

Russia: the end of a time of troubles?



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Four major problems: Trust Decision Making Government and Business Legal System Trust Throughout the case, one theme that seems to reappear is the issue of trust. Without trust in the federal government, people take it upon themselves to do what is necessary to survive. They no longer trust the government to provide a safe environment for them to live.

This issue might start small but gradually affect areas such as the business transaction, the monetary system, the tax system, and ultimately the sovereignty of the government. Distrust in the government led to an increase in bartering. This leads to two major problems – the inability of firms to pay wages and the inability of the government to collect taxes.

Additionally, the weak monetary policy led to many quasi-monies to appear in Russia, making it difficult for the government to enact any monetary policy. Another significant problem due to the lack of trust in the federal government is its inability to impose its will on local or regional authorities.

The federal government was unable to collect taxes from local and regional authorities. Some regions violated federal law, while others claimed that regional laws took priority over federal law. Some went as far as claiming the right to control its own natural resources and conduct foreign trade. On a more personal level, Putin stated that individuals could not trust in the stability of the businesses, because they could not rely on the law or the honesty of officials. This leads to dissatisfaction and the unwillingness to pay taxes. The inability to collect taxes leads officials to take bribes, and this is a never ending cycle.

Solution – Reorganize federal system to concentrate strong central government A strong central government is needed to impose change in Russia. It will show people that the government still has the power to act for the greater good of the people leading to a building of public trust. Without it, the many regional and local authorities will continue to chip away at its power, leaving the central government unable to act. Pros – A strong central government acts as a guide to align the goals of the nation at all levels.

A strong government can impose its will on local authorities and force them to align their goals with that of the federal government. This process of aligning goals will help clarify the inconsistencies that exist between federal and local laws and give the federal government the power to implement any changes it believes to be necessary. This will enable the government once more to collect taxes and bring in much needed funds. A strong government can also enact a monetary policy, and remove corruption by monitoring judges and local authorities..

Cons – Giving the federal government power can lead back to communism or dictatorship. The new government can impose its will on anyone that it believes is not in line with its objectives. This can lead to an abuse of power.

Alternative – Allows Russia to continue its course Russia had a lot of western advisors helping it during the transition phase, but ultimately they all failed. Forcing these changes through a strong government might make it worse. The best course maybe to allow Russia to find its own course.

This might take longer but the saying goes “ slow and steady wins the race. ”

Pros – Russia will learn how best to operate through its own mistakes. The

United States took over 200 years to get to where we are now to become the most powerful economy in the world. Cons – This process might not work, and Russia could break down in to smaller independent states before they can find a solution to this problem. Government and Business The problem of business and government could not be more evident than in the case of the “ rise of the Oligarchs. ” By 1995, the Russia’s budget was in deep trouble, with expenditures rising faster than revenues.

Yeltsin and the government negotiated a deal with a few powerful private banks to auction shares of the government’s highly prized mineral and oil asset for a time frame of one year. The catch was that if the government chooses not to repay back this loan at the end of one year, then the government would forfeit control of these assets. In order to ensure that obtain these shares for as low a price as possible, the banks made an agreement that each would have their own share of the pie and that outside bids were magically void. The second part of their plan was to ensure that the government did not repay their loans, thus transferring ownership of the strategic resources. Yeltsin was an underdog for the upcoming elections, and the oligarchs felt that a new president might now honor the pledge auctions.

The Oligarchs assembled formed a coalition with the goal to re-elect Yeltsin back to the office. In the end, they were successful and after the election, Yeltsin announced that the government would not repay the loans. The problem in the relationship between the Russian government and its dealings with the Oligarchs deals with business ethics. Where should the line be drawn between doing business ethically and doing business unethically.

The problem here is that the oligarchs are looking out for their best interest, but that interest may not be best for Russia or the public.

The paradox of government and business is that if government interferes too much, then it will slow down innovation and reduce efficiency, but if the government remains passive, then there is no one to protect the public's interest, or to regulate the economic in such a way that promote equality and free trade. Solution – Create new rules and regulation and give amnesty for past events The government needs to create laws and enforce these laws so that business will not be able to wield so much power. There will always be a relationship between business and government, but when business becomes government, problems will arise. The new laws should be strictly enforced to prevent Oligarchs from gaining too much political influence. Also the government should forgive events that past. This will foster a focus that looks toward the future.

Pros – Form new relationship with business, and have a clean good start with business to build cooperation and foster a competitive environment. Cons – Some people might feel cheated due to Oligarchs theft of power.

Government gave up valuable resources to Oligarchs for almost nothing, and some of those resources are vital to the health of the government.

Alternative – Enforce present laws and punish those who broke the laws.

The oligarchs stole and committed lots illegal acts to obtain power. The government should redistribute this power as originally intended. Pros – Monopolies that were formed by Oligarchs are now distributed fairly and

allows for competition and increase efficiency in operations. The government will re-acquire the vital assets that the Oligarchs won through illegal acts.

Cons – Relation with some of the richest men in Russia will be fierce and demoralizing for the economy. Many smaller firms will be worry that the government is seeking to punish those committed illegal acts in the past. During privatization, evading taxes and other illegal acts were the norm, and so this policy will lead to an uncooperative relationship. Legal System Reform & Business Law Issue Before 1991 the Russian Federation never existed. After Yeltsin took control of the parliament, the government tried to work on the legal system reform transforming Russia from one extreme “ socialism” to the other extreme “ capitalism”. Yeltsin’s plan was to totally eliminate the old Soviet economic and legal system and replace it with a new one.

He was eager not to set a Russian precedent for re-centralizing federal authority within the Soviet Union, and told the leaders of Russia’s regions to “ take as much sovereignty as you can swallow”. This lead to a problem where between 25 and 35 percent of regional legislation no longer conformed to federal laws. Tax collection problem was popular as well. Russia’s tax laws taxed gross revenues rather than profits and the business was subject to different taxes that in some case added up to 110 percent of revenue. Russian court system was not effective, even though western advisors aided in the government’s attempts to place the economy on a sound legal foundation. Russia lacked an independent judiciary and also lacked trained judges that could properly interpret these laws in a Russian context.

In addition, the courts were unable to enforce these ruling due to the government's inability to pay regional judges or properly maintain the courts. After centuries of corruption and arbitrariness, Russian society no one trusted the law or the legal system. All these problems hindered the development of the Russian Federation. If these were not able to solved, Russia could never be what Yeltsin hoped.

Solution – Totally destroy the old system and build up a brand new one By destroying the old system, we can create a new one with one that emphasis a decentralized federal authority but balances federal and region power. The new government should model their tax laws after those of European countries and with a focus on profit instead of revenue. There is also a need to establish an independent judiciary system and train judges to interpret these new laws in a Russian context. Pros – New tax laws are already proven to be effective in developed countries with a little modification, they should work well in the Russian environment.

In the long term it will be beneficial to Russia and expedite the reform progress. This will save time and money. Cons – There are already opposition to western advisors and their ideas and this new system cannot be guaranteed to work. There is also the problem that Russians have become accustomed to the old system and it will not be easy for them to adopt this new system with its potential side effects. Even if the new system is implemented properly, political and economic pressure might render the system to fail.

Alternative – Improve the current system and slowly implement it
Centralizing the authority between the federal and the regions. Tax businesses based on gross margins instead of revenue as it is a better indicator of business success. Build up trust between the law and legal system and the society
Pros – The public already understands the laws and can get digest the improved system gradually. The will lead to a better understanding of the acceptable behaviors.
Cons – The progress will be a lot slower and society might try to hold on to old values and revert to old ways if it is not guided properly.

Decision Making/Strategy This Soviet economic system, based on resource mobilization, started its decline from the 1960 and never recovered. The Soviet government knew that change was necessary to save USSR, and in 1985 Gorbachev's attempt to fix it, but was unsuccessful. In 1991, Yeltsin gave it a second attempted by attempting to destroy the old system and implement a new system. Yeltsin believed that he could change Russia within a year and set in motion an extremely ambitious plan. He entrusted the reform process to a group of young professional economists, who for all their knowledge were considered to be inexperienced.

In making this decision, Yeltsin did not factor in the Russia's political environment, which seriously hinder any progress made the young professionals and causes more problems for the future. The two problems the group encountered was its attempt to conduct a tight monetary policy to control inflation, and its attempt to at privatization. The entire process was conducted too rapidly for the common Russian to fully understand what was happening. In addition, there were loopholes and opposition to each progress

that should have been eliminated or minimized before the actual implementation of the process. Yeltsin deal with the Oligarch further complicated the situation, as it gave the oligarchs enormous political power over the soviet president, and cause the privatization process to largely deviated from its original goal. In addition, Yeltsin did not address the issues of demonetization, tax and the federal authority.

Solution – Make a long term plan and focus on a selected few problems at any one time. The Soviet government should plan for the long term if they want success for Russia. They need to form committees, such as we have here in the US. These committees will debates the benefits and consequences of each action before voting. This process might be slower, but will make sure as much information is known before proceeding.

The consequences of looking for immediate success are that it might require sacrificing resources that are needed in the long term. An example is when Yeltsin signed over Russia's most valuable assets to the Oligarchs. This gave the government money on the short run, but ultimately it did not resolve the problem. If Yeltsin kept those assets, they would help the government more over the term of its life. Pros – Long-term goals can help guide the government more successfully toward a better future.

In addition, the government might try to limit its resources on just a few problems instead of trying to solve all problems. This allows them to focus and more fully understand each problem. Cons – Short term goals build momentum, and without this momentum, Russia might not be able to make any initial progress. Covering all problems might also lessen each problem

until it reaches a manageable state, where Alternative – Try to fix as many problems as possible in the short run. The government should try to fix as many of the problems as soon as possible.

Even if they can't solve all problems, at the very least, it will at least bring the problems out in the open, so people are aware of it. Pros – The government can cover more in a short time. The public will know the government is doing all it can to fix all the problems. Cons – Problems might be addressed the problems but the real reason for the problem might be hidden. Without deeper understanding of the real problem, any and all decisions made can still be wrong. Conclusion The new government under Putin, not only has to reform Russia to become a capitalism country but also has to solve the problems which were caused while Yeltsin was in position.

The new government should make a long term plan to solve those problems step by step. They have to 1)Form a powerful and stable central government that people can trust to get things done. This governments needs to impose its authority in order to create an effective monetary policy, and implement a new tax system. 2)Change the laws on its tax system to reflect relevant information, and collaboration is needed between local and federal authorities. Currently, the tax system focuses on revenue, which is a misleading indicator of success, and cost can vary from industry to industry.

The new system needs to focus on gross margin. In addition, the tax systems need to clarify the distinction between local and federal taxes, and reduce confusion by eliminating any duplication or similarities in the old legal system.)Have a long term strategy mapped out and have the government

form decision making committee that can debate the points in question, rather than just have one person decide. This creates a form of checks and balance system necessary to eliminate personal agendas that might interfere with national goals. 4)And last is to forgive past crimes and start a new positive relationship with business.

This way, Russia can focus on the future instead of trying to correct the past. Focusing on past mistakes will only deteriorate the relationship and foster distrust.