumption of the said services while the tariff remains stable.

1. The growing outstanding liabilities of natural monopolies services' consumers on the background of lacked mechanisms of negotiation and claiming of the liabilities which results in:

- drop in liquid assets and price rises;
- non-guaranteed issuing credit to consumers;
- undue initiation of the procedures relating to the consumers' actual insolvency;
- authorities' economically inexpedient and irresponsible interfering in the matters relating to the bilateral relationship between suppliers and consumers-debtors.

2. The current system of budgetary subsidies allocated to the subjects of natural monopolies is not economically and socially justified, since it is orientated to the supplier of services, and not to the specific consumer which needs a support, and this leads to a constant growth in the volume of such subsidies, given that their efficiency is low.

3. A lack of an efficient mechanism for the separation of the maintenance budget from the investment budget of the subjects of natural monopolies, which results in the regional authorities' inability to manage investment processes.

4. Incomplete natural account of resources consumed and services provided by the subjects of natural monopolies which, together with imperfect methodology of calculating them, consumption normatives and obsolete apparatus base, results in inadequacies in planning and price -setting.

5. Imperfect accounting policy and technology against the background of a practical lack of managerial accounting inherent in the natural monopolies' subjects, which results in inadequacies in planning and price -setting.

6. General lack of stimuli and incentives to lowering costs, failure to introduce resource- saving technology and tender-based placement of orders and contracts. Lack of government support to resource- saving programs. Lack of government efforts to organise tender procedures.

7. Lack of an actual regulation of contracting relations between the subjects of natural monopolies and consumers of their services which results in unprofitable and unfair essential terms concerning the respective contracts which therefore become a burden to the customers.

8. Considering that the payment for the services provided by the subjects of natural monopolies is in fact (by its economic nature) pseudo-analogous to the individually consumed public wealth, the current taxation system entails a payment of taxes from taxes (i.e. double taxation).

9. Lack of strictly defined rules of interaction between the state bodies and the subjects of natural monopolies established in various institutional and legal forms, relationship with management of the said subjects.

10. Imperfection (contradictions and inadequacies) of the Federal and regional legislation in the sphere of regulation of the activities of the subjects of natural monopolies (including the methodology of regulation, taxation, price-setting, etc.)

Hence, a strict setting and resolution of the tasks in the aforementioned problematic fields, taking into account of the specifics of the Kaliningrad oblast, require, first and foremost, an implementation of a comprehensive evaluation of the subjects of natural monopolies and elaboration of recommendations on formation and pursuance of the respective regional policy.

The other aspect of the housing reform, which is not less crucial than the above-mentioned one, is a step-by-step increase in a share of the population expenses on housing maintenance. The transition to the population's complete payment for the services provided by the housing enterprises, given that the social guarantees for the poorest strata are kept, would particularly lead to resolving the current paradoxical situation, in which less money is paid for a better housing. The "Institute Ekonomiki Goroda" Foundation calculated the justified need in the budgetary spending on housing by the Subjects of the Russian Federation in 1998 (in prices as of mid-1997). Table 15. represents the results of the said calculation by the Kaliningrad oblast and RF as a whole.

The extrapolation of the present calculation onto the conditions of 1996 shows that (see Table 15.) one may economise almost Rbl. 80 bln. compared to the planned budgetary spending on the housing sector. However, the actually executed spending covers only 63.7% of the justified spending ( against 56.3 planned spending).

Because of the lack of data on stratification of the Kaliningrad oblast's population by the amount of the per capita income, we used the average data on the Russian Federation, with a correction to the overall value of the per capita income in the oblast in 1996. Upon receipt of the precise data, we would be able to analyse in detail possible variants of a change in the Administration's policy with regard to financing the housing sector. However the data available allowed us to built distribution models of the



monetary flows between the population and the budget. Such an approach allows us to observe a trend towards a change in budgetary spending and an increase in the share of expenses falling on the population, as long as different variants of the social protection of the poorest strata of the population are taken into account.

Table 15

**The requirements for direct budget expenditures on housing in 1998  
(in the mid-year prices of 1997)**

	Kaliningrad oblast	Russian Federation
Nominal Personal Income (thousand Rbl. per month)	653,3	841,1
Coverage of costs at the account of individuals' payments (%)	50	50
The share of families entitled to subsidies according to estimation made on the grounds of the requirements for budget expenditures on housing (%)	49,6	30,1
The requirements for direct budget expenditures on housing (mln. Rbl.)	49812	6808071
The requirements for the compensations of preferences (mln. Rbl.)	4981	680807
The requirements for subsidies (mln. Rbl.)	12142	1033655
The requirements for direct monthly budget expenditures on housing (mln. Rbl.)	68149	8625899
The requirements for direct annual budget expenditures on housing (mln. Rbl.)	817788	103510783

Let us analyse possible variants of the increase in a share of the population's payments in the overall volume of financing the housing sector. In addition to that, it is understood that population stratification by income is constant. During the next stage of the present research we may reject these rather strict assumptions; however, to do that, one needs to conduct an additional survey.

1. The share of the population makes up 50% of spending on housing.
2. The share of the population makes up 60% of spending on housing.
3. The share of the population is increased up to 75% of spending on housing.

At the same time, three options are considered for each of the above mentioned variants: the population spends on housing services and utilities not more than 15%, 20% and 25% of their income, respectively.

The first variant, in the situation in which the population spends not more than 15% of their income on the housing sector's services, practically coincides with the respective calculation of the "Institute Ekonomiki Goroda" Foundation. Apparently, the discrepancies were caused by a lack of information-data on a stratification of the population in the Kaliningrad oblast by income groups and housing needs, in a situation in which the level of the social protection of the population is naturally declining (the level of the population's minimum housing payment rate grows up to 20 and 25% of the family's total income), the value of subsidies allocated to the population is going down,

thus decreasing the need in the budgetary spending on the housing sector. However, the probability that the majority of the population would not pay at all rises must be taken into account. Due to this, the budget's potential losses may become superior to the value of the benefits resulted from the reduction in subsidising. The second variant entails, of course, a substantial economy for the budgetary resources (a total of a Rbl. 90 mln.) forwarded directly to the housing sector and in a growth (approximately 1.5 times) in the volume of subsidies for each of the cases in question. At the same time in view of the budgetary spending, the case of the 15% limit of the population's income is an intermediary case compared to the cases of 20 and 25% limits for the first variant. The last variant results in a reduction of the budgetary resources due to be directly allocated to the housing sector, which is still at Rbl. 135 bln., but this variant also provides an increase (over 1.5 times) in the subsidies which one needs to allocate for the purpose of compensating for the costs of the housing services provided to the poorest strata of the population.

Table 16

10 Schemes of budget expenditures on housing in 1996 (bln. Rbl.)

	Plan	Institute for the economy of a city	1 scheme (50%)			2 scheme (60%)			3 scheme (75%)		
			15%	20%	25%	15%	20%	25%	15%	20%	25%
Total expenditures		scheme	897,8	897,8	897,8	897,8	897,8	897,8	897,8	897,8	897,8
Direct budget expenditures			448,9	448,9	448,9	359,1	359,1	359,1	224,4		224,4
Expenditures of individuals			448,9	448,9	448,9	538,7	538,7	538,7	673,4	673,4	673,4
Subsidies			109,4	102,7	70,7	49,5	150,4	108,4	79,7	231,4	176,3
Preferences compensation			44,9	44,9	44,9	44,9	44,9	44,9	44,9	44,9	44,9
Requirements for budget expenditures	682,6		603,2	596,5	564,5	543,3	554,4	512,4	483,8	500,8	445,6
											404,9

Hence, the transition to a more complete payment for the housing services by the population leads to a substantial economising of the budgetary resources. At the same time, a pursuance of a sound social policy in this field allows us not to hamper the interests of the poorest strata of the population, whose real spending on the housing maintenance remain on the affordable level at the expense of targeted subsidies. The

economising of budgetary resources is made at the expense of a growing rental payment for the elite housing made by that part of the population which can afford it.

Some increase in the share of the population's spending in the overall volume of resources in the housing sector does not have a substantial impact on the general situation (proceeding on from the data available). Naturally, the volume of subsidies will be growing.<sup>2</sup> However, the calculations showed (it may become possible to establish this in course of further work and receipt of additional data) that the growth in subsidies allocated for the poor strata, with a change in the share of the population's capital due to the housing sector, is well compensated by a decrease in the budgetary capital earmarked for the respective expenses. It should be noted that should the housing sector's services be paid for by the population at a full scale, the volume of subsidies for the three cases in question would amount to Rbl. 382.8, 308.6 and 250.6 bln., respectively. At the same time, the subsidies would be granted to the majority of the population (with the 15% limit - 72.6 % of the population, 25% limit - 53.9%)

The results we have gained are based on rather strict assumptions and the data available at the moment. That is why we may consider only the main trends revealed in the course of the research. Better substantiated findings with regard to the analysis of a housing reform and may be achieved only with the use of a more scientific sociological survey on the population. In addition to this, in order to achieve a really qualitative elaboration of proposals on the respective issues, it will be necessary to consider separately local budgets, the oblast's budget and the balance sheets of enterprises directly tied to the housing sector.

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<sup>2</sup> The volume of subsidies provided to the population may be reduced at the expense of pursuing a sound policy on providing cheaper housing (for instance, of a smaller living area) to the poor strata of the population.

