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MARCH 29, 2007

## Russia's Good Fortune: The Flat Tax Reform

Charles Ganske

By Jon Hellevig



Something Bush and Putin both have in common - tax cuts

Jon Hellevig, a Finnish citizen currently practicing business law in Moscow, sends us this article about the tremendous success of the supply side tax reforms implemented in Russia since 2002. In addition to a better climate for investors and businesses, these changes have given millions of Russians the freedom to travel, to communicate instantly via email and cellphones, and greater access to Western media networks. The social and political consequences of all of this for Russia are now being vigorously debated, but no one can deny that Russia's economy has surged forward in the last six years.

### -The Editors

Putin's efforts to pull Russia out of political and social anarchy and strengthen statehood are starting to pay off transforming Russia into one of the best investment climates in the world while rewarding the nation with unprecedented increases in living standards. At the same time there have been big advances in the judiciary and the legal culture at large; relaxation in the bureaucratic press and reduction in corruption. In all of this, tax reform has played a crucial role in bringing stability and predictability back to Russian society.

After the anarchy of 1990s, the Russian government set out in the year 2000 to implement transparent and predictable tax laws. Gradually over the years from 2001 to 2005 this goal has been achieved through enacting the new Russian Tax Code. And today Putin's tax reforms stand out as the prime example of success achieved during the years of his presidency.



### ABOUT RUSSIA BLOG

Russia Blog presents up-to-date news, facts and commentary on the state of events in Russia and the former Soviet Union. The blog is managed by Yuri Mamchur, Director of Discovery Institute's Real Russia Project and a composer in his spare time. The blog is edited by Charles Ganske.

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### **Another win for The Gipper - the former "Evil Empire" adopts his supply side ideas**

At the heart of the reforms lies the classical liberal tax theory according to which lower taxes translates into increased tax revenues. The best known theorist behind this idea was the late Arthur Laffer, but the person whose name is most associated with them is President Ronald Reagan. Therefore, it is an interesting historic irony that Russia, a country where the socialist creed reigned strong still very recently, has now been converted into the international showcase of economic liberalism. In America, President Reagan and his supporters were known for campaigning for such tax policies, but it is Putin's Russia that has actually implemented them. Reagan could never have dreamed of pushing such measures as Putin's 13% flat income tax rate through Congress. It would be fair to say that never before has there been such a dramatic and speedy shift from socialist tax policies to classical liberalism, and the results could hardly have been more impressive.

The tax reform as a model for far-sighted and well-thought out legislation also had the side-effect of helping to improve the overall lawmaking process and stabilizing the task of state administration. It has also improved the judiciary, which is showing encouraging signs of moving towards a system where court precedents are awarded a significant role that would more closely resemble the Anglo-American system than the more rigid Continental European practices.

Having consolidated these achievements in tax administration, the government has concentrated its recent efforts on reigning-in notorious abuses in the fields of customs. The effects of this crack down on customs corruption and gray import schemes began to be felt last year among the foreign suppliers that have relied on such scoundreling for their profits. By now there is something resembling a panic among Russian importers as many declare that they no longer can continue import operations as before with the government's demand for transparent sales domestically in Russia. Customs values on imported goods are also catching up with market values, a sign of increased risk and stiffer penalties for cheating.

My prediction is that the government's efforts in streamlining customs will during the next two years deliver similar results as those achieved in taxation. Most would argue that the success of the tax reforms has been pivotal in ushering in the economic upsurge, a boom that we can now start calling an economic miracle.

### **The Russian Economic Miracle**

In dollar terms, Russian GDP has increased fivefold from 2000 to 2006. According to our source, Deutsche Bank, the total growth will be six fold by end of 2007. At end of 1999, per capita Russian GDP was just \$1,334 (the dollar to ruble exchange rate being 27.0). By the end of 2005 per capita GDP had risen to \$5,346 annually, for the year 2006 it was \$6,879 and by the end of 2007 it is expected to reach \$8,350. This is more than 600% growth in 7 years.

It is difficult to understand why economists question whether the government's goal of doubling Russian GDP within 10 years is achievable, considering that it already has already grown more than fivefold between 2000-2007 in real, inflation-adjusted dollar terms! These numbers can be verified by looking at any macro economic charts that carry Russian GDP figures. The problem is that an element of confusion is often introduced by trying to adjust the figures to "real growth", which supposedly would clear the performance of emerging markets from inflation, asset value hikes etc. But GDP figures for Western economies are not calculated this way, and therefore the comparison is not apples to apples. Nothing can be more real than comparing the dollar denominated Russian GDP of 1999 with the GDP of 2006. And these figures speak for themselves.

Every now and then we hear the misleading claim that the Russia's GNP is roughly equal to that of the Netherlands, or of Sweden. Even with the formal, PPP adjusted figures, the Russian economy is still the 9th or 10th biggest economy in the world. There is good reason to believe that Russia in a not so distant future will surpass Brazil, Italy, France and even Great Britain to become one of the six largest economies in the world.

Often the GDP numbers for various countries are made comparable by adjusting them using so-called purchasing power parity (PPP). This is done in order to attempt to take into account the differences in the relative price level in various countries e.g. the price for a hair-cut in France versus in China (or the fact that there are places where the hair cuts are done at home for no pay). In that regard Russian GDP would on a PPP measure be \$12,000. which is already more than one third of the average for Western Europe. It also more than half of the

year 2000 level of GDP in Finland, to take the European showcase of my homeland as an example. This should show how deceptive it is to try to read in too much structural difference to these statistics.

According to some estimates the ruble is very much undervalued, and therefore the correct purchasing parity figure could be as high as \$18,000 per capita. If we were to consider the huge differences in general price levels across this biggest country in the world (with housing and food being much cheaper in the regions than in Moscow and St. Petersburg), then this adjusted figure could, in fact, be closer to the truth.

### From Rags to Riches During Putin's Presidency

When Putin took over the presidency in year 2000 the country was on the brink of ruin. For many Russians and Western observers it seemed that the fall was inevitable and final. GDP per capita was at the level of third world countries; the external debt was \$150 billion or more than 100% of the country's GDP; Russia had recently gone through a devastating devaluation and received an emergency loan of \$10 billion from the International Monetary Fund (many claim that even this money did not reach the state coffers, but was stolen by corrupt officials in the Yeltsin Administration). By contrast, in June 2006 Russia's external debt had dropped to \$60 billion or less than 6% of GDP, which makes Russia practically debtless compared to the world's leading economies. The debt rates in European countries are significantly higher e.g. in the same year in Germany the total was 67.7%, in France 66.8%, in Finland 41.1% and in Italy 106.4% (2006 figures from the European Central Bank). The problem for Russia's creditors in recent years has not been to extract payments from Moscow on its outstanding debt, but to keep Russia from paying them off ahead of schedule. The Paris Club, an elite group of Western creditor nations, was shocked to experience Russian prepayment last year.

The currency and gold reserves of the Russian Central Bank were a mere \$36.6 billion in 2001, but today they have ballooned to a staggering \$315 billion (Source: www.minfin.ru). Russia's cash reserves today are the third largest in the world, trailing only China and Japan. On top of this the Finance Ministry has created a Stabilization Fund where surplus proceeds from oil revenues are saved; by January 1, 2007 the fund had accumulated \$88.7 billion (source: www.minfin.ru).

The officially calculated average monthly salary in Russia was \$81 at the time when Putin took the helm of a very shaky country. But at the beginning of 2006 the average salary was \$371 and by December 2006 it had already reached \$550. This is the highest level of salaries paid in all of the CIS countries. Still these absolute figures should not be compared with Western salaries; the differences in purchasing power and the economic structure hide a different reality more favorable for Russia.

In 2001 the World Bank estimated that 27.3% of Russians or 40 million people lived below the poverty line; by the end of 2005 the number of people living in such dire poverty had been halved down to 15.8% of the population or 22.6 millions. According to recent EU statistics this figure corresponds with the EU average which is the same unfortunate 16% (*Business Week*, February 2007).

### The Russian Economic Miracle is the Result of Sound Policies, Not Just Higher Oil Prices

Russia's critics dismiss all of this by arguing that the economic upsurge is exclusively "oil-driven", that Russia simply enjoys "windfall revenues" from export of oil, gas and raw materials buoyed by surging world market prices.



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These critics of Putin's reforms forget that the raw materials have been under Russian soil for ever, but it is only now, under Putin's leadership, that they have brought unprecedented growth and prosperity to the country. Putin

did not create the raw materials; he created the conditions for a democratic market economy that can leverage natural resources to diversify the economy. It is through consistent and well-planned economic and social reforms, along with the rule of law that the economy has taken off. Therefore, when we put aside all of the exiled oligarch-funded propaganda designed to paint Russia in black, we will be reminded that during Putin's presidency Russia has been placed on a solid foundation for a competitive democratic market economy.

### **How Putin's Tax Reforms Are Fueling the Economy**

The great tax reform undertaken in Russia under the Putin presidency in years 2000 through 2005 has been the decisive contribution to the reforms and by far the most remarkable achievement in building a democratic state of free individuals. These reforms have given Russia Europe's most liberal system of taxation. Today in Russia there are transparent tax laws and internationally low tax rates, which provide good incentives for hard work. The corporate profit tax rate is 24 % and Russians enjoy a European-low 13% flat tax rate for all income brackets. With this low rate, Russia is near the top of world rankings for individual tax freedom as shown by Avenir's World Individual Tax Freedom Survey (see chart below). Thanks to the low flat tax rate, Russia avoids the European trap of punishing hard work with big taxes. The employer's social contributions are paid in form of a social tax charged on a regressive scale from 26% to 2%, meaning that the more salary the employer pays to an employee the smaller the tax. Thus the employer is also stimulated to increase salaries. This is in line with the overall business friendly approach inherent in Russian tax laws.

The legislative initiatives are supported by a general improvement in tax officers' professional skills, spearheading a breakthrough in administrative transparency. This progress has been possible thanks to major advances in the judiciary with enhanced predictability and court precedents increasingly shaping a Russian legal framework.

Legislation, administration and the judiciary aside, perhaps the biggest change has occurred in the taxpayers themselves who are busy shaking off the burdens of the old "kryshe" black market economy and memories of the chaotic 1990s, and are now "going white", as they say in Russia. In spite of some infrequent and spectacular crimes by the people who formerly benefitted from the anarchy of the Nineties, most companies and individuals are increasingly valuing the benefits of operating within the legal system of the country. Russian businessmen realize that one both earns more and sleeps better at night by staying within the official legal system. There is an increased awareness of the primacy of creating shareholder value and that this is exclusively the product of legally sound business practices within a transparent economy.

The Kremlin made a major impact by targeting the most flagrant examples of tax evasion schemes (e.g. Yukos). The resulting public discussion, administrative guidelines and ensuing court practice have all contributed to create a more transparent and professional business climate. The outcome is a tremendous growth of tax revenues as corporations have repatriated capital from offshore tax havens and eliminating illegal money laundering schemes.

Behind all of these achievements there is the determination to establish the rule of law necessary to sustain a democratic legal order, market principles, competitive plurality, and a window of political stability giving time to enact major reforms. Some of these reforms, of course, by strengthening the state, have produced criticism from around the world. But many of these critics did not seem to mind when Russia was weak and could not enforce the rule of law or control access to its natural resources.

### **Lower Taxes Contribute to Individual Freedom in Russia**

The tax reform is also a strong statement about the liberal orientation of Russian reforms, for there can hardly be any more significant issue affecting individual freedom than levels of taxation, which leaves the individual with a real choice about how to spend his resources and live his life. By this measure, Russia is becoming a showcase for the growth that record low tax rates can stimulate. To a great extent this is evidence of a political system that encourages individual freedom, not only in speech, but more importantly in action. In the early to mid 20th century, Europe and the United States successfully created a large middle class, and this is the road now being taken in today's Russia.

Even the favorite hack topic of Russia critics, freedom of speech, comes out in new light when considered against this measure of the tax freedom ranking. After all the human freedom to keep one's own income and decide how to use it must be regarded as fundamental.





**Shoppers at Moscow's Stockmann Department store**

Clearly when the tax burden is less, then there is more personal discretion as to how to use one's income. Today Russians have a wide choice in this respect. When tired of Russian television they can e.g. choose from international satellite channels, from CNN to Sky Channel, all serving Russia with the best truth that money can buy. There is a wide choice of domestic newspapers, but the Russian reader may also pick up his copy of the Financial Times or, for the sake of more objective coverage, the International Herald Tribune. Half of Russia's college students are enrolled in paid tuition programs, thus parents and students may choose from the market those schools and programs that best suit their own world-view. The mobile phone networks cover practically all the country encompassing all the economically and politically active population. Russians were not more free to access the outside world through the Internet in the 1990s when it did not exist, nor to post their views online uncensored by their government (unlike say, citizens of America's leading trading partner China or of its Arab allies).

Today Russian citizens can, for the first time in history, freely communicate with each other from one part of Russia to another, spreading real-time information through eleven time-zones from east to west. Russians can also travel abroad - and return home, like never before. And they are making use of this newfound liberty. In year 2005 (Rosstat) Russians made 15 million trips abroad to Western countries. That number equals about 10% of the population. (There is some overlap because the statistics register the number of trips and not individuals traveling, but on the other hand these figures do not register travel to neighboring CIS countries, such as Ukraine and Kazakhstan).



**Heading out - a Russian traveller (Photo by: St. Petersburg Times)**

On their trips abroad the Russians have a good chance to verify whether they have truly been victimized by restrictions on freedom of speech or brainwashed by state television into supporting Putin, as is claimed in the West. But for some reason Russians return home without experiencing the sensation of having become privy to previously hidden facts of life back home in Russia. With enough patience and a sense of humor they could, however, read about ex-FSB agent Litvinenko being lifted to the ranks of Andrei Sakharov and declared a "Russian dissident", about "friends of Litvinenko" on Boris Berezovsky's payroll serving for the British press as the most reliable sources possible on all things Russian; about Russia allegedly using energy to intimidate its neighbors, the fragile democracies of Georgia, Estonia and (a the latest "victim") Belarus; or the investigative journalist Anna Politkovskaya having discovered that there was a brutal guerilla war going on in Chechnya; and that only the super rich have benefited from economic reforms, which puts all those 15 million that traveled abroad in the category of Russia's new "super rich".

#### **Avenir Corporate's Survey of World Individual Tax Freedom**

For this survey Russian personal tax rate was compared with a sample of other developed countries (data from Finnish Taxpayers Center and Avenir Corporate, Russia). Of all the countries surveyed, the tax rates were by far the lowest in Russia according to Avenir's World Individual Tax Freedom Survey. In Russia the individual is left with a record 87% of his income, to be used as that person wishes. Also taking into consideration the low cost of utilities in Russia; free education; and the comparatively low level of other living costs outside Moscow and St. Petersburg, we may conclude that in Russia a middle class person in reality is free to decide on his own discretion how to dispose of his income and how to live.

#### Annual Income Level 31,400 euros

1. Russia 13,0%
2. Ukraine 15,0%
3. Slovakia 19,0%
4. Switzerland 14,6%
5. Japan 18,6%
6. USA 22,1%
7. Estonia 22,4%
8. UK 23,4%
9. Australia 24,3%
10. Spain 24,4%
11. Norway 24,9%
12. Austria 25,1%
13. Canada 26,1%
14. Sweden 30,1%
15. France 30,7%
16. Finland 30,8%
17. Holland 31,2%
18. Italy 33,8%
19. Denmark 36,8%
20. Germany 39,6%
21. Belgium 39,8%

#### Annual Income level 102,500 euros

1. Russia 13,0%
2. Ukraine 15,0%
3. Slovakia 19,0%
4. Estonia 23,2%
5. Switzerland 25,4%
6. Japan 29,0%
7. USA 35,2%
8. UK 33,4%
9. Spain 36,7%
10. Canada 36,8%
11. Norway 37,4%
12. Australia 39,4%
13. Austria 39,6%
14. France 40,1%
15. Italy 43,6%
16. Holland 43,9%
17. Germany 46,3%
18. Finland 46,8%
19. Sweden 47,0%
20. Denmark 52,5%
21. Belgium 53,0%

(Sources: Finnish Taxpayers Center and **Avenir Corporate**)

The writer is a Finnish lawyer active in Russia. He is the co-author of *Avenir Guide to Russian Taxes*, with recent launches of updated editions in both English and Russian. He has written the book *Expressions and Interpretations* discussing Russia's social development from the viewpoint of philosophy and philosophy of law. He is also the author of several books on the Russian tax and labor law.

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Posted by Charles Ganske on March 29, 2007 12:00 AM | [Permalink](#)

#### TrackBack

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<http://www.discovery.org/scripts/mt/mt-tb.cgi/2165>

#### Comments

I'd like to add some facts:

1) Russian stock index  
2000 - 143  
2001 - 260  
2002 - 359  
2003 - 567  
2004 - 614  
2005 - 1125  
2006 - 1922

1344% growth for last 6 years.

<http://www.rts.ru/en/index/stat/monthlyhistory.html?code=RTSI>

2) Money flow  
2000 -\$25 billions  
2001 -\$15 billions  
2002 -\$8 billions  
2003 -\$2 billions  
2004 -\$8 billion  
2005 +\$1 billion  
2006 +\$42 billions

We can see money is not running out the country anymore, but just opposite, money rush into Russia.

[http://www.cbr.ru/statistics/credit\\_statistics/print.asp?file=capital.htm](http://www.cbr.ru/statistics/credit_statistics/print.asp?file=capital.htm)

3) Russian IPO statistic  
Russian companies received only \$0.64 billions with IPO for the period from 1991 to 2002.  
2003 \$0.14 billions  
2004 \$0.55 billions  
2005 \$4.55 billions  
2006 \$20.1 billions

Numbers speak for themselves.

4) Direct foreign investment grown 7 times under Putin's rule (from \$4.4bn in 2000 to \$31bn in 2006)

5) Inflation dropped 4 times, from 36% to 9% in 2006.

6) Budget income growth 1095%, from \$24bn (2000) to \$263bn (2006).

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Posted by: dim | March 29, 2007 6:59 AM

Dim,

...great FACTS...

But facts aren't popular in the news today...

News is mostly spread with hope, assumption, and dreams...

On Dec of 1991, the communists packed up and moved from Moscow to Washington DC. I say this because America, the symbol of capitalism takes loans from communist China... it simply cracks me up... Then the capitalists packed up and moved to Moscow, figuratively speaking...

But, it looks like Putin has proven that Reaganomics works... Steven Forbes ran for president on the concept of a 12% flat tax for the US.... Forbes "talked" about, Putin "implemented" it.

Why do America yap about things? Yet the "new" Russians "do it" and "implement" with substantial deliverables?

Bush with his constant yapping of how great everything is, yet the bottom line looks like Enron, Tyco, GlobalCrossing, United Airline, WorldComm, and Lucent accounting books.

I love capitalism, and market economics with a dose of protectionism to squelch out the Yukos like companies that lived on rapping Russia.

Mathew Simmons said that oil was really worth \$250 / brl, and the market agrees while Putin prepared Russia for such tectonic shifts.

Why the heck do American business men, republicans have such a difficult time understanding that Russia stopped with the idealism and got to work?

Anyway... the speculators are now wondering what will be after Putin. I think more of the same, I'm damn sure.

And for the US after Bush? More of the same. sorry to sav.

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Posted by: **Luther G. Quick** | **March 29, 2007 8:00 PM**

The low income tax in Russia is impressive when compared to other countries, but considering the large class gap, isn't some degree of redistribution of wealth in order and thus a progressive tax system? I understand the argument that low taxes for the high tax brackets can stimulate the business class, spur the economy, and lead to a trickle-down effect. But I would be interested to hear economists weigh in on what would be the most socially beneficial in the case of Russia-- a low, flat income tax that lets the extremely wealthy off the hook, or a progressive tax system that would speed up the "trickling down" process.

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Posted by: **upthera44** | **March 30, 2007 12:44 PM**

upthera44,

I firmly believe that after Yeltsin took over, and gave 20 offices inside the Kremlin to 20 US State Department consultants, spreading and sharing the same "Yankee Know How" that we see today in Iraq, I believe that this is what created and extended the class gap, the income gap.

Flat tax, low tax will eventually make a larger middle class for Russia. It's not overnight, no instant gratification, but my guess within 1/2 a generation.

And income redistribution is a communist concept. This eludes that you must take from A and give to B. When in fact, in Russia, income and wealth is new and is being created, not only transferred. Over time, income and wealth created at the source, will stay at or near the source with minimal taxation.

Russia is growing, and recovering, and she is doing it from within, not invading over some delusional pretext such as "wmd or he did 9/11". Russia is growing despite Western NGO's, Russia is creating wealth from its own labor and innovation, not like America taking out massive trillion dollar loans to buy cheap crap from China. At least whatever cheap crap Russia buys from China, it's purchased, debt free.

I believe that today Russia has a great tax system that is more modern than say the US. Slowly western investors are realizing that Russia is one of the best places to invest.

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Posted by: **Luther G. Quick** | **March 30, 2007 4:06 PM**

Flat taxes....good idea. One of the smarter moves which Russia has done on the economic front. Calculating salaries is still a headache in the Russian Far East though.

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Posted by: **Tim Newman** | **March 30, 2007 4:31 PM**

Luther,

Thanks for the response. Redistribution of wealth (via income tax) as I was suggesting is more of a mixed economy concept than a communist one. To my knowledge, almost every capitalist economy in the world engages in redistribution of wealth to some degree.

I'm not an expert on the Russian economy, but from my layman perspective it seems that the privatization scandals and seizure of Russia's assets by oligarchs and other elites in the 90s (enabled by U.S. advisors) created a very uneven playing field from the outset. So the standard benefits of a flat income tax rate, while still applicable, seem insufficient. One has to wonder what the real reasons behind the flat tax rate are (to promote business as you suggest, or to preserve the wealth of the very rich). New wealth is being generated, as you point out, but there was also a lot of old wealth that was stolen and this was never rectified. What are your thoughts on this?

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Posted by: **upthera44** | **March 31, 2007 6:53 AM**

Dear Tim Newman,

Gee... you are worried about the far east? that's old news, this isn't the 1990's Yeltsin era.

Then I think about Walter Reed where America can't take care of those that sacrificed their lives over this delusional war... And then I think about the Walter Reed VIP rooms.

Great photos here of the Walter Reed Presidential Suit:

**[http://www.usatoday.com/news/gallery/2007/n070315\\_reed/flash.htm](http://www.usatoday.com/news/gallery/2007/n070315_reed/flash.htm)**

You see, if you are important, you don't get a room at Walter Reed with mold and rats. Personally, I think an Army private is far more important than some commander or general. But what do I know...

Then I think about the 10 million plus American children that live below poverty... I think about the vets that getting nothing and I think about our current soldiers in Iraq that can't get decent armor...

Bringing up the far east of Russia from the 1990's will not make Walter Reed better. Worry about the US, stop worrying about Russia.

Russia is recovering just fine.

Right now Russia is packed with money, and if carefully invested within it's economy, the success found in Moscow & Saint Petersburg will spread to the far east and across all regions (it has already in fact), this is the post Putin phase which I have full confidence will work and will include nearly all CIS member states as all the CIS+SCO+BRIC countries work together for such mutual success while binding to NAM (none alignment movement) or if needed some temporary hegemony with Russia + China in the lead. So long as US "good intentions" and "Yankee Know How" stay out, everything will be just fine.

Please Mr. Bush, don't bring Walter Reed, Katrina, or Iraq reconstruction "project management" skills to Belarus, Russia or Ukraine, nobody believes America anymore.

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Posted by: **Luther G. Quick** | **March 31, 2007 1:33 PM**

Hello upthera44,

I jumped the gun when responding to your post before, sorry.

Honestly, I think the "current" Russian government must (they are / will) honor "most" agreements from the Yeltsin era. And future Russian gov must honor whatever wealth transfers and agreements were created during the 2000-2008 time.

With that said, sure, there was a lot of stealing from the state. Many people were simply lucky and were in the right place at the right time, but they kept the wealth home.

This activity is getting tired in the west. Haliburton is now moving offshore after raping the Pentagon - like Yukos, let's see if this comes up in the 2008 election.

Anyway, when someone like Khodorkovsky became lucky, he should have taken that wealth and rolled it back into Russia. Instead, Khodorkovsky collaborated with Western nations, used illegal transfer pricing (the IRS doesn't tolerate it, and applies RICO laws for the same in the US) not only to evade taxes but to also prepare the transfer of Yukos into the hands of a Western oil major. This was treason. Let alone the fact that some of Khodorkovsky's tools were forgery. The US and the EU won't stomach this kind of behavior, so why should Russia?

A lot of wealth left Russia, and there isn't much anyone can do about it. But these new tax laws have a lot of benefit that will not only bring some of the wealth back (there is tax amnesty) but a tremendous amount of wealth will be created as Russia's capitalist economy is going to see very good growth, even as oil goes down (temp).

And I understand the main theme of this article is about flat tax, and I'm off on a tangent with the Yukos stuff. But there is so much to the new Russian tax laws that are going to make investment so attractive. A flat tax in Russia will be different than a flat tax in the US. The economies are very different. The US is highly subsidized and enjoys access to massive debts, unearned value of it's currency via hegemony, and in doing so has many working business models that would normally fail (once energy goes up). For Russia, it is held to a higher standard and can not enjoy such sloppy administration.

To this end, Russia will honor all past agreements that will not jeopardize her future. Yet the new tax laws will make it (eventually) costly for exports of energy and raw material. The best way for Russia to avoid the Dutch Disease is to stop exporting energy and raw material and consume them at home, for value added product exports. And tax laws are optimizing this, over time, the economy will adjust and the markets had better worry about the absences of Russian energy and commodities.

So to answer your question, there is no need to rectify anything at this point. The wealth that Russia has pent up will dwarf the 1990's virtual depression. And Russia will enjoy the fruits of this recovery with Belarus and Ukraine and other CIS nations.

The EU and US looted the CIS, let them enjoy it, because they will need it as they start burning the furniture to keep their cul-de-sac houses warm and the SUV's running .

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Posted by: **Luther G. Quick** | **March 31, 2007 6:23 PM**

*Gee... you are worried about the far east?*

No, I'm not. I simply made a comment on the complications of calculating salaries in the Russian Far East. Given that I am a general manager of a business operating in the Russian Far East, and I must understand this subject if I wish to stay out of a courtroom, this probably gives me some authority on the subject.

As for the rest of your comments, especially regarding the reinvestment of Russia's wealth in the Far East, all I can say is that what I am witnessing on a daily basis contradicts rather sharply with your own statements.

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Posted by: **Tim Newman** | **April 1, 2007 5:42 PM**

I'm not sure what cul-de-sacs and SUVs in America have to do with the pros and cons of the flat rate in the Russian economy. Anyone else have any thoughts about my original question?

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Posted by: **unthera44** | **April 2, 2007 6:01 AM**

Posted by: **upthera44** | April 2, 2007 9:01 AM

Tim,

Well, sounds like you are working for a UK or US oil major (ref to Sakhalin on your site - I had no time to read)... Not quite sure, but anyway, our business hopes to be doing the same by the end of 2007 or early 2008 for a large medical project in Russia/Belarus for service to the US.

Calculating what to pay by the locals must be difficult for foreign firms focused on transferring as much wealth out of Sakhalin as the local law can stand...

However, for us, we believe it's a better for investment to leave the wealth locally as western economies and currencies are pent up for big problems with debt and lack of resources... to this end, future calculation should focus and sending the minimum out of Russia and CIS countries.

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Posted by: **Luther G. Quick** | April 2, 2007 10:03 AM

Upthera44,

Boy, your right, I do get side tracked... But, my deeper point is this. Flat tax or low tax behaves different in different economies. Giving low tax isn't the holly grail. Someone like Ronald Reagan, if he wanted to really worry about the future of America, and really make America strong, they should have made energy expensive as hell (tax it), then whatever flat tax they created (on income), the money for investments into alternatives, the incentives for people to avoid the SUV or the cul-de-sac society would have made America much different today... Suburbia would not be... And you can bet 9/11 would not have happened, and old Genius Bush Jr would have taken his internship into Iraq.

Europe and Russia are far more energy efficient than the US. They do planning, they think about depleting resources and they give tax breaks when it's good, and subsidize things to make positive change...

A small example. I read the entire 1700 pages of the US energy act of 2005, great ideas, but it will never work. If I blow \$100,000 tomorrow making my home highly energy efficient, I will pay property tax on that extra 100k... screw that...

In Spain, whatever energy you produce with renewables, you can sell back to the energy company at TWO times the retail rate, now that's progressive... In America, you get 1/2 the retail rate... and you will be taxed for your effort.

Taxes are one thing, but there are so many other laws that need to change. The US simply doesn't look like a progressive capitalist nation for long term view point. Sure, its tax laws are optimized where eventually incentives propagate thought the system to invent excuses to invade say "Iraq", sure... Reaching out and manipulating other nations, that's what the US laws are designed in creating. Efficacy? Productivity? Jobs in America? Tax laws don't want that in America.

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Posted by: **Luther G. Quick** | April 2, 2007 10:18 AM

upthera44: *"One has to wonder what the real reasons behind the flat tax rate are (to promote business as you suggest, or to preserve the wealth of the very rich)."*

Good point. One may as well wonder if the true purpose of Bush's tax cuts is to promote growth of the economy or to preserve the wealth of the very rich: **Bush offered a budget that offers \$32.7 billion in tax cuts to the Wal-Mart family alone, while cutting \$28 billion from Medicaid.**

The good thing (for Russia) it appears to be working, as illustrated by the facts above, so why fix it if it's not broken?

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Posted by: **Petr Pustota** | April 2, 2007 1:06 PM

*Calculating what to pay by the locals must be difficult for foreign firms focused on transferring as much wealth out of Sakhalin as the local law can stand...*

I'm sure it would be, but I have yet to come across a foreign firm operating in Sakhalin which is focused on this.

*However, for us, we believe it's a better for investment to leave the wealth locally as Western economies and currencies are pent up for big problems with debt and lack of resources... to this end, future calculation should focus and sending the minimum out of Russia and CIS countries.*

Well, good luck with that. Let's hope your shareholders/owners/creditors share your sentiment.

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Posted by: **Tim Newman** | April 2, 2007 6:58 PM

Dear Tim,

You know... this language thing is silly. The way you link calculating pay with Russia and court. As if people start to have images of the Gulag.

Well, try to not paying your employee's FICA in the US ! Try skipping out on paying State sales tax in the US ?

Not only will your go to court in the US but you will go to jail.

If Kenny Boy Lay of Enron did his thing in Russia do you think Russia should be any softer than the US? Look up RICO laws in the US, I'll bet Russia is softer than the IRS with a RICO warrant.

And look how Russia is canceling tax evation fees, this break you will never see in America. And maybe that's why Halliburton is moving.

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Posted by: **Luther G. Quick** | April 3, 2007 10:50 AM

*You know... this language thing is silly. The way you link caluculating pay with Russia and court. As if people start to have images of the Gulag.*

As somebody who says they are about to start a business in Russia, you might do well to wise up a bit about how the law works over here. As you rightly point out, if you mess up the tax payments in the US, you go to court (and possibly to jail). In Russia it is the same. Why is this so hard for you to believe?

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Posted by: **Tim Newman** | April 3, 2007 1:31 PM

Tim,

So then, we agree, learn the local tax laws, be it US or Russian. You are eluding that both simply want compliance. And that generally, such compliance is fair in Russia.

What I don't understand is why did you bring it up in the first place?

This reminds me of a joke about Americans.

This American goes to Europe and stands there in the middle of a street and yells "look at all these foreigners".

---

Posted by: **Luther G. Quick** | April 4, 2007 8:27 AM

*What I don't understand is why did you bring it up in the first place?*

Why did I bring up the issue of tax compliance in Russia on a thread about Russia's flat tax?

I dunno. I suppose I just like hijacking threads with off-topic comments.

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Posted by: **Tim Newman** | April 4, 2007 7:48 PM

Tim,

**You said "Given that I am a general manager of a business operating in the Russian Far East, and I must understand this subject if I wish to stay out of a courtroom, this probably gives me some authority on the subject."**

The way the English was dropped eludes that Russia is some new frontier, some wild west. But in truth, whether you are in the US, EU, none compliancy gets you in court as well, just as easy.

Ebbers of WorldCom avoided compliancy just as Mikhail Khodorkovsky of Yukos did. However, Ebbers got 25 years for a few billion \$ mistake, Khodorkovsky got 11 years for a 25 billion \$ mistake. Sounds to me like Russia is more liberal, fair, and forgiving, thus, more democratic.

I read too much about some Russian legal issue when in fact, Western society is at the same footing if not worse.

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Posted by: **Luther G. Quick** | April 5, 2007 7:41 AM

Luther,

As a native speaker of English who uses the word "elude" in the proper context (for future reference "elude" means to avoid, "allude" means to imply or make reference to), I disagree that Tim's tone or wording implied anything inferior or backwards about the Russian legal system. I believe all he was saying was that it is his job to know the inner-workings of calculating salaries and if he doesn't do it correctly, he could go to jail. The same, of course could be said for an employer in the U.S.

Interpreting every innocuous statement as provocation and using it as a reason to bring up cul-de-sacs, Walter Reed, Hurricane Katrina, "Kenny Boy Lay", and various irrelevant topics is silly and detracts considerably from the credibility of any more legitimate argument you might be making.

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Posted by: **upthera44** | April 5, 2007 7:27 PM

*Sounds to me like Russia is more liberal, fair, and forgiving, thus, more democratic.*

Yes, longevity of prison sentences is an excellent measure of the democratic process.

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Posted by: **Tim Newman** | April 6, 2007 6:53 AM

Hello upthera44,

Gee... I'm embarrassed... Thanks... "Allude", thanks.

I lived in Spain as a child, and learn Spanish first and to this day, I spell acoustically. English has always been rough for me, even though I have been in the US for 35 years. Add to this that I am a software engineer and every command has wild and cryptic spellings.

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Posted by: **Luther G. Quick** | **April 6, 2007 8:13 AM**

Dear Tim Newman,

Since you are bring up prison sentences... here is how we run US prisons, I'm sure, somehow all this abuse is for "democracy"?

**<http://www.therussiansarehere.com/vid/0-US-Failures/prison.wmv>**

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Posted by: **Luther G. Quick** | **April 6, 2007 1:06 PM**

*"...longevity of prison sentences is an excellent measure of the democratic process."*

I think most people would prefer a long sentence in a Russian prison then even a day in this fine **bastion of U.S. democracy**.

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Posted by: **Petr Pustota** | **April 6, 2007 7:51 PM**

*Since you are bring up prison sentences...*

No, it was you who brought up prison sentences, remember?

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Posted by: **Tim Newman** | **April 7, 2007 2:08 PM**

I don't think it makes much sense to constantly compare the U.S. to Russia, much less to bash America to build Russia up. Instead, I think it makes sense to compare Russia today to where it was in the recent post-Soviet past.

If you compare Russia, India, and China now to where they were in the early 90s, then the growth appears phenominal. If you use the median U.S. standard of living as your baseline, of course they still lag behind. But is the average Russian better off today than he was in 1991, 1995, or 2000? I have little doubt that the answer for the vast majority of working Russians would be yes.

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Posted by: **Charles D. Ganske** | **April 16, 2007 5:08 PM**

Charles,

I would agree with not comparing the US & Russia. But it's the US that claims it's trying to make everyone like the US. It's the US that claims it's the standard (let's forget about Gitmo or AbuGarib or whatever). With this, bashing America goes along the same lines... Imagine some guy with 10 divorces giving you advice on marriage, or some homeless guy giving you financial advice... This is what the US is doing not only to Russia but the entire world. I mean now, the IMF is trying to dictate what Russia should be doing with its hard earned money while the US can't keep it's on financial house in order... Anyway, maybe I watched too much M\*A\*S\*H and too much George Carlin... I just don't believe claimed US motives and I have no faith in US management from corporate to government because I'm still waiting for sustainable results... Sure, we have good show, and this millisecond all is stable, but the foundation is cracking. And to this, leave the CIS alone, they will find their place and will (continue) succeed. It just seams better to allow internal mistakes, with external guidance than to constantly induce chaos with a colored revolutions. And anyway, this article is about taxes, and I'm still waiting for my flat tax in America, Forbes promised it, Reagan dreamed of it, Putin delivered it and for goodness sakes most of the CIS has lower taxes than the US.

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Posted by: **Luther G. Quick** | **April 18, 2007 3:07 PM**

Grew up in Spain, waiting for his flat tax in America and trying to take medical a business (with no need for returning a profit) to the CIS, **and** has lots of time to make pointless illogical rantings on the internet. Hmm, sounds more like the resume of a garden variety Internet troll to me.

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Posted by: Anonymous | **April 19, 2007 6:38 PM**

Avenir's World Individual Tax Freedom Survey

I cannot find any reference to this survey on the web. Can you post the URL to the original? Recall the quote from Mark Twain, There are lies, damn lies, and then there are statistics.

Who is Avenir Suisse and how was the survey conducted?

thanks

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Posted by: dgd | April 28, 2007 1:06 AM

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