

@DECENTRALIZATION AND RECENTRALIZATION: RECENT DEVELOPMENTS IN RUSSIAN FISCAL FEDERALISM

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1. INTRODUCTION

This study represents the third and final report in a three-phase series of reports. In the first phase undertaken under the joint supervision of Professors Robin Boadway and Ronald Watts on behalf of the Institute of Intergovernmental Relations at Queen's University, four studies were undertaken on intergovernmental fiscal relations in Canada, the United States and Germany, the fourth being a comprehensive comparative overview of these three examples. In the second phase, a study of intergovernmental relations in eight further countries was undertaken. The resulting report covered two mature developed federations, Switzerland and Australia, four transitional federations, Brazil, India, South Africa and

Spain, and two decentralized unitary systems, Sweden and Japan. That report also included comparative references to the three mature federations covered in the earlier first phase. This current report represents the third and final phase of the project. It is a comparative review of the evolving institutional relationships within the Russian Federation, comparing these to the countries covered in the previous studies.

The previous reports identified both a number of common patterns and some significant variations among the various federations and decentralized unitary states. In all nine federations and two decentralized unitary systems, there has been a greater decentralization of expenditure responsibilities than of taxing powers. The former were relatively decentralized both for administrative efficiency and in the interests of subsidiarity and governmental accountability. On the other hand, revenues have been relatively more centralized in the interests of efficiency, of providing a base for redistribution among regional units, and of effective economic stabilization policy. The corollary of this situation has been the need in all these cases for substantial transfers by means of tax-revenue sharing and unconditional and conditional grants. There have, however, been variations in the degrees and extent of expenditure decentralization and of revenue centralization and hence in the size and composition of the transfers.

A second pattern common to every case has been the existence among constituent units of considerable horizontal disparities, and hence the establishment in all these cases (except the United States) of systematic equalization transfers. These too have, however, varied in form and scope.

A third common pattern has been the prominence of political factors in influencing the shape of intergovernmental financial arrangements. Despite the useful analyses of such economic theorists as Musgrave, Oates, McLure, Buchanan and Boadway, actual arrangements have been determined less by

normative economic theory than by political compromises.¹

Within these common patterns noted above, the previous reports in this series have, however, noted wide variations in the eleven countries examined. Interestingly the differences among federations appear to be wider than those between the federations and the decentralized unitary systems. Variations among federations in the constitutional and political context have had a particularly significant impact on the financial arrangements. These have included variations in the degrees of internal homogeneity or diversity, in the degrees of relative constitutional centralization and noncentralization of legislative and administrative jurisdiction, in the extent to which central legislation is administered by constituent units, and in how far constitutional jurisdiction is exclusive to each government or concurrent.

As a result, in the allocation of combined governmental expenditure responsibilities, the constituent unit share has varied from the more centralized examples (e.g. Brazil 36 percent, Australia and the United States each 46 percent) to the more decentralized (e.g. Canada and Germany each 63 percent and Switzerland 68 percent). These are substantial differences. Interestingly the two decentralized unitary systems fall within the same range (e.g. Sweden 43 percent and Japan 62 percent). Similarly, there are considerable variations in the degree of 'own source' revenues (before receipt of revenue-sharing and grant transfers) assigned to the constituent units. These range widely among federations from the least decentralized (e.g. South Africa 5 percent and Spain 17 percent) to the more decentralized (e.g. Canada 56 percent and Switzerland 60 percent). The unitary systems (e.g. Sweden 43 percent and Japan 42 percent) again fall in the middle of the range. Not surprisingly therefore, the gap between 'own source' revenues and expenditures

requiring correction by transfers also varies considerably, being largest in South Africa and Spain and lowest in Sweden, Brazil, Canada and Switzerland.² This has resulted in considerable variations in the percentage of state and local revenues constituted by transfers (made up by shares of centrally levied taxes and unconditional and conditional grants), these being highest in South Africa (96 percent) and Spain (73 percent) and lowest in Switzerland (25 percent), Canada (20 percent) and Sweden (16 percent).³ If as an indication of limitations on discretionary 'expenditure autonomy', we consider the proportion of constituent unit total revenues made up by conditional transfers, these have ranged from the highest (Spain 42 percent and United States 30 percent) to the lowest (Canada 16 percent, Germany 10 percent, Brazil 8 percent and Sweden 4.4 percent). In considering expenditure autonomy one must, of course, also take account of the extent of "unfunded mandates" occurring mainly where concurrent jurisdiction leads to lack of clarity in the distribution of jurisdiction. This is a feature that has become particularly significant in the United States, and has led some to describe the situation there as "coercive federalism".⁴

An interesting point about the comparison of the degree of expenditure and revenue decentralization in these eleven cases, is that in general the degree of decentralization in federations and in the two unitary systems does not differ significantly. The main difference is in the legal basis for that decentralization. While in the federations the allocation of expenditure responsibilities and a major proportion of their revenues are established by constitutions which are not unilaterally amendable by either order of government, in the unitary political systems these are derived from central legislation and therefore are established at the discretion of the federal government.

1. R. L. Watts, "Introduction: Comparative Research and Fiscal Federalism," *Regional and Federal Studies*, Special Issue on "Money Matters: Territorial Finance in Decentralized States," eds. Charlie Jeffery and David Heald, 13 (4) Winter 2003, pp. 4-6.

2. See Table 1, column 3.

3. See Table 2.

4. J. Kincaid, "From Cooperative to Coercive Federalism," *Annals of the American Academy of Politics*, 509 (1990), pp. 139-152.

While all of the countries examined, except the United States, have systematic financial equalization transfers, there is again considerable variation among them.⁵ In some, such as Australia and India, the equalization arrangements are integrated into the transfers correcting vertical imbalances, while in others such as Canada and Germany they constitute a separate distinct set of intergovernmental transfers. Some are based on measures of revenue capacity only, as in Canada, while others take account also of expenditure needs, as in Australia and India. The processes for setting and adjusting equalization transfers has also differed. In some the equalization transfers are based on constitutional formulae, as in Germany, in some upon the recommendation of independent commissions, as in Australia and India, in some upon intergovernmental negotiation of changes followed by federal legislation, as in Canada and Switzerland, and in some simply upon federal legislation, as in Nigeria and the decentralized unitary countries. Emphasis upon the criterion of equity might lead one to expect that the greater the inter-regional disparities within a federation the greater is likely to be the scope and effort involved in correcting these through equalization transfers. Comparisons of actual practice, however, lead instead to counter-intuitive conclusions. Australia and Germany, where the disparities are less, have done more to reduce these than Canada and Switzerland, where the disparities are greater. In the latter, it would appear that the political culture has placed a counter-balancing emphasis upon not undermining the political autonomy of the constitutional units.

In the previous reports assessment of the financial arrangements in the eleven federations and decentralized unitary systems were analysed in terms of both economic criteria (e.g. efficiency, equity and effective stabilization policy) and political criteria (e.g. relative revenue and expenditure autonomy of the

federated units, degree of central coordination and influence, democratic transparency and accountability, influence on political stability and adaptability). These indicate that the prevailing political culture and political compromises have often been a major factor shaping the variations in the intergovernmental financial arrangements, indeed even more so than variations in the technical arrangements.

2. DEFINITIONAL ISSUES

In turning to a comparison and assessment of the evolving intergovernmental financial relations in the Russian Federation compared to the eleven federations and decentralized unitary systems previously analyzed, there are some definitional issues that need first to be clarified if we are to ensure meaningful comparisons. These relate particularly to the definition of 'own source revenues', different kinds of revenue sharing, and different kinds of intergovernmental transfers.

First, in analysing relative federal and constituent unit expenditures, to avoid double counting and give an accurate and comparable analysis of relative expenditure responsibilities, we have throughout these reports compared the scope of federal and constituent unit expenditures after transfers. Intergovernmental transfers have, therefore, in each case not been included among federal expenditures.

Second, the meaning of 'own source revenues' needs to be clarified and applied consistently. Much of the Russian literature on intergovernmental fiscal relations seems to take a very broad interpretation including among 'own source revenues' the regional portion of shared tax revenues. Some German literature follows the same approach. The more general practice elsewhere, however, and that used throughout our previous reports has been to treat as 'own source revenues' only those taxes over which the federated units have legal control in setting the tax base and rates. That is, only where the federated units are accountable for the size of these revenues are they treated as 'own source revenues'. It is important here to take note of the

5. For details see Tables 5 and 6 in the previous report, R.L. Watts, *Intergovernmental Financial Relationships in Eight Countries: Final Report* (Kingston: Institute of Intergovernmental Relations, Queen's University, 2004), pp. 102-3.

distinctions between levying taxes (setting the base and rate), collecting taxes, and receipt of proceeds. It is the first of these that determines whether federated units control the level of taxation, thus constituting genuine 'own source revenues'. Where the federal government regulates the taxation, but a portion of the proceeds are transferred to the federated units or collected by them, these are more akin to intergovernmental transfers and therefore better classified as a form of transfer, than as the 'own source revenues' of the federated units.

As applied to Russia, Tables 3 and 4 (based on OECD analyses) provide accordingly a break-down of 'own source revenues', and of different categories of shared taxes regulated by the federal government and which, even in cases where collected by the federated units, are classified as transfers in the form of shared revenue receipts. When analyzed in this way in order to be consistent with the analyses in the previous reports, it becomes clear from Table 3 that by comparison with most other federations, the genuinely 'own source revenues' of the federated entities, are highly limited in the Russian Federation.⁶ This is so even though the collection of these may in comparative terms be more decentralized. The pattern in the Russian Federation contrasts with most other federations where the federated units have full constitutional or legal discretion to set the rates for a much wider range of taxes, and thus have considerably greater revenue autonomy.

Third, it is also important to note, that while in most federations, shared tax revenues constitute an unconditional transfer, that is not necessarily always the case. Where such transferred tax revenues are targeted, as for example in some cases in Switzerland, those are in fact a conditional form of transfer. Documents about the financial arrangements in the Russian Federation do not always make this clear,

6. See also Table 4 of this study, and also OECD, *Economic Survey of the Russian Federation* (Paris, France: OECD Publication Services, 2002), Table 37, and G. Kurlyandskaya, "Is Russia Ready for New Federalism?" (Moscow: The Gorbachev Foundation: Feb 2, 2004) Table 3.

although there are some instances of targeting of shared tax revenues.⁷

Fourth, another definitional issue is related to differing degrees of conditionality of transfers. Generally, in our previous reports financial transfers have been broadly categorized as unconditional or conditional. But a wide range in the degree of conditionality is possible. For instance, in the United States and Australia, conditional grants in aid to the federated units tend to be precisely targeted or have specific matching requirements which have a significant impact upon the setting of priorities in the constituent units. In Germany, a substantial portion of transfers represent funded mandates for federal legislation administered by the Länder. By contrast, in some other federations, conditional grants may take the form of block grants with only very general conditions. An example is the Canada Health and Social Transfer (CHST) for which the conditions are so general that the provinces are left with substantial discretion in their expenditure. These are substantial. They represent 14 percent of provincial revenues and by far the greatest part of the total 15 percent of provincial revenues constituted by conditional transfers. While these have been appropriately classed as conditional transfers in the previous reports in this series, it is important to recognize the differing impact upon the expenditure autonomy that flows from the differing degrees of conditionality within the category of conditional transfers.

Fifth, the distinction needs to be made between 'budgeted' figures and 'actual' figures. Much of the literature on intergovernmental financial relations in the Russian Federation focuses upon budget figures. But one must note the significance of actual revenues, expenditures and transfers and how far these differ from the budget figures. For example, in the case of Russia, there are the significant variations resulting from the fluctuation of oil revenues and

7. E. Andreeva and N. Golovanova, "Decentralization in the Russian Federation," (Moscow: Centre for Fiscal Policy, 2003, available online at <http://english.fpcentre.ru>).

from the extra-budgetary funds transferred to the federated units. Indeed the latter have led to concerns about the extensiveness of soft budget constraints which affect the behaviour and efficiency of the federated units and the federal government.⁸ The phenomenon of extra-budgetary transfers and resulting soft budget constraints appears to have been substantially greater in the Russian Federation than in the eleven other federations and decentralized unitary systems to which it is being compared. Indeed, while much of the literature about financial arrangements in the Russian Federation tends to focus on the formal budgetary arrangements as adopted in the reform programs, at least one study suggests that there still remains in practice a much higher degree of informal subnational autonomy which stands in contrast to the centralizing character of the evolving formal system.⁹ But if this is so, it is extremely difficult to measure accurately for comparative purposes the significance of these informal processes.

3. THE POLITICAL CONTEXT

In our previous reports, we have noted the importance of the political context in shaping intergovernmental financial relations in federations and decentralized unitary systems. By contrast with those as a group, a noteworthy feature of the Russian Federation over the period 1992-2005 has been the fluidity of the evolving intergovernmental relationships and the frequent and almost continuous negotiation and adjustments to these. In general terms, we may distinguish four distinct periods.¹⁰ The first of these followed the dissolution of the Soviet Union in 1991, and spanned the period 1992-3. In a situation of acute economic crisis, lack of

federal regulation of the distribution of authority between institutions at various levels, and the proclaimed granting of sovereignty to the federated units of the Russian Federation, there was a strong polarization between the federal government and the constituent units. In this context regions lobbied hard for larger shares of tax revenue and transfers while the federal government pushed down expenditure responsibilities to the regional level. The actual division of tax authority between federal, regional and local governments mostly followed bilateral negotiations. These negotiations typically favoured more politically problematic regions. Expenditure assignments were particularly unclear and unstable. The Federative Agreement of 31 March, 1992, included neither uniform provisions on the distribution of authority and economic responsibilities between levels of government, nor the mechanisms for the realization of these responsibilities.

The Constitution of 1993 marked the beginning of the second phase in the political and financial evolution of the Russian Federation lasting up to 1998. The new constitution strengthened the position of the federal government, and articles 71 and 72 formally set out the general competencies of the federal and subnational governments, stipulating that all entities were equal in their relations with the federal government. In the realm of financial relationships this resulted in attempts to introduce uniform norms for the distribution of the tax revenues between the federal government and the regions, and the allocation of a large share of federal transfers was moved to a new explicit formula-based Fund for the Financial Support of the Subjects of the Federation. But the subsequent practice during this period differed substantially from these formal arrangements. In the attempt to maintain the unity and territorial integrity of the Russian Federation, the federal government entered into numerous bilateral variations in the arrangements concerning the allocation of competences and finances which varied from the formal constitutionally stipulated arrangements. Indeed, by the end of this period the federal government had concluded bilateral treaties involving

8. S. Selenikov-Murylev, P. Kadstchnikov, I. Trunin, S. Tchetvenikov, "Budget Policies of Subnational Governments under Soft Budget Constraint," (Paper presented to Queen's University, Nov. 2004).

9. Aleksei Lavrov, J.M. Litwack, and D. Sutherland, "Fiscal Federalist Relations in Russia: A Case for Subnational Autonomy," Paris: OECD Centre for Co-Operation with Non-members, January 2001), pp.7-8.

10. I.V. Trounin, "Economic Reforms in the Early 1990s and Transition to New Principles of Federative Relations" (paper presented at Queen's University, Nov. 2004) combines the first two of these.

different arrangements with some 40 subjects of the federation, and 14 more were preparing such treaties, leaving only 35 which had neither concluded a bilateral treaty with the federal government nor were in the process of preparing one.¹¹ As a result, the intergovernmental financial arrangements had become arbitrary in character, depending heavily on the decisions of the federal Ministry of Finance and the lobbying capacities of individual regional leaders.

The third phase began in 1999 which marked the ending of the Yeltsin era in the Presidency and the beginning of the Putin era. The radical change in the political situation and a growing realization of the cost of the variety of informal financial arrangements that had grown during the preceding period, led during the period of 1999-2001 to comprehensive reform in the Russian intergovernmental financial relations. This was aimed at replacing the special fiscal and taxing powers to individual federated entities by a more uniform scheme. These reforms included new principles of intergovernmental financial assistance to the federated entities. The new methodology for distribution of equalization transfers was modified to use both an “index of budgetary expenditure” (reflecting interregional differentiation in cost of budgetary expenditure due to a variety of factors) and a “tax potential index”. In addition a compensation fund came into operation in 2001 as a form of targeted transfer to compensate the federated units for certain federally mandated expenditures. This was intended to reduce the problem of unfunded mandates which had become particularly serious. A feature of this period was the signing in 2001 and 2002 of agreements with 34 of the constituent entities of the federation terminating the previously concluded bilateral agreements on the division of authority and economic responsibilities.¹²

The fourth phase, 2003-2005, has been marked by the effort of the Putin regime to strengthen the relative role of the central government in order to resist the common

perception that the federal government had become too weak to enforce its own laws in the 1990s thus raising the threat of disintegration. The reassertion of federal powers has been exemplified by “super-presidentialism”, by the changed composition of the federal second chamber (the Federation Council), and by reverting from elected governors in the federated entities to their appointment by the President. This has in effect converted the federation into a quasi-federation. This has been accompanied by further comprehensive reform of intergovernmental financial relations aimed at state administrative reform, a clear delineation and definition of expenditure authority, the elimination of non-funded mandates, the development of objective and transparent mechanisms for federal financial assistance to region and local budgets, and federal control over possible financial mismanagement at the subnational level. In this process the Kazak Commission reporting late in 2002 played an important role leading to a full-scale legislative reform in 2003.

For comparisons with other federations and decentralized unitary systems, no effort will be made to compare directly each of the phases through which the political and financial arrangements have evolved over the period 1992-2005. Apart from noting the rapidity and fluidity of the changes within the Russian Federation that has contrasted greatly with the more stable and gradual evolution in other federations and decentralized unitary systems, the main focus of this report will be upon comparing and assessing the current intergovernmental financial arrangements as they have developed since 2000 with those in the eleven countries covered in our previous reports.

4. EXPENDITURE DECENTRALIZATION

Table 6 sets out the proportion of combined federal and regional expenditures (after transfers) that have been carried out by the federated entities in the Russian Federation over the period 1992-2003. By 2002-3 these appeared to have stabilized at around 50 percent. This is broadly similar to the transitional federations as

11. Trounin, op. cit. pp. 13-16.

12. Ibid., p. 16.

a group: Spain with 49 percent, South Africa percent, and India with 55 percent, but more than Brazil with 36 percent.¹³ It is slightly more than Australia, the United States or Sweden, each with 46 percent, but substantially less than Japan with 62 percent, Germany and Canada with 63 percent and Switzerland with 68 percent.

But certain features of the Russian situation are particularly significant. While over the period since 1992 some order and standardization on expenditure assignments has eventually been achieved, and the current assignments now roughly resemble the expenditure responsibilities of federated entities in other federations, these measures have not yet been sufficient to guarantee a workable degree of clarity and stability in the allocation of expenditures.

To begin with, from the formal point of view, current legislation still leaves many expenditure assignments unclear. Even the new Budget Code allows for rather wide areas of ambiguous 'joint' financial responsibility. A substantial share of specific federal legislation and regulation does not specify which level of government bears responsibility, or state that this responsibility belongs simultaneously to both levels. As a result, regional and local levels of government end up financing a part of expenditures formally under federal responsibility (including various federal programs and utilities and rents for federal institutions), while the federal government has, on many occasions, at least implicitly taken on responsibility for subnational finance (for example, wage arrears).

Second, given the high degree of disparity in the wealth of different regions, the delegation of virtually all social expenditures to the regional and local levels has meant that despite the equalization transfers, relatively wealthy regions have typically remained in a position of being able to provide higher income subsidies for their populations than the poorer ones. This has put pressure on the federal government to meet the

with 50 drastically different social needs of particular individual regions, hindering the uniformity and transparency of such policies.

Third, and perhaps most important, is the existence of unfunded mandates. Some progress has been made towards reducing these. The creation of the Compensation Fund for two of the largest such mandates together with a transfer of an additional 15 percent of the income tax revenues as compensation for a third has improved the situation. Furthermore, the new Budget Code has formally banned unfunded mandates. But in practice subnational budgets continue to be hampered by numerous unfunded federal mandates. Federal mandates continue to be interpreted by the population and also by the courts as obligatory objects of subnational finance. The position of the courts has derived from the ambiguous wording in federal documents to the effect that mandates are accounted for in the general calculation of federal transfers to the regions. But in reality these transfers have not come close to accounting fully for existing unfunded mandates, and there appears at present to be no study attempting to account for all unfunded federal mandates. The situation is accentuated by the fact that, unlike most other federations, Russian legislation, and in particular the Budget Code, contains references to federal expenditure norms that must be observed by all levels of government in forming their budgets. Furthermore, in the Putin era, the presidential decrees (ukazy), the Presidential envoys they have appointed to bring regional laws and administration into conformity with federal norms, and the replacement of elected governors by presidential appointees all represent a degree of federal regulation of administration in the federated entities to a degree not found in other federations and more typical of decentralized unitary systems.

Fourth, is the continued reliance upon extra-budgetary federal funding to make up shortfalls in budgetary funding of regional expenditures. The resulting degree of soft budget constraint upon the federated entities is far greater than in the other federations and has a significant impact

13. Table 2.

upon the transparency and accountability of

Thus, while in nominal statistical terms the level of regional expenditure in the Russian Federation is broadly comparable to that in many other federations, and particularly to the transitional ones, this assessment must take account of distinctive qualifications governing the exercise of the expenditure responsibilities of the federated entities in Russia. Instead, as a result, it would appear that in actuality the regional and local governments have had substantially less real discretion than the nominal 50 percent of combined expenditures would suggest. The federal government directly or indirectly has in reality had control over substantially more than 50 percent of the consolidated budget of the federation would suggest. The Russian Federation, therefore, has considerable distance yet to go to obtain the benefits of administrative efficiency and political accountability that have been achieved by the autonomy of decentralized expenditures in most other federations and decentralized unitary systems.

5. REVENUE CENTRALIZATION

It is in the allocation of control over revenues that the centralization of the financial arrangements in the Russian Federation becomes even clearer in comparative terms. Keeping in mind the definition of 'own-source' revenues referred to earlier in this report (and applied in the previous analyses of nine federations and two unitary systems), 'own-source' revenues of the regional units in 2000 amounted to a mere 17 percent. Of these, 11 percent constituted 'own-source' taxes and 6 percent 'own-source' non-tax revenue (see Tables 4 and 5). In the case of these 'own-source' taxes, the rates, tax bases and exemptions are set decentrally, but within a federal legal framework. The taxes within this category for regional budgets are: sales tax, property tax (enterprises), licenses and registration fees, and simple imputed income tax (personal). In the case of local governments the taxes within this category are municipal tax (up to 5 percent rate to the base of the profit tax, introduced in 2001), licenses and registration fees, property tax (persons), advertising tax,

regional governments for their expenditures. social infrastructure and other local taxes (mainly cancelled in 2000-2001).¹⁴

A further 57 percent of total regional revenues in 2000 came from shares of centrally regulated taxes, but because their bases and rates and sharing rules are totally or predominantly set by the federal government, they are more appropriately classed as transfers than as 'own-source' revenues of the regions.¹⁵

In comparative terms, the limited percentage of 'own-source' regional revenues is particularly striking. Only South Africa with a comparable figure of 3.9 percent is more centralized in the authority to regulate taxes.¹⁶ Moreover, as Table 3 indicates, in terms of 'own-source' revenues as a percent of total constituent unit revenues, the Russian Federation at 17 percent is substantially below that in all the other federations and unitary systems (except South Africa). In these other cases, 'own-source' revenues range among the transitional federations between 27 percent (Spain) and 60 percent (Brazil), and in the mature federations between 55 percent (Australia) and 80 percent (Canada). Thus, comparatively speaking, the federated units in Russia have remarkably less revenue autonomy, i.e. the ability to control and be accountable for the size of their revenues, than do the constituent units in other federations (except South Africa) and decentralized unitary systems. The regulation of taxes and revenues is clearly highly centralized within the Russian Federation with 91 percent of the combined revenues coming under central regulation.¹⁷

The control of regional borrowing should also be noted here. The period from 1992 until the crisis of mid-1998 witnessed a steady growth of borrowing, debt and loan guarantees at the regional and local levels of government. A federal law of 1993 had guaranteed regional and

14. OECD, Report 2002, op. cit., p. 163.

15. See Table 4; see also Kurlyandskaya, op. cit., Table 3.

16. See Table 1 and 3.

17. See Table 1.

local administrations the right to borrow and recent Budget Code, 2000, together with the Law on the Financial Foundations of Local Self-Government for the first time placed restrictions on the overall debt position of subnational governments. However, the number of these restrictions, combined with accounting ambiguities, has generated so far a considerable degree of confusion in interpretations which still needs to be worked out in subsequent legislation and instructions. A large number of regions clearly already exceed the prescribed norms, one of which is a 15 percent of revenue limit on debt service.¹⁸

In many federations an important issue has been that of the degree of intergovernmental tax competition and of tax harmonization that has taken place. Indeed, in our previous reports specific sections have been devoted to this. In the case of the Russian Federation, the high degree of centralization in the regulation of taxation and the very limited degree of tax autonomy possessed by the federated entities, although creating other problems, has limited the extent of tax competition or the seriousness of the need for intergovernmental tax harmonization. Even where tax collection is more decentralized, the extent to which the federal government has regulated the levying of taxes and shares of the proceeds to be distributed to the regional governments has minimized problems of intergovernmental tax competition as an issue. Thus, one of the benefits of what might otherwise be regarded as excessive centralization in the regulation of tax revenues within the federation has been effective control over intergovernmental tax competition.

6. TRANSFERS

Given the limited level of regional 'own-source' revenues indicated above, the gap between these and the expenditure responsibilities of the federated units in the Russian Federation is substantial. Indeed as Table 2 indicates, the vertical gap (at 45 percent of combined total revenues) is similar to that in

issue their own debt under few restrictions. The South Africa and much higher than the range between 3 and 32 percent in the other federations and decentralized unitary states. This gap has, therefore, made necessary very large transfers of revenues from the federal to the subnational units of government. These transfers have taken four forms. One is revenue sharing, i.e. the transfer of a share of all or of specified centrally regulated tax revenues. The second is in the form of unconditional equalization grants. The third is a set of targeted conditional transfers. The fourth is the provision of extra-budgetary funds. Table 3 provides a comparison of total central transfers and of conditional transfers as a percent of total constituent unit revenues in different federations and decentralized unitary states, including the Russian Federation. Tables 4 (for 1998-2000) and 5 (for 2000) show the composition of these transfers in the Russian Federation.

Revenue sharing represents the largest form of transfer from centrally regulated taxes in the Russian Federation. As Table 4 indicates, in the Russian Federation in 2000, shares of federally regulated taxes collected or received represented some 57 percent of total regional revenues. This revenue sharing took three forms. The first is taxes for which the rates and sharing rules are set annually by the federal government. In this category are the VAT, personal income tax, excises, and tax for natural resources (except payments for natural deposits and land tax). In the second category are taxes for which the rates are entirely set by the federal government and the sharing rules are fixed by federal legislation. In this category are payments for natural deposits. In the third category are those taxes for which the rates and sharing rules are primarily set by the federal government but with allowance for some discretion to change tax rates (bases) within fixed federal ceilings (norms) and/or to introduce additional tax exceptions. In this category are the profit tax, simple imputed income tax, and road tax. Particularly significant among the various revenue-sharing of taxes has been the profit tax, the proceeds of which in 2000 represented 21 percent of the total regional revenues (i.e. 37 percent of all shared tax revenues). By itself this

18. OECD, *OECD Economic Survey: The Russian Federation* (Paris, France: OECD Publication Services, pp. 143-146.

constitutes more than the total of regional ‘own-shared revenues from federally regulated taxes, the Russian Federation follows a practice found in a number of federations elsewhere, notably Germany, Switzerland, Australia, India, Spain and South Africa, and also in Japan, but to a greater degree.¹⁹

A lesser but not insignificant portion of transfers in Russia from the central government to the regional governments consists of the unconditional transfers for equalization of regional revenues (see further below under “Equalization”). As Table 5 indicates, in 2000 these were substantial, representing in aggregate 16 percent of total regional revenues. These unconditional grants when combined with shared revenues from taxes predominantly regulated by the federated government, represent a total of block transfers comprising 73 percent of total regional revenues. These contrast with the targeted conditional nature of the transfers in the third and fourth categories of transfers below which together in aggregate in 2000 constituted 9 percent of total regional revenues (see Table 5).

The third category of transfers are budgetary transfers targeted for specific purposes. By 2003 this category was comprised of several types of grants: Compensation Grants (funding of major federal mandates) which have been the largest in this group, Regional Finance Reform Grants, Social Expenditure Matching Grants, and Regional Development Grants (directed at specific purposes).

The fourth category of transfers has been the transfer from the federal government to the regional governments of extra-budgetary funds. Among the uses of these, a prominent one has been for meeting shortfalls between revenues and expenditures in the regions. The regular use of such a category of transfers contrasts with federations elsewhere which have only rarely used such transfers, and then usually only in response to natural disasters or emergencies. The

source’ revenues. In relying so heavily upon more extensive use of such transfers in the Russian Federation has given rise to the inefficiencies of soft-budget constraints referred to earlier in the section on expenditures.

Total conditional transfers in Russia in 2000 (categories 3 and 4 above) constituted 9 percent of total regional revenues (Table 5). In comparative terms, as Table 3 indicates, this is comparable to the levels in Germany, South Africa, Brazil and Sweden, but considerably less than in most other federal and unitary polities where the figure ranges from 16 percent in Canada and Japan and 17 percent in Switzerland to 30 percent in the United States and 42 percent in Spain. Consequently, while the revenue autonomy (i.e. ability to control revenues) of the regions is extremely limited by comparison with other federal and unitary regimes (as noted in the previous section), the regional governments in comparative terms possess considerable expenditure autonomy (discretion in their expenditures within the limits of established revenues) because of the relatively limited extent of central transfers that are conditional and the extent of the block transfers that are in the form of revenue-sharing and equalization transfers.

7. EQUALIZATION

The huge disparities in degree of economic development among the subjects of the federation has caused an acute problem because of the severity of the resulting horizontal fiscal imbalances. This has been of economic concern, but also has had a political resonance within the Russian Federation. The issue of which regions are donors and which are recipients has caused political concerns, but these depend on the set of factors that are taken into account.²⁰ In any case, what is clear is that the horizontal disparities among the federated units are larger than in most of the mature federations and even most of the transitional federations.

19. See Watts, *Intergovernmental Financial Relationships in Eight Countries: Final Report*, op. cit., pp. 42-46.

20. See , for instance, Aleksei Lavrov et. al., op. cit. See also I.V. Trounin, op. cit. pp. 10-11.

The development of horizontal fiscal equalization in Russia has taken place in several of revenues. The main source of equalization funds during this period was the Fund for Financial Assistance to Regions (FFAR). The methodology applied in order to distribute these transfers formally aimed at the distribution of funds in proportion to the gap between the potential tax revenues and the necessary expenditure in the regional budgets.²¹ In addition, further financial aid was aimed directly at compensating either the projected or existing gap between the revenues and expenditures of regional budgets. The net effect was a relatively arbitrary distribution of funds determined by decisions of the Ministry of Finance and the lobbying of individual regions.²²

In the period beginning in 1999, and still in force in 2005, a new methodology was adopted for the FFAR transfers based on an ‘index of budgetary expenditure’ and a ‘tax potential index’. The former “reflects the interregional difference between the price and the amount of granted budgetary services on the basis of indirect factors determining the extent of the need for certain types of public benefits in various regions that relates to interregional differences in the age structure of the population and in geographical, climatic and other conditions.”²³ The latter “reflects the interregional correlation between a regional budget’s potential tax revenues with consideration of the industry structure of the added value produced in such a region subject to application of a country average level of tax load (effective tax rate).”²⁴

Although the precise indices used are not modelled on any one specific example elsewhere, there are fundamental similarities to the systematic equalization transfers employed in a number of federations.²⁵ First, unlike

21. I.V. Trounin, op. cit., p. 8.

22. Ibid., p. 9.

23. Ibid., p. 10.

24. Ibid., p. 10.

25. For a review of these see Watts, *Intergovernmental Financial Relationships in Eight Countries*, op. cit., pp. 48-53 and Table 5.

steps. Before 1993 the focus was on equalization

Germany and Sweden, equalization does not involve formal inter-regional transfers, but as in most other federations takes the form solely of proportionately larger central transfers to the poorer regions. Secondly, like Australia, India, South Africa and Spain, equalization in Russia is now based on the assessment of both revenue capacities and expenditure needs. This contrasts with such equalization schemes as that in Canada and to a large extent Germany which are based solely on an assessment of the revenue capacities of the federated entities. Third, unlike Australia, India, South Africa and Sweden which have relied on standing or periodic independent advisory commissions, or Switzerland, Canada, Germany, Spain and Brazil where the equalization arrangements are largely determined by formal intergovernmental negotiations producing multilateral intergovernmental agreements (usually implemented subsequently by federal legislation), it would appear that in the Russian case the allocation of equalization transfers is largely determined by the federal Ministry of Finance applying federal law subject to approval by the Federation Council.²⁶

In terms of achievement in reducing financial disparities among regions in Russia, it would appear that the methodology has been significantly improved and that some progress has been achieved, but because the disparities were so large to begin with, there is still a very long way to go. In this respect the situation in the Russian Federation resembles most that in Brazil.

8. DECISION-MAKING PROCESSES FOR INTERGOVERNMENTAL FINANCIAL RELATIONS

Because the relative values of revenue resources and of expenditure responsibilities invariably change over time, federations and decentralized unitary states have usually found it necessary to establish or develop formal and informal

26. See also “Decision-making Processes for Intergovernmental Financial Relations” below.

processes to facilitate regular or periodic arrangements.²⁷ Typically, a variety of formal institutions and processes have been established either in the constitution, as in Germany, India and South Africa, by intergovernmental agreement, as in Australia and Canada, or by federal legislation, as in Spain and Sweden. Furthermore, in addition to the variety of constitutional or other formal institutions and processes for dealing with intergovernmental financial issues, in most federations and decentralized unitary states there has been extensive intergovernmental consultation and negotiation on issues related to intergovernmental financial arrangements.

Nevertheless, in practice there has been considerable variation in the patterns of decision-making relating to intergovernmental financial issues in different federations and decentralized unitary states. A number of factors have affected these patterns. For instance, where there has been strong and influential territorial representation in the central institutions, exhibited for instance by the United States and Brazilian Senates and the German Bundesrat, these bodies have played a major role in the decision-making processes relating to intergovernmental financial relations. Where such regional representation within the central institutions has been weak or virtually absent, as in Canada and Spain, there has been a particularly heavy emphasis on the role of negotiation through intergovernmental institutions and processes.

In contrast to Canada and Spain with their inconsequential senates, the Russian Federation has had the foundations for more effective territorial representation within the central institutions through the Federation Council. But President Yeltsin, rather than face the potential of collective action by the regions, preferred the flexibility of bilateralism to hammer out the balance of financial power within the federation. During the period subsequent to Yeltsin's presidency, the failure to develop the role of the

adjustments to the intergovernmental financial Federation Council to balance the "super-presidentialism" of President Putin, has left the regions vulnerable to attempts to recentralize power. Changes in the composition of the Federation Council and in the method of appointment for regional governors have reinforced the current tendency for a relatively dominant role of the federal government in decisions relating to intergovernmental financial relations. In this respect, of the different patterns of decision-making about financial arrangements identified in our previous reports, Russia has come to resemble most those in the decentralized unitary systems rather than those in the federations.

This trend in financial decision-making in the Russian Federation is related to a major issue often raised about decision-making concerning intergovernmental financial arrangements. This is the degree to which the actual decision-making processes for these matters contribute to maintaining a balance between the relative roles of the federal and federated-entity governments, or distort it by making one level of government or the other dominant in these processes. Given the general tendency in most federations (particularly transitional federations) and decentralized unitary states to concentrate tax power and revenue resources in the central government, the question arises whether in such cases this pattern has in practice undermined the federal balance. In considering this issue it is important to note both the constitutional and legal relationships, on the one hand, and also on the other, the extent to which in practice either level of government exerts particularly significant influence upon the key decisions.

The current situation within the Russian Federation would appear to represent a reaction from the relatively weak federal government position leading to a variety of asymmetrical bilateral arrangements during the Yeltsin period. Now, the Russian Federation is moving in the opposite direction to one where the decision-making on key issues relating to intergovernmental financial arrangements has increasingly been dominated by the federal government, and particularly its presidency.

27. For a summary of these, see Watts, *Intergovernmental Financial Relationships in Eight Countries*, op. cit., pp. 56-59 and Table 6.

At the same time, it should be noted that these decision-making processes have not been without some degree of interaction with representatives of the regional legislatures and administrative bodies. Such interaction has been essential for carrying out major reforms. Furthermore, changing the amounts of financial aid calculated and embodied in draft laws on the federal budget in Parliament has in practice involved a standing group consisting of interested representatives of the State Duma, Federation Council, the Government Administration of the President of the Russian Federation and various ministries and departments. This has meant that the proposals of the Ministry of Finance have been approved by the Federation Council more easily and without considerable changes.²⁸ But then, as noted in our previous report, even in such decentralized unitary systems as those in Sweden and Japan, where it is central legislation which determines the overall pattern of devolution in the financial arrangements, regional and local interests have been regularly consulted and have had considerable influence upon the decisions that have resulted.²⁹

9. ASSESSMENT IN RELATION TO ECONOMIC AND POLITICAL CRITERIA

In our previous reports we included a comparative evaluation of the economic and political performance of the various federations and decentralized unitary systems.³⁰ For this purpose a number of economic and political criteria were taken into account. These were economic criteria such as economic efficiency, equity, and effective fiscal management and stabilization policy, and political criteria, such as the impact on the relative autonomy of the constituent units, the degree of intergovernmental coordination, the degree of central government influence upon the governments of the constituent units, the transparency and democratic accountability of financial decision-making, the influence upon

political stability and adaptability, and the relative significance of institutions and of political culture. We turn now to a comparative assessment of the intergovernmental financial relations in the Russian Federation in terms of these various criteria.

1. Economic efficiency

The reforms in the intergovernmental financial relations since 1999 were clearly intended to improve the economic efficiency of the Russian Federation. Since the previous *OECD Economic Survey of 1999-2000*, the Russian economy has experienced a number of favourable trends and developments. Output, employment, consumption and investment have grown significantly. This recent growth has reversed the previous years of economic decline. Indeed, by 2001 GDP had already been brought back to the recorded level of 1993.

Admittedly, much of this has to be attributed to the role of external factors and other favourable macroeconomic trends supporting the recent growth. Relative prices and terms of trade improved for many Russian firms in the period since the 1998 crisis. A four-fold depreciation of the ruble in 1998-99 gave a major boost to firms oriented towards exports or import-substitution. A subsequent strengthening of oil and other commodity prices on world markets has further increased the average profitability of exports, and augmented investment demand, foreign reserves, and federal budgetary revenues.

But the reformed intergovernmental financial arrangements have also contributed by establishing a much more orderly financial regime than that which existed during most of the 1990s. The concentration of federal government control over revenue raising has been one factor here. On the other hand, as noted earlier in the section on expenditure decentralization, there remain by comparison with most other federations some continuing economic inefficiencies. While these inefficiencies have been reduced from the Yeltsin period, there remain issues arising from vagueness in the distribution of expenditure responsibilities, from some continued unfunded

28. Trounin, *op. cit.*, pp. 11-12.

29. Watts, *Intergovernmental Financial Relationships in Eight Countries*, *op. cit.*, p. 58.

30. See, for instance, *ibid.*, pp. 67-94.

mandates, and from the failure as yet to eliminate practices creating soft budget regional expenditures. Thus, the Russian Federation has yet to achieve the full potential economic efficiency that could be obtained from decentralized expenditures.

2. Equity

Here too recent reforms in Russia to the equalization arrangements have exhibited significant progress, particularly in methodology. But continued sharp regional financial disparities and the degree of poverty in certain regions remain a key problem, as witnessed by continuing disturbing trends in some demographic and health statistics. Since most of the responsibility for social expenditures currently rests with the regional and local governments, equalization of their revenues occupies a particularly important role in achieving inter-regional equity. A negative factor has been the reallocation under recent reforms of a significant amount of revenue from the regions to the federal government, imposing constraints generally upon regional efforts to finance social expenditures. The previous *OECD Economic Survey of 1999-2000* recommended a much greater federal responsibility for financing social policy, particularly in support of the poorer segments of the population. The long-term economic program of the federal government has been consistent with this recommendation, proposing a reallocation of state investment funds towards social policy. But other than the creation of a new transfer fund to back some federal mandates with financing, this reallocation has yet to be realized. In comparative terms, because the inter-regional disparities have, to begin with, been so much larger than in the mature federations and indeed some of the transitional federations, correcting these has been much more difficult. The Russian Federation is still a long way from achieving the reduction of disparities achieved by the most successful federations in this regard, Australia and Germany.

3. Fiscal management and stabilization policy

The concentration of central control over taxing powers in Russia has in general facilitated

constraints upon

the central management of the economy and of stabilization policies. In recent years the Russian government and the Central Bank have maintained responsible macroeconomic policies, exercising the financial restraint necessary for stabilizing expectations, normalizing relations with foreign creditors and improving the credibility of fiscal and monetary policy commitments. The Russian authorities quickly succeeded in restoring at least some degree of macroeconomic stability in the immediate aftermath of the crisis in 1998. Since then fiscal and monetary policy has received an important boost from the subsequent strengthening of oil and gas prices on world markets.

Even though the federal government took a decision in 2001 to resume servicing foreign debt in full, it has continued to maintain a tight fiscal policy, not allowing federal expenditures to increase along with significantly higher tax revenues. Given the uncertainty over oil prices and exceptionally high foreign debt repayments due in 2003, the Russian government came under some pressure to generate surpluses. Consequently, in 2001 it created an implicit 'stabilization fund', committing itself to surpluses in 2001 and 2002. With a strong dependence of the federal budget on oil and gas prices this type of stabilization fund made good sense, paralleling funds of this nature created in a number of other countries facing fiscal risks from commodity price fluctuations.

4. Autonomy of constituent units

Since the essence of federations is the combination of 'shared rule' for certain purposes (through the common institutions of a federal government) with 'regional self-rule' for other purposes (through autonomous governments of the constituent units), a significant political criterion is the degree of autonomy of the federated entities. An important issue, therefore, is whether the intergovernmental financial arrangements support or undermine this objective. For purposes of assessment, it is useful to distinguish 'revenue autonomy' and 'expenditure autonomy'. The first relates to the

ability of the constituent units to control and hence the scale of the expenditures. The second relates to the degree of expenditure discretion that they are able to exercise within the revenues that are available to them.

In terms of revenue autonomy, the highly centralized regulation of taxing powers that we have already noted, which is considerably more centralized than all but South Africa among federations and even decentralized unitary systems, means that the subjects of the federation have in comparative terms very restricted revenue autonomy. When we turn to the issue of expenditure autonomy, within the inflexibility of the revenue levels largely imposed upon them, the relatively large proportions of their total revenues consisting of unconditional revenue sharing or grants (73 percent of total constituent unit revenues)³¹ means that the regional governments would appear to have considerable expenditure autonomy. Indeed, the total of conditional transfers as a percent of total regional revenues is 9 percent, placing the Russian regional governments among those constituent units in other federations and decentralized unitary systems that have lesser constraints on their discretionary expenditure.

This assessment of expenditure autonomy for the constituent units in the Russian Federation has to be qualified, however. In the section on expenditure decentralization we have already noted the impact of a number of factors affecting the expenditure autonomy of the constituent units. Among these have been continued ambiguities concerning areas of 'joint' financial responsibility, the constraints upon regions with more limited resources, the impact of continued unfunded federal mandates, and the uncertainty engendered by practices resulting in soft-budget constraints. Furthermore, to this have to be added the recent assertion of presidential controls over regional administrations through the appointment, instead of the election, of regional governors. The result is in practice a considerably higher degree of federal regulation over the expenditures of the

accountable for the size of their revenues and federated entities than found in most other federations. Indeed, it is more akin to that found in the decentralized unitary systems.

Nevertheless, despite the recent measures aimed at increasing federal control, the situation should not be exaggerated. In terms of expenditure autonomy, subnational administrations in the Russian Federation do possess considerable means for conducting their own policies, and there remains a significant degree of expenditure autonomy which stands in contrast with their extremely limited degree of revenue autonomy.

5. Coordination and degree of central influence upon constituent units

The analysis in the preceding sub-section indicates that currently through its regulation of most revenue sources and the constraints it can impose on regional expenditures, the central government is in a position to exercise considerable coordination and influence over the regional and local governments. In comparative terms this clearly contrasts with most other federations, and particularly the more decentralized ones like Switzerland and Canada. But, of course, this has been achieved in the Russian Federation by sacrificing the degree of regional autonomy found in most other federations.

6. Transparency and accountability

The heavy reliance upon a large variety of intergovernmental transfers and the almost constant shifting and changing of these arrangements has placed severe limits upon their democratic transparency. The financial arrangements are complicated and difficult enough for specialist scholars to interpret and understand, and so it is not surprising that they lack transparency for politicians and electors within the system. This has seriously weakened the democratic control of decision-making.

Similarly, the often ambiguous relative roles of governments, the complex nature of the financial arrangements and calculations, and the

31. See Table 5.

heavy reliance of regional governments upon have seriously limited their political accountability. Where regional governments do not control the source and size of much of their revenues, it is difficult to hold them accountable. Thus, the principle that governmental responsibility and accountability for expenditures is best achieved when they have themselves to raise the taxes and revenues to cover those expenditures, is to a large extent missing. In those federations where regional governments typically rely on a much higher proportion of own-source revenues than in Russia, democratic accountability has tended to be clearer, although even in those cases, the use of considerable intergovernmental transfers has moderated this accountability.

7. Political stability and adaptability:

Political stability and flexibility may appear to be contradictory criteria, but both are essential for the effective operation of federations. Political stability relates to the extent to which the processes of intergovernmental financial relations are carried out with a minimum of conflict and have a stabilizing influence upon the operation and development of the country. Clearly political stability is an important objective for a federation to remain sustainable. But conditions change over time and the ability of the fiscal arrangements to assist the federation or decentralized unitary system to respond to these and to adapt over time to changing circumstances is also an important objective. Taken together, these criteria mean that adaptability should be sought but without destabilizing the polity.

In the period since 1992, the financial arrangements within the Russian Federation have certainly proved flexible, undergoing virtually constant change. The financial arrangements have fluctuated from the decentralizing and asymmetrical relations of the Yeltsin period to the current more uniform and highly centralized arrangements. Many of these fluctuations and frequent reforms were, of course, necessary to respond to clear crises. But, by comparison with the other federations and decentralized unitary systems analysed in our previous reports, the Russian Federation stands

transfers rather than their 'own source' revenues out as having been marked by far less stability in its financial arrangements. It may be that as the recent reforms are refined, a greater stability will come into effect. But the recent introduction of new arrangements directed at recentralizing authority and strengthening what President Putin calls the "vertical of power" suggests that intergovernmental relations within the Russian Federation have not yet achieved a stable equilibrium.

8. The relative significance of institutions and political culture:

In assessing the operation of federations and decentralized unitary systems in our previous studies we have noted that the prevailing political culture has been as important in shaping their development as the particular structure and character of their institutions. Indeed, their effectiveness has depended as much on the widespread public acceptance within them of the basic values required for federal systems: the explicit recognition and accommodation of multiple identities and loyalties within an overarching sense of shared purposes and objectives, the cherishing of diversity and an emphasis upon tolerance and accommodation, respect for the rule of law and constitutional legality, and the realization that compromise is not a weakness but a strength.

Given the path-dependency of the development of the Russian Federation out of the preceding Soviet institutions, the fluidity of the evolution since, and the recent perceived necessity to re-assert centralized authority in order to hold the federation together, it is not yet clear whether a federal political culture has firmly taken root or is still awaiting development behind a thin veneer of formally federal institutional structures. If experience elsewhere is any guide, the long-term effectiveness of the intergovernmental financial arrangements will depend heavily on the extent to which the prevailing political culture evolves to support these arrangements.

10. CONCLUSIONS

In formal terms, the intergovernmental financial arrangements within the Russian Federation possess the features found in most federations and decentralized unitary systems. During the period since 1992, these intergovernmental financial relations have, however, gone through major fluctuations and refinements. The current trend to centralizing authority appears to be weakening the federalizing aspects, and to be bringing the arrangements closer to those in the decentralized unitary states. It should be noted that even in those, as also in all the federations, regional heads of government or governors in Japan and Sweden are directly elected by their citizens rather than appointed by the central government. The essence of federalism lies in constitutional non-centralization rather than the top-down decentralization that characterizes decentralized unitary systems.³² If Russia is to gain the benefits of authentic federalism, then the most important task that the Russian authorities will need to address immediately is the reinforcing of the self-governance of most of the regional governments.³³ If that is to be achieved, regional institutions will need to have a financial basis of their own and to be responsible and accountable to their own electorates for the provision of public services and benefits directly related to their daily needs.

32. Daniel J. Elazar, *Exploring Federalism* (Tuscaloosa, AL: University of Alabama Press, 1987), pp. 34-36.

33. I.V. Trounin, op. cit., p. 44, comes to a similar conclusion.

TABLE 1: COMPARATIVE CENTRAL GOVERNMENT SHARES OF TOTAL (ALL GOVERNMENTS) REVENUES AND EXPENDITURES¹

Country	Percent of Total all Governments Revenue	Percent of Total all Governments Expenditures
<i>Russia:</i>	91	46
<i>Mature Federations:</i>		
Australia	69	54
United States	67	54
Germany	65	37
Canada	44	37
Switzerland	40	32
<i>Transitional Federations:</i>		
Spain	83	51
South Africa	95	50
Brazil	69	64
India	66	45
<i>Mature Unitary Systems:</i>		
Japan	58	38
Sweden	57	54

1. Revenue shares are before transfers of shares of taxes regulated by the central government and grants to regional and local governments (see text regarding definitions). Expenditure shares are after transfers of shares of taxes regulated by the central government to regional and local governments. Figures are rounded to the nearest percent. Countries in each category are listed broadly in descending order of centralization. Depending on source, figures are for 2000 or 2001; Russian figures are for 2000.

Sources: R.L. Watts, *Intergovernmental Financial Relationships in Eight Countries: Final Report* (Reform of Fiscal Federalism in Russia Project, Institute of Intergovernmental Relations, Queen's University (April 2004), Table 1; OECD, *OECD Economic Survey: The Russian Federation* (Paris, France: OECD Publication Services, 2002), Table 36, 37.

TABLE 2: COMPARATIVE REGIONAL AND LOCAL GOVERNMENT SHARES OF TOTAL (ALL GOVERNMENTS) REVENUES AND EXPENDITURES¹

Country	Percent of Total all Governments Revenue	Percent of Total all Governments Expenditure	Vertical Gap ²
<i>Russia:</i>	9	54	45
<i>Mature Federations:</i>			
Australia	31	46	15
United States	33	46	13
Germany	35	63	27
Canada	56	63	7
Switzerland	60	68	8
<i>Transitional Federations:</i>			
Spain	17	49	32
South Africa	5	50	45
Brazil	31	36	5
India	34	55	21
<i>Mature Unitary Systems:</i>			
Japan	42	62	20
Sweden	43	46	3

1. Revenue Shares are before transfers of shares of taxes regulated by the central government and grants to regional and local governments. Expenditure shares are after transfers of shares of taxes regulated by central government and grants to regional and local governments. Figures are rounded to the nearest percent. Countries in each category are listed broadly in ascending order of decentralization. Depending on source figures are for 2000 or 2001; Russian figures are for 2000.
2. Vertical gaps are identified by difference between total regional and local expenditures and total regional and local own-source revenues (before transfers of shares of central taxes and grants).

Source: As for Table 1. See also Table 6.

TABLE 3: COMPARATIVE CENTRAL TRANSFERS AS PERCENT OF

TOTAL CONSTITUENT UNIT REVENUES¹

Country	Own-Source Revenues	Total Transfers ²	Conditional Transfers
<i>Russia:</i>	17.0	83.0	9.0
<i>Mature Federations:</i>			
Australia	54.7	45.3	21.3
United States	70.4	29.6	29.6
Germany	56.2	43.6	9.8
Canada	80.2	19.8	15.8 ³
Switzerland	75.2	24.8	17.0
<i>Transitional Federations:</i>			
Spain	27.2	72.8	41.9
South Africa	3.9	96.1	11.0
Brazil	60.0	30.0	7.5
India	54.0	46.0	18.7
<i>Mature Unitary Systems</i>			
Japan	62.8	37.2	16.2
Sweden	84.2	15.8	4.4

1. Figures are mostly for 2000 and 2001 except for those for Canada, United States and Germany, which are for 1995 or 1996 (derived from previous studies for this project).
2. Total transfers consist of shares of taxes regulated by central government plus unconditional and conditional grants.
3. If CHST transfers which are semi-conditional are considered unconditional, the percentage for Canada would be 0.9%.

Sources: R. L. Watts, *Intergovernmental Financial Relationships in Eight Countries: Final Report* (Reform of Fiscal Federalism in Russia Project, Institute of Intergovernmental Relations, Queen's University (April 2004), Tables 2, 3, 4. See also sources for Table 1.

TABLE 4: COMPOSITION OF REGIONAL AND LOCAL BUDGETARY REVENUE IN THE RUSSIAN FEDERATION IN PERCENT

	1998		1999		2000	
	Regional	Local	Regional	Local	Regional	Local
Total revenues	100	100	100	100	100	100
<i>of which:</i>						
A. Shared Taxes	50	52	60	56	57	53
<i>Regulated</i> ¹	30	38	25	42	22	39
<i>(of which: profit tax)</i>	-	(10)	-	(17)	-	(14)
<i>Fixed federal</i> ²	3	12	4	12	4	12
<i>Subject to federal Ceiling</i> ³	17	2	31	2	31	2
<i>(of which: profit tax)</i>	(15)	-	(20)	-	(21)	-
B. Own-source taxes ⁴	14	12	15	15	11	14
C. Non-tax revenue	6	4	6	4	6	3
D. Transfers from higher-level budgets and extra-budgetary funds	30	32	19	25	25	30

1. Rates and sharing rules are set annually by the superior level of government.
 - a) For regional budgets: VAT, personal income tax, excises, and tax for natural resources (except payments for natural deposits and land tax).
 - b) For local budgets: VAT, personal income tax, profit tax, single imputed income taxes, and taxes for natural resources (except payments for natural deposits and land tax).
2. Rates are set entirely by the superior level of government and sharing rules fixed by federal legislation.
 - a) For regional budgets – payments for natural deposits.
 - b) For local budgets – payment for natural deposits, sales tax, and property tax (enterprises).
3. Rates and sharing rules are set primarily by the superior level of government, but allowing some discretion to change tax rates (bases) within the fixed federal ceilings (norms) and/or to introduce additional tax exceptions.
 - a) For regional budgets – profit tax, single imputed income tax (legal entities), and road tax.
 - b) For local budgets – land tax.
4. Rates, tax bases and exemptions are set decentrally, but within a federal legal framework.
 - a) For regional budgets – sales tax, property tax (enterprises), licenses and registration fees, and single imputed income tax (personal).
 - b) For local budgets – municipal tax (up to 5% rate to the base of profit tax, introduced in 2001), licenses and registration fees, property tax (persons), advertising tax, social infrastructure and other local taxes (mainly cancelled in 2000-2001).

Source: OECD calculations based on data and information of the Ministry of Finance; OECD, *Economic Survey: The Russian Federation* (Paris, France: OECD Publication Services, 2002), Table 37.

Note: Rounding of figures may not add up to 100 percent.

TABLE 5: COMPOSITION OF TRANSFERS TO REGIONAL GOVERNMENTS IN RUSSIAN FEDERATION, 2000, IN PERCENT OF TOTAL REVENUES

Total Regional Revenues:	100 %
1. Own-Source Revenues:	
Taxes	11
Non-tax revenue	6
<i>(Total)</i>	<i>17</i>
2. Shared taxes predominantly regulated by Federal Government (for categories see Table 3)	57
3. Equalization grants from federal government (2 + 3. <i>Total Block transfers</i>)	16 <i>73</i>
4. Conditional transfers from Federal Government budget and extra-budgetary funds	9

Note: Rounding of figures may not add up to 100%.

Sources: OECD, *OECD Economic Survey: The Russian Federation* (Paris, France: OECD Publication Services, 2002).

TABLE 6: SHARES OF REGIONAL EXPENDITURES IN CONSOLIDATED BUDGET IN THE RUSSIAN FEDERATION, 1992-2003 (in percent)

1992	34.0
1993	40.3
1994	37.7
1995	43.4
1996	45.4
1997	48.1
1998	54.1
1999	51.9
2000	54.4
2001	54.2
2002	49.3
2003	50.0

Source: Data provided by Ilya Trounin.

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