

Russia's Small Entrepreneurs

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Introduction

Many governments have recognized that fostering entrepreneurship has become an effective tool in promoting economic growth and expanding employment. Small and medium-sized enterprises (SMEs)¹ serve as the backbone of local industries. These enterprises promote competitiveness and efficiency.

In Russia, the expansion of the small business sector is crucial for the development of local markets, job creation, innovation and the promotion of new technologies, and improvements in the standard of living. With the economic structure retaining elements inherited from the past, the share of the small business sector in GDP is estimated as being between 13% (independent estimates) and 9% (government estimates).

In Japan, Germany, United States and the United Kingdom, SMEs' share of GDP is above 50%, while in France and Italy it is close to 60%. In Finland, small business is closely interconnected with medium-sized enterprises and large corporations, playing a strategic role in maintaining international economic competitiveness.

Many economies in transition in Eastern and Central Europe also demonstrate remarkable progress in the development of the small business sector. In Hungary, small enterprises' share of GDP is about 50%; they support two-thirds of employment and generate 20% of exports. Of the total number of enterprises, the share of small businesses is close to 99%, while in Russia it is only 30% according to independent estimates, and significantly less according to official statistical standards.² Estimates provided by independent experts demonstrate that there are about 25-30 small enterprises per 1,000 people in Russia (government estimates suggest that this figure is only 5-6). In Hungary, this number is about 75-80, while in France, Germany, the United Kingdom, Japan, Italy and the United States it ranges between 35 and 74 per 1,000.

SMEs in Northeast Asia

In Northeast Asia, SMEs' share of the total number of enterprises is about 90%, while shares in production and employment are also high. On the average, SMEs account

for about half of the output and value added in manufacturing and about two-thirds to three-quarters of the total work force. The SMEs' activities are spread across a wide range of traditional areas and involve innovative approaches to all major business functions, including marketing, organization and distribution.

Japan has developed a comprehensive policy of support for SMEs. Government policies for SMEs include efforts to develop consulting and guidance services, improve education, promote networking and subcontracting, provide loan guarantees and tax incentives, and promote structural upgrading and venture businesses. Governments play an important role in facilitating local entrepreneurship. In Niigata, for example, there are 33 industrial parks with a combined area of more than 1,000 hectares and land prices ranging from 5,000 yen to 36,000 yen per square meter.

In China³, SMEs and rural township enterprises are the key to market transformation and employment expansion. The SME support policies of the central and provincial governments are aimed at achieving a level playing field in terms of competition by providing training and education for managers and workers. The government also supports entrepreneurs undertaking business abroad.

In Taiwan⁴, SMEs constitute the backbone of the economy. Unlike many other economies with conglomerates in the dominant position, Taiwan's manufacturing industry and foreign trade have traditionally been dependent on SMEs. More than 98% of Taiwan's one million registered enterprises are SMEs that employ nearly 80% of the work force and account for half of the island's aggregate export value. SMEs constitute a large portion of Taiwan's overseas investment as the island has emerged to become a major investor in China and Southeast Asia. The government has made five revisions to the *Small and Medium-sized Enterprise Guidance Regulations*, first stipulated in 1967. All changes were geared to creating a sounder environment for SMEs to increase productivity.

In South Korea⁵ the number of SMEs is approaching 2.7 million. SMEs are particularly active and well established in machinery and equipment production, metal cutting, textiles, apparel and wool products, food and

¹ SMEs are defined differently in different countries. See footnotes in the text for these definitions. In Hungary, for example, enterprises with fewer than 10 staff are defined as micro-enterprises, those employing fewer than 50 are considered small, while those employing fewer than 250 are classified as medium-sized.

² In addition, there are 265,500 individual farms, as well as 2.5 million family plots that sell their products on the market. Their combined share of national agricultural output is estimated at 20%. At the same time, an estimated 5 million people are self-employed. A significant share of small business activity (estimated at 30% to 50%) belongs to the "shadow" economy.

³ In China, for example, small enterprises are those with 50 - 100 employees, while for medium-sized enterprises this range is 101 - 500 employees. In Hong Kong, SMEs are defined as those with 100 employees or fewer in manufacturing and 50 employees or fewer for non-manufacturing activities.

⁴ In Taiwan, in the mining, quarrying, manufacturing and construction industries, the number of employees in small enterprises is 200 or fewer (NT\$60 million or less of invested capital), while in the service sector and other areas the number of employees is 50 or fewer (NT\$80 million or less of sales volume).

beverages, and rubber and plastic goods production. In these sectors SMEs account for more than half of manufacturing output and two-fifths of exports. The government intends to strengthen the competitiveness of SMEs, and promote start-ups, automation and computerization, relying in part on SMEs.

In all these economies, support for SMEs on the part of governments is considered to be among the most important economic and political goals. Indeed, governments that are dealing with economic transition need to assist potential entrepreneurs by complementing markets and encouraging the creation of SMEs, with the aim of promoting growth, employment, overall competitiveness and economic vitality.

Small enterprises in Russia

The total number of small enterprises (SEs)⁶ in Russia registered in official statistics is close to 900,000. About 40% of all SEs are concentrated in Moscow and its vicinity, 10% in St Petersburg and the surrounding region and about 3% each in Krasnodarskiy Krai, and Rostovskaya and Novosibirskaya oblasts. These enterprises are predominantly concentrated in the fields of trade, the restaurant and catering business, and the service sector.⁷

The share of small enterprises in industrial output is estimated at 5-6%, but is higher in certain industries, including machine-building and metal-cutting (7%),

logging, timber processing and pulp-and-paper manufacturing (8-10%), food processing (9-12%) and light manufacturing (9-11%).

It seems that in 2002, the overall dynamics related to small enterprises improved somewhat compared with 2001 (Table 1).

In 1996-2001, the number of small companies in industry decreased by 7,000 (5.5%), and by 16,000 (13%) in the construction sector, while the banking, finance and insurance sectors lost half of all SEs (4,200 small enterprises). By 2001, the total number of registered small enterprises was 875,500 with the total number of jobs they supported estimated at 7.6 million, including 6.6 million core staff.

As of January 1, 2002, the number of SEs decreased to 843,000, but rebounded again in April, when their total number reached 875,000 and employment increased by almost 6% compared with the first quarter of 2001, to a total of 7.5 million. The combined output reached 216 billion rubles in the first quarter.

Small enterprises' share of industrial output is estimated at 4%. Their combined assets are estimated at about US\$11.5 billion (2% of the national total). Small enterprises support about 13% of employment. Their share of retail trade is close to 26%, while in wholesale trade it is above 50%. In 2000, small enterprises in the construction sector were involved in the construction of 4,000 new

Table 1 Small enterprises in Russia by sector, 2001

| | Number (as April 1, 2002) | | Employees '000 | Output | |
|-------------------------------------|------------------------------|------|-------------------|----------------|------|
| | '000 | % | | Billion rubles | % |
| Industry | 125.1 | 14.8 | 1,529 | 214.9 | 25.2 |
| Construction | 121.9 | 14.5 | 1,545 | 220.4 | 25.8 |
| Agriculture | 13.4 | 1.6 | 160 | 8.5 | 1.0 |
| Transport | 18.8 | 2.2 | 231 | 28.1 | 3.3 |
| Trade and catering | 388.1 | 46.0 | 2,554 | 198.0 | 23.2 |
| Wholesale trade (industrial goods) | 15.9 | 1.9 | 133 | 19.1 | 2.2 |
| Commerce | 34.7 | 4.1 | 232 | 23.7 | 2.8 |
| Health, fitness and social services | 17.4 | 2.1 | 132 | 8.0 | 0.9 |
| Science and services | 28.5 | 3.4 | 177 | 33.0 | 3.9 |
| Other | 79.2 | 9.4 | 743 | 100.2 | 11.7 |
| Total for Russia | 843.0 | 100 | 7,436 | 853.9 | 100 |

Source: State Statistical Committee of the Russian Federation (Goscomstat)

⁵ In South Korea, SMEs are defined as 300 employees or fewer in manufacturing (20-80 billion Won of capital assets), 300 employees or fewer in mining and transportation, 200 employees or fewer in construction, and 20 employees or fewer in the commerce and service sector.

⁶ Before 2000, the State Statistical Committee of the Russian Federation provided data only for small-sized enterprises registered as legal entities. Individual entrepreneurs and small enterprises without judicial status were left out, despite the fact that there is almost no difference between these two categories. As a result, the total number of small enterprises has been grossly underestimated.

⁷ In 1991-1996, the category of small enterprises in the industrial and construction sectors included entities with fewer than 200 employees, with up to 100 employees in the fields of science and R&D, up to 15 employees in trade, catering and services, and up to 50 employees in all other non-production activities.

From 1996, after the legislation on state support for small-scale entrepreneurship was enacted, the size of small enterprises was reduced to 100 employees (industry, construction and transport), while in agriculture and science and technology the limit was set at 60 employees. In wholesale trade the maximum size became 60 employees, while in retail trade and services the limit was set at 30 employees. In 2002, a new definition was introduced—a maximum annual turnover of US\$500,000 compared with US\$1 million in the latest definition. On the other hand, Russia's official statistics still lack a definition for medium-sized enterprises, making international comparisons difficult and domestic accounting complicated

buildings with a total floor space of 2.1 million square meters (5% of the national total), including 73% of new floor space in residential houses.

The qualitative impact of SEs on the Russian economy is particularly significant. The labor productivity of small enterprises in the retail trade is almost double the average level, while in industry the range is between a factor of 1.2 and 6 in favor of small businesses. The output per unit of the cost of fixed assets compared with the average level is 220% in industry, 190% in construction and 150% in retail trade.

The phenomenon of higher than average efficiency can be explained by higher rates of depreciation of fixed assets (20% for SEs compared with 5% for medium and large companies) and a much higher suspension (bankruptcy) rate (8% for SEs compared with 1% for all others). Also, the total cost of SEs' fixed assets increased in 1996-2001 by 16% compared with only 1% for medium and large enterprises. SEs' investment in renovated and new capital stock reached almost US\$2 billion (4.6% of the national total). Almost 60% of this amount was allocated for new production equipment and machinery (the average for Russia was 36%). Small enterprises allocated about one-quarter of their total investment in non-production assets such as buildings and other infrastructure, compared with a national average of 44%. Finally, more than 30% of investment by small enterprises is concentrated in industry, 21% in construction and 18% in the trade sector.

Simplified tax system

For about a decade, Russian SMEs faced quite an unfavorable policy and regulatory environment. The registration and licensing procedures grew more complicated. The legislation regarding SEs adopted on December 29, 1995 in order to simplify the system of SE taxation did not retain a clause on separate accounting for the "incoming" value-added tax (VAT) in the cost of their products, affecting competitiveness and creating disincentives for customers. This law also replaced profit tax with gross income tax. Under the law, individual entrepreneurs—unlike organizations—had to pay VAT.

On July 1, 2002, the Lower House of the Russian Parliament enacted legislation with the aim of supporting small enterprises by modifying and reportedly simplifying tax rules. The comprehensive social tax, property tax and sales taxes have been abolished, while payments made to the Pension Fund were made tax deductible.

Switching over to this system is voluntary, but if a company decides to do so, it should have fewer than 100 employees on average and annual earnings should be a maximum of US\$500,000. In addition, no other company or organization should control more than 25% of its assets and depreciated capital stock must not exceed US\$3.3 million.⁸ Small enterprises can choose whether to pay 6% tax from gross proceeds or a 15% profit tax. Moreover, a new 15% rate for imputed profit (income⁹) tax was

introduced and has been brought under federal control, preventing regional authorities from raising it.

Immediately after the legislation was adopted, Evgeniy Primakov, President of the Chamber of Commerce and Industry and former Prime Minister, criticized the new law, appealing to the Chairman of the Upper House. In his opinion, the amendments made to the tax regime under this new law would worsen conditions for entrepreneurs by raising the imputed tax rate, abolishing the patent system for individual entrepreneurs and complicating bookkeeping.

What is worse is that the new system is not applicable to SEs in the real sector. Under the new law, VAT can be waived, but only if a given company sells its products to final customers. These new regulations could benefit micro-businesses in the retail and service sectors, making it difficult for other small companies with "transit VAT" to expand production and sales, preventing cooperative relations particularly important in manufacturing sector. Venture companies that could promote the introduction of new technologies and boost international competitiveness are also ineligible for tax concessions. In short, the simplified system makes the enterprises that use it "unwelcome partners" for those companies who purchase from them, unless supplying SEs are willing to reduce their prices by 20% (VAT rate).

More generally, entrepreneurs, whom the Chamber of Commerce and Industry is representing, are skeptical not only about new regulations, but also the overall position of authorities with regard to small businesses. The hope is that legislation on small and medium-sized enterprises will keep improving, involving larger segments of economic activity and a greater number of firms from a variety of new fields.

Trends in provinces

A solution for both new and already established SEs could be found in special support funds, both national and regional. However, regional support funds lack resources both in terms of direct assistance and credit guarantees extended to commercial banks. Federal and regional authorities are expected to enhance their capacity to serve as supporting and credit risk-absorbing institutions, but also lack sufficient financial resources and adequate institutional and regulatory infrastructure.

Yet another way for authorities to assist SEs is to promote their involvement in government procurement programs. But again, Russian authorities have yet to use this tool to change the current situation in which large, well-established enterprises are almost exclusively awarded state orders. For example, in the first nine months of 2000, more than 88,000 SMEs filed applications for tenders to supply goods to federal, regional and local agencies, but contracts (about 16% of the total number of contracts) were granted to less than 40,000 entities. Moreover, fewer than 8,000 contracts were granted at the federal level and only 7,300 at the regional level. The total value of all contracts granted, including 24,000 of them extended by

⁸ The simplified taxation system is not applicable to gambling, the mining of rare metals and stones, Production Sharing Contract schemes, banking and insurance, non-state pension and investment funds, stock-broking agencies or private notarizing activities.

⁹ Income is calculated as gross revenue minus expenses.

municipalities, was as low as 4% of the value of procurement programs, or about US\$310 million, with only about US\$20 million coming from federal coffers and another US\$60 million from the executive authorities of the 89 provinces.

According to the Russian Center for Economic Development (RCED), federal legislation on SEs leaves regional authorities considerable freedom to introduce measures and regulations that support small business development within their regions. In addition, the provinces are free to specify regional priorities for SE development in specific sectors, in addition to those determined at the federal level.¹⁰ Moreover, provinces were granted the right to reduce taxes in the parts attributed to regional and local budgets, as well as to enact legislation on the preferential tax treatment of SE support funds, investment and leasing companies, and credit and insurance businesses that provide services to SEs. Regional authorities were also permitted to allocate quotas for SEs in government procurement programs.

The right to introduce laws in support of small businesses has yet to be utilized fully. In Magadanskaya Oblast, as well as many other provinces, in the absence of regional legislation, federal law regulates SEs' activities. Some provinces "copy" federal regulations in their own regional legislation on SEs.

Surprisingly, out of the 72 provinces surveyed by RCED, only 11 had clearly stated provisions on preferential profit tax treatment for SMEs. Seven of them, including Primorskiy Krai, and Sakhalinskaya and Amurskaya oblasts specified "priority sectors" for SEs' activities, other than those defined by federal law. In addition, preferential rates for property tax were introduced in Chitinskaya and Amurskaya oblasts, as well as in Primorskiy Krai. Primorskiy Krai and Sakhalinskaya Oblast enacted laws determining the share of state procurement programs (20%

and 15% correspondingly) to be allocated to small businesses, while a similar provision enacted by Chitinskaya Oblast does not define the share of SEs numerically.

It is worth noting that the Far Eastern economic region seems to lag behind other regions in terms of the total number of SEs and their employment figures (Table 2).

Furthermore, the Far Eastern regions' relative value is low in terms of output and capital investment. On the other hand, the share of small enterprises in regional GDP is reportedly higher than the national average; in this respect the Far Eastern region occupied the third position after the Northwestern and Central federal districts in 1999.

In 1997-2000, the number of employees of SEs was rising in Primorskiy Krai and Evreiskaya Oblast, while somewhat stable in Khabarovskiy Krai, but all other provinces registered considerable decreases in the number of jobs generated by SEs.

During the same period, the number of SEs in Primorskiy Krai increased from 10,400 to 16,100 enterprises, while the rise in Evreiskaya Oblast was from 3,300 to 4,800 enterprises. All other provinces registered a decline in the number of SEs, including Khabarovskiy Krai, which dropped from 9,100 to 8,300 enterprises.

The bottom line is that only a few provinces offer concessions and extend support to small enterprises that operate on their territories. On the other hand, of the 79 provinces undergoing the region-by-region review of SE performance, Kamchatskaya and Magadanskaya oblasts joined Moscow and St. Petersburg in the same leading group of only four provinces classed as administrative entities with good potential for SE development. Sakhalinskaya and Irkutskaya oblasts belong to the second group, consisting of five provinces with small enterprises affected by the 1998 financial crisis, but retaining the capacity for SE development. Primorskiy and

Table 2 Small enterprises in Far Eastern Russia, 2001

| | Number | | Employees | | Output | | Investment | |
|----------------------|--------|-----|-----------|-----|----------------|-----|----------------|-----|
| | '000 | % | '000 | % | Billion rubles | % | Billion rubles | % |
| Russia | 843.0 | 100 | 7,435.8 | 100 | 852.7 | 100 | 43.02 | 100 |
| Far Eastern region | 40.4 | 4.8 | 313.6 | 4.2 | 50.2 | 5.9 | 1.04 | 2.4 |
| Yakutia | 2.3 | 0.3 | 21.3 | 0.3 | 5.5 | 0.6 | 0.07 | 0.2 |
| Primorskiy Krai | 16.1 | 1.9 | 104.7 | 1.4 | 11.3 | 1.3 | 0.30 | 0.7 |
| Khabarovskiy Krai | 8.3 | 1.0 | 88.9 | 1.2 | 13.4 | 1.6 | 0.13 | 0.3 |
| Amurskaya Oblast | 3.8 | 0.5 | 24.2 | 0.3 | 2.7 | 0.3 | 0.07 | 0.2 |
| Kamchatskaya Oblast | 1.6 | 0.2 | 15.9 | 0.2 | 5.0 | 0.6 | 0.16 | 0.4 |
| Magadanskaya Oblast | 2.9 | 0.3 | 20.6 | 0.3 | 5.4 | 0.6 | 0.12 | 0.3 |
| Sakhalinskaya Oblast | 4.9 | 0.6 | 34.6 | 0.5 | 6.2 | 0.7 | 0.18 | 0.4 |
| Evreiskaya Oblast | 0.6 | 0.1 | 2.4 | 0.0 | 0.3 | 0.0 | 0.01 | 0.0 |
| Chukotskiy Okrug | 0.1 | 0.0 | 1.0 | 0.0 | 0.3 | 0.0 | 0.05 | 0.0 |

Source: Goscomstat

¹⁰ In 1993, among the priority areas for SEs support announced by the government were agricultural products and their processing, foodstuffs and manufacturing products, consumer goods, medicine and medical equipment production, construction of housing, as well as buildings for commercial and public needs, and some services and innovative activities. In 1999, the government reiterated that the priority areas eligible for state support for SEs included innovative activities in machine-building, metal-cutting, microbiology, biotechnology, construction and manufacturing of construction materials, food processing, storage, processing and packaging of agricultural products, and consumer goods manufacturing.

Khabarovskiy krajs were included in the third group, of 31 provinces with a moderate level of small enterprise development, but some negative trends in the sector. Finally, Amurskaya and Chitinskaya oblasts, as well as Yakutia and Buriatia were included in the fourth and largest group, of outsiders with a low level of SE development.

Problems and expectations

Russia and the majority of its regions lack an effective and comprehensive support framework for promoting small enterprise development and entrepreneurship. Commercial banks are not interested in providing funding for SEs. There is no legal framework that regulates their mutual credit and insurance efforts. Federal and regional support agencies lack the resources and capacity to develop risk-sharing schemes that could support commercial banks in providing loans to small enterprises.

Representatives of small business entities demand that a stable, relaxed taxation system be put in place for them for a period of at least five years. They collectively complain about the lack of clarity and consistency in requirements for bookkeeping and accounting standards, asking for a simplified system for paperwork. They propose to allow SEs to be included in the "VAT accounting chain" to support local market development, foster cooperation with larger companies and promote inter-regional linkages. SEs are interested in accessing state-owned "business incubator" facilities. They also propose to develop leasing infrastructure designed for SEs, introducing a preferential tax regime for leasing companies that deal with small businesses.

Entrepreneurs have no guaranteed access to information concerning federal or municipal property that goes on lease, or could be sold, or privatized. The procedures necessary for such transactions are complicated and take a long time. There are no long-term lease conditions (transparent and stable) in place. With only a few exceptions, state procurement mechanisms do not account for the needs and potential of SEs in distributing contracts. This happens at both the federal and provincial level, despite the legal obligation to contract out 15% of state orders to small enterprises.

Entrepreneurs' strongest complaint addressed to the government is the lack of credit support, including micro-credit. They propose to put together an institutional framework for promoting micro financing and enabling legal regulations, ensuring public-private partnership in investment risk sharing. Entrepreneurs are also asking for preferential treatment in accessing low interest rate leasing of available production facilities and idle equipment at state-owned facilities and access to regional and local databases on related opportunities.

Indeed, access to affordable credit is the most serious problem that SEs in Russia are facing. Many banks and investment funds claim that they support small companies, but in reality they do not allocate any significant resources for their financing. For example, over the last two years, 15 Moscow offices of Russia's Savings Bank (Sberbank)

provided more than 2,000 credits to SEs, including about 1,600 micro-credits of US\$30,000 with a maturity period of up to one year. These micro-credits are mostly suitable for the replenishment of working capital. Two-year maturity investment credits are also available, but the amount is limited to US\$125,000. The good news is that 80% of applicants were approved for credit.

However, for these purposes Sberbank—the largest Russian bank—is mostly using funding provided by the European Bank for Reconstruction and Development (EBRD), which allocated about US\$150 million for a special support program, while the same amount was obtained from the G7 members and Switzerland. The program is named the Russia Small Business Fund (RSBF). It was established in 1994 and extended to 2010 with a recommendation to increase the EBRD share to US\$450 million.

The EBRD considers the RSBF to be a highly successful and profitable program, partly because of the fact that the interest earned from projects in Russia is about twice as high as that earned from similar projects in Europe. To expand its presence, the EBRD established the KMB-Bank, which is serving as the main agent in RSBF financing activities. In 2000, the EBRD decided to increase its capital share in the KMB-Bank, broadening its ownership to 35% and doubling its lending portfolio to US\$60 million.¹¹

External sources of assistance and know-how

All this is greatly indicative of a situation in which support for SEs in Russia could be viable commercially, not only for multilateral development banks such as the EBRD, but also domestic banks and investment funds. However, Russian banks provide SE financing on a very limited basis. Moreover, both the EBRD-supported activities and domestic commercial banks require applicant enterprises to provide collateral, using not only the enterprise's assets, but also personal property assets. This makes it almost impossible for venture entrepreneurs to get funding for start-up projects.

Yet another option for SE support could be the leasing of equipment. In advanced market economies, about 30% of capital investment is made through leasing financing schemes. In contrast, in Russia, the share of leasing financing is negligible. For example, the EBRD established a US\$12 million leasing framework facility in Russia to finance leases of Caterpillar equipment on a risk-sharing basis. This would benefit both the vendors and the ultimate lessees in particular, as they would have access to modern equipment and the means to finance it.

In addition, the EBRD proposes to lend about US\$10 million to Delta Leasing, which will make financial leases available to small enterprises in Russia. Delta Leasing is a wholly owned leasing subsidiary of the US-Russia Investment Fund (TUSRIF). The project supports Delta Leasing's efforts to increase its lease portfolio of small clients in 17 cities in Russia.

On the other hand, the U.S. government is taking quite an active stance on entrepreneurship promotion in Russia.

¹¹ The non-profit George Soros Economic Development Fund (SEDF) also has a 35% stake in the RSBF.

USAID (U.S. Agency for International Development) assisted in drafting regulations on leasing and consumer cooperatives. USAID has helped channel resources by creating a network of non-bank financial institutions. The number and value of USAID-supported microfinance loans doubled in 2001 to 32,000 loans worth \$34 million. In the same year, a program was launched to create a national center to support non-bank financial institutions through credit and training.

A network of business support centers managed by the University of Alaska/Anchorage's American-Russian Center and the Russian Academy of Management and the Market provided training and consulting services. In addition, USAID proposed to exempt interest payments on loans by non-bank financial institutions from VAT, giving micro-finance institutions the tax advantages that banks receive. Finally, six professional firms supported by USAID offer fee-based courses as part of their services.

The organization also provides funding for the Sakhalin Island American Business Center's advisory services to foster foreign investment in Sakhalin's SEs. It plans to expand its business support institutions initiative to the Far Eastern region.

Japan also pioneered economic and technical assistance to Russia, beginning in 1992. The Japanese government established the Regional Venture Fund (RVF) in 1994 in cooperation with the European Bank for Reconstruction and Development (EBRD), to develop small and medium-sized private businesses in the Russian Far East and Eastern Siberia. In Moscow, the Japan Center was established, followed by similar centers in Khabarovsk, Vladivostok and Yuzhno-Sakhalinsk.

Conclusions

The freedom to be an entrepreneur in Russia is guaranteed by the Constitution, but threatened by the administrative system and government bureaucracy. It is still early days and difficult to judge whether the administrative pressure on Russian SEs is receding. Reportedly, more than half of SEs in Russia are in the "shadows" in terms of compliance with official regulations, including tax payments. On the other hand, there is no clear commitment on the part of authorities to allowing this new sector to grow without constraints.

As recent amendments to the tax law demonstrate, the government wants to keep tax rates higher and maximum earnings lower to reduce the number of SEs eligible for tax benefits. The number of the various inspections is decreasing, but recently introduced regulations on the frequency and nature of such inspections exempted about 15 agencies out of the total of about 40 that are dealing with small businesses.

According to Evgeniy Primakov, the Russian

administrative system needs to undergo revolutionary change in terms of dealing with and supporting SEs. On the other hand, the 2001 and the 2002 federal budgets allocated less than US\$1 million for support programs aimed at small businesses. The Federal Fund for Small Enterprise Support lacks financial resources, although it is authorized by the government to raise money from sources such as the EBRD. Therefore, the federal government is avoiding taking responsibility for alleviating risk in this important segment of the Russian economy.

The external sources of funding for supporting SEs, made available by the G7 through the EBRD, or similar programs supported by the United States and Japan on a bilateral basis, are very important, but are no substitute for an integrated and consistent strategy for small business development and the promotion of entrepreneurship. The new Russian elite, including the government and lawmakers, should put together this strategy itself, if it aspires to build a competitive, advanced and economically democratic society.

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