TITLE: The Local Budget in the Changing Role of Municipal Government in Russia: A Case Study of Yaroslavl’

AUTHOR: Beth Mitchneck

THE NATIONAL COUNCIL FOR SOVIET AND EAST EUROPEAN RESEARCH

1755 Massachusetts Avenue, N.W.
Washington, D.C. 20036
PROJECT INFORMATION:

CONTRACTOR: University of Arizona

PRINCIPAL INVESTIGATORS: Beth Mitchneck
                                Daniel Berkowitz

COUNCIL CONTRACT NUMBER: 807-09

DATE: April 16, 1993

COPYRIGHT INFORMATION

Individual researchers retain the copyright on work products derived from research funded by Council Contract. The Council and the U.S. Government have the right to duplicate written reports and other materials submitted under Council Contract and to distribute such copies within the Council and U.S. Government for their own use, and to draw upon such reports and materials for their own studies; but the Council and U.S. Government do not have the right to distribute, or make such reports and materials available outside the Council or U.S. Government without the written consent of the authors, except as may be required under the provisions of the Freedom of Information Act 5 U.S.C. 552, or other applicable law.

The work leading to this report was supported by contract funds provided by the National Council for Soviet and East European Research. The analysis and interpretations contained in the report are those of the author.
CONTENTS

Executive Summary ........................................... i
Summary and Conceptualization of Current Changes ...... i

Yaroslavl' Case Study ......................................... ii
Budgetary Revenues ......................................... ii
Off-Budget Revenues (Discretionary) .................... ii
Tax Collection ................................................ iii
Budgetary Expenditures ....................................... iv
Off-Budget Expenditures ...................................... v

Summary and Conclusions ..................................... vi

INTRODUCTION ................................................... 1
The Russian City Government and Budgetary Policy .... 2
Budgetary and Extra-Budgetary Revenues ............... 4
Budgetary and Off-Budgetary Expenditures ............. 6
Summary and Conceptualization of Current Changes .... 7

Data and Methodology .......................................... 9
Tax Instruments ............................................... 9
Tax Collection ................................................ 9
Composition of Local Expenditures ....................... 10
Interviews and Data ........................................... 10

The Yaroslavl' Case Study .................................... 10
Budgetary Revenues .......................................... 11
Off-Budget Revenues ......................................... 11
Tax Collection ............................................... 12
Budgetary Expenditures ..................................... 13
Off-Budget Expenditures .................................... 14

Summary and Conclusion ...................................... 16

Table 1 ......................................................... 18
Table 2 ......................................................... 19
Table 3 ......................................................... 20

References ..................................................... 22
EXECUTIVE SUMMARY

This paper demonstrates the empowerment of local government as it evolves from an administrative arm of the center to a semi-autonomous, policy making body. Local government bodies now use the fiscal system to carve out a new economic role and to develop jurisdictional boundaries. This paper traces fiscal decentralization in one Russian city, Yaroslavl'. The main data sources are interviews with city officials in June 1992 and January 1993 and city and district government documents, (e.g. resolutions of the legislative branch).

Summary and Conceptualization of Current Changes

Soviet local state institutions historically insured local consumption of both public and private goods and administered central directives. City and oblast activism in the late 1980s, combined with central legislation, brought about a redistribution of the loci of economic means, authority, responsibility, and information from higher government levels to the local level.

The de-legitimization of the word Soviet has caused the redefinition of territorial jurisdiction and of the economic role of local government. Soviet, as a national term, signified central authority throughout the territory. In this system, the central state viewed the entire territory as subject to its priorities. Territorial jurisdiction constricts with the de-legitimization of the highly centralized system. A concomitant splintering of government priorities occurs. Local property rights, the right to use tax instruments and the right to establish independent expenditure policies shift to the local level meaningful territorial jurisdiction and, thereby, provide it with the means to change its economic role.

The processes of changing the meaning of territorial jurisdiction and the economic role of local government are not complete. Substantial continuity from the past system remains (Mitchneck and Berkowitz, 1992). One of the important questions to answer is in what concrete ways does the local government push the boundaries of past limitations over its actions? From where does it draw the power and authority to independently change its economic behavior? By answering these questions, we can analyze the impact of government decentralization on cities. The case study of Yaroslavl' begins to answer these questions.
YAROSLAVL' CASE STUDY

Yaroslavl' is an industrial city of about 640,000 people in the Central Economic Region of Russia. It has a history of industrial activity stretching back into the 16th and 17th centuries when it was the Volga river port for Moscow. The surrounding oblast is agricultural and tends to have more conservative political leanings than Yaroslavl' city. The city is viewed as having a reformist government (see Hahn 1991). The population is 95 percent Russian. While the case study can not claim to be representative of all Russian cities, the perception of its average Russian qualities and its history permit its description as a typical Russian city.

Budgetary Revenues

Total budgetary revenues increased about nineteen fold between 1991 and 1992. These figures are, however, fairly meaningless since they do not account for inflation. Formal budgetary revenues are still limited since fines and fees, new revenue sources, form the main source of extra-budgetary income. Profit tax on enterprises and individual income taxes are traditionally major revenue sources for the city; in 1992 they comprised 82 percent of total city budgetary revenues which is a slight increase from 74 percent in 1991. The third traditional major revenue source was the turnover tax (21 percent of total budgetary revenues in 1991); however, Yeltsin replaced this with a value-added tax that accounted for 11 percent of total budgetary revenues in 1992. Clearly, the city government still must rely upon the collection of relatively few revenue sources to fund its budgetary expenditures.

The city began to collect new tax sources in 1992, but the new sources remain a relatively small proportion of the total revenues and are difficult to collect. In 1992 the city collected budgetary revenues from privatization, bonds, a tax on property, a land tax, fees and payments such as those due on water use and transportation vehicles. A new revenue source in 1992 was the carry over of budgetary funds. Higher levels of government could confiscate these funds until 1992. The ability to carry over funds represents a substantial increase in independence for Russian cities.

Off-Budget Revenues (Discretionary)

A substantial change in the composition of off-budget revenues and the number of sources of extra-budgetary revenues occurred between 1991 and 1992 in Yaroslavl'. Vodka
sales accounted for all of the city's extra-budgetary revenues in 1991. By 1992, the city accounting office no longer included extra-budgetary revenues as a single line item in its budgetary accounting, but produced a separate accounting sheet for extra-budgetary revenues and expenditures. Total extra-budgetary revenues increased more than eight times to 182.2 million rubles in 1992. Revenues from vodka sales declined dramatically in both absolute and relative terms. This revenue source formed only 7 percent of total extra-budgetary revenues in 1992. The dramatic increase in extra-budgetary revenues means that the city has greater ability to conduct independent expenditure policy.

Tax Collection

Formal tax collection mechanisms for the city are still under the jurisdiction of the federal government level. As under the previous system, the city tax inspection office is responsible for collecting all tax revenues due to all levels of government. The Yaroslavl' city government has accomplished an innovation in the sphere of local tax collection. At the initiation of the city-level Office of Finances and Prices, the city now has "a single budget." Under the previous system, the city had a single budget with the oblast. Also under the previous system, districts within the city had bank accounts into which their own formal tax revenues would flow. Now there is only one city bank account for each revenue source. This allows for a more equitable spatial distribution of revenues between districts that accounts for population variations within the city. By in effect taking over lower level revenues, the city can conduct a more integrated, city-wide expenditure policy. Two other cities in Russia (Krasnodar and Kaliningrad) adopted the same system after consulting with the Yaroslavl' city government.

The single budget for the city clearly defines its formal jurisdictional authority and power throughout the territory of the city, rather than limiting its power and authority as under the previous system. The city, however, has not left districts completely powerless. District governments still have extra-budgetary revenues and make independent expenditures using those revenues. The size of extra-budgetary revenue funds varies according to district level initiative to form them. District level sources include the registration of private firms and cooperatives located in their districts. The industrial, rather than the residential, districts
form more substantial extra-budgetary funds; thereby, they perpetuate the previous spatial inequalities between need and means within the city.

**Budgetary Expenditures**

During the transition period, the city government has increased the level of its formal budgetary expenditures. Absolute figures are misleading in that they do not account for high inflation levels. The composition of the formal budget for the city is still largely controlled by higher government levels. Several significant changes have occurred in the formal budgets of Yaroslavl’ city during the early 1990s. First, central laws giving greater fiscal responsibility to cities also have decentralized to the city and oblast levels funding the social safety net. Beginning with the 1991 budget, a new line item appears for wage compensation for families with children. Depending on the fiscal "health" of the city, it passes resolutions allocating additional funds during the year for wage compensation.

Second, the 1992 budget has a new line item - development budget. The development budget funds capital construction in the city for city property. This line item in Yaroslavl’ consists entirely of funding new construction and reconstruction of city property and social and economic infrastructure. This fund is formed through the combination of surplus revenue, extra-budgetary funds, and a small amount from the oblast budget. In 1991, the development budget fund appeared as a line item in the accounting of surplus and extra-budgetary expenditures (i.e. as an off-budget expenditure). In the past, these expenditures were made in the city only through informal or higher level means. The inclusion of a development budget in the city budget marks a significant change in the formal responsibility and authority of the city government.

Third, the city included a reserve fund as a line item expenditure. This institutionalizes a practice used by state enterprises to carry over funds to allocate for investment purposes. The practice began in Yaroslavl’ as the city was unable to spend the planned amount but needed to allocate the funds within their budget. They now set aside up to ten percent of their planned expenditures for this reserve fund. Yaroslavl’ city officials called this their way of being able to put out fires. Other large cities also reportedly created reserve funds.
Off-Budget Expenditures

Off-budget expenditures have changed significantly since the late 1980s. Under the previous system, the city made few such expenditures. The composition of off-budget expenditures varies according to revenue source. Surplus revenues are used to supplement planned budgetary expenditures. Supplements to social security and the social safety net are made off-budget. Given that the city perceives federal normatives as inadequate, a city’s ability to over-fulfill the planned revenues and then to direct funds into maintaining local infrastructure and quality of life takes on paramount importance to the city government.

While the expenditures from surplus revenues mainly target quality of life issues, extra-budgetary expenditures in the first half of 1992 were geared toward maintaining the physical infrastructure of the city and supporting the morale of the inhabitants. A total of nearly 32 million rubles were allocated for extra-budgetary expenditures in the first half of 1992. The morale and place-related expenditures focus on financial support of sports clubs, restoration of historical landmarks (e.g., Vlas’evskaya tower), and a contest and prize for a Yaroslavl’ city emblem. The city’s expenditures endeavor to advertise the city and support place-related consciousness. Next, the city subsidizes its enterprises to compensate for price liberalization. For example, a municipal newspaper received funds to compensate for the increased market price of printing paper. Soviet enterprises have always been subsidized, but this is clear evidence that the city government is taking on a role of protecting enterprises from the vagaries of the market.

Data on extra-budgetary expenditures by the city in December 1992 alone indicate that towards the end of the year, the city substantially subsidized local enterprises through direct grants and credits. Credits amounted to about six percent of its budget. Without commenting on the wisdom of such subsidies, the city has clearly turned its attention toward supporting and developing economic activity within its boundaries. Despite legal constraints that define only the “communal economy” and retail and service sectors as municipal property, the city gives financial assistance to enterprises of any type located on its territory. These kinds of expenditures on foreign relations, enterprise subsidies, morale, and entertainment indicate both priorities of, and substantial new authority for, the local level of government. The priorities and authority place city governments in direct conflict with
priorities as defined by the President of Russia, but do not indicate an unwillingness to reform.

SUMMARY AND CONCLUSION

Elements of independent fiscal policy, evident in an examination of the local budget in Yaroslavl’, indicate that the economic role of local government has grown. The increasing importance of off-budget revenues and expenditures, the creation of a single budget for the city of Yaroslavl’, and the city-level subsidies to both the population for the social safety net and to enterprises for propping up the local economy, represent significant changes in local finance during 1992.

The case study of Yaroslavl’ shows an activist city government attempting to produce a new system, not to reproduce the previous system. The case study indicates the importance of looking beyond the formal budget to the off-budget accounts of specific cities to grasp the implications of fiscal decentralization. Detailed analysis shows cities striving to develop into new entities, but not necessarily by the same path as dictated from above. The shrinking of territorial jurisdiction complicates and obscures the central economic role of Russian cities.
INTRODUCTION

Local public finance provides the backdrop for the political and economic transition underway on the subnational level. Tracking the creation of an independent local fiscal system measures the institutional response to transition in the Russian economy. City budgets fund most expenditures on quality of life and social welfare and, therefore, reflect central budgetary requirements and local priorities. In Russia, local budget composition received serious attention within the rubric of reforms beginning in the mid-1980s. However, until recently, information was not available to measure the reforms' impact at the city level. Using recently available detailed city budget data, this paper traces fiscal decentralization and the increased authority to tax and to develop independent expenditure policies at the local level in one Russian city, Yaroslavl'.

Field work in Yaroslavl' and analysis of budgetary data from Yaroslavl' and from other localities in Russia shows that, in a formal sense, local governments continue to have little control over the formation of their budgets and the structure of budgetary expenditures. Yet, in reality, there is substantial evidence of decentralization, growing independence in the spheres of local tax and expenditure policies, and mounting initiative in local governance. Local government has gained incentive to tax and to collect taxes in order to pursue an independent fiscal policy, particularly through the use of off-budget revenues.

This paper provides an overview of the Soviet (i.e., pre-1992) and current role of the Russian local government and the budgetary system. The information from the case study of

---

1 Yaroslavl' is an industrial city about 175 northeast of Moscow along the Volga River in the Central Economic Region. The city is the capital of Yaroslavl' Oblast and has a population of about 640,000.
Yaroslavl' documents and interprets the formal and informal changes during the transition period. The purpose is to demonstrate the empowerment of local government as it evolves from an administrative arm of the center to a semi-autonomous, policy making body. The evolution illustrates how the concept of local government changes along with the changing concept of territory during the decentralization process. It is hypothesized that local government bodies use the fiscal system to carve out a new economic role and to develop a new meaning of territory or jurisdiction. In the new institutional environment, territory becomes a place over which local authority and power may be extended rather than a place subject to jurisdiction from above alone.

Previous literature on local public finance and on local government has ignored the Soviet and Russian cases. Prior to the break-up of the former Soviet Union, few studied public finance in the centrally-planned economy. Some notable exceptions provide a foundation and background on which we can begin the analysis of the transition period (e.g., Friedgut 1983; Lewis 1976 and 1983; Raimondo and Stuart 1984 and 1986). Continual examination of the transition period allows us to trace the evolution of fiscal decentralization (Berkowitz and Mitchneck 1992); but only case studies can document the actual processes. Analyses of Russian cities during the transition period provide a rare opportunity to observe the attempt to create a market-type system. In addition to empirical evidence that we can collect, the Russian city is a laboratory in which we may trace the evolution of the empowerment of local government and the governing of territory.

The next section reviews what we do know about the role of city government and the local budget system as it functioned in the past and as it appears to function during the transition. The following section discusses some theoretical issues inherent in the analysis of the Russian city and the data and methodology used to construct the case study. The final two sections are the case study itself and summary and conclusion.

THE RUSSIAN CITY GOVERNMENT AND BUDGETARY POLICY
In the Soviet case, the local government included the local Communist Party and government institutions and the central economic bureaucracy like the local office of the State
Planning Committee (Gosplan) in addition to the local executive (the city hall or mayor’s office) and the legislative branches of government (the local soviet or the Council of People’s Deputies). The current city level legislative branch is divided into the City Council of People’s Deputies (city soviet) and the Small Soviet (Maliy Soviet), which is a subgroup of the larger city soviet. In the formal political system of the Soviet Union, the local state apparatus was structurally part of the central apparatus. Personnel, regional development, and fiscal policies were directed by the central state. However, studies focusing on the informal system have noted local influence over development decisions through the intervention of local party and government organizations (see Hough 1969; Bahry 1987; Ruble 1990). These studies and others (e.g. Moses 1982; Breslauer 1986) on the role of the local state in the USSR also suggest that the local state did not act only as the simple administrative apparatus of higher levels of government, but did act in its own interest particularly while demanding attention to regional issues at central forums.

Structural changes have occurred since the late 1980s and since 1992 that set the legal framework for new authority at the city level through a substantial redistribution of fiscal powers (Berkowitz and Mitchneck 1992). This fiscal decentralization allows for local public policy formation and the evolution of a new role for local government. The central government passed new legislation governing these relations. Russian Republic laws from 1991 and 1992 give broader fiscal rights to administrative units below the republic level. (See Sovetskaya Rossiya, December 30, 1990, FBIS-SOV-91-003, 7 January 1991, and Ekonomicheskaya Gazeta No. 11 March 1992.)

Despite new legislation, the formal political and economic responsibilities of the local government remain firmly in the area of social and economic infrastructure. The economic responsibility of city and oblast governments in the 1980s was limited to public utilities, housing, passenger transportation, education, culture, health, and the retail system. These formal authority areas have been carried over into the Russian structure as evidenced by the distribution of state property during 1992. The city retained property and enterprises involved in what is termed the communal economy and the retail system while the oblast, the immediate higher level of government, received property belonging to the productive sector of the economy. The formal sphere of influence of city government remains in those areas
that influence the development and maintenance of social overhead capital with only limited responsibility for economic overhead capital and the industrial sector. The case study of Yaroslavl' indicates that city government is able to push the formal boundaries of authority and responsibility into other, non-traditional areas, mainly due to their manipulation of the formal budgetary system.

**Budgetary and Extra-budgetary revenues**

Under the previous system, the budget had limited sources of own income (i.e. tax revenues that flowed directly into the local budget). Therefore, much of the revenue generated on a specific territory flowed directly into either the Russian Republic or Soviet budget in the form of turnover taxes or profit taxes. Cities had three sources of revenue - own income, regulated income, and transfers from higher level budgets. Own income consisted of profit taxes on local enterprises and cooperatives, (in the case of the city, local enterprises consisted of the state-run retail system), the bachelor tax, and local duties. These sources amounted to a relatively small proportion of the amounts needed to fulfill planned expenditures; the proportion does vary by place and over time. Local officials negotiated yearly with higher level officials for payments out of regulated sources like the turnover tax and profits tax on enterprises under the jurisdiction of the republic or the all-Union (federal) level. A large portion of revenues from Yaroslavl' went to higher level budgets. For example, in 1988, 83 percent of budgetary revenues produced in Yaroslavl' Oblast were sent to the republic and all-Union budgets (Goskomstat RSFSR 1990). Oblast, or provincial, and city officials then negotiated for the return of these revenues through the system of regulated income or direct grants. Also under the previous system, the city officials had little control over the surpluses (hold-over funds) over planned revenues. Higher level officials could command the bank in which the local government had an account to transfer these surpluses to higher level accounts. These latter two aspects have changed -- deductions into the city budget, in theory, come from all enterprises located in the city and the city government has legal right to use its surplus revenues.

In Yaroslavl', according to information obtained in interviews, fifty percent of the budgetary revenues are supposed to come from locally generated tax receipts (i.e. profit taxes, income tax, and other local taxes) with the remaining fifty percent coming from higher
level budgets. These figures vary by locality in Russia. Officials in each locality stressed that the amount of the subsidy varies according to the locality's ability to generate revenues. If Yaroslavl' could generate more than fifty percent of the needed revenues, it would receive less than fifty percent from higher sources. So, even in the "reformed" system, tremendous incentive exists not to maximize planned revenues. The excess amount cannot be freely directed into additional areas of unplanned social expenditures. Interviews indicated that a portion of surplus revenues must be used to pay for the planned deficit, with the remainder financing extra-budgetary expenditures and additional budgetary expenditures. The incentive for city government lies in maximizing extra-budgetary revenues, over which the central government has no legal control. This means that we will not see tremendous changes in the planned budgets of cities; the changes to indicate the presence of independent fiscal policy will be found in the use of budgetary surplus and the use of local legislative means to create sources of income outside of the budget.

Under the previous system, few sources of off-budget revenues existed for the city government. In 1991, the city of Yaroslavl' had off-budget revenues from two sources: over-fulfillment of planned revenues, and a portion of the price of vodka sold in the city. The city government needed to rely on off-budget expenditures from enterprises and ministries functioning in the city but not necessarily under its jurisdiction. In the informal system, city officials would routinely approach enterprise and ministry officials conducting economic activity in the city to make expenditures such as on road construction and other capital construction. Thus, the off-budget expenditures of non-locally subordinate enterprises and ministries became an integral part of regional development for which the local government was responsible. Currently, off-budget revenues are formed from two sources: over-fulfillment of planned revenues and extra-budgetary revenues. Extra-budgetary revenues are formed mainly from penalties (fines) levied against enterprises and individuals within the jurisdiction (e.g., traffic fines, economic sanctions, and fines for late payment of taxes), vodka sales, privatization of city property, and fees for registering local businesses.
Both the executive branch of the city and of districts\(^2\) within cities can legally form extra-budgetary funds. The size of a city's and a district's extra-budgetary fund differs greatly by place, thereby spatially differentiating a locality's ability to independently determine expenditure policies and priorities. One local official jokingly stated during an interview that its minuscule extra-budgetary resources were formed from penalties and humanitarian aid.

**Budgetary and Off-budgetary expenditures**

City government officials of Yaroslavl', as well as smaller cities, such as Pushkin and Petrodvorets, (under the jurisdiction of St. Petersburg), stress that city budgets form the mainstay of social protection for the local population. Indeed, the traditional role of the city budget is to fund, at centrally-determined, minimum normatives, non-productive portions of the local economy, services for the population and the maintenance of infrastructure. Budget expenditure items traditionally include the maintenance of housing, heating, local transport, education, culture, health, sports, city planning and the provision of social security. The city budget also funds upkeep of militia and local government. Recent additions to city budgetary expenditures include subsidies to local entertainment establishments and the provision of a social safety net, for example, subsidies on the prices of meat and milk products, and wage compensation for price increases appeared in the 1991 city budget of Yaroslavl'. Due to central legislation, cities have much greater financial responsibility to finance these expenditures, without central subsidies. The obligation to provide a large portion of the social safety net at the local level places tremendous stress on local resources to cover the social service without dramatically increasing the budget deficit (Mitchneck 1992).

Despite the planned nature of city budgetary expenditures, cities have the greatest amount of discretion over expenditures from extra-budgetary funds and budgetary surplus (over plan fulfillment). For example, Petrodvorets used a portion of its budgetary surplus to create a local police force. It had, until 1992, relied upon St. Petersburg for its police protection. The same city also used extra-budgetary funds to subsidize food establishments

\(^2\)Districts are either subdivisions of cities or smaller cities under the jurisdiction of the dominant city.
over the winter. These expenditures compensate for inadequate central normatives for expenditures; the composition of these expenditures reflects traditional budgetary expenditures. Some notable exceptions and distinctions between the two types of off budget expenditures, however, will be discussed in the case study of Yaroslavl’.

Summary and Conceptualization of Current Changes

Cities and districts grew increasingly vocal and active during the 1980s with respect to the need for autonomy and the implementation of locally generated reform. For this reason, we sought evidence of local initiatives within the fiscal system and regional development planning. Although some evidence of local initiatives in the development sphere exist, and are enumerated below, we also found that since the August 1991 coup, city and district governments had thought little about local development. City and the district governments are beginning to use independent expenditure policy to create a set of local priorities; such examples will be enumerated below in the case study of Yaroslavl’.

The changes in local public finance and the level and type of initiatives by local government in the economic development sphere are a local response to and a reflection of central restructuring. We see a new definition of the role of local government evolving. Soviet local state institutions historically have insured local consumption of both public and private goods and have administered central directives; in other words, the local government reproduced the status quo. By the late 1980s, city and oblast governments began to publicly call for decentralization of economic and political decision making and spontaneously legislate changes at the local level. The local activism, combined with central legislation, brought about a redistribution of the loci of economic means, authority, responsibility, and information from higher government levels to the local level. In effect, a highly concentrated system of economic power and authority began to disperse and reconcentrate at the local level.

The process of change suggests a redefinition of territorial jurisdiction and of the economic role of local government. The meaning of territory has changed along with the delegitimization of the word Soviet. Soviet, as a national term, signified central authority throughout the territory, including central authority over localities. In this system, the central state viewed the entire territory as subject to its priorities. The previous expansive
view of territorial jurisdiction accounts, in part, for interregional mobility of resources. As the concept of territory constricts with the de-legitimization of the highly centralized system, a concomitant contraction of resources and interregional flows occurs. The process of change then endows local government with new economic authority and power. Local property rights, the right to use tax instruments and the right to establish independent expenditure policies shift to the local level meaningful territorial jurisdiction and, thereby, provide it with the means to change its economic role.

The economic role of local government is changing from insurer of consumption and production to producer. The production role encompasses the essence of change and represents the critical departure both in time and space from the previous system of government. In the past, the local government could not develop its own expenditure policies; it can now with designated revenue sources. In the past, the local government insured the consumption of public and private goods solely at centrally-set, minimum normatives; it can now modify those norms according to its own ability to make the expenditures. These are examples of the development of a new role. In the past, the local government had no legal or regulatory recourse to influence industrial location; it can now actively pursue economic partnerships and participate in the production process. In the past, enterprises received subsidies from central state sources; the local government currently subsidizes production on its territory. These are examples of the new role of local government in the production process.

The processes of changing the meaning of territorial jurisdiction and the economic role of local government are not complete. Substantial continuity from the past system remains (Mitchneck and Berkowitz, 1992). Neither have all local governments participated to the same degree in the redefinition of the economic role of local government. One of the important questions to answer is in what concrete ways does the local government push the boundaries of past limitations over its actions? From where does it draw the power and authority to independently change its economic behavior? By answering these questions we can analyze the impact of government decentralization on cities in the socialist context and begin to trace the ways in which the institution of local government defines itself and its jurisdiction. The case study of Yaroslavl' begins to answer these questions.
DATA AND METHODOLOGY

Information was collected from several sources to construct the case study. The author held in-depth interviews with officials in the State Tax Inspection Offices and Finance Departments of the Meriya in Yaroslavl' during June 1992 and again in January 1993. In addition, data was collected during interviews with officials at the executive level in Yaroslavl' city. The interviews focused on five broad topics: traditional and new tax instruments, tax collection mechanisms, the structure of local expenditures and any restrictions placed on them, inter-governmental fiscal relations, and local economic initiatives (see Mitchneck and Berkowitz 1992 for complete discussion of June 1992 interviews).

These areas are important for the following reasons:

Tax Instruments

If Yaroslavl' implements independent tax policies, then tax policy has become a matter of policy choice for the local government. We should also then see variation between localities. A manipulation of the system can substantively change the amount of financial resources (own income) available to the local government that it can then in turn apply toward creating an independent expenditure policy. The new forms could represent a direct response at the local level to new, central tax policies and indicate both a new role for local government and an extension of local power over territory.

Tax Collection

The government level and physical location of tax collection could influence who has ultimate decision making power over the transfer of those revenues. The locus of collection defines possible bottlenecks to which other levels are beholden to obtain their revenues. This specifies the conflict points and the areas in which the local level would seek change. If the local level can set and collect new taxes, this shows a tremendous amount of fiscal decentralization and some freedom over the use. If changes have occurred in the collection process, they could signify a further extension of local authority over its jurisdiction.

---

3The Meriya is currently the executive branch of the city government. It handles day to day operations and implements policy. It was formerly called the city executive committee. The head of the Meriya is the mayor, an official who is appointed by the legislative branch and approved by the central government.
Composition of Local Expenditures

First, how have formal budgetary expenditures changed during the transition process? Do we see any different types of expenditures going through the formal budget? Answering these questions can determine the extent of fiscal decentralization and the changes to the fiscal system. This will help us understand the dimensions of fiscal decentralization and indicate to what extent the local government has extended its own influence.

Interviews and Data

The purpose of the interviews was to obtain budgetary data and information from practitioners in order to assess the evolving role of local government officials and their impact on the Russian economy and population. The initial results of the interviews reveal that substantial changes in the system of local public finance were not implemented until 1992 despite Soviet laws to the contrary. The results show continuity between pre-reform Soviet practices and current local public finance (Mitchneck and Berkowitz 1992).4

The main data sources are city and district government documents called Protokols. Protokols present resolutions taken during Maliy Soviet meetings and are an important new data source. They give primary information regarding financing social and economic infrastructure and the development of local institutions relevant for market-type reforms. Resolutions document the formation of the budget and of many off-budget expenditures. The Protokols provide evidence to help understand the evolution of the economic role of local government by being a window into the local implementation of central reforms aimed at "marketizing" the former Soviet economy and by recording locally sponsored legislative acts. The level of implementation and results of those reforms are still unclear.

THE YAROSLAVL' CASE STUDY

Yaroslavl' is an industrial city in the Central Economic Region of Russia. It has a long history of industrial activity stretching back into the 16th and 17th centuries when it was the Volga river port for Moscow. The surrounding oblast is agricultural and tends to have more conservative political leanings than Yaroslavl' city which is viewed as having a

---

reformist government (see Hahn 1991). The population is nearly one hundred percent
Russian. Yaroslavl', like other cities in the Central Economic Region, is considered an
average Russian city. While the case study can not claim to be representative of all Russian
cities, the perception of its average Russian qualities and its industrial history do permit its
classification as typical.

Budgetary Revenues

Total budgetary revenues increased about nineteen fold between 1991 and 1992.
These figures are, however, fairly meaningless since they do not control for inflation. The
greatest increases are naturally from new revenue sources intended to replicate market
economic conditions. Formal budgetary revenues are still limited since fines and fees form
the main source of extra-budgetary income. Profit tax on enterprises and individual income
taxes are traditionally the major revenue sources for the city of Yaroslavl'; in 1992 they
comprised 82 percent of total city budgetary revenues which is a slight increase from 74
percent in 1991. The third traditional major revenue source was the turnover tax; however,
Yelstin replaced this with a value-added tax that decreased in importance from 21 percent of
total budgetary revenues in 1991 to 11 percent in 1992. Clearly, the city government must
rely upon the collection of relatively few revenue sources to fund its budgetary expenditures.

The city began to collect new tax sources in 1992, but the new sources remain a
relatively small proportion of the total revenues and are difficult to collect. In 1992 the city
collected budgetary revenues from privatization, bonds, a tax on property, a land tax, fees
and payments such as those due on water use and transportation vehicles. A new revenue
source in 1992 is the carry over of budgetary funds. These funds could be confiscated by
higher level budgets until 1992. The ability to carry over funds within the formal budget
represents a substantial increase in independence for Russian cities.

Off-Budget Revenues

Yaroslavl' appears to be in an advantageous position with respect to over-fulfilling its
planned revenues, funding its planned deficit, and forming extra-budgetary revenues. A
substantial change in the composition of off-budget revenues and the number of sources of
extra-budgetary revenues occurred between 1991 and 1992 in Yaroslavl'. In 1991, the city
had 29.5 million rubles of over plan fulfillment and 21.4 million rubles to spend off-budget.
According to city accounting sheets, vodka sales accounted for all of Yaroslavl’s extra-budgetary revenues in 1991. By 1992, the city accounting office no longer included extra-budgetary revenues as a single line item in its budgetary accounting, but produced a separate accounting sheet for extra-budgetary revenues and expenditures. Total extra-budgetary revenues increased more than eight times to 182.2 million rubles. Revenues from vodka sales declined dramatically in both absolute and relative terms. This revenue source dropped to 7 percent of total extra-budgetary revenues from 100 percent the previous year. Table 1 displays most sources of extra-budgetary revenues in Yaroslavl’ in 1992. Since fines are a major source of extra-budgetary revenues, the local governments have great incentive to collect the fines and enforce compliance with these laws. This is a situation where collecting fines will assist the city in a meaningful way to conduct independent expenditure policy. The dramatic increase in extra-budgetary revenues means that the city has greater ability to conduct independent expenditure policy.

**Tax Collection**

Formal tax collection mechanisms for the city are still under the jurisdiction of the federal government level. As under the previous system, the tax inspection office, physically located in city hall, is still responsible for collecting all tax revenues due to all levels of government. Interviews indicate that the workers in the office view their jobs as implementing federal government laws on taxation and as insuring that the law is followed at the local and individual levels. The city government appears to have little or no control over tax collection of federally levied taxes or over tax revenues that they share with higher levels of government.

The Yaroslavl’ city government has accomplished an innovation in the sphere of local tax collection. At the initiation of the city level Office of Finances and Prices, the city now has "a single budget." Under the previous system, the city had a single budget with the oblast. Also under the previous system, districts within the city had bank accounts into which their own formal tax revenues would flow. Now there is only one city bank account for each revenue source. Under the previous system, the practice of distribution of taxes on the income of the population did not equitably account for population variations within the city. The tax remained in the district of employment rather than of residence. Urban
planning created a structure in which the industrial districts did not coincide with residential ones. The creation of one budget for the city consolidates the budgetary revenues and expenditures at the city level. This means that rather than having seven budgets for the city of Yaroslavl', one for the city and one for each of six districts, there is one single budget. Not only has this simplified the budgetary system, but also the city government can then redistribute tax revenues, theoretically, in a more equitable manner. The city has in effect taken over lower level revenues allowing it to conduct a more integrated, city-wide expenditure policy. Two other cities in Russia (Krasnodar and Kaliningrad) adopted the same system after consulting with the Yaroslavl’ city government.

The single budget for the city clearly defines its formal jurisdictional authority and power throughout the territory of the city, rather than limiting its power and authority as under the previous system. In a reformist city like Yaroslavl’, the city government can then carry out its decisions by minimizing interference from, and the power of, district governments. The city, however, has not left districts completely powerless. District governments do still have extra-budgetary revenues and make independent expenditures using those revenues. The size of extra-budgetary revenue funds vary according to district level initiative to form them using sources such as the registration of private firms and cooperatives located on their territories.

**Budgetary Expenditures**

During the transition period, the city government has increased the level of its budgetary expenditures. Absolute figures are misleading in that they do not account for high inflation levels. The composition of the formal budget for the city is still largely controlled by higher government levels. The Yaroslavl’ Oblast government instructed the Yaroslavl’ city government to set its planned budget for 1993 at 150 percent of the 1992 level. It is thought that this increase will account for inflation and additional expenditures. The formal budget continues to fund mainly quality of life expenditures as it did under the previous system.

Several significant changes have occurred in the formal budgets of Yaroslavl’ city during the early 1990s. First, central laws giving greater fiscal responsibility to cities also have decentralized to the city and oblast levels funding the social safety net. Beginning with
the 1991 budget, a new line item appears for wage compensation for families with children. The city would pay to the oblast amounts to be added onto worker wages in the city. The oblast would then pass on to enterprises a form of social welfare payments from the city, oblast, and federal levels. Depending on the economic situation of the city, it passes resolutions allocating additional funds during the year for wage compensation. The city level funding of the social safety net did not significantly occur until 1992 and the formal break up of the former Soviet Union.

Second, the 1992 budget has a new line item - development budget. The development budget funds capital construction in the city for city property. This line item in Yaroslavl' consists entirely of funding construction and reconstruction of city property and social and economic infrastructure. This fund is formed through the combination of revenue sources from surplus budgetary revenues, extra-budgetary funds, and a small amount from the oblast budget. In 1991, the development budget fund appeared as a line item in the accounting of surplus and extra-budgetary expenditures (i.e. as an off-budget expenditure). In the past, these expenditures were made in the city only through informal or higher level means. The inclusion of a development budget in the city budget marks a significant change in the formal responsibility and authority of the city government.

Third, the city included a reserve fund as a line item expenditure. This institutionalizes a practice used by state enterprises to carry over funds to allocate for investment purposes. The practice began in Yaroslavl' as the city was unable to spend the planned amount but needed to allocate the funds within their budget. They now set aside up to ten percent of their planned expenditures for this reserve fund. Yaroslavl' city officials called this their way of being able to put out fires. Other large cities also reportedly created reserve funds. Several of the financial officers with whom we spoke had previously worked for industrial enterprises. The spread of reserve funds into local public finance could represent the diffusion of enterprise financial practices into local government.

**Off-Budget Expenditures**

Off-budget expenditures have changed significantly since the late 1980s. Under the previous system, the city made few such expenditures since it did not have a legal right to form off-budget revenues as discussed above. The composition of off-budget expenditures
varies according to revenue source. Certain revenue sources can only be used to make specific categories of expenditures and, furthermore, the right to use surplus budgetary funds or extra-budgetary funds varies within city government between the legislative and executive branches.

Table 2 displays most of the items that were financed by surplus funds in Yaroslavl' during the first three quarters of 1992. Many of these expenditures are funded by the formal budget too. The exceptions, however, indicate that the federal level has decentralized expenditures to the city level. For example, local elections, funded by the republic in 1991, are now funded by the city. Activities of federal importance, like the Committee on Land Reform obtain local funding in addition to federal funding. Social security and protection also becomes a local responsibility (e.g. compensation for lunches and grants to poor).

Given that the city perceives federal normatives as inadequate, a locality's ability to over-fulfill the planned revenues, and then to direct funds into maintaining local infrastructure and quality of life, takes on paramount importance to the city government.

While the expenditures from surplus revenues mainly target quality of life issues, extra-budgetary expenditures in the first three quarters of 1992 were clearly geared toward maintaining the physical infrastructure of the city and supporting the morale of the inhabitants. Table 3 displays extra-budgetary expenditures in Yaroslavl' during the first three quarters of 1992. There were few significant departures from traditional municipal expenditures, however, several items merit further discussion. First, the morale and place-related expenditures focus on financial support of sports clubs, restoration of a historical landmark (Vlas'evskaya tower), and a contest and prize for a Yaroslavl' city emblem. The city makes expenditures aimed at advertising the city and at creating (if not supporting) place-related consciousness. Second, the city makes expenditures that clearly support local enterprises. For example, the city government subsidized a municipal newspaper in order to compensate for the increased market price of printing paper. Soviet enterprises have always been subsidized, but this is clear evidence that the city government is taking on a role in protecting enterprises from the vagaries of the market.

Data on extra-budgetary expenditures by the city in December 1992 indicates that towards the end of the year, the city substantially subsidized local enterprises through direct
grants and credits. This, too, is a new function of city government, one that under the previous system only the central government could do. Without commenting on the wisdom of such subsidies, the city has clearly turned its attention toward supporting and developing economic activity within its boundaries. Despite legal constraints that define only the retail and service sector as municipal property, the city will give such financial assistance to enterprises of any type located on their territory.

The increasing importance of extra-budgetary expenditures, noted above, highlights an additional political factor of the budgetary system in Russia. Only the executive branch, the mayor’s office, may expend the extra-budgetary revenues. The legislative branch, the City Soviet and Maliy Soviet, monitors these expenditures but can independently expend funds only from the budget surplus. Since only the executive can expend the extra-budgetary funds, these expenditures do not necessarily reflect legislated policy. A detailed accounting of December 1992 extra-budgetary expenditures from city hall shows a wide variety of expenditures from one million rubles on a Soviet-German Society to almost 150,000 rubles to the oblast executive branch. In addition, substantial expenditures are made to subsidize city enterprises, as well as to continue to develop the cultural infrastructure of the city. These kinds of expenditures on foreign relations, enterprise subsidies, morale, and entertainment indicate both priorities of, and substantial new authority for, the local level of government.

**SUMMARY AND CONCLUSION**

The case study of Yaroslavl' city leads to the conclusion that while a new fiscal system appears to function in Russia, elements of continuity with the previous system still exist that limit the city’s ability to conduct independent fiscal policy. Despite Soviet laws to initiate fiscal decentralization, major changes in the formation of local budgetary revenues and the composition of local budgetary expenditures did not occur until the break up of the Soviet Union. Elements of independent fiscal policy evident in an examination of the local budget in Yaroslavl' indicate that the economic role of local government has grown and that the local government itself, not the central government, is pushing the boundaries of political and economic influence over territorial-administrative jurisdictions. The increasing importance of off-budget revenues and expenditures, the creation of a single budget for the city of Yaroslavl’, and the city-level subsidies to both the population for the social safety net
and to enterprises for propping up the local economy represent significant changes for local public finance during 1992.

Yaroslavl' city redefined both its economic role vis-a-vis central authority and its territorial power by independently forming revenues and by creating new areas of fiscal responsibility with its off-budget expenditures. The city moved from using budgetary revenues to finance limited elements of social infrastructure to financing the industrial sector of the economy with subsidies and credits. The city also took on the role of financing the social safety net above and beyond the criteria set by the central government. The city extended its fiscal authority and power throughout the districts of the city by forming a single budget that reduced district-level fiscal means. The case study of Yaroslavl' shows an activist city government attempting to produce a new system, not to reproduce the previous one.
| TABLE 1  
Sources of Extra-budgetary Revenues  
Yaroslavl', 1992 |
|---|

**Fines**

- Traffic fines
- Public transportation fines on passengers
- Fines related to use & protection of land
- Fines against employers for violating Law on Employment of Population in Russia (re: firing of workers).
- Fines for using economic sanctions for the violation of state discipline of prices
- Fines for presenting fraudulent documents to the Office of Finance and Prices
- Fines for overstating prices

**Other**

- Privatization of municipal property
- Liquor and Vodka sales mark-up of 25% on commercial prices
- Fees for forming private motor transport establishment
- Enterprises
- Allocation of land
TABLE 2

Yaroslavl' City Expenditures from the Over-Fulfillment of Planned Revenues, January through November 1992

City economy
- Purchase stevedore for road administration
- Sister Cities exchanges
- Compensation for lunches for workers in the following sectors: education, District Soviets, Trade-Union Committee, cultural organizations
- Committee on Land Reform
- Reimburse cafeteria # 13 for expenses
- Purchase of ambulance for city health administration
- Reimburse city enterprises for credits given to schools & grants to poor
- District elections (1991 paid by republic)
- Purchase auto transport for municipal militia
- Repair facade of historic military hospital
- Repairs to buildings of Philharmonic Society
- Repairs to the shop for the needy in Dzerzhinskiy District
- Organization of city electric and automobile transportation
- Public defense of workers of the city health administration and decontamination station
- Seasonal procurement of potatoes and vegetables from 1992 harvest
- Purchase of ten city busses
- Newspaper "Gorodskie Novosti" (subscriptions for the needy)
- Purchase of IBM 386 computer for Department of Theoretical and Experimental Physics at Ya.G.P.I. (city institute)
- Supplemental finance of housing for fourth quarter of 1992
- Bureau of Technical Inventory (to assess value of buildings)

Education
- Administration
- Awards and stipends to pedagogical workers of schools, pre-schools and vocational training schools
- Assuming the management of the preschool system
- Presentation of medals to graduates of city schools

Health
- Funding purchase of supplies for the cafeteria of a medical institute
- Creation of Pharmacy Section in city's Health Care Administration

Sports
- Mayor's hockey partnership with professional club "Torpedo" (physical culture)
### TABLE 3
Extra-budgetary Expenditures in Yaroslavl' Approved by Maliy Soviet, January through November 1992

<table>
<thead>
<tr>
<th>Capital investment</th>
<th>Education</th>
</tr>
</thead>
<tbody>
<tr>
<td>Development of urban infrastructure</td>
<td>Annex to schools</td>
</tr>
<tr>
<td></td>
<td>Worker's areas at educational-production enterprise (Dzerzhinskiy)</td>
</tr>
<tr>
<td></td>
<td>Health, annex to hospital</td>
</tr>
<tr>
<td>Communal Construction</td>
<td>Water supply</td>
</tr>
<tr>
<td></td>
<td>Roads</td>
</tr>
<tr>
<td></td>
<td>Engineering network</td>
</tr>
<tr>
<td></td>
<td>Equipment for main pumping station</td>
</tr>
<tr>
<td></td>
<td>House building cooperative &quot;Dizyel&quot;</td>
</tr>
<tr>
<td>Social Security</td>
<td>Other</td>
</tr>
<tr>
<td></td>
<td>Restoration of Vlas'evskaya tower</td>
</tr>
<tr>
<td></td>
<td>Small-scale wholesale base in Dzerzhinskiy District</td>
</tr>
<tr>
<td></td>
<td>Construction and design of &quot;City M&quot; on Moscow Avenue</td>
</tr>
<tr>
<td></td>
<td>Construction and design of &quot;Signal&quot; on October Avenue</td>
</tr>
</tbody>
</table>

**Health and Welfare**

- Organization of confectionery at the Yaroslavl' Medical Institute
- Social assistance to families with three or more (or ill) children
- Community Red Cross (charity services)
- To cover losses of oblast Soviet 's International League of Sobriety and Health
- New Year's party and gifts for 570 foster children and 180 children whose parents have not paid alimony
- To Organize city medical insurance fund

**Sports**

- Sports club travel
  - Participation of tennis team in "Karelian Cup" Tournament
  - Tournament for technical sports and for participation of Yaroslavl' teams in Russian tournaments
  - Participation of basketball team "Spartak" (Kirovskiy District) in the championship of Russia
- Firing ranges at youth sports-technical schools
- Subsidy to enterprise for physical culture and sports
- Purchase of equipment for children's baseball
- Annual prize for track and field teams at local newspaper
- Reception of sports delegation of school children from German sister city

20
TABLE 3 (cont.)
Extra-budgetary Expenditures in Yaroslavl' Approved by Maliy Soviet,
January through November 1992

<table>
<thead>
<tr>
<th>Sports</th>
</tr>
</thead>
<tbody>
<tr>
<td>V. A. Sokova Memorial International Checkers Tournament</td>
</tr>
<tr>
<td>Mayor's Soccer partnership with professional club &quot;Shinnik&quot;</td>
</tr>
<tr>
<td>Participation fees for Russian-Canadian tournament &quot;Sport for All&quot;</td>
</tr>
</tbody>
</table>

<table>
<thead>
<tr>
<th>Subsidies to enterprises</th>
</tr>
</thead>
<tbody>
<tr>
<td>Subsidy of newspaper</td>
</tr>
</tbody>
</table>

<table>
<thead>
<tr>
<th>Other</th>
</tr>
</thead>
<tbody>
<tr>
<td>Contest &amp; prize for Yaroslavl' city emblem</td>
</tr>
<tr>
<td>Contribution to Tolgsky Sacred-Introduction Monastery</td>
</tr>
<tr>
<td>Concert for citizens of Yaroslavl'</td>
</tr>
<tr>
<td>Participation in seminar conducted by Association of Oblasts and the Cities of Central Russia</td>
</tr>
<tr>
<td>Improving the work of the tax assessor</td>
</tr>
<tr>
<td>Annual dues to the Union of Russian Cities</td>
</tr>
<tr>
<td>Publication of Book of Memories, about those from Yaroslavl' killed in Afghanistan</td>
</tr>
<tr>
<td>Organization of exhibits dedicated to the historian N. V. Kuznetsova</td>
</tr>
</tbody>
</table>
REFERENCES


_____.


Rechko, Galina N. "Increasing the Role of Financial Resources of the Region in Social-Economic Development (in Kuzbass case)." Kemerovo, Russia, 1992. (Typewritten.)

Romaindo, Henry J. and Stuart, Robert C. "Financing Soviet Cities." In Henry W. Morton