

The Flat Tax at Work in Russia: Year Two

By Alvin Rabushka

On January 1, 2001, a 13% flat-rate tax on personal income took effect in Russia. (On the general principles and beneficial economic effects of the flat tax, see *The Flat Tax*.) Russia's 13% flat tax replaced a three-bracket system, which imposed a top rate of 30% on taxable income exceeding \$5,000.

During its first year, the 13% flat tax exceeded all expectations. In 2001, personal income taxes increased 46% in nominal rubles, or 28% in real rubles after adjusting for ruble inflation of 18%. Personal income tax as a share of consolidated budget tax revenue rose from 12.1% in 2000 to 12.7% in 2001. Since economic growth of 5.0% in 2001 was lower than the record 9.0% growth in 2000, the rise in revenue cannot be attributed solely, or even largely, to growth in 2001. For a detailed treatment of Russia's 13% flat tax, see "The Flat Tax at Work in Russia."

Data for 2002 are now available, posted to the Russian government's Ministry of Finance web site. ([Http://www.nalog.ru](http://www.nalog.ru)) Personal income taxes in 2002 amounted to R357.1 billion (\$1=R31.7), up from R255.5 billion in 2001, an increase of 39.8%. Annualized average ruble inflation in 2002 was 15.8%. Thus, real ruble tax revenues rose 20.7%, another large increase. Moreover, economic growth of 4.3% in 2002 was lower than the 5.0% growth the previous year. Real ruble revenues continued to rise in 2002 despite slowing growth, suggesting greater compliance and efficiency in tax administration.

Since the implementation of Russia's flat tax, personal income taxes have contributed a growing share of Russia's consolidated budget. In 2002, the flat tax generated 15.3% of total tax revenue, up from 12.7% in 2001. From relative unimportance as a source of revenue a few short years ago, the 13% flat tax on personal income now exceeds excise taxes and taxes on natural resource use, and is fast catching up with corporate income tax and value added tax.

To date, the governments of Estonia, Latvia, and Russia have enacted flat-rate taxes on personal income. Russia has also implemented a reduction in the corporate rate of tax, from 35% to 24%, effective January 1, 2002. Russia has also enacted a flat-rate small business tax, the lesser of 6% of gross turnover or 15% of profits. (See "Further Extending Russia's Tax Reforms," "Tax Reform Remains High on Russia's Policy Agenda," and "Completing Small Business Tax Reform") A Chinese edition of *The Flat Tax* is scheduled for publication by China's Ministry of Finance in early 2003.

(Anjela and Diana Kniazeva, graduate students in the Department of Economics, Stern School of Business, New York University, provided research assistance for the preparation of this article.)