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1. A Survey of Soviet Research
2. Sizing Up the Shadow Economy:
Review and Analysis of Soviet Estimates

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REVIEW AND ANALYSIS OF SOVIET ESTIMATES**

Valeriy M. Rutgaizer

Paper No. 34, February 1992

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SUMMARY NOTE

Prepared by NCSEER Staff

This survey of Soviet research and publication on the Second Economy up to the summer of 1991 identifies two still diametrically conflicting viewpoints; a traditional "liquidatory" one which views private entrepreneurial activity and commercial mediation as an unalloyed evil, a criminal activity to be repressed by every means; and a "constructive" approach, which recognizes the merit of some aspects of these activities for their social and economic benefits. The author traces the evolution of both schools of thought and illustrates their practical consequences by the ineffectual exchange of 50 and 100 ruble banknotes for the former, and the legalization of lease-operated enterprises for the latter. The significance of the paper lies in the fact that both schools still prevail and conflict, and its implication that, should market reforms fail and be repudiated, the triumph of a "liquidatory" mentality and the consequent effort to wipe out the Second Economy would lead to reprisals and restoration of the tyrannical aspects of an authoritarian regime.

The second paper, by the same author, which begins on page 39, was also written in June of 1991. It covers two topics: public attitudes toward the Second Economy based on opinion polls through 1990, which suggest that, while mixed and selective on some aspects, the Second Economy was associated in most minds with criminal "mafia" activity and condemned; and an analysis of Soviet estimates of the size of the Second Economy in which the author not only illustrates the variety and ingenuity of activities encompassed, but concludes that estimates differ widely, are poorly substantiated, but are grossly correct at about 100 billion rubles of trade annually in the late 1980's. After brief discussions of estimates of black market capital, and hard currency circulation, the author's most telling conclusion is that as soon as estimates of the shadow economy are published, they are employed for political ends, where evidence does not really matter.

Part I

The Shadow Economy in the USSR: A Survey of Soviet Research*

Valeriy M. Rutgaizer**

1. Introduction.

There is no doubt that the "shadow" or "underground" economy in the Soviet Union,*** as a form of activity concealed from official control of income derivation and state participation in the distribution of profits, which became a focus of attention in the mid-eighties, originated well before our day. Apparently, this hidden economic activity will exist forever. In the future it is also an inevitability.

At the same time there is a widespread belief that the underground economy in the USSR appeared mainly in the post-Khrushchev period. Under Khrushchev it was only

* The following article was written (in Russian) expressly for Berkeley-Duke Occasional Papers. It has been only slightly edited from an English translation done in the USSR. The author, a prominent Soviet economist specializing in problems of household consumption and related matters, pioneered internal studies of the Soviet "shadow economy" while holding a senior position in the Research Institute of Gosplan USSR.

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*** This paper was completed in June 1991, before the dramatic changes that have made the terms "Soviet," "Soviet Union," and "USSR" anachronistic. Hence, they are retained in this paper and are used in their traditional sense.

beginning to emerge. And it was supposedly non-existent under Stalin.

For the most part I agree with this assessment.¹ The development of the shadow economy in the USSR is determined by the transformation of the authoritarian regime of the '50s-'70s. "It seems to me," writes A. Katsenelinboigen, "that in the Stalin period corruption in the Soviet Union was less widespread than in the post-Stalinist period." (2, p. 95). He relates the growth of corruption in the USSR in the early the '50s to the fact that the authoritarian leadership had become less tyrannical.² Whereas earlier the "authoritarian leadership" sought to consolidate its "own authority" via mass reprisals, in the absence of repressions the "overriding corruption, at all levels of social structure, creates fertile ground for materializing the threat of imprisonment or execution by a court decision" (2, p. 95). Thus, corruption as one of the key elements of the shadow economy expands together with the transition from a tyrannical version of the authoritarian regime³ to less repressive manifestations thereof.

I believe that corruption and the shadow economy have common ground (properly speaking, corruption is one of the elements of the shadow economy). The fewer elements of tyranny in an authoritarian regime, the more substantial the base for an underground economy. But if corruption becomes a method of preserving authority in the conditions when tyranny has been abandoned, then the shadow economy becomes an instrument of ensuring the well-being of a substantial part of the population which is incapable of earning its livelihood by working in the "above-ground" economic sector on a legitimate basis.

I therefore tend to agree with the opinion expressed by G. Grossman that the shadow economy in the USSR encompasses a wide range of diversified types of activity involved in

production and barter, which meet at least one of the two following demands:⁴ for one thing it is carried out with the aim of deriving a direct personal benefit; and secondly, it directly or indirectly runs counter to existing legislation (4, p. 25). It seems to me that these conditions are sufficient to explain the existence of most types of "underground" economic activity under an authoritarian regime. Hence it is quite clear that such a regime, together with an administrative-and-command system of government inherent in it, begets the underground economy. G. Popov maintains that the apparatchiks as well as the shadow economy operators are the "legitimate children of the ineffective system of socialism" (7, p. 7).

However, there is also another point of view on this issue. Certain authors in the West refer the "second," alternative economy under socialism to "shadow capitalism" (see for example, H. Hemann, A. Bezanson in 5, p. 106). Many Soviet authors regard the shadow economy as the result of commodity-money relations untypical of socialism, as a kind of "underground capitalism." For example, Professor A. Yeremin, a well-known opponent of market economics theories, has no doubt whatsoever that the "existence of the shadow economy and the unearned incomes derived as a result from it are a kind of payment for monetary indicators..., a profit..." (8, p. 126). He thinks that it is extremely easy to close all sources of the so-called unearned incomes in "public production" - it is "necessary to pursue more consistently and vigorously the activity of ... economic cells ... guiding them ... towards the production of consumer values..." (Ibid.), i.e. without using market relations typical of capitalism. Similar ideas are expressed by other writers. Thus, V. Mineev believes that the "main cause of unearned income is the use of commodity-monetary relations" (9, p. 115). This view is shared by V. Dolgov, who thinks

that "in the framework of market mechanisms it is impossible to cut off the sources of unearned income. This must be done on a fundamentally new basis - on the basis of laws of consumer value" (Ibid.). However, it remains unclear just what these laws are.

The existence of the shadow economy in the Soviet Union is often explained as a legacy of capitalism, inherited historically. In the above-mentioned work (3) it is maintained that the present capital of the underground economy was partially formed as far back as the pre-revolutionary period (before 1917). This is not only an attempt to impart to the shadow economy an enemy image, so customary to the Soviet people - the image of a capitalist, a rich landowner or a kulak (well-to-do peasant), but also an attempt to give a political and economic appraisal of this phenomenon in Soviet society. The underground economy, which has inherited part of pre-revolutionary capital, is in its essence "a form of underground capitalism, as opposed to socialism in its Leninist interpretation" (3, p. 68). Hence, the appeal to "fight the 'underground economy' in real earnest, as though this were a matter of life and death" (Ibid.).

This approach to problems of the "shadow" economy in contemporary Soviet society imparts a strong political flavor to all discussions, debates, and the accompanying practical actions. It is not accidental therefore that the subject of "struggling against the shadow economy" has become one of the key features in the election programs of many parliamentarians, who eventually won the elections. The Soviet people seem to be transfixed by arguments to the effect that in the Soviet Union there exist millionaires,⁵ and that the shadow economy is a ubiquitous phenomenon.

The public is particularly impressed by figures about the volume of underground "turnover" [i.e., gross aggregate

sales per year -- G.G]. In Tatyana Koryagina's estimates, the underground turnover amounted at the end of the 1980s to 90 billion rubles (10), while the accumulated illegal capital reached some 200-240 billion rubles (11). Other authors assert that this capital is at least twice as big and may be estimated at 500 billion rubles (3, p. 62), while income from the shadow economy amounts to 160-180 billion rubles annually, with an illegal yearly turnover (i.e. the sum of material expenses and gross income) estimated at approximately 210 billion rubles (*Ibid.*).

Unfortunately, none of the authors reveals the methodology of calculating these figures. They assume that the gross turnover is a sum total of all trade, the total proceeds received from the sale of goods and services provided to consumers of the underground economy. If we eliminate from the gross turnover the material expenses, we shall get as a result the pure product of the underground economy. This indicator is analogous to value added, the only difference being that the latter also includes amortization (depreciation) costs. However, no one has so far indicated what share in the gross underground economic turnover amortization accounts for. I think that it is totally ignored. As for the accumulated underground capital, this represents all monetary savings of its participants plus material inputs in real estate, the use of which generates income.

In our opinion, the proportion of the accumulated underground capital is greatly exaggerated. This in particular has become clear during the partial exchange of high-denomination banknotes in the Soviet Union in January 1991, a subject that will be dealt with in more detail below. However, the analysis of estimates of the underground economy turnover, presented by different authors, constitutes a problem of its own.⁶ We do not intend to dwell on it

within the scope of the present survey. Rather, here we attempt to systematically survey Soviet publications on problems of underground economy in the USSR.

First publications on this subject appeared at the very beginning of the 1980s. "It is impossible to ignore the 'shadow' economy any longer," wrote Tatyana Zaslavskaya in 1980. "The results of its latent forms of operation substantially reduce the effectiveness of planned regulation..., distribution and consumption. What happens is a covert re-distribution of incomes among various social groups, quite often causing appreciable damage to state interests" (14, p. 30).

A similar conclusion was made a bit later in a survey published by the USSR State Planning Agency's (GOSPLAN's) Scientific and Research Economic Institute. The results of the survey indicate that the scale of redistribution of public incomes in the framework of the underground economy "is quite large" (15, p. 59).

This is why statistical analysis has become the most natural direction in the studies of underground economy and the related processes. This direction - we shall call it statistical - abstracted itself, as it were, from the causes of this phenomenon. It saw as its main task a correct appraisal of the size of the national income. A whole range of studies was of an ancillary, secondary character, subjugated to the aim of making a correct taxation in the shadow economy. This line of studies has failed to receive much following in Soviet literature on the subject. It is more fully represented in works by foreign authors, in particular G. Grossman and V. G. Treml.

At the same time the study of the shadow economy in the USSR has nonetheless always been based on statistics. Moreover, the idea about the expansion of the shadow economy in the Soviet Union predetermined the very need of

its profound study. And here it was essential for analysts to come to a conclusion as to what has brought about its rise and development in Soviet society.

Two approaches can be stressed here. The first approach saw the shadow economy within the scope of the administration-and-command system of government. This system excluded the possibility of the shadow economy directly integrating into the "open", legitimate economy. This approach aimed at transforming the economic system so as to ensure a combination of the useful part of the shadow economy with the legitimate economy.

The second approach ruled out the very possibility of any shadow economy existing in Soviet society under socialism. This approach was ultimately aimed at uprooting, liquidating the shadow economy, and can therefore be described as a "liquidatory" approach (in contrast to the first one, which can be termed "constructive.")

2. The constructive approach.

This line of studies of the underground economy raised problems whose resolution involved substantial transformations in the Soviet economic system. We have in mind leasing and cooperatives. Leasing and cooperation were regarded as instruments to overcome the total "statization" of economic life, to escape which most initiative and enterprise was forced into the underground sector.

The constructive direction began with an analysis of the shadow economy and its impact on the public's incomes in the services sector. This approach was developed at Gosplan's Scientific and Research Economic Institute under the present author's direction. This was in particular where most works by Tatyana Koryagina originated.

The very first articles written within the scope of the constructive approach maintained that the redistribution of income was for the most part due to hidden activity in the provision of public services (16, p. 53). However, this activity is useful to society; therefore, we thought at the time that it should be legalized and appropriate conditions provided for it.

Later, problems of the shadow economy in the services sector were considered in our article called "Measure of Labor and Measure of Consumption." We believed that it was "highly promising... to organize the work of individual craftsmen or small groups thereof, under contract with state-run enterprises in the services sector..." The creation of cooperative ventures (17) is also worthy of consideration. All this could be achieved only by transforming the economic system. Leasing and cooperative arrangements, both directed at legalizing a socially useful part of the shadow economy⁷ were precisely aimed at transforming the general economic system.

We will present a history of the evolution of contractual economic relations in the services sector, which eventually developed into a leasing model. The concept of contractual relations was developed at the beginning of the eighties at Gosplan's Scientific and Research Economic Institute, jointly with heads of the Ministry of Service of Estonia, Yu. Sillaste and E. Truve (19). We presumed that the worker "must himself be interested in expanding the volume of his services." For this purpose the leasing mechanism was the most suitable one (19).⁸ The leasing schemes based on contractual relations which we developed were used in preparing the resolution of the CPSU Central Committee and the USSR Council of Ministers on expanding communal services, published in February 1984 (21).

This resolution allowed the appearance in the communal services sector of the so-called contractual form of labor remuneration with a fixed volume of proceeds to be remitted to the state.

The Estonians were the first in the Soviet Union to use this scheme. What is known as the second contractual scheme provided real possibilities for the legalization of the so-called "receipt-free" form of servicing. On days when comprehensive checks and inspections were carried out by state agencies the actual proceeds of the communal sector were found to be 1.5-2 times higher (22, page 23). Usually the proceeds for the "receipt-free" services stayed in the pockets of workers who drew state salaries. With the introduction of the second contractual scheme, on a long-term basis, the temptation to hide money was lost. Now all proceeds, with the exception of earlier established sums to be remitted to the state, belonged to the workman. He earned this money himself and did not receive it from the state.⁹

The application of the second contractual scheme drastically changed the entire system of relations in the state-controlled services sector. In 1987 with T. Koryagina, Yu. Sillaste, E. Truve, and I jointly presented a report at a session of the USSR Academy of Sciences' Scientific Council, chaired by A. Aganbegyan. The main ideas of the report provided for the transformation of the shadow economy in the communal services sector in the USSR into legitimate lease-based and cooperative forms of economic activity, as well as the abolition of republican ministries of communal services, as unnecessary entities of administration under the new economic conditions of leasing and cooperatives. Subsequently the daily Izvestiya published an interview with T. Koryagina and I. Kruglianskaya on the subject of our joint report, under a somewhat unusual title "Does a Barber Need a Minister?" (24).

Later, leasing was used as an instrument to change the system of public catering in Moscow. We are currently rendering assistance to a Moscow-based cafe, Sever, which was the first to start operating on a leasing basis,¹⁰ and later on the practice was taken up by the Butovo construction-materials plant. (Its manager, Mikhail Bocharov, eventually made a brilliant career. At present he is a deputy of the USSR Supreme Soviet and of the RSFSR Supreme Soviet, Chairman of the RSFSR Supreme Economic Council and one of Boris Yeltsin's closest advisers.)

The leasing model that we developed quickly gained ground as of mid-November 1988.¹¹ And its development, as we have already mentioned, began with the study of underground economic processes in the services sector, of forms of private hidden entrepreneurship.¹² Thus the analysis of the shadow economy within the framework of the constructive approach yielded definite practical results. While we do not wish to exaggerate, it can be stated that lease-operated enterprises are playing an appreciable role in the present-day organizational structure of the Soviet economy, and the idea for this scheme, we repeat, emerged as a result of studying the functioning of underground activity in the services sector.

3. The liquidatory approach.

This line of studies of the underground economy was originally related to the analysis of hidden and illegal aspects of its activity. With these aims in view at the beginning of the 1980s a special subdivision was created within the framework of the USSR Procurator's Office Scientific and Research Institute for the Studying and Prevention of Crime, headed by A. Larkov. According to A. Larionov, who in 1983 published the first results of studies

conducted by his department, "there are still manifestations of ineffective economic management and administration of the assets of certain enterprises and organizations..., facts of mismanagement, waste, embezzlement and other economic offenses, including abuses, negligence and misappropriation, quite often involving considerable deficits of material values (29, p. 71.-- my emphasis).

As can be seen, this line of research originally analyzed phenomena connected with the development of the underground economy being as purely temporary and localized. These phenomena by themselves originated from "legal shortcomings", including primarily the non-observance of the principle of the inevitability of punishment and responsibility of all persons guilty of these offenses.

Special attention was focused on the issue of the so-called unearned incomes. "In this country," wrote A. Larkov, "there are quite a few citizens who engage in individual labor activity with considerable benefit to society. At the same time there are also persons among them who use forms of individual labor activity for the aims of private entrepreneurship, to derive unearned, illegitimate incomes..." This author related the emergence of unearned incomes to partial deviation from the conditions established by the state for the operation of self-employed individuals. Therefore, as it appeared to the USSR Procurator's Office research institute, it was possible to overcome these deviations only by stepping up control and monitoring of the individual labor activity itself. In order to do that it was necessary "to place under total state control all types of activity generating incomes, classifying them into legal, illegal, those involving or not involving socially useful activity, unearned, criminal, etc. incomes" (29, p. 79). Hence the intention to elaborate special legislation directed against unearned incomes.

The rationale behind this sort of legal activity was to create conditions that would exclude the very possibility of generation or utilization of unearned incomes. "It is a unique feature of our society," wrote Vasiliy Seliunin at the time, "that a private individual's money cannot be used to make new money. It is only the person's individual work effort that is the source of steadily rising living standards of his family" (30). Fortunately, V. Seliunin eventually changed his views. I think that it was the USSR Procurator's Office research institute which came up with the initiative to work out special legislation directed against unearned incomes. This activity materialized in the shape of a Law on Combatting Unearned Incomes,¹³ adopted in 1986.

Another research center within the framework of the liquidatory approach of underground economy studies was set up in early 1980s under the umbrella of the USSR Interior Ministry, where a separate division was created, specialized in combining studies of economic and legal aspects of struggle against the so-called misappropriation of socialist property. One of the directors of this division was A. Sergeev, who later became an research associate at the USSR Academy of Sciences Institute of Economics. In January 1987 he presented a report entitled "The Origin and Structure of Unearned Incomes and Economic Methods of Fighting Them". Reviews of a public discussion of this report were published in the journals Voprosy ekonomiki and Planovoye Khozyaystvo.

According to L. I. Abalkin, director of the USSR Academy of Sciences Institute of Economics, this report is "especially interesting in that it offers an unorthodox view on the problem at hand, whereby the main source of unearned incomes is not individual labor activity, "underground economy" or other analogous processes, but the nationalized sector of the economy (9, p. 105). This view is echoed in

the debates and reviews of A. Sergeev's report published in Planovoye khozyaystvo. "The main part... of unearned income," writes A. Sergeev, "is income generated as a result of the exploitation of labor... This form of unearned income was abolished at the end of the transitional period....[i.e., in the thirties --G.G.]" (9, p. 124). A. Sergeev supposed at the time that "the main cause of unearned income in the national economy on such a wide scale is the loss by workers and employees of a collective feeling of master and owner of the national property as well as of the feeling of being the owner of one's own enterprise" (31, p. 92-93).

It is noteworthy that eventually A. Sergeev considerably revised his views on the origin of unearned incomes, as well as of the underground economy as their main source. But at that time, at the beginning of 1987, A. Sergeev thought that it was necessary to simply "thwart "the derivation of unearned incomes in public production sectors..." (31 p. 88). What was required for that? 1) Improve accounting practices; 2) clarify the responsibilities of individual subdivisions within the enterprise; 3) improve inventory procedures; 4) to enhance the effectiveness of monitoring and supervision procedures; 5) to improve the organization of audits and inspections; 6) substantially increase the responsibility of officials for the accuracy and authenticity of information and reports presented; 7) keep better and fuller accounts of losses and waste;

8) reveal more cases of report padding and falsification;¹⁴

9) prevent price hikes.

This covers all concrete recommendations made by A. Sergeev. Obviously, they did not go outside the habitual scope of demands involving "intensification," "improvement," "enhancement," etc. Later on, having found the main cause of the underground economy in the existence of "underground capitalism," A. Sergeev proposed quite different measures,

which proved their worth during the period of fighting capitalism in the so-called transitional period of the 'twenties-the first half of the 'thirties. Therefore if one consistently pursues the idea of excluding commodity-money relations, and with them the underground economy, it will be perfectly logical to come to the conclusion that was arrived at by the end of the transitional period - i.e., the Stalinist economic model.

The first step along this path should be a monetary reform. "It is proposed," wrote A. Sergeev, "to exchange for each individual a fixed sum of money (say 10,000, 15,000 or 20,000 rubles). Any money in excess of the established limit would involve the filing of an income declaration and documents certifying the legitimacy of this money, at the request of fiscal agencies" (3, p. 72-73).

In addition to a cash reform, A. Sergeev proposes urgent implementation "of such a democratic measure as the adoption of a law on progressive inheritance taxation..."¹⁵ (3, p. 76). At the same time, he goes on, "it is necessary to create, as a matter of urgency, a countrywide smoothly operating mechanism of monitoring and controlling the incomes of citizens... which would ensure... reliable protection against excessive incomes of "black market operators" (Ibid.). It is unclear, however, just what these "excessive incomes" are.

Another proposal made by A. Sergeev is the limitation of the cooperative sector: "The attack on the shadow economy should proceed via streamlining the cooperative movement, cutting it off from the illegal business. It is necessary to restore the experience of the 'twenties, when on Felix Dzerzhinsky's initiative an authoritative commission was created to detect and cut short the activity of underground capitalists and pseudo-cooperators" (Ibid.).

This is the essence of ideas arising from the liquidatory approach to the study of the underground economy. All these ideas have produced a certain impact on the present government headed by Valentin Pavlov. A. Sergeev maintained that as a result of a cash reform within the framework of combatting the underground economy, "not less than 100-150 billion rubles¹⁶ would be withdrawn from circulation, which would be tantamount to overcoming the state budget deficit" (Op. cit., p. 74). It appeared very enticing to liquidate the budget deficit by this method.

In his interview with the Financial Times V. Gerashchenko, Chairman of Gosbank, said that the cancellation of 50- and 100-ruble denomination banknotes was designed to withdraw from circulation 25 billion rubles. In actual fact, 3-4 times fewer rubles were confiscated.

"It was not our idea," V. Gerashchenko said, "but we passively supported it. We were fed up with ... demands from all sectors of public opinion that there should be money reform. We thought that this kind of exchange would show that it is not the main problem in our economy" (33).

The British correspondents who quoted this statement by V. Gerashchenko pointed to his relative independence from the central government and also to his deep cynicism in appraising this unhappy cash reform. It is clear, however, that now hardly anyone will succeed in implementing a general monetary reform any time soon. At any rate, the old motive of struggling against the shadow economy by carrying out a monetary reform is not likely to work any longer. And now I think that the very idea of a cash reform, after the cancellation of 50- and 100-ruble banknotes, will never be able to gain enough public support, especially because in order to exchange old banknotes for new ones it would be necessary to put into circulation a considerable portion of

new money, which, far from reducing a budgetary deficit, would on the contrary increase it.¹⁷

I should also like to point out that the small difference between the pre- and post-exchange volumes of 50- and 100-ruble banknotes calls into question the colossal figures of the underground economic turnover published in the press and in scholarly works. According to G. Zoteev, during the exchange of banknotes it was only on very few occasions that sums in excess of 100,000 rubles were declared (34, p. 407). Following appropriate checks and inspections, even these sums of money were usually exchanged. At any rate, it is not clear how many black market operators were found out as a result of the January 1991 cash reform. Not a single name has been named.

4. Classification of underground economic activity

First publications about the underground economy contained only general classifications of types of activity involved. Thus, the above-mentioned article said: "The redistribution... is caused, among other things, by some fairly legitimate reasons... and semi-legal phenomena..., and also by illegal forms of activity..."¹⁸ In fact, this three-fold classification of illegitimate incomes generated by the underground economy is repeated in subsequent classifications of the underground economy.

The most detailed classification was offered by A. Shokhin,¹⁹ who wrote: "The structure of the "underground economy" can be presented as a combination of the following four elements: the illegal part of the 'second economy', the 'informal' economy, the fictitious economy and the 'black economy'" (36, p. 69).

According to the author, the "first" economy includes "large state and cooperative enterprises and collective

farms, which up until very recently have been regarded as a purely socialist economic sector" (p. 69). Hence the "second" economy is not a large-scale but small-scale production, and, in all likelihood, up until recently has not been considered to be truly socialist. At the same time A. Shokhin includes only the illegal part of the "second" economy in the shadow economy. However, an illegal component also exists within the framework of the "first" economy, for example, in the cooperative and collective farm sector, writes A. Shokhin.

In A. Shokhin's opinion, the next element of the shadow economy are the actually illegal methods of management within the framework of the administrative system (p. 74). This in particular refers to "mutually beneficial arrangements that suit both sides - the centralized planning agencies and sectoral administrative bodies, on the one hand, and on the other - enterprises and production associations." The "over-fulfillment" of obviously lowered planned production targets yielded a large number of tangible benefits and advantages in the shape of bonuses, allowances and various other material incentives" (p. 74). The author also relates to the informal economy the "actual existence of the market in means of production,²⁰ together with strict mechanisms of allocation and rationing thereof..." (p. 76). Meanwhile "bribery acts as form of redistributing incomes..."²¹

We consider somewhat questionable what A. Shokhin terms the informal economy as an element of the underground economy. This form of activity ensured the functioning of the economy under the command-and-administration system.²² Only bribery can be regarded as a special part of the underground economy, and it can well be considered as an illegal form of activity in its own right.

As for the so-called fictitious economy (report padding and falsification), Shokhin is apparently right.²³ This

element of the shadow economy was obviously lacking in our 1981 classification of the shadow economy. However, later on, in 1987, together with Yu. Sheviakhov, I presented a detailed analysis of this aspect of the underground economy in a journal article (40).

The next element of the underground economy, according to A. Shokhin, is the "black" economy, including such forms of "economic crime that involve illegal production activities" (p. 80). It needs to be pointed out that "private" professional practice within the scope of public health system and public education was unfairly included here (p. 80), as well as "the state-controlled part of the housing and communal economic sector" (p. 80). We regard this as regular forms of fee-charging services that exist outside state control - there is nothing "black" about them.

A. Shokhin assigns to the "black" economy:

- the underground economy, when whole enterprises²⁴ or separate subdivisions of state-controlled enterprises operate beyond state control, within the framework of shadow economy (p. 81);
- the "mixed", diversified economy;
- embezzlement and theft of private property (p. 82);
- speculation (p. 82);
- "machinations with shortages for gainful purpose..., the perpetrators of these machinations being for the most part workers in the retail trade sector²⁵ and workers in allied sectors..." (p. 82);
- bribe taking;
- "payments or tips for information...time when commodities arrive at particular retail-trade outlets" (p. 82);
- "the creation of a steady market...and steady buyers" (p. 82).

According A. Shokhin, "it is advisable to link measures designed to suppress 'black' market operations... with intensified legal controls imposed on receivers of illegal incomes, with a corresponding development of irreconcilable public attitudes towards them..." (p. 83). Essentially, here A. Shokhin falls in with proponents of the "liquidatory" approach in the studies of the underground economy.

5. "In defense of economic freedoms".

Punitive sanctions against the shadow economy have up until recently been based on a number of articles of the RSFSR Penal Code, including Article 153 (as well as analogous articles in the criminal legislation of other union republics). This article prohibits private entrepreneurial activity and commercial mediation in the Soviet Union. Under part I of Article 153 of the RSFSR Penal Code "private entrepreneurial activity with the use of state, cooperative or other public forms of activity is punishable by a sentence of up to 5 years with confiscation of property or a banishment of up to 5 years with a confiscation of property or a fine between 200 and 1,000 rubles." The punishment for commercial mediation is somewhat less severe (2.2, Article 153): "commercial mediation, practiced by individuals... in the interests of personal enrichment, is punishable by imprisonment... banishment or fine" (41, p. 305). Wherein lies the actual evil of private entrepreneurial activity?

According to V. Vladimirov, a jurist, "the public danger inherent in private enterprise consists in that it violates the socialist principles of organized planning and economic management and principles of labor remuneration. This form of activity generates unearned, illegitimate incomes..."

Private entrepreneurial activity, V. Vladimirov goes on, discredits the socialist principles of economic activity, "revitalizing the principles of private production and distribution, alien to a socialist society" (41. p. 305).

A greater part of Soviet legal experts agreed that private entrepreneurship and commercial mediation were inadmissible in Soviet society, as hostile, alien elements thereof. And almost none of them had any doubts whatsoever as to the legitimacy of demands for ruthless struggle against these elements. Even such a renowned Soviet lawyer as Alexander Yakovlev, who has the reputation of a man committed to democratic traditions, rejects out of hand private entrepreneurial activity and commercial mediation. Answering a question put to him by a Planovoye khozyaystvo correspondent about the "illegitimate actions" in the underground economy that carried criminal responsibility, he enumerated several of these crimes, including in particular "private entrepreneurial activity and commercial mediation" (42, p. 113).

Alexander Yakovlev's view is shared by the well-known Soviet philosopher I. Galperin, who believes that "illegal income is income derived from criminal activity, and there is no need therefore to choose any specific methods of struggle against it: it is recorded in the penal code" (40, p. 12). This, in his opinion, refers to a number of activities, including "private entrepreneurial activity and commercial mediation" (Ibid.).

Thus, a struggle against the underground economy, and in this particular case, such manifestations thereof as private entrepreneurship and commercial mediation, is taking on the form of struggle against criminal offenses. Significantly, many notorious trials, referred to the category of private entrepreneurship, with time turned out to be nothing more than soap bubbles.²⁶ At the end of February 1981 several

papers in the United States ran a report about the arrest of a certain Kolevatov, director general of Soyuzgostsirk (State Circus Association). "In a scandal," The Los Angeles Times wrote, "police have arrested the national director of Soviet circuses and confiscated \$1.4 million worth of diamonds and illegal foreign currency in his apartment" (46). He was charged with being involved with the black market, practicing private entrepreneurial activity, bribery, illegal operations in foreign exchange and so on and so forth.

However, in the summer of 1990 reports were published about A. Kolevatov's complete acquittal and rehabilitation. He was released from custody. All charges levelled against him proved to be false.

The same refers to many cases initiated under Article 153 of the RSFSR Penal Code. This in particular was graphically demonstrated by an independent group of Soviet citizens, "In Defence of Economic Freedom," led by V. Sokirko. The group launched an underground journal by the same name, by 1982 ten issues of the journal appeared.

The journal devoted much attention to the exposure of unfair convictions present under Article 153. The present author is well-acquainted with V. Sokirko and he knows that the Sokirko group has compiled enormous records on criminal cases on those who were convicted under this Article. The group considers that Article 153 was used to punish those who had to work under the condition of forced planning, looking for ways of producing competitive goods.

The group organized show trials with a panel of jurors who reconsidered the cases which had ended in convictions. As a rule, the juries acquitted the convicts. V. Sokirko managed to create an atmosphere of public censure of Article 153. His activity largely accounts for the fact that at present virtually no charges have been levelled under this article. V. Sokirko demanded the abolition of Article 153 at

the USSR Supreme Soviet's Committee on Legal Affairs. As far as I know, this committee has supported V. Sokirko's demand.

However, according to V. Sokirko's estimates quoted by The Wall Street Journal, several thousand convicts are still kept in penitentiaries and labor camps, serving sentences under Article 153 (and some other articles) in punishment for so-called economic crimes. At present V. Sokirko has an archive including 102 such cases. One of them is the case of Pavel Bulov from the city of Ulianovsk, who engaged in "illegal" shipments of gravel under a contract with a collective farm. Pavel Bulov, employed by the collective farm was sentenced to 11 years of corrective labor. When he got into the labor camp, he met killers and murderers there, who were serving lesser sentences for their crimes.

V. Sokirko presented the Pavel Bulov case to a US newspaper correspondent, who subsequently visited the camp where Pavel Bulov was serving his sentence and also met his mother Antonina and wife Olga. After that in the spring of 1981 he asked Justice Minister S. Lushchikov to comment on this case. S. Lushchikov commented: "Today, there is no criminal responsibility for such types of phenomena" (47). It would seem obvious that if these activities carry no criminal responsibility, these people must simply be released. Nonetheless, the Soviet Justice Minister has his own explanation of why this should not be done: "To the extent that people were convicted when the law was in effect, it is still in effect, and we don't have any grounds to say that it wasn't legal or correct and they should be released" (Ibid.). This position seems quite strange. But if indeed the Minister does not see any reason why these people should be released for crimes that, as he now admits, do not carry any criminal responsibility, they could be released under an amnesty. However, I think that purely political reasons prevent the Minister from interceding on their behalf. I

suppose he is afraid of accusations of aiding and abetting private entrepreneurship in the USSR.

6. Conclusions.

To sum up, according to a widespread belief, the shadow economy in the Soviet Union is generated by the administration-and-command system. The transition to a market economy will inevitably eliminate the need to penalize a greater part of activities related to it.²⁷ What will remain? Only the criminal portion of the shadow economy, "illegal" under a 1981 classification. The very assortment of prohibited types of activity needs to be revised, proceeding from the transformations in the economic system as a result of marketization of the economy.²⁸

These are the conclusions of the constructive approach to the study of the shadow economy.²⁹ The liquidatory approach, for its part, leads to somewhat different conclusions. They are presented in a book entitled Alternative: Choosing a Path. The authors point to the "extremely limited scope of the 'shadow economy' in the Stalin period" (3, p. 53). And at the same time they say that one should not be afraid of any return to the past (as though in the past there was nothing but reprisals, violence, and hunger). The authors of the book allow the possibility of a "return" to the past, believing that the conditions characteristic of the Stalinist system can ensure "extremely limited proportions of the 'shadow' economy". Exponents of the liquidatory orientation do not say this in so many words. Nonetheless, they give preference precisely to the Stalinist methods of suppressing the underground economy, based on a powerful repressive apparatus.

We believe that if we were to return to the situation of "the Stalin personality cult period," the shadow economy

would undoubtedly be wiped out.³⁰ But in order to do this, as A. Katsenelinboigen correctly pointed out in the above-mentioned article, it is necessary to step up reprisals and, in more general terms, to restore the tyrannical orientation of the authoritarian regime. We should very much like to hope that this turn of events is impossible.³¹

May - June 1991

Endnotes

The author is grateful to Prof. G. Grossman and Prof. V. G. Treml for being given the opportunity to study their records and materials during the preparation of this article. The author has used works published outside the USSR only in connection with views expressed by Soviet authors.

1) Nonetheless, it is not advisable to idealize the Stalin period even here. Corruption and bribery were rampant in those days, too. In 1949 a USSR Supreme Court plenary session noted: "Courts often minimize penalties vis-a-vis officials offering bribes supposedly in the interests of service needs..." (1, p. 240).

2) "The 'shadow' economy," says a book lately published in the USSR, "rapidly gained momentum in the country at least 30 years ago (i.e. since new banknotes were introduced)." (3, p. 63).

Apparently the authors believe that the shadow economy has been waiting for its day to come since the Stalin period, because many of the present-day black-market operators, the authors maintain, have inherited the capital created in the pre-revolutionary period, during the times of NEP (New Economic Policy initiated by Lenin) and the years of war" (*Ibid.*). However, the authors do not mention the sources that led them to this conclusion. I think that even if some capital accumulation remained after the 1917 revolution, they were wiped out by mass reprisals and confiscations or directly appropriated by the state. While, something did remain, to be sure, it can hardly be regarded as anything substantial.

3) I think, however, that these arguments by A. Katsenelinboigen, which he has presented as the second law of corruption, generally true vis-a-vis the USSR, are hardly justified with reference to such a tyrannical regime as has taken shape as in Cuba. The personal experience of the author, who worked there for a very long time, testifies to extremely varied and diversified threads of corruption under the Castro tyranny. The latest trials of some of the top commanders of the Cuban army, charged with involvement in international drugs trafficking, is a direct vindication of this conclusion.

It appears that with reference to present-day Cuba it is hardly appropriate to talk about the possibility of replacing a tyrannical version of an authoritarian regime with another, "less tyrannical" variant. The Cuban model of socialism is only possible as a tyrannical one. And here I consider as totally unrealistic any anti-tyrannical transformations like

those that occurred at the end of the eighties in East European countries.

4) This position by G. Grossman was presented in Soviet literature by S. Khavina and L. Superfin in (5). A similar definition of the prerequisites for the existence of the black economy and resultant unearned incomes is presented in works by A. Shokhin (6, p. 85). He relates these incomes to "mercenary interests, leading to offenses against the law." (In G. Grossman's view, they are caused by personal self-interest.)

5) In October 1990, the author had occasion to witness slogans with demands to publish full lists of Soviet millionaires at a public rally organized by the United Workers' Front in Moscow.

Several Soviet millionaires have formed a Young Millionaires Club. However, the composition of the Club, with the exception of the President's name, is kept secret. The Club's President, German Sterligov, 27, points to the enormous difficulties involved in using the money they have accumulated: "I could buy a house or a Rolls-Royce or a ship or a plane... But what would be the use? Gorbachev would issue an ukaz and it would all be taken. Nobody knows what will be allowed tomorrow" (10).

6) Quite often chilling statistics are cited in order to substantiate the necessity of combatting the shadow economy, but with reference to only "one of the country's regions: three per cent of bank depositors hold half the overall sum of private bank deposits at savings banks" (see V. Rogovin's article in Izvestiya (13)).

Whence these figures? They were published in a volume of abstracts of a scientific conference in Riga 1975 and bore on the distribution of savings banks deposits in Latvia. Statistics released in 1990 by the USSR Savings Bank on the structure of household bank deposits did not confirm the above figures. At any rate, their extrapolation to the entire amount of deposits of the Soviet public is unjustified.

7) This approach was also characteristic of Dr. Rimashevskaya, who, in contrast to a widespread negative attitude to "moonlighters," raised the question differently: "Is our unqualified negative attitude to them always justified? Quite often these are industrious people who want to earn extra incomes in their spare time, using their own tools, motor-transport, etc. Why then should they not be allowed to engage in what is not prohibited by law?" (N. Rimashevskaya. "Grimasy levogo rublia." Sotsialisticheskaya industriya, February 1986).

8) Later, an analogous idea was set forth by A. Aganbegyan. Speaking about taxes and small boutiques in the USSR, he wrote: "Why not try leasing them on a contractual basis?... Some might think that my proposals can hardly be applicable to a socialist country..." (20)

9) However, the heads of other republican ministries of communal services opposed the second contractual labor remuneration scheme. They realized that this system of payment demonstrated that the state system of administration of the communal services sector was totally unnecessary. The main argument against using the second contractual form was that it restored petty-proprietary instincts of workers in the services sector.

Curiously, Posev also treated rather disparagingly this system of work remuneration. Literaturnaya gazeta published an article by A. Chernichenko about a shoe shop in the Estonian town of Paida, whose employees in 1985 adopted the second contractual scheme of labor remuneration (Literaturnaya gazeta, March 5, 1986). The author of an article in Posev, commenting in this publication, questions the expediency of the contractual system. After all, he writes, the premises, tools, and the materials (the means of production) remain state-owned (23).

However, the whole point is that this system, which ultimately transformed itself into leasing arrangements, has demonstrated how disastrous and ruinous state interference in the economy can be. As for the premises and even shoe-makers knives, they can well be in private ownership. Such is the logic of natural evolution, away from state regimentation of economic activity.

10) See Izvestiya, No. 298, 1987.

11) According to A. Volsky's estimates, already in early 1991 already 11 million people were working at lease operated enterprises (25, p. 54) and there is reason to think that along with cooperative ventures lease-operated enterprises are relatively more stable than state-run enterprises in the present-day economic situation. According to Volsky, the semi-privatized sector of the Soviet economy (lease-operated enterprise plus newly-created cooperative ventures) has boosted production in the first quarter of 1991 by 4.5 per cent, while the output of the state economic sector declined by 10 points (26). We suppose that leasing could yield still bigger results if the proposed model was not so unhappily "improved." The changes that occurred as a result were a concession to the bureaucracy. This is why, according to G. Popov, the law on leasing, prepared by a group of experts led by P. Bunich, was adopted by the USSR Supreme Soviet "in

circumvention of all other laws and in such great haste..." (7, p. 7).

I think that a favorable attitude on the part of the powers-that-be towards the leasing laws of the USSR and the Union republics, prepared by the Bunich group, is explained by the fact that his "improvement" of our leasing scheme tones down, if not completely eliminates the anti-departmental orientation of our lease-holding scheme, developed jointly with Mikhail Bocharov.

12) We cannot fully agree with A. Zinoviev's opinion on the "fate of private entrepreneurship in the USSR." "Ideally," he writes, "in a communist society all private entrepreneurship should be excluded..." He goes on to say that the shadow economy in the USSR is "in one way or another begotten by society... Each citizen in some way or another comes across it... This phenomenon will in no way shake the country's social foundation. Because people employed in the private sector work better than in corresponding public and state-controlled sectors, various ideas emerge about the possibility of expanding the private sector in the framework of communist society. However, private enterprise under communism has no future..." (28, p. 100).

Of course, this is correct, but it is also obvious that communism itself has no future. At the same time, private enterprise makes it possible to destroy the monopoly of the communist state over economic management. Herein I see the historic role of leasing, originating and developing initially within the framework of a state sector. It has vividly demonstrated the ineffectiveness of comprehensive nationalization and statization of the economy.

13) The preparation of this law was entrusted to the USSR Procurator's Office in summer of 1985. The work was headed by the renowned lawyer V. V. Naidenov, deputy procurator general of the USSR. When he worked at the USSR Procurator's Office he exposed a criminal group headed by Medunov based on Krasnodar territory and closely linked with the Leonid Brezhnev family. On the insistence of S. Medunov, first secretary of the Krasnodar territorial executive CPSU Committee, V. Naidenov in the early eighties was removed from the post of deputy Procurator General of the USSR. He was given the rank of Colonel of the Interior Service and for a while taught at the USSR Interior Ministry's Academy. When Yuri Andropov came to power, V. Naidenov returned to the USSR Procurator's Office in his former capacity.

V. V. Naidenov invited me, along with other experts, to work on the draft of a law on combatting unearned incomes. This law, envisaging constructive mechanisms of transforming illegal activities into legal, was prepared at the USSR

Procurator's Office at the end of 1988. This version was absolutely different from the one which was eventually adopted. I asked V. Naidenov why this had happened. "I feel ashamed," I told him, "to have anything to do with this law."

"I also feel ashamed," Victor Naidenov admitted. "But I swear that I had nothing to do with the later versions of this draft. They were all concocted at the CPSU Central Committee's administrative department under the guidance of Chief of Division Pavlov (Dr. of Law)."

14) However, in order to be able to say this with good reason, it is necessary to know what part of falsified reports is revealed. I do not think A. Sergeev knew this.

15) The idea of imposing a progressive tax on inheritance was advanced and substantiated in works by V. Rogovin. The mere idea of imposing an inheritance tax met with strident criticism from G. Lisichkin. In an article in Izvestiya he wrote that in the Soviet Union "inheritance is part of a pent-up demand...", and therefore it is unethical to tax whatever people have not managed to spend during their lifetime (32). A. Sergeev disagreed with this. He wrote, "In our system, an inheritance is generally not a part of deferred demand...but, rather, unsatisfied demand" (3, p. 76). But deferred and unsatisfied demand are the same.

16) The book mentions a figure of 100-150 million rubles, apparently through the fault of the proof-reader. Obviously, it should be billion rubles.

17) The idea of a money reform (cancellation of high-denomination banknotes) in 1990 was supported by US professor Wassily Leontief. However, he subsequently announced he did not know new money would be printed to carry out the exchange. It is not quite clear, however, how this operation could have been conducted without the issue of new money in view of the rising deficit of the state budget.

18) Here we referred to the category of semi-legal forms of activity "private medical and sanitary services, tuition and manufacture of goods on private orders." Our generally benevolent attitude towards covert forms of activity in the communal services sector ran counter to the contemporary opinion on the issue. Almost simultaneously with our article of October 28, 1981 an article by A. Rubinov in Literaturnaya gazeta was published. The author wrote: "A workman who operates without a license is simply a rogue..., who robs the state and eventually the client." And A. Rubinov called for "things to be set to order by a common effort" (35).

19) I do not see any substantial difference between the classification of the shadow economy presented by A. Sergeev and a detailed classification made by A. Shokhin. The latter was used by the authors of the 500-Days program, who suggested the following structure of the shadow economy: criminal economy, fictitious economy, informal illegitimate part of the "second" economy..." (37, p. 124).

The composition of particular structural elements of the shadow economy as presented in the 500-Days program is the same as in A. Shokhin's classification. However, concrete estimates are made out of context with the proposed shadow economy structure.

20) A. Shokhin does not see anything useful in the activity of what is known as "tolkachi", the legendary Soviet middlemen operating in the means of production market. Similar views are expressed by other authors. "Quite often," writes one of them, "this kind of 'initiative', is only a cover for lack of discipline and inability to plan production..." (38). This activity, he goes on, would be non-existent if "production is planned intelligently."

21) "Pre-revolutionary Russian law," writes A. Chalidze, "made a distinction between several types of bribery, - "mzdoimstvo" and "likhoimstvo." The former included the acceptance of gifts and presents by state or public officials in connection with the execution of their official duties, if this particular action did not constitute a violation of their duties. On the other hand, "likhoimstvo," defined as the acceptance of a present for the performance of an action running counter to service duties, was regarded as a more serious offense" (1. p. 235).

22) This circumstance is pointed out by L. Khotin, a US sociologist, who writes that the "alternative" economy somewhat tones down the rigidity of the system, facilitating the country's functioning. Another contributory factor is the non-observance of instructions and orders, i.e. formal functions, and their supplementation by informal instructions. Herein the Soviet economic system displays a certain flexibility (39, p. 30).

23) The authors of the 500-Days program are wrong in referring double counting to the underground economy (30, p. 125). Double counting reflects a multiple counting of the production turnover, which was inevitable in using gross public product indicators, up until recently widely used by Soviet statistics. Double counting is not a criminal offence but an inevitable result of calculations of the gross public product in Soviet statistics practices. By itself double

counting is merely a statistical abstraction and has nothing to do with the underground economy.

24) I wish I could just take a look at this "whole enterprise" working "wholly" within the framework of the "black" economy. There is much talk about it but so far no one has ever seen such an enterprise. A. Sergeev, too, writes about "underground factories" (p. 56).

25) Retail-trade employees come in for scathing attacks from experts on underground economy. Thus, A. Dolgova, an associate at the USSR Procurator's Office institute, asserts that "workers in the retail trade sector had a substantially greater number of luxury goods as compared to workers in the heavy industry who receive higher wages" (8, p. 124). Hence she makes the conclusion that workers in retail trade are more closely connected with the underground economy than workers in the heavy industry.

26) E. Evelson wrote a book about judicial procedures on economic cases in the USSR. Unfortunately, I have not seen the book itself but read a review of it (44, p. 4-5). The review quotes the author as saying in particular that convictions on hard currency, private entrepreneurship and embezzlement cases were in fact a form of severe punishment and reprisals of leaders of the "alternative" economy. According to E. Evelson, the very existence of this economy has become possible only as a result of the selfish interests of the Party and state officials at all levels, their readiness to divert raw materials and equipment allocated for state-run enterprises, for a bribe, to the "alternative" economy. She states that very often court cases on economic crimes in the USSR had an anti-Semitic coloring (her book contains a list of 163 Jews executed for economic crimes in the Khrushchev period). This fact was also brought up by the well-known British author Bertrand Russell, who in his letter to Nikita Khrushchev, published by Pravda on February 2 1961, wrote that he was deeply concerned about the executions of Jews in the Soviet Union and the official encouragement of anti-Semitism in the country (45).

27) According to the author of the 500-Days program - and here I agree with them - over 90 per cent of shadow economy operations can be easily checked as a result of marketization measures, primarily envisaging the abolition of "centralized planning and state monopoly of property ownership" (37, p. 127).

28) It is necessary, the author of the 500-Days program believes, after a transition to a market economy, to ensure the adoption of new legislation, providing for

"scientifically substantiated criteria of criminalization and de-criminalization of economic offenses. At the same time, it is required that higher criminal liability be imposed for more dangerous types of economic crimes (organized criminal activity, concealment of incomes from taxation, legalization of criminally-derived incomes, etc.)" (37, p. 126).

29) However, not all authors who began to study the shadow economy within the framework of the constructive approach believe that this form of its transformation, i.e. via marketization, is promising enough. Thus, for instance, Tatyana Koryagina assesses the possibility of this transformation of the shadow economy, in particular on the basis of promoting leasing and cooperative relations: "I don't share the optimism of those, who believe that results will come gradually through the development of the cooperative movement, lease brigades and other new forms of influencing our economy, though I am not against them as such." In her opinion, the shadow economy is closely linked with the numerous army of officials and bureaucrats, with the result that its transformation depends on whether their influence in society can be neutralized. However, this is essentially a political stance, and not a system of real proposals vis-a-vis the transformation of the shadow economy in the conditions of expanding market relations in society.

30) It should be pointed out that specific sets of measures designed to combat the shadow economy, singled out within the framework of the constructive and liquidatory approaches, are approximately the same: they include proposals of undertaking a cash reform, the necessity to introduce income declaration (this proposal is contained in the 500-Days program as well as in the book Alternativy puti...), and the idea of creating a strong tax inspection mechanism.

So the differences between the said orientations are not tactical but strategic. And the main difference between them consists in their attitude toward market economics.

Proponents of the liquidatory approach are against it. But here I think that they can hardly count on wide popular support. It is not accidental that A. Sergeev, who ran with General A. Makashov during the June 12, 1991 Presidential elections in Russia (the General chose A. Sergeev as his vice president), suffered a dismal defeat. Only a negligible part of the Russia's population voted for A. Makashov and A. Sergeev.

31) In December 1990, the All-Union Center of Public Opinion Research conducted a countrywide poll (the national sample included 4,580 respondents). The question asked was: "Is a return to mass reprisals possible in the Soviet Union?" Here is the distribution of the answers:

yes - 17

no - 38

not sure - 45.

Nearly half the respondents could not answer this question. Nonetheless, the proportion of those believing that new reprisals are impossible was double the number of those who believed that this turn of events is quite possible.

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Part II

Sizing Up the Shadow Economy: Review and Analysis of Soviet Estimates*

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1. Introduction.

Quantitative estimates of the size of the shadow economy (black market) in the Soviet*** press are growing at an amazing pace. This is how A. Sergeev comments on this: "The estimated scale of the shadow economy grows like a snowball. Only recently experts cited a comparatively modest figure of 5 billion rubles, while today it has soared to the astronomical 300-500 billion" (1, 54). These figures evidently date back to the late 1980s. As for economic indicators employed by Soviet researchers of the shadow economy (turnover, potential), their description may be found

* The following article was written (in Russian) expressly for Berkeley-Duke Occasional Papers. It has been only slightly edited from an English translation done in the USSR. The author, a prominent Soviet economist specializing in problems of household consumption and related matters, pioneered internal studies of the Soviet "shadow economy" while holding a senior position in the Research Institute of Gosplan USSR.

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*** This paper was completed in June 1991, before the dramatic changes that have made the terms "Soviet," "Soviet Union," and "USSR" anachronistic. Hence, they are retained in this paper and are used in their traditional sense.

in the first part of this publication "The Shadow Economy in the USSR: A Survey of Soviet Research."

The earliest estimates of the black market by Soviet economists caused turmoil (2). Today they no longer raise any eyebrows.

Researchers of the shadow economy have recently tried to estimate the rate of its growth. Experts of the USSR Interior Ministry estimate annual turnover on the black market at between 110 and 130 billion rubles as against 70-90 billion at the early stages of economic reforms, i.e. in 1985 apparently. The Interior Ministry expects annual black-market operations to grow to 170-200 billion "in the immediate future" (a vague notion. - V. R.), which will put the mafia in control of 30-40 percent of GNP in the USSR (3).

This paper will consider the reliability of these published statistics. The difficulty of our task stems from the fact that they are mainly based on expert appraisal which is subject to random variations. Let me cite personal experience. The first estimates of the size of black-market trade were made by the Economic Institute at the USSR Planning Committee (Gosplan) in 1984 and covered only consumer services. The estimates indicated that the shadow economy did 14-16 million rubles of annual trade and involved 1.7-2.0 million people. These findings were made public in a paper presented by Tatyana Koryagina, Yuri Sillaste and your author to the academic council of the Institute in late 1984 (4).

V. Tolstov, a journalist with Izvestiya, obtained a pale photocopy of the paper where decimal points could hardly be seen. As a result, in his article in Izvestiya, the Institute was quoted as estimating the number of employees in the shadow economy at 17-20 million (5). The figures took Koryagina and me aback but subsequently we decided they were probably true; in the services sector of the shadow economy

people often worked part-time, sometimes only on week-ends. We decided 17-20 million could be a realistic assessment of the number moonlighting in the services sector.

Some time later we read a study by the Estonian economist I. Raig, whose findings suggested that 17-20 million could be the correct figure.

In 1988 Raig conducted a survey among representative groups of the populace selected by the Statistical Board of Estonia and the Estonian branch of the Institute of Market Research at the USSR Ministry of Trade, which showed that members of 22-27 percent of Estonian households provided sporadic construction, transportation and repair services to other people for pay (6,71). If these statistics are projected to 85 million, the overall number of households in the Soviet Union, it appears that as many as 17-20 million may do odd jobs in the shadow economy.

Still later, 1.7-2.0 million - the number of full-time equivalent employees - and 17-20 million people holding odd jobs in the shadow economy - were cited in an article written by this author, together with V. Kostakov, for the newspaper Sovetskaya Kul'tura (7).

Today, all assessments of the shadow economy invariably surmise that it employs 20 million people. The figure was cited, for example, by deputy interior minister N. Demidov in the television program "Perestroika: Problems and Solutions." It is also taken to be correct by the authors of the relevant section in the book Alternativa: vybor puti (1,52).

This paper contains an assessment of published statistics on the size of the shadow economy in the USSR. It will be preceded by a presentation of new and hitherto unpublished material regarding the public's view of the shadow economy.

2. The shadow economy in public opinion.

Most data on the public attitude toward the black market come from studies made at the Public Opinion Research Center led by Tatyana Zaslavskaya.

The center started its life in spring-summer of 1988 and today conducts monthly surveys of public opinion on major political, economic and social matters. Researchers rely mainly on polls of adults, between the age of 16 and 75, permanently residing in urban and rural communities of different sizes and locations. The country is stratified by geographical zones, in each of which field work is done by one of 36 regional branches.

Pollsters visit people at their homes, hold interviews or offer questionnaires. A pollee is normally interviewed at least three times. Pollees are selected in numbers representative of population statistics in terms of age, sex, and education, and other criteria, with the margin of error up to 0.6 percent.

Most of those questioned in the poll in November 1990 in the Russian Federation (8)¹ hold the black market and the mafia responsible for most problems besetting the country. When asked "What is the root cause of recent economic setbacks?," the pollees gave answers which can be summarized as follows (percent of the total):

What is the root cause of recent economic setbacks? (percent of total)

1. action by the commercial mafia	27
2. collapse of the central planning system	22
3. attempts by the Communist Party apparatus to get back to the old ways	19
4. stop-go approach to market reforms	13
5. the policy of radical reformers in power	2
6. the policy of nationalists and separatists in non-Russian republics...	3
7. do not know	14

The above represents the results of a poll in the Russian Federation. The respondents were required to choose only one option from the list of possible answers. A different picture emerges when respondents are allowed to list more than one reason for economic deterioration. Mafia and organized crime still rank top of the list, mentioned by an even bigger percentage of the pollees: those who look for different explanations of the economic crisis think this is also a factor. This shift of emphasis was displayed in a poll conducted on a nationwide scale in December 1990 (9).² The following is a summary of answers given to the question: "What is the main reason behind problems facing the country

today?" (percent of the total, which exceeds 100 because respondents often mentioned more than one reason):

What is the main reason behind problems facing the country today? (percent of total; total exceeds 100)

1. mafia and organized crime	51
2. mistakes of the leadership	47
3. technological backwardness of industry	36
4. thievery	30
5. bureaucratic red tape	29
6. lack of incentives for good work	26
7. corruption	25
8. a drop in the number of decent and honest people	20
9. low professional standards	19
10. egalitarian philosophy stifles initiative	17
11. exodus of highly-qualified people from this country	16
12. moral degeneration, the cult of sex and pornography	14
13. disregard of the needs of ethnic minorities	13
14. decline of religious values	12
15. subversive activities by secret enemies	11
16. decline of traditions	11
17. legacy of Stalinism	8
18. dissemination of free-market theories, pluralism and freedom of ownership	7
19. shift away from socialist principles	5
20. policies of imperialist countries	1
21. other reasons	2
22. no opinion	5

The poll suggests that most Soviet people think they know what brought their country to crisis (only 5 percent of the pollees gave a "No opinion" answer). The overwhelming majority fix the blame on the shadow economy. Put together, answers containing a reference to the shadow economy total over 100 percent, 106 percent to be exact (option 1 [mafia] was chosen by 51 percent, 4 [thievery] by 30 percent and 7 [corruption] by 25 percent). Accusations against the leadership are the second-most-popular explanation, given by 76 percent of the respondents (47 percent who chose option 2

[mistakes of the leadership] and 29 percent who chose option 5 [bureaucratic red tape]).

This kind of sentiment was also reflected in answers to another question in that same survey, "Who do you think lives a life of plenty in the USSR?" (the total exceeds 100 percent):

Who do you think lives a live of plenty
in the USSR? (percent of total; exceeds
100)

1. crooks and "speculators"	65
2. Party and government apparatchiks	45
3. employees of co-ops	36
4. those who emigrate from the USSR	13
5. foreigners	8
6. those who want to and can work well	7
7. private entrepreneurs	6
8. others	1
9. no opinion	6

It is a widely-held view that in transition to the market economy black-marketeers will be able to launder their dirty money. In a survey conducted by the Public Opinion Research Center (10)³ respondents were asked, "Some people object to plans to let individuals buy government-owned property in the belief that this will open the way for laundering ill-gotten money. Do you share this view?" This is how opinions were divided :

Yes	36
No	35
No opinion	29

A predominant part of the population evidently tends to believe that the mafia, the offshoot of the black market, is in league with the apparatus. In a study by a Ukrainian branch of the Public Opinion Research Center in Kiev (10)⁴

respondents gave these answers to the question: "What is your definition of the mafia?" (percent of the total).

What is your definition of the mafia? (percent of total)	
1. never heard of it	2
2. a large group of criminals	3
3. an organization of criminals in control of the underworld	5
4. criminals engaged in racket	2
5. a criminal network with accomplices in law-enforcement agencies and governmental organizations	80
6. other answers	1
7. no opinion	7

Most people in Kiev see the mafia as melding with the authorities, a most ignominious thing in the public view. All evidence of such links, e.g., bribe-taking by officials, causes intense outrage. The public takes a much more tolerant attitude to other illegal and semi-legal activities on the black market. People have mixed feelings about illegal incomes, including gifts (just a version of bribes), received by employees of medical and educational institutions. Such double standards were revealed by a special survey conducted by the Public Opinion Research Center in December 1985 (12).⁵ The pollees were asked, "Which of the following judgments about illegal income would you subscribe to?" (percent of the total):

Which of the following judgements about illegal income would you subscribe to?

- | | |
|---|----|
| 1. Many problems cannot be solved legally so one has to employ illegal means, which is where illegal "left" incomes come from | 54 |
| 2. There is often nothing improper about receiving illegal ("left") income | 6 |
| 3. Illegal ("left") incomes and furthering them are unacceptable | 26 |
| 4. no opinion | 14 |

Questions about different kinds of illegal incomes provide further evidence of the equivocal nature of public opinion about making money "on the left." Here are the results of a Public Opinion Research Center survey conducted in December 1989 (12).

Public opinion regarding various kinds of income from the shadow economy (percent of the total, omitting "no opinion" answers)

	Condemned	Not Cndm'd
1. Prostitution	90	10
2. Cheating customers in retail outlets	88	12
3. Resale of agricultural produce at kolkhoz markets at higher prices	86	14
4. "Speculation"	82	18
5. Bribes, gifts to officials	78	22
6. Resale of foreign-made goods purchased from foreigners	69	31
7. Extra pay for scarce commodities and services	68	32
8. Gifts and side payments to medical doctors, nurses, teachers in state-owned institutions	57	43
9. Use of a government-owned car for personal gain	56	44
10. Theft from place of work	48	52
11. Tips	48	52

It appears that Soviet people are quite tolerant of theft from work places. Over half of respondents do not object to this kind of black-market operations. This may stem from the deeply-ingrained view that everyone is underpaid by the state, so stealing from the state is not a major sin.⁶

Nor are tips and payment for free services frowned at: over half of the respondents do not object to tipping and almost just as many would turn a blind eye to illegal incomes derived from transportation services. Everybody has benefitted from such services at least once. The same perception exists with regard to gifts or extra pay to medical doctors, nurses and teachers. This kind of remuneration is believed to be in appreciation of the quality of services or in compensation for the miserly pay received by doctors and teachers in the USSR.

The attitude is markedly different when it comes to gifts meant for officials, even if these are medical officials. Such bribes, a staple of Soviet life, are condemned by the overwhelming majority.

People also have strong feelings about illegal income derived from black-marketeering in retail trade. They denounce cheating, profiteering and re-sale of government-owned agricultural produce in the farmers' market (82-88 percent). The public feels differently about extra pay for scarce commodities and services, considered normal by 32 percent of the respondents. This kind of illegal income is the product of personal contacts established by shop workers with their favored customers. Unlike profiteering, where all buyers are ripped off on equal terms, scarce commodities at higher-than-official prices are only provided to the most trusted clients.

Nor do Soviets fly into rage against those who sell foreign-made goods at several times their price: this seems to be the only way to purchase those items.

Prostitution is deprecated by as many as 90 percent of the pollees. But public opinion is changing. There have been reports that in Astrakhan, for example, "the commission for youth affairs at the city council has prepared a package of decisions on improving the sexual culture of young people," which envisages, in part, study of possibilities for opening a brothel. True, the commission admits the plans are far-fetched and points out that "there is more sense in "organizing a meeting-place for young couples(!)" (14).

The survey of the Public Opinion Research Center also aimed to sound out the public on reasons for wide presence of illegal incomes. Only 7 percent of the respondents brushed the problem aside while others, except for the 6 percent who gave a "No opinion" answer, offered the following explanations (the sum total exceeds 100 because several reasons were sometimes listed):

Public Opinion on the Reasons for the Wide Presence of Illegal Incomes

1. pervasive shortages of goods and services, the need to break the law in order to obtain them	51
2. loose administrative controls and record-keeping	27
3. dishonesty of officials	23
4. ineffective law-enforcement	18
5. imperfect laws, lenient punishment for black-marketeering	18
6. public tolerance of ill-gotten gains	17
7. insufficient publicity in regard to efforts to combat the black market	12

The main reason given for pervasive black-marketeering is pervasive shortages. But this is not the only reason. People go to the black market because they are not satisfied with the quality of officially provided goods and services. This transpired in a survey conducted by the USSR Statistical Committee in the second quarter-year of 1985.⁷ In this poll, 75 percent of the respondents complained of low quality of services and repairs of TV sets; 71 percent, of shoddy workmanship in shoe-repair shops; and 66 percent were dissatisfied with the quality of watch repairs and photography services. Most pollees also said orders were seldom fulfilled on time. This forces the public to go to private operators who get things done better and quicker than in the government-owned sector.

The illegal private sector was said to do a better job by 53 percent in repairs of consumer electronics and by over 30 percent in repairs of footwear, watches and photography. Between 50 and 66 percent of the respondents noted that private orders got fulfilled quicker in dress-making, house repairs, construction and car repairs.

Most people believe the shadow economy in the services sector is very helpful. Anyway, many find it more attractive than government-run services. This prompts respondents to look favorably on transformation and legalization of the illegal services in transition to the free market. On the other hand, as many as 27 percent of the respondents prefer "law and order" and reject free-market relations.

3. Estimating the size of the shadow economy.

Statistics on the make-up of and turnover on the black market in the late 1980s are available from two Soviet sources,⁸ the 500- Days Program (16), hereinafter "the

Program," and the monograph Alternativa: vybor puti, hereinafter "the Monograph" (1).

3.1. Misappropriation of public property.

The Program puts "damages inflicted by misappropriation of state and public property" (p. 125) at 5.2 billion rubles, based on data supplied by the Interior Ministry and close to those provided by the USSR Statistical Committee, which valued stolen government and public property at 4.9 billion rubles.

We do not know how the Statistical Committee arrived at this estimate, but authors of the Monograph explain (p. 57) that their findings derive from the following data: in 1988, 250,000 petty thieves were caught stealing a total of 100 million rubles worth of produce in agriculture which, the monograph reminds us, "employs one-third of all people at work" (the Monograph refers to (18, 111)). Since theft from workplaces is rampant in all economic sectors the figure must be multiplied by three, which gives us 300 million rubles. The Monograph asserts that "at best, only 5 percent of thefts are uncovered" (p. 57) so 300 million must be multiplied by 20 to produce the final result - 6 billion rubles. The Monograph, however, cited the value of 5 billion (p. 57).

This includes petty theft only. Yet public property also gets stolen on a large scale. The Interior Ministry maintains that 62 percent of stolen property was misappropriated by only 4 percent of the overall number of perpetrators. Sergeev, who wrote the section of the Monograph which deals with the black market, believes petty theft accounts for only two-fifths of all misappropriation of public property. Large-scale theft then is valued at 7.5 billion rubles. Overall, therefore, property worth 12.5 billion (5 billion plus 7.5 billion) is stolen annually. "In

our opinion, of this amount items worth at least 10 billion are sold on the black market," Sergeev writes (Monograph, p. 57).

These estimates are open to dispute. First, it is unclear why the scale of theft in agriculture should be projected onto the economy as a whole. Second, it is unclear why only 5 percent of thefts are uncovered. You must know how many thefts are really committed before you can estimate the percentage of uncovered crimes. Third, there is no reason why the proportion of small-scale and Large-scale theft - 40 to 60 - should be projected onto uncovered theft: probably small-time theft is easier to detect. Fourth, assertions that stolen items worth 10 billion are sold on the black market are also doubtful.

I tend to think the data provided by the Statistical Committee - 4.9 billion, or 5 billion rubles, if rounded, - are more credible.

Incidentally, Sergeev also gives a much higher estimate of the value of stolen public property. "Socialist property worth 35 billion rubles gets stolen," he writes (p. 61). It remains unclear which of the two figures - 10 billions rubles' worth of goods sold on the black market or 35 billion rubles' worth of goods "directly stolen" Sergeev trusts more. Apart from "direct theft" Sergeev also talks of "theft of materials obscured by report-padding, worth 30 billion rubles" (p. 61). This is how he arrives at the figure.

1. Sergeev estimates the scale of report-padding. He assumes it to be equal to 4-5 percent of GNP, or 65 billion rubles. The key is the proportion of report-padding--4-5 percent. The figure is reported without any basis.

2. He then calculates the proportion of labor costs in overall costs in different economic sectors to be 23 percent. This leads him to believe unearned income stands at 15 billion rubles -- 23 percent of 65 billion rubles (p. 60).

3. Next, Sergeev assumes "the average ratio of unearned pay to resources written off due to report-padding to be 1:2" (p. 61). So materials whose theft is covered up by means of report-padding are valued at 30 billion rubles (15 billion rubles of labor pay x 2). It is debatable, however, whether in report-padding materials are always written off together with unearned pay.

4. Finally, he estimates direct theft to be worth 35 billion rubles -- 65 billion less 30 billion. So 65 billion rubles includes theft covered up by report-padding (30 billion) and direct theft (35 billion). The question arises where 15 billion rubles, Sergeev's estimate of labor pay produced by report-padding, fits in. But then, the original figure of 65 billion is suspect.

3.2. "Speculation".

These are statistics on speculation provided by the USSR Statistical Committee:

<u>Type of Revenue</u>	<u>Value in Rubles</u>
trade in cars	5.7 billion
trade in auto spare parts	1.0 billion
trade in non-food goods	1.3 billion
trade in alcohol	0.1 billion

According to Sergeev, trade in foreign- and Soviet-made goods unavailable in government-run stores is worth 15-20 billion rubles. Black-market prices are normally 50-100 percent higher than government-fixed prices.⁹

The difference constitutes profits which, if we are to believe Sergeev's data, stand at 7.5-10 billion rubles. This estimate of black-market trade looks more realistic than the information provided by the USSR Statistical Committee. For all we know, even Sergeev's findings may be an underestimation. Regardless, the black market undoubtedly charges higher prices than assumed in his calculations.

Significantly, in the early 1990s the USSR Statistical Committee revised its estimate of black-market trade in scarce commodities to 23.1 billion rubles (20). Presuming items in short supply are available on the black market at twice their official price, net profits from such operations reached 11.5 billion rubles in the early 1990s and stood at no less than 10 billion in the late 1980s. At any rate, Sergeev's estimate for the late 1980s seems to be more true to life than the data of the Statistical Committee cited in the 500 Days Program.

3.4. Trade in smuggled goods.

Sergeev estimates the black market to do 15-20 billion rubles of trade in smuggled goods and derive net profits of 10-15 billion (Monograph, p. 61). Since he provided no substantiation for these figures, we decided against including them in calculations of the volume of black-market trade for fear that Sergeev may have defined smuggling too broadly, and included the sale on the Soviet market of all items purchased by Soviet nationals abroad. Many of these cannot be qualified as contraband.

3.5. Trade in products of "shadow" production.

In terms of products manufactured in the shadow economy and unrecorded output of government-run businesses, Sergeev writes it is "logical" (?) to suppose that 15-20 billion rubles worth is traded (pp. 56-57). To me the figure does not seem justified, let alone logical. What he regards as sale of black-market products is in actual fact trade in items stolen from the government sector. There is no reason to add another 15-20 billion rubles to turnover of black-market trade.

3.6. Home-brewed alcohol (samogon).

Sergeev maintains home-brew worth 30 billion rubles is annually produced (see Izvestiya, October 27, 1989) of which alcohol worth 10-15 billion is offered for sale (Monograph, p. 57). The Program contains a similar assessment, based on the Statistical Committee data: "Production of home-brew is estimated at 30 billion rubles of which 9.0 billion rubles' worth of alcohol is produced for sale." (Program, p. 176). I think 10 billion rubles may be safely added to the turnover

of black-market trade. The rest is for personal consumption and, from this perspective, does not differ from any other item produced for these purposes.

The newspaper Vechernaya Moskva carries data from the USSR Statistical Committee which indicate revenues from home-brewing, as of the early 1990s, total 35 billion rubles (20). Proceeding from the earlier ratio of produced and sold home-brew (23:9), it appears that of 35 billion rubles' worth of home-brew 14 billion rubles is sold, a result close to Sergeev's, though his estimate referred to the late 1980s.

To sum up, black-market trade proceeds from sale of home-brew is taken to equal 10 billion rubles.

3.7. Drug business.

The Program, with reference to the Statistical Committee, estimates turnover of drug trade at 0.3 billion rubles (Program, p. 126). Sergeev's estimate is 50 times higher, 15 billion rubles, a figure which I would not trust at all.

Sergeev cites official statistics putting the number of drug addicts at 130,000. "Evidently, at least as many have been left outside records," he writes. Why? This is not evident at all. But let us assume 260,000. Sergeev refers to newspaper reports that drug peddlers in Ashkhabad sell 20 kg of drugs a day, the consumption of 15,000 addicts. If one kilogram of a locally-produced narcotic is priced at 160,000 rubles and 1,000 addicts consume 1.3 kg a day (20 kg divided by 15 is 1.3), 260,000 addicts need 346.6 kg a day, or 123,400 kg a year (346.6 kg x 356 days) worth 19.7 billion rubles (123,400 kg x 160,000 rubles). If we price one kilogram of opium at 100,000 rubles, as Sergeev does, the result will be 12.3 billion rubles (1,234,000 kg x 100,000

rubles). Evidently Sergeev based his estimate on 15 billion, the average of 12.3 and 19.7 billion rubles.

Daily usage of addicts in Ashkhabad does not have to apply to other localities in the Soviet Union. Daily consumption also depends on the drug used.

For lack of a reliable figure, estimates of drug trade have to be based on the reports of the USSR Statistical Committee, though its figure of 0.3 billion is probably too small.

3.8. Prostitution.

Gross revenues from prostitution are estimated in the Program to reach 0.7 billion rubles a year (p. 126). No statistics on prostitution are available in Sergeev's paper.

3.9. Bribes.

This is how the USSR Statistical Committee classifies bribes (Program, p. 126):

<u>Type of Bribe</u>	<u>Value in Rubles</u>
co-ops' bribes of officials	1 billion
the general public's bribes of officials to obtain or exchange apartments, garages, gardens	1 billion

Though this may be an underestimation, so far it is the only figure available.¹⁰ The Statistical Committee, however, values bribes given by co-ops to officials in early 1990's at 1.2 billion rubles (20).

3.10. Cheating in retail trade.

The Program cites two estimates of revenues derived by shop workers by means of cheating customers: the USSR Statistical Committee puts the figure at 4.4-9.8 billion rubles, and the Public Opinion Research Center at 10.7 billion (p. 125). We can safely add another 10.7 billion rubles to the volume of black-marketeering. In July 1991 the Statistical Committee came up with a much larger figure - 24.3 billion rubles a year (20). To us, the gap between two figures is inexplicable, but there is an unquestionable tendency in the retail sector to cheat less amid worsening shortages. In sizing up the black market we proceeded from the Statistical Committee appraisal of 10.7 billion rubles a year, though in actual fact the figure is likely to be much larger.

3.11. Illegal price rises.

The USSR Pricing Committee maintains illegal price increases at 1.2 billion rubles (Program, p. 125).

3.12. Unearned wages and bonuses for phony work.

Revenues from such operations total 30-35 billion rubles a year, the Interior Ministry reports (Program, p. 126). According to Sergeev, report-padding in the USSR accounted for 65 billion a year in the late 1980s, including 15 billion rubles of unearned wages (Monograph, p. 60). These statistics inaccurately reflect the amount of unearned payments; 30-35 billion looks a lot more realistic. In our calculations we shall assume this amount to equal 33 billion rubles.

3.13. Services in the shadow economy.

Sergeev estimates services provided on the black market to be worth 10-12 billion rubles a year (Monograph, p. 57). The actual figure must be much higher. The Program, with reference to the Statistical Committee, put the figure at 14-16 billion rubles. Both estimates date back to the mid-1980s. A study made by S. Titov, of the Economic Institute at the Planning Committee, operations in the services sector of the shadow economy have grown to 20 billion a year in the late 1980s.

In a study done together with Yu. Sillaste and me, Tatyana Koryagina based her estimates of black-market services on regular reports of the Statistical Committee on consumer spending on services in the Soviet Union as a whole and in individual regions; on the population's balance of revenues and spending, in particular, information on spending on services; and on various sociological studies, especially on leisure, with due account to expert opinion (22).

The major component of the services sector is consumer services. Statistics on incomes and spending of the population in the USSR only included the so-called non-productive services, such as hair-dressing, laundry and funeral. Services connected with manufacture, such as repairs, construction of housing and dachas, dress-making, are recorded as spending on commodities and included in GNP. Non-manufacturing services, according to the philosophy espoused until very recently by the Statistical Committee, are left out of GNP.

In estimating consumer spending on services the Economic Institute at the Planning Committee employed a variety of techniques.

First, it drew information from special studies of consumer services. When inspected by the taxing authorities,

hair-dressers, for instance, have been shown to report twice the amount of their normal revenues (23, p. 23). This indicates that in actual fact they do annual business of 1.7 billion rubles while official statistics puts it at 800 million. Clients pay a total of 0.9 billion a year for illegal services.

Second, the Planning Committee studied time-spending patterns with relation to statistics on construction of private houses. The amount of time consumed by construction of a private house was reduced by the amount of time consumed by work performed by the owner. Studies of how much time is consumed by different kinds of activity yielded an overall estimate of time spent on services in construction of private houses. Time estimates were used to calculate the scale of services received by owners of private houses on the black market. The amount of work known, experts assumed pay rates on the black market are 1.5-2 times as high as in the government-owned sector. As in preparing statistics on official construction services, spending on building materials was left out of calculations. Tatyana Koryagina puts overall consumer spending on construction services (less the cost of building materials) at 1.5-1.8 billion rubles, 2-2.3 times as much as the volume of services provided by the government-run sector (22, p. 13).

Third, the Planning Committee built its estimates on requirements for servicing consumer durables. Experts calculated the funds required to pay for maintenance repairs of a car and polled car-owners to find out what repairs they made on their own. Given official statistics on consumer spending on car-repair services, the value of car-repairs done in the shadow economy could be easily calculated.

Tatyana Koryagina applied the above approach to estimate consumer spending on other services offered on the black market. In so doing, she drew on the findings of special

studies on the number of holiday-makers in health resort areas, average length of stay and the average cost of accommodation at a private house in health resort areas.

These studies eventually produced the following estimate of consumer spending on shadow-economy services in the mid-1980s (billion rubles):

Estimated Consumer Spending on Services
in the Shadow Economy (billion rubles)

1. consumer services	5-6
2. recreational services	3.5
3. medical services	2.5
4. educational services	2.5
5. rent (other than accommodation during annual holidays)	0.7
6. cultural services (e.g. hire of video cassettes) ¹¹	0.3
7. Total	13.5-14.5

In our paper presented to the academic council of the Economic Institute at the Planning Committee in 1984, Tatyana Koryagina and your author estimated black-market services at 14-16 billion rubles a year.¹² This being an average value, the estimates ranged from the minimum of 8.10 billion to the maximum of 22-24 billion rubles a year (22, p. 15). Of course, these assessments are largely approximate. Yet they do reflect the scale of black-market operations in the services sector. Information underlying the estimates was drawn from sources of varying degrees of authenticity. More reliable findings can only be obtained through special sociological studies of the black-market services sector. Such studies could also be instrumental in singling out categories of black-market services.

3.14. Final estimate.

Here is the final assessment of trade on the black market in the late 1980s (billion rubles):

Final Assessment of Black Market Trade (billion rubles)	
1. theft	5
2. profiteering	10
3. sale of bootlegged alcohol (samogon)	10
4. drug trade and prostitution	1
5. bribery	2
6. retail cheating	11
7. illegal price rises	1
8. unearned wages and bonuses	33
9. services	20
10. total	93

This estimate differs but slightly from figures that appeared in the press. The 500 Day Program puts "aggregate revenues on the black market, from all operations which were examined by experts, at 66-146 billion rubles" (17, p. 126).

According to Sergeev, "overall annual revenues of the black market total 90-112 billion rubles" (1, p. 57). Tatyana Koryagina values black-market operations in the late 1980s at 90 billion rubles (2). Thus, economists in the Soviet Union, whatever sources they rely on and whatever techniques they use, agree that annual black-market operations must be appraised roughly at 100 billion rubles.

It is noteworthy that Sergeev, though he fixes an average value of 100 billion rubles on the black market, writes the maximum figure could be as high as 170 billion rubles a year (1, p. 58).

Here is how Sergeev obtained the figure (1, p.58):

Components of Sergeev's Total Black Market
Trade (billion rubles)

1. "Annually provided goods and services less commodities worth 10 billion rubles funnelled onto the black market" ¹³	418.2
2. growth of savings deposits	30.5
3. unregistered savings	10
4. "hot" money (legally earned)	10
5. annual worth of black-market goods and services	100
6. total approximately	560

"Now we must deduct from this the 387 billion rubles of official consumer earnings" (*Ibid.*). The result is 170 billion rubles. Yet the figure makes you wonder.

First, it is incorrect to value monetary earnings of the populace at 387 billion rubles. Sergeev cites statistics on annual trade in commodities and services (418.2 billion rubles) and the amount of goods siphoned off to the black market (10 billion rubles). In 1989 consumers spent a total of 431.8 billion rubles on goods and services (24, p.31(, or 421.8 if we deduct the 10 billion they paid on the black market. Judging by the proximity of Sergeev's findings to official statistics , he employed the 1989 data on consumer spending. But the 1989 balance of payments values overall monetary incomes of the populace at 533.9 billion rubles, if not more, rather than 387 billion cited by Sergeev.

The value 533.9 billion rubles is the sum of consumer spending on goods and services, plus 16.6 billion rubles (24, p.3(of surplus of revenues over expenses, plus 35 billion rubles in taxes,¹⁴ plus 30.5-billion-ruble growth of savings deposits,¹⁵ plus 20 billion rubles of other payments (repayment of housing loans, contributions to public organizations). If the result, 534 billion rubles

(rounded),¹⁶ is deducted from 560 billion rubles, the aggregate turnover of the official economy and the shadow economy, we are left with 24 billion, clearly "an underestimation of annual revenues on the black market," Sergeev writes (1, p. 58). It remains inexplicable where 387 billion rubles, Sergeev's estimate of "all official monetary incomes of the population," came from (1, p. 58). An entirely unrealistic figure.

Second, an estimated 10 billion rubles of "squirreled-away savings" is also open to doubt. Sergeev refers to experts who "put overall monetary hoardings at 100 billion rubles" (1, p. 58). Another 300 billion is deposited in savings banks. Deposits grow annually by 30 billion rubles. The ratio of money socked away in homes to money in bank accounts being 1:3, Sergeev extends the proportion to growth of savings and gets his result: 10 billion rubles of "unregistered savings." It has yet to be proven, however, that bank savings and money hoarded in homes grow at an equal pace.

Third, why should the amount of loose money chasing goods be put at 10 billion rubles? The Economic Institute at the USSR Planning Committee cites a much larger figure of unsatisfied demand, 25-30 billion rubles.

By way of conclusion I must point out that only one figure in Sergeev's assessment, annual trade on goods and services on the black market, is beyond any shadow of doubt. The estimate of annual black-market revenues, 170 billion rubles, has been shown in this paper to be based on wrong assumptions.

4. Black-market capital.

Profits fetched by black-market operations are either consumed by black-marketeers or saved. Retained earnings constitute accumulated black-market capital. Its value is estimated differently. Tatyana Koryagina puts it at 200-240 billion rubles (16) but provides no commentary on her data.

Not so Sergeev, who values aggregate capital of the black market at 500 billion rubles (1, p. 62). Sergeev adds to annual earnings of the shadow economy (170 billion rubles) 30-50 billion of labor costs to receive 210 billion of "gross revenues" of the shadow economy.¹⁷ This value is subtracted by 45-50 billion rubles' revenues of small-time black-marketeers, who in the main provide services, re-sell goods at mark-ups and trade in boot-legged alcohol (1, p.62), and unearned wages. The difference stands at 120-125 billion rubles, "the booty of large-scale and medium-size black-market businesses, Soviet capitalists," according to Sergeev (1, p. 63). Of this sum, 60-170 billion rubles is accumulated annually (1, p. 63) and total capital has now reached 500 billion (Ibid.).

The calculations are based on the very shaky figure of 170 billion rubles. There is no evidence that labor costs on the black market total 30-50 billion rubles. The revenues of small-scale black-marketeers seem to be underestimated. Sergeev puts them at 45-50 billion rubles but if we take trade on the black market to be worth 93 billion rubles a year one would think small-time black-marketeers make more than Sergeev believes. In my opinion, most of the black-market profits are consumed. What is left - between 10 and 12 billion rubles a year - is accumulated in Soviet rubles or converted into foreign currencies. Conversion into internationally-traded currencies is prominent in the shadow economy of the late 1980s. It is far-fetched to estimate

accumulated black-market profits at 500 billion: they are meant primarily for immediate consumption.

5. Circulation of hard currency.

Estimates of incomes and savings of the shadow economy that have appeared in Soviet sources are in rubles only. Hard currency is considered by only a few authors, who regard it as a form of accumulating profits. Sergeev, for example, mentions "conversion of ill-gotten money into hard currency" (1, p.56). However, hard currency in this case is more than just a store of value. Its circulation is significant in its own, or so it seems to me. It constitutes a whole sector in the shadow economy and its growth bears increasingly on the operation of many processes within the framework of the shadow economy.

Illegal foreign-exchange transactions in the Soviet Union date back to 1956, when the Iron Curtain was slightly lifted in the wake of the World Festival of Youth and Students. Ian Rokotov, the foreign-exchange dealer whose name became widely known after his trial in the early 1960s, began his valuta operations just then. At that time the Penal Code was quite lenient towards foreign-currency dealers, and few cases were yet tried. What is the point of buying foreign exchange in a country walled off from the outside world? But when the Curtain was raised, if only so slightly, Ian Rokotov started a new form of business in the Soviet Union, trading in currency.

Confident that he was risking only short imprisonment, Rokotov cooperated with the investigators and filled them in on all details of his dealings. The story he had to tell stunned the leadership of the Party, and State -- and reportedly, in particular, Nikita Khruschev. Even before Rokotov was brought to trial, the Penal Code was amended to

extend imprisonment for hard-currency dealings to the longest term possible, and then amended again to provide for capital punishment. Ian Rokotov was executed by a firing squad contrary to millennium-old legal practice which precludes the use of laws promulgated after the offense was committed. Today Rokotov's is a textbook case for law students: law is not retroactive, except in the USSR.

Circulation of hard currency on the black market has now taken on a qualitatively new significance because its amount has reached that critical mass beyond which it begins to affect overall monetary circulation in the USSR. The Wall Street Journal (25) puts the amount of foreign exchange on the black market at between 300 million and 2 billion dollars.¹⁸ What is the significance of these figures? Since one US dollar traded for 32 Soviet rubles on the black market in Moscow in mid-May 1991, the figures amount to between 9.6 billion rubles and 64 billion rubles, and look impressive even next to the stunning estimates of overall black-market operations.

Importantly, even if the amount of foreign exchange circulating in the black market remains unchanged, its ruble equivalent will continue to grow due to inflation, which is estimated to have reached 100 percent in 1991 and thus to bring the ruble value of 0.3-2 billion dollars to 15-120 billion rubles by year-end. Further growth of the ruble equivalent can be predicted.¹⁹

Some Soviet nationals keep their foreign-exchange earnings in special accounts of Vnesheconombank. This money cannot be withdrawn unless the depositor travels abroad. L. Hays, the correspondent of the Wall Street Journal, discussed the topic with three oil drillers from Tyumen whom he met in the Soviet-Swiss store "Sadko," a retail outlet trading in hard currency only. "Although each man," L. Hays wrote, "earned about \$5,000 working on pipelines in Iraq they cannot

use the money. If he did, says one man who won't give his name for fear of trouble, he is sure his bank deposit would be confiscated." "Russian people don't believe in their government," he says. "It's insulting that it's my money and I can't get any of it" (25).

This is why many Soviets who have foreign-currency earnings keep them either in their homes or in bank accounts abroad. Soviets seek to open a bank account as soon as they arrive in a country with a freely-convertible currency.

In previous years, too, quite a few Soviets had hard currency holdings. Small amounts were carried over from before 1917. In the 1920s Soviet branches of foreign foundations, like the Nansen foundation, and international organizations, paid their Russian employees in hard currency.

These holdings - dating back to before the Bolshevik revolution and to the 1920s - came to the surface in the late 1960s and early 1970s, in particular in the USA, when international contacts of the Soviet people gained in scale. The following was recounted to the author by Prof. V. Treml (USA).

In 1972, Prof. Treml hosted Soviet track-and-field athletes during a meet at Duke University where he was (and is) employed. All went smoothly until one day Treml was summoned to the police, together with the leader of the Soviet team. They were told that a Soviet athlete had tried to pay in dollars which had long been out of circulation. In 1931 the shape of US bills was modified and all old-style bills were gradually retired. This is when US dollar bills acquired their present form. But bills from before 1931 were not invalidated. When the Soviet athlete offered them to a salesperson the latter suspected counterfeit and called police. Policemen were helpless: they had never seen such bills before.

Such incidents with Soviet nationals were not infrequent. Treml was equipped to handle the situation: he invited an expert, who confirmed the validity of the bills. The owner of the money would have done much better had he sold the bills to collectors who paid two or three times their par value.

In the late 1960s and early 1970s Soviet nationals occasionally produced still older securities - US government obligations, issued early in the century, before 1919 and marketable until 1925. The bonds were subsequently redeemed by the US government. Some bonds, however, remained in the USSR whither, in all probability, they had been taken before 1917. Arriving in the U.S., some Soviets tried to sell these obsolete bonds and raised eyebrows because younger financial staff was not knowledgeable about them. Financial experts, however, never failed to approve the bonds and allow their owners to exchange them into regular dollar bills.

For all their exceptionality, these stories serve as proof that, contrary to what D. Brooks asserts (28), "the black-mafiosi" are not the only group of Soviets to hold and spend foreign exchange. Soviet citizens employ a variety of ways to obtain foreign currency. Here are several, listed by A. Hochschild (29):

1. some are privileged Soviet officials, especially those whose work takes them abroad;
2. some are Moscow taxi drivers, who now demand payment in dollars when they have a foreign passenger;
3. others are prostitutes... Many work only for hard currency, which they must share with doormen, pimps and protection-racket extortionists who control certain streets;
4. those whose relatives have emigrated to Israel or to the United States.

The list can be easily continued.

5. Western businessmen in the USSR often pay their Soviet employees in hard currency.²⁰ Soviets who work under contract for foreign firms get paid in

hard currency. Business services are also paid for in hard currency. A Western firm recently paid in hard currency for an advertisement in a Soviet newspaper. The person who arranged the deal got a hard-currency fee.

In another example: A group of Western businessmen, who are expected to pay for hotel accommodation in hard currency only, was allowed to pay in rubles "as a special favor." Their hosts were remunerated in hard currency.

6. Soviet managers have been buying business tours to the USA. With tacit consent of the hosting firm such tours are often overpriced but travellers receive the difference when they reach their destination. They are provided with a receipt confirming payment for lectures, in case the Soviet customs ask for an account of dollars and purchased goods.

7. Soviet nationals travel to the USA on private invitations, valid for the term of 6 months but extendable for another 6 months. Throughout this period Soviet visitors work on the sly, as I believe they do in other countries as well.

8. Soviets who leave the country for good are entitled to up to 100 US dollars' worth of foreign exchange per person, and those who go abroad on a private invitation -- up to 200 dollars each. Banks which are licensed to effect such transactions suffer from a shortage of hard currency, but one does not have to wait if one is prepared to part with 50 out of 200, and 25 out of 100 dollars or, at the black-market exchange rate, 1,500 and 750 rubles respectively.

Circulation of hard currency on the black market is believed to be unavoidable until the ruble becomes convertible.²¹ It should be remembered, too, that emigrants will take with them a hefty sum in hard currency. If their annual number reaches 500,000 in the near future, they will take 250 million dollars' worth of hard currency (not just in U.S. dollars).

The impact of black-market circulation of hard currency on Soviet finance is often underestimated even by specialists.

In the report cited above (22, p.38-39) G. Zoteyev, deputy director of the Economic Institute at the USSR Planning Committee, provides his own estimates of the velocity of cash in the USSR. He assumes that, at the beginning of 1991, 142 billion rubles of cash circulated in the Soviet Union, data supplied by V. Geraschenko, chairman of the USSR Gosbank. According to Zoteyev,

This value was used as the starting point of reference for calculations of dynamics of growth of cash in circulation between 1955 and 1990 by means of the continuous-inventory method. The method assumes that the population's earnings exceed their spending by the value equal to annual issue of money (less retired old bills).²² Given annual data in the balance of earnings and spending and subtracting the value of annual surplus of incomes over spending from official statistics on cash in circulation, one can calculate growth of cash in circulation in the Soviet Union in the past 35 years (24).

This approach yields a result which shows a drop in the velocity of cash in circulation : 11.8 in 1955, 8.1 in 1961, 5.3 in 1965, 4.8 in 1980, 3.5 in 1990.

This is an erroneous approach in our opinion. It cannot be employed to calculate the velocity of cash in circulation. I would not put too much trust in statistics on surplus of revenues over spending. The balance fails to take full account of expenses. First, it leaves out of consideration money hoarded at home as a store of value. Second, it ignores the need for transaction balances by the shadow economy.²³ Third, uncontrollable export of rubles is overlooked.²⁴ Fourth, the most important oversight is disregard of money spent by the populace to buy hard currency. All this explains why calculations cannot simply

divide consumer spending on goods and services, as reported in the balance of the population's income and expenditures by the amount of cash in circulation.

The Soviet balance of the population's revenues and expenses is obsolete and incomplete. It appears to me that if Zoteyev's estimates could be supplemented with some of the above considerations, the result would not show a drop in the velocity of cash. Significantly, Zoteyev's estimate indicates a sharp drop in cash in circulation in the late 1980s, at a time when the populace started to convert savings into hard currency on a larger scale.

6. In lieu of conclusion.

Statistics on shadow-economy operations are still poorly substantiated, if at all. Researchers who made those data public did not anticipate the effect they would produce on political debates. Crusaders against the black market usually hit only small fry suspected of contacts with the shadow economy while the black-market tycoons emerge unscathed. Tatyana Koryagina, on one side, inveighs against the apparatus and bureaucracy, believed to be bribed by the black-market dealers. On another side, Sergeev points an accusing finger at co-ops. "The black market may be eliminated if the cooperative sector is put in order," he writes, "and cut off from illegal business" (1, p.77). An excellent idea, but how to implement it? Surely "public inventory-taking" proposed by Sergeev (Ibid.) will not do it.

It seems to me that the shadow economy in the Soviet Union merits more attention than it has so far received from Soviet researchers. The fact of the matter is that as soon as their estimates of the shadow economy are published, their findings are employed for political ends, where evidence does not really matter.

Endnotes

1. The poll was conducted by 9 regional branches and involved 1,341 respondents in urban and rural communities of different age, sex, and education groups, with the marginal error of 0.2 percent in comparison with statistical averages [sic].
2. A total of 4,580 respondents were interviewed.
3. The poll was conducted in the Russian Federation in October 1990 and covered a representative group of 1,420 respondents.
4. The survey was conducted in Kiev and involved a representative group of 542 adults.
5. A representative group of 3.518 people was interviewed.
6. In 1986, 260,000 people faced charges of theft from food-processing factories. Police found them to have stolen foodstuffs worth a total of 1.7 million rubles, or slightly over 5.5 rubles per offender.
7. Pollsters interviewed 45,000 households. More about their findings can be found in (15).
8. Tatyana Koryagina also provides some estimates of the shadow economy. She values the wealth of black-marketeers at 200-240 rubles and turnover at 90 billion (16).
9. The difference may be a lot bigger than that. Experts of the business weekly "Commersant" (V. Kirichenko, A. Malov, S. Titov, Yu. Filenkov, M. Shapiro, A. Shmarov) believe foodstuffs trade on the black market at 2.2 (brandy) to 4.8 (chocolate) times their official price, clothing at 2.8 (women's winter coats) to 3.6 (men's winter coats) times, footwear at 3.5 (ladies' shoes) to 4.8 (men's winter boots) times, household items at 2.5 (synthetic rugs) to 4.0 (knitting machines) times, electrical goods at 2.6 (washing machines) to 5.6 (pressing-irons) times and consumer electronics (TV sets and VCRs) at 2.5-2.6 times their officials price.(19, p. 16).
10. In a survey conducted by the Public Opinion Research Center in conjunction with the Sociological Center at the USSR Academy of Sciences 40 percent of respondents admitted to paying bribes, and 10 percent said they have to give bribes regularly.

11. Consumer spending on cultural services provided by the black market looks underestimated today. S. Titov of the economic institute at the USSR Planning Committee put annual turnover in the black video market at 5 billion rubles in the late 1980s.

12. Tatyana Koryagina's findings were subsequently publicized by the Financial Times which cited her estimate of black-market services of 16 billion rubles.

13. A. Sergeev means "commodities bought up wholesale while still in storage facilities" which never reach official retail outlets but go directly to the black market (1, p. 56).

14. A. Sergeev put taxes in 1987 at 34.2 billion rubles (1, p. 55).

15. The figure is cited by A. Sergeev (1, p. 55).

16. The same result may be obtained in a different way. Tatyana Koryagina cites statistics on categories of consumer spending: 84 percent of overall expenses goes to pay for goods and services in the late 1980s (22, p. 4). In 1989 consumer spending on goods and services totalled 431.8 billion rubles (24, p. 3) so overall spending must be estimated at 514 billion. Add to that surplus of revenues over expenses, 16.6 billion rubles (24, p. 3). Overall spending then equals 530.6 billion rubles, a value close to the amount calculated on the basis of statistics on revenues and spending for different purposes.

17. This includes "funds used to bribe the apparats" (1, p. 62). Yet they can hardly be classified as costs.

18. Estimates of the amount of freely convertible currency in private hands in the Soviet Union vary. S. H. Hanke of the Johns-Hopkins University in Baltimore, for example, believes that "individual Soviets probably hold \$10 billion in foreign currency, or about \$30 per person" (26).

19. "... The World Bank warns of economic collapse and 1,000-percent inflation " in the USSR (27).

20. These days, Soviets also pay foreigners in hard currency. O. Danielyan emigrated from the Soviet Union 25 years ago and took up residence in the USA. He has recently returned to Armenia as the owner of a US firm. He brought with him to Yerevan eight Cadillacs and set up the joint venture "Any." He offers cars for hire with payment in hard currency only. One exception is hearses, which are available

for rubles. The story about his business in a newspaper was therefore headlined "For rubles you can only go to the cemetery" (30).

21. In Poland, for example, the zloty-to-dollar exchange rate has remained unchanged, at 9,500 zloty for one US dollar, for 18 months despite inflation which in Poland devalues the dollar as well as the zloty.

22. The author does not explain how the number of retired old bills was calculated. He may have no access to these data.

23. Soviet consumers are taking an increasing interest in firearms. Press reports indicate as many as 500,000 pieces of firearms may be in private hands. If each is priced at 3,000 rubles (this is said to be the going rate) the public has firearms worth a total of 1.5 billion rubles (31).

24. G. Zoteyev cites a study by V. Geraschenko who claims only 0.5 billion rubles is still outside the USSR after the January 25, 1991, money reform, while "premier Pavlov put the figure at 7 billion" (24, p. 40). Maybe. But there is no way of knowing which of the two values is correct.

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