Volume Title: Money, Financial Flows, and Credit in the Soviet Union

Volume Author/Editor: George Garvy

Volume Publisher: NBER

Volume ISBN: 0-884-10475-3

Volume URL: http://www.nber.org/books/garv77-1

Publication Date: 1977

Chapter Title: Payments and Financial Flows

Chapter Author: George Garvy

Chapter URL: http://www.nber.org/chapters/c4157

Chapter pages in book: (p. 76 - 105)

5

Payments and Financial Flows

The Separation of Payments Circuits

IN the Soviet Union, household money (currency) is differentiated from enterprise money (bank deposits), and household banking from enterprise banking. All payments are separated into these two different circuits, which correspond to the separate markets for consumer goods and producers' goods.[1] Their focal point is the State Bank, whose staff (particularly at the local branch level) devotes much of its time to their management. A further institutional separation of the flow of payments under the standard system was the assignment to the State Bank of all payments relating to current production, while the accumulation and disbursement of all funds relating to fixed capital formation in the state-owned sector went on the books of the Investment Bank.

The difference between the two kinds of money is both physical and functional. For the population at large, currency alone serves as medium of payment, except for a relatively small amount of payments via savings accounts. By contrast, all payments among enterprises, economic and civic organizations, and government agencies (except for petty cash disbursements) involve deposit transfers on the books of the banking system. Currency and deposit money are not interchangeable. Deposits are exchanged for currency almost exclusively through payroll withdrawals.

Separation of payments flows, in the Soviet Union as well as in other socialist countries, is a basic mechanism for avoiding excess

[1]See Chapter 4, "The Investment Bank."

demand. A necessary condition for macroeconomic equilibrium in the household sector is that the amount of income paid out equal the value (at set prices) of all goods and services available for household consumption plus voluntary household savings. The total bill for consumer goods is determined by the combined effect of output plans, factory prices, and the turnover tax applicable to each product. Turnover taxes are differentiated by product, and are designed to raise prices for consumer items sufficiently to prevent effective demand from exceeding available supplies.

Once the major macroeconomic decisions are made concerning the apportionment of the social product between private consumption, on the one hand, and collective consumption, investment, and the cost of general administration, on the other, the share of net output earmarked for the population determines the size of the wage fund (after allowing for other sources of income, such as stipends and pensions, as well as for the small amount of personal taxes paid by the population). To achieve the goal of matching these two magnitudes, wage rates and total payroll costs of individual enterprises are strictly controlled.

Separation of payments into two circuits facilitates financial planning as well as central accounting control over the flow of resources within the socialized sector and prevents leakages of goods and services from there into private consumption. It also facilitates detection of bottlenecks and shortfalls in the execution of economic plans. Finally, it gives consumers some choice within the range of goods and services offered by planners (which may guide future production), while preserving the planning authorities' control over inputs and outputs in the enterprise sector. After the abolition of wartime rationing, which was made possible in 1947 by the increased flow of consumer goods, the range of available options widened and household money gradually acquired a higher degree of "moneyness." Options have been limited by the planners' choice of the "assortment" of goods produced and by the lack of a workable mechanism to feed back consumer preferences into production planning. While availability of options does not guarantee rational choices, the limited nature of these options prevents the system from developing procedures for evaluating preferences and demand elasticities.

THE CURRENCY CIRCUIT

Wages and other monetary income are paid in currency, except for a relatively small amount paid directly into savings accounts. Consequently, virtually all consumer expenditures are also made in currency.

Through currency withdrawals, note liabilities are substituted on the books of the State Bank for liabilities to enterprises and to the Treasury: thus, creditor balances are reduced to only a fraction of loans. Indeed, because of cumulative currency withdrawals resulting from the continuous increase in aggregate loan volume, deposit balances of enterprises at the end of 1969 were equal to only about one-tenth of their aggregate loan balances.

Collectivized farmers now receive a very large part of their income in cash, but prior to 1953 payments in kind were prevalent. The remonetization of relations between the *kolkhozes* and the state, and the subsequent changeover of the members' remuneration from an annual distribution on the basis of work performed to periodic money payments, have increased the circulation of currency as well as its rate of turnover among the rural population. Members of collective farms and workers on state farms, as well as the small number of independent farmers still in existence, also receive currency through direct sales of crops and animal products from their privately farmed plots.

Consumer goods and services are obtained almost entirely from state-owned retail stores (the network of "cooperative stores" in villages is, de facto, state-operated).[2] As a result, currency normally returns to the State Bank after only one transaction—when currency paid out as wages is spent in retail stores and is redeposited by them—but some part changes hands within the population itself, with one group purchasing goods from another. In addition to the free-market sales of farm products, such transactions include sales by artisans and cooperative producers, sales of second-hand goods, and payments for services to domestics and other individuals (including moonlighters) and for various forms of illicit transactions. Of all these transactions, farm prod-

[2]Capital goods cannot be acquired by the population at large, but a limited amount of building materials has become available in recent years for repair purposes and new construction.

ucts purchased directly from the rural population are by far the most important. Farmers use the proceeds of their sales to the urban population to acquire goods and services from the socialized sector. As long as claims on the socialized sector are merely transferred from one group of the population to another, few problems arise for planners and controllers of currency flows, even though the resulting shifts in the structure of demand require adjustments in the bill of goods produced for the consumer sector.

The bulk of the demand for currency is met from the supply of currency returning to the monobank when individuals make retail purchases as service expenditures, pay income taxes, and add to their savings accounts. State-owned and cooperative retail stores or service establishments are required to make daily deposits of all currency receipts in excess of a stipulated amount of petty cash.

Prompt recovery of as large an amount of currency put into circulation as possible is one of the shibboleths of Soviet monetary management. Continuous efforts are made to prevent consumers from hoarding currency which might spill over into black market and other illicit activities and make possible sudden surges of spending that typically create shortages in retail stores. Much emphasis is placed on channeling the cash receipts of trade and service establishments into State Bank offices as promptly as possible and on minimizing the amount of till cash that such establishments, as well as industrial establishments, are permitted to hold. Any inflow of currency that results in vault cash holdings ("operational reserves") at a local bank office in excess of stipulated maximum levels is transferred to the centrally controlled "general reserves," from which notes and coins can be released only on specific orders from the head or regional offices of the State Bank. Conversely, elaborate precautions are taken to prevent issuance of currency to enterprises and government units except in strict conformity with the cash plan.

THE DEPOSIT TRANSFER CIRCUIT

The deposit transfer circuit ("noncash circuit," in Soviet terminology) encompasses all payments related to the production and disposition of the gross national income not paid out in currency to the population, as well as transactions relating to the extension and repayment of credit.[3] (Only payments up to a small specified amount—currently 100 rubles—may be made in currency.) Trade organizations are authorized, in strictly circumscribed situations, to make cash payments for certain direct purchases made locally, and state procurement agencies pay for their purchases from *kolkhozes* largely in currency. With those minor exceptions, only amounts needed for meeting payrolls can be converted into currency.

The deposit transfer mechanism is designed to place payments between economic units on a semi-automatic basis while assuring prompt fulfillment of all obligations to the state budget. A primary task of the banking system is to provide a smooth deposit transfer mechanism that will promptly return to every enterprise all working capital spent in producing the output delivered to the next link in the chain, and to provide credit for bridging any payment gaps.

Claims among socialist enterprises arising from production and distribution give rise only to settlements through deposit transfers between the accounts of the buyer and the seller, or through mutual offsetting of claims. Payments are made as goods move through production and distribution channels for purposes determined by the planners according to rigid schedules.

Goods must normally be paid for, in accordance with a fixed time schedule, shortly after documentary drafts (the main means of settlement) are received by the purchasers. One of the frequently criticized aspects of this procedure is that (particularly where shipments to distant points are involved) the buyer's account is sometimes debited before he has received and examined the shipment. Monthly or other periodic billing has not been used until recently; hence each individual transaction requires a separate payment to facilitate control.[4]

[3]The use of deposit transfers is obligatory for the socialized sector only. *Kolkhozes* are obliged to use them in their dealings with the budget, with state-owned enterprises, and with the credit system, and for all accounts related to capital formation which they must keep at the State Bank, but otherwise they may use currency and keep their cash assets either in currency or in savings accounts. Although great efforts are made to induce *kolkhozes* to bank their cash receipts, only 20 to 70 percent of such receipts, depending on the region, are actually deposited.

[4]The requirement that each freight bill be settled separately on receipt illustrates the

Also, for certain categories of transactions, specified payments instruments are prescribed, while in other cases the payer has a choice. But as a rule, the nature of the transaction and the location of the parties involved determine the way in which payment must be made. Whatever payment instrument is used, all types require documents establishing the purpose of the transaction.

A variety of techniques is employed in making interenterprise and other payments involving transfers of deposits, including arrangements for mutual offsets of claims. These techniques grow out of a continuous search for the best methods to combine optimal control with speed. Arrangements frequently are different for local and out-of-town payments.[5] The form and frequency of transfers have been changed from time to time by administrative action aimed at specific categories of transactions, types of payments, or industries.

The use of money as a tool of administrative control as well as a means of payment has ruled out widespread use of checks, as well as the development of a nationwide check-clearing system (as in the United States) or a centralized deposit transfer (giro) system (as in most countries of Western Europe). Instead, it has created a complex and cumbersome payment system in which documentary drafts and other payment orders are used in preference to checks and which requires processing a large volume of documents. In recent years, steps have been taken to automatize the payments mechanism, but progress has been slow, partly due to shortages in electronic equipment.

Even before the 1965 Reform, there was a growing tendency to widen the choice of available payments instruments and procedures and to let the enterprises involved agree directly on settlement procedures. However, in the Soviet Union even relatively

---

extreme to which the general principle is pushed. Delinquent payers are penalized for the benefit of the payee by a fee of 0.03 percent a day for the amounts past due (only 0.01 percent before the Reform). This fee is automatically collected by the bank and credited to the account of the payee.

[5]Clearing arrangements to offset counterclaims differ for local and out-of-town payments. On clearings and compensating arrangements, see Baskin and associates [10], Boguslavskiy [14], Gindin [178], Piletskiy [67], Shenger [74], Shvarts [77], and Taflya [83]. See also Mitel'man [194]. In the late sixties, about half of all payments were offset by various clearing arrangements (with only residual balances credited or debited), but this proportion declined between 1965 and 1970.

minor changes, which elsewhere would be made routinely by management on the advice of efficiency experts, are considered to be of such importance that they are frequently the subject of formal decisions by the Council of Ministers.

Delays in settling for goods occur mainly when consumer goods reaching retail outlets are selling slowly or not at all. This is the point in the deposit transfer circuit where the greatest "unplanned" use is made of short-term bank credit. It takes the form of an automatic (but not unlimited) extension of loans, either to the seller to bridge the settlement gap, or to the purchaser to enable him to make payment on the date due.

The volume of payments related to the production of goods is geared in large measure to the degree of vertical integration of industry. On the whole, the number of intermediate transactions is presumably smaller in the Soviet Union than in the nonsocialist industrial countries because raw materials and intermediate products reach manufacturers more directly and because final products pass through fewer stages of distribution before reaching ultimate purchasers. Also, no debits are created by payments related to trading in financial assets. On the other hand, the Soviet economy generates payment flows peculiar to it, such as those related to its budgetary system and reimbursements for various kinds of containers—returned to shippers. Deposit transfers in 1970 amounted to nearly 1½ trillion rubles, several times the value of GNP, just as bank debits in the United States are a multiple of the dollar value of GNP.

Financial Flows

In the Soviet economy, financial flows arise in the course of the central authorities' disposition of the social product (surplus value—in Marxian terminology, that part of the gross product that exceeds expenditures for labor, raw materials, and capital consumption) and from credit operations. In contrast to nonsocialist economies, flows related to investments never represent an exchange of money for financial assets through specialized institutions or instruments, but merely deposit transfers on the books of the State Bank and the Investment Bank.

Before the 1965 Reform, financial flows consisted essentially in one-track intermediation via the unified budget, which centralized all social income and redistributed it among the various levels of government and the economy. Financial flows also included loans and their repayment. The size, direction, and form of financial flows were determined by inventory norms, the allocation of "funded" commodities, the investment financing mechanism, et cetera. Any changes in these arrangements were automatically reflected in the financial flows. The amount of bank credit that might be required to facilitate and speed up planned flows depended on rules and regulations spelled out in considerable detail and changed infrequently (see Chapter 6).

The financial system of the Soviet Union, as depicted in a recent Soviet text book,[6] is summarized in Figure 5.1. Some of its components, such as social, personal, and property insurance and finances of consumer cooperatives, are outside the scope of this study.[7] Numerous Western students of the Soviet economy, such as R. W. Davies,[8] have also constructed schematic presentations of Soviet financial flows.

Note that the bulk of the social income, except for the growing portion retained by enterprises since the Reform, goes into the national budget, which distributes it to various lower-level units of government as well as to the various ministries and other economic organizations that undertake new investments; a smaller portion is transferred directly to special investment accounts of individual enterprises at the Investment Bank. Before 1965, about 90 percent of the social income was channeled through the budget, but the Reform inaugurated a multi-channel system of distribution of the social product, discussed more fully in the following section.

The fact that more than half of the national income flows through the budget—a much larger proportion than in the United States and other leading industrial countries—primarily reflects two decisions made early in the development of the Soviet eco-

[6]Ipatov [41], p. 7.

[7]Textbooks on Soviet finances, including those listed in the bibliography, provide detailed descriptions of the institutional arrangements in these areas, but availability of financial data is very limited. See Sitnin [78], Slavnyi [80].

[8]See [228].

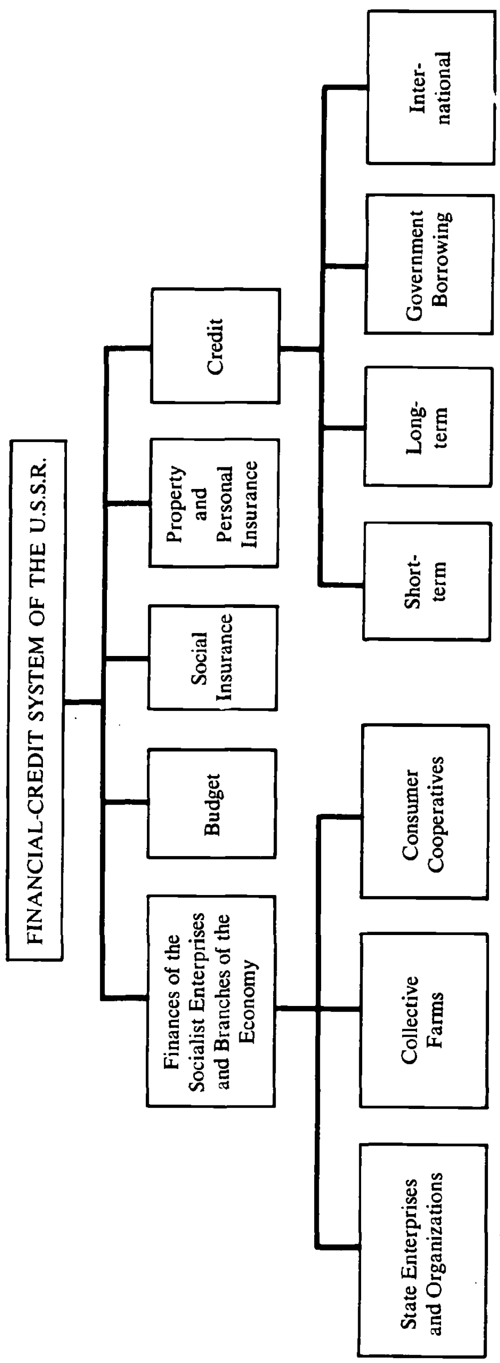

FIGURE 5.1

nomic system, o
fiscal system esta
obtaining adequa
be solved by dire
the abolition of t
fixed capital in *k*
producers' coop
tion) remained
financed investm
Secondly, nea
units are finance
and, to a small d
to them. Budget-
expenditures" t
cover the bulk o
addition to free
for housing, tran
cialist countries
insurance funds
which all social s
The only signific
separate reserve
prises, and a nati
insurance organi
Investment, la
nent of governm
before the Refor
central governme
constituent repub
ipalities, with p
Municipal govern
public services b
supply the popul
as with repair an
fixed plant.
The relative i
levels of governm
reorganizations.
(Sovnarchoz), w
the supervision o

nomic system, once the currency was stabilized and an efficient fiscal system established. First, it was decided that the problem of obtaining adequate financing for state-initiated investment should be solved by direct pre-emption from the social product. Prior to the abolition of the machine-tractor stations, even the bulk of the fixed capital in *kolkhozes* was largely financed by the state. Only producers' cooperatives (mostly engaged in handicraft production) remained outside the area of state-planned and state-financed investment.

Secondly, nearly all expenditures of the lower governmental units are financed from a single, unified budget through transfers and, to a small degree, by certain categories of revenue allocated to them. Budget-financed expenditures, in addition to "ordinary expenditures" typical of the budgets of nonsocialist countries, cover the bulk of "collective consumption," which includes—in addition to free education—health, and other services subsidies for housing, transportation, and the like. Flows which in nonsocialist countries are normally channeled through separate social insurance funds are an integral part of the Soviet budget, from which all social security and social assistance payments are met. The only significant financial circuits outside the budget are a separate reserve fund for meeting casualty losses of state enterprises, and a nationwide state-operated personal property and life insurance organization.

Investment, largely in plant and equipment, is a major component of government expenditure at all levels. This constituted before the Reform about 50 percent of the funds spent by the central government, an average of 25 percent of the budgets of the constituent republics, and about 30 percent of the funds of municipalities, with particularly heavy expenditures in major cities. Municipal governments not only provide the various utilities and public services but also operate a variety of enterprises which supply the population with bread, milk, and other staples, as well as with repair and similar services, which all require investment in fixed plant.

The relative importance of the expenditures at the various levels of government has changed over time due to administrative reorganizations. The creation in 1957 of regional administrations *(Sovnarchoz),* which placed a large number of enterprises under the supervision of the fifteen republics, automatically expanded at this level since enterprise profits create revenue for the supervising government unit. The subsequent reorganization, which returned individual industries of national importance to the supervision of national ministries, left a larger number of enterprises of local or regional significance under industry ministries of individual republics (or lower-echelon administrations) than before. Thus, some decentralization was carried over into the system now in effect. As a result, and largely because of increased spending for the economy, the 1969 share of the republics in the unified budget was 45 percent, as compared with about 25 percent between 1940 and 1955, and close to 60 percent between 1959 and 1965.

Some revenues, such as the turnover tax, are apportioned between the national budget and the budget of the republic in which they are collected. A variety of systematic and specific transfers of funds from higher-level to lower-level administrative units is required to balance the budgets of some units whose assigned fiscal resources are normally inadequate to cover all expenditures. This typically occurs in areas where spending on new investments is particularly heavy.

Budget receipts in 1971 reached almost 166 billion rubles, nine times the level of 1940. The main source of budgetary receipts and the distribution of expenditures between financing the economy and the other main categories of expenditure are shown in Table 5.1.

Nine-tenths of the budget receipts are obtained from enterprises. Nearly all revenues of the state enterprises in excess of prime costs (which, prior to the Reform, did not include the cost of capital) are siphoned off into the budget, either by transfer of the bulk of profits or through the collection of "turnover" (sales) taxes which are imposed on most consumer and some producers' goods. In 1971, the turnover tax alone accounted for 33 percent of total budgetary receipts, even though its relative contribution has been declining in recent years (to some degree due to an upward revision of factory prices for producers' goods in 1966 undertaken as part of the Reform). As late as 1950, enterprise profits provided only a little more receipts than the turnover tax, but since 1964 they have been exceeding its contribution by a rising margin. Periodic payments into the budget are based on estimated profits,

TABLE 5.1

The Budget of the USSR, Selected Years, 1940–1971
(in billions of rubles)

	1940	1950	1960	1970	1971
Receipts					
Turnover taxes	10.6	23.6	31.3	49.4	54.5
Payments from profits of state enterprises[a]	2.2	4.0	18.6	54.2	55.6
Social security taxes[b]	0.9	2.0	3.8	8.3	8.8
Income taxes paid by *kolkhozes*, other cooperative organizations and enterprises operated by organizations[c]	0.3	0.6	1.8	1.2	1.4
Individual income taxes and other receipts from the population	0.9	3.6	5.6	12.7	13.7
Government loans	1.1	3.1	0.9	0.5	0.3
Miscellaneous	2.0	5.4	15.1	30.4	35.7
Total	18.0	42.3	77.1	156.7	166.0
Expenditures					
Economy	5.8	15.8	34.1	74.6	80.4
Social and cultural purposes	4.1	11.7	29.4	55.9	59.4
Defense	5.7	8.3	9.3	17.9	17.9
General administration	0.7	1.4	1.1	1.7	1.8
Government loans[d]	0.3	0.5	0.7	0.1	0.1
Miscellaneous	0.8	3.6	8.5	4.4	0.6
Total	17.4	41.3	73.1	154.6	164.2

SOURCE: For 1971 [86], p. 481; for earlier years, various earlier volumes.
NOTE: Items do not add up to totals because of receipts and expenditures not specified. Footnotes added by author.
[a] For capital used, rents, charges against profits and remaining profits.
[b] Paid by employers.
[c] "Organizations" include trade unions, voluntary associations, etc.
[d] Amortization, interest, and administrative expenditures.

and so are substantial proportions of depreciation allowances and deductions for various special-purpose accounts (called "funds") of the generating enterprise. They are normally made automatically by the State Bank at frequent intervals (in some cases, every five days or weekly) from the general enterprise account to which sales proceeds are credited. If the accrual of funds in the enterprise's accounts is not adequate, obligatory payments into the budget are financed through bank loans.[9]

[9]See Chapter 6, footnote 7.

The expenditures side of the unified budget plays the key role in the redistribution of the national product. It embodies all major macroeconomic decisions, the division of current output between investment and consumption, the size and structure of collective consumption, and the apportionment of public spending between the various levels of government. The national budget thus fulfills a most important allocative function[10] with regard to investment flows (between industry and agriculture, among manufacturing industries, and between regions), which, in nonsocialist economies, is performed largely through the capital and credit markets.[11] Investment expenditure, mainly for plant equipment, rose from exactly one-third of total expenditures in 1940 to 47 percent in 1960. They have stayed close to this level through 1972, in spite of the much-emphasized claim that decentralization of investment financing was one of the main objectives of the Reform.

Kolkhozes are the only sector in which virtually all financial flows involve debtor-creditor relationships, and in which self-investment does not involve circuitous routing via the budget and its agent, the Investment Bank. Indeed, since the agricultural reforms of 1958, financial flows in the only sector of the Soviet economy that has no counterpart in any nonsocialist country have become quite similar to those generated by the agriculture sector in capitalist countries.

Financial flows not related to current household expenditures generated by the population are relatively small. Since the discontinuance of forced sales of government bonds in 1957, they involve mainly transactions in savings accounts.

[10]Konnik has estimated that, while only 56 percent of the turnover tax was collected from basic producers' goods industries in 1964, 88 percent of all capital investments were made in that group of industries [48], p. 98. See also Hahn [119], Lavigne [128], Leptin [130] and Seidenstrecher [144].

[11]At the same time, a large volume of transfers of investment funds between individual industries may by-pass the budget. Thus, in 1969 the automobile industry required transfers of funds amounting to 575 million rubles from other industries, while 800 million was siphoned off from the electric power industry. These are large amounts compared with total net fixed investment in industry.

Depreciation reserves not spent for capital maintenance and repair, profits and turnover taxes periodically transferred into the budget, together with retained enterprise profits, constitute what is known in Soviet planning as "financial accumulation." The concept is of limited analytical value since it does not include all funds, such as those of the *kolkhoz* sector, household savings, and a number of other sources available to meet investment needs.

Financial Flows of Enterprises

The restructuring of financial flows is the only significant change that has occurred in the financial area in forty years.[12] The Reform has given the enterprise somewhat more autonomy in the use of the profits it generates. Another important aspect of the Reform is the role assigned to profits.

PROFITS SINCE THE REFORM

Profits are now expected to depend increasingly on decisions of the enterprise manager and not on the proper execution of detailed plans handed down from above. Profitability has become a key criterion for the distribution of incentive rewards, but as a guide for resource allocation it has acquired only limited significance.

A lively discussion has been under way in the Soviet Union on whether the profit ratio determining the size of the social product should be related to labor inputs, to fixed capital only, or to different variants of total production costs.

Higher profit retention is a related aspect of the Reform. One of its main purposes is to induce individual enterprises to design schemes for additional compensation that would offer meaningful incentives to management and workers. The other is to enlarge, within limits, the investment independence of individual enterprises.

When actual profit and sales targets are exceeded the attached rewards are relatively large, as payments into the government budget on extra profits are at reduced rates and decline with the rise in "unplanned profits." Profits in excess of the planned targets expand retained earnings, permitting the manager to undertake additional minor investments to spur productivity and, within set limits, to raise the real income of workers through improved fringe benefits and additional cash payments in the form of various premiums.

However, a higher profit retention does not influence directly the distribution of investments. In particular, on a macroeconomic level, the higher profit rates in consumer goods have not

[12] There have been some minor changes, such as the introduction of loans to finance small-scale mechanization discussed in Chapter 6, "Medium-term Credit."

resulted in a rechanneling of funds into this sector from producer's goods industries, since overall economic targets are set independently of profit considerations. The notion that investment decisions should be related to enterprise profits remains irrelevant for the Soviet Union.

With regard to prices, the only flexibility available to plant managers is to discontinue production of profitless or low-profit items and to replace them with virtually identical products embodying minor modifications, entitling the enterprise to submit to the price-fixing authorities a request to set a higher price on the "new" product. For example, by replacing a wooden frying pan handle with a plastic one, or by moving a zipper on a blouse from the back to the side, the enterprise can obtain a reclassification of the product, and thereby a higher price tag. Thus, over time, the price index is protected (since it is ostensibly based on standard merchandise), while the enterprise improves its profitability.

With prices of inputs and outputs still fixed by outside authority, improving productivity is the only way to increase profits. Since the technological equipment of existing plants tends to be frozen largely at the level of initial construction, although the new system makes it easier to allocate funds for the acquisition of superior and new technology, most of the improved productivity must come from labor inputs, better management, and avoidance of disruption in production due to such factors as breakdowns in the flow of physical inputs and in equipment and unbalanced inventories. Given these limitations, it is understandable that the Reform was presented largely in terms of a new system of management rather than as a new approach to the restructuring of the basic mechanism of the Soviet economy.

Furthermore, ministries and other higher-echelon administrative units are not interested in enterprise profits alone but in the performance of the whole set of overall indicators. Those expressed in physical quantities remain of key importance, since the goals of administrative units in charge of the economy, on the national, regional, and local level, continue to be set in terms of physical targets. Profit targets continue to be administratively set as a percentage of total factor costs, and there is relatively little fluctuation in this percentage among, and practically none within, industries. While the range of key indicators designed to guide the enterprise's activities has been reduced, with financial indicators gaining prominence, higher economic authorities continue to issue various kinds of binding directives to the enterprise, including indicators *(direktivnye pokazately)* stipulated in real rather than monetary terms.

In fact, the redefinition of targets appears to be a mere formality for a large segment of output. This is particularly true of goods contracted for in advance (typically, producers' goods and defense industries), and of staple items (such as basic raw materials, fuel, building materials, and most food products) where supply shortages are the rule and demand growth is secular. The area in which the new system has led to greater responsiveness to final demand, with the recognition that not all of the output may be salable, or that it is salable only with price concessions, does not seem to extend much beyond semidurable and durable consumer goods.

Indeed, with factory prices fixed, total sales targets are actually identical with targets previously specified in quantitative terms. The important difference arises from calibrating the target on goods actually sold rather than produced, and from the greater flexibility in the composition of output. Enterprise managers have been reluctant, however, to introduce new products requiring radically new technology, while at the same time they have been eager to make small changes in design that may enable them to obtain upward price revisions. To combat management inertia in promoting technology innovations, additional measures were taken in July 1972 requiring enterprises to set specific sales targets for new products "corresponding in technico-economic terms to the highest domestic and foreign achievements."

Before the Reform, virtually all of an enterprise's profits went to the budget, except for a very small statutory proportion retained for designated special-purpose funds. Now profits are distributed via three main channels according to their three main functions: as a fiscal source, a source of fixed and working capital for the enterprise, and a source of various special-purpose funds "for stimulation" controlled by the enterprise. The distribution of profits under the new system is summarized in Table 5.2.

The budget's share consists of three parts: charge on invested capital, quasi rent ("fixed payments"), and a residual remaining

TABLE 5.2

Use of Profits After the Reform

Payments into the budget	Charge on fixed investment and allotted working capital Fixed payments (rentals) Residual profits
Planned expenditures of the enterprise	Financing of centrally planned capital investment Increase in working capital Reserves for giving temporary financial assistance Amortization of loans for financing fixed investment Amortization of loans for temporarily supplementing own working capital Absorption of losses in operating factory housing and other facilities for the benefit of the staff
Formation of funds for stimulation	For material stimulation For socialist competition For socio-cultural projects and dwelling construction For stimulating output of consumer goods For development of production

NOTE: Profits are from the sale of output and some other sources, such as the sale of redundant equipment. This list is adapted from Darkov and Maksimov [23], p. 103.

after all statutory deductions for funds that the enterprise can retain are made. On the whole, in many enterprises this residual is still quite large in relation to total profits. (It is, of course, nonexistent in the case of enterprises with planned deficits which receive subsidies, including those designed to nourish some of the statutory "funds for stimulation," discussed below.)

A second major portion of the profits goes to finance certain categories of fixed capital investment or to increase working capital. As illustrated in Table 5.2, such funds can be used either (see Chapter 6) for projects that are centrally planned but financed from retained earnings, or to repay bank loans obtained in previous years for such projects. Profits of a given year can be used to finance not only current and past investments but also future investments by building up balances at the Investment Bank.

Other uses of retained earnings are for bridging temporary flow gaps in special funds for the payment of subsidies for housing and other facilities built by the enterprise for the benefit of the staff, and, finally, to expand working capital or repay loans obtained in previous periods for this purpose.

The various "funds for stimulation" replace the "directors' fund," which had existed before World War II, was reinstated between 1946 and 1956, and was subsequently renamed the "enterprise fund." Earlier attempts at using part of enterprise profits to stimulate productivity by providing limited financial incentives had little success. Payments into the directors' or enterprise funds depended largely on overfulfillment of the plan. Enterprise managers were understandably interested in inducing planners to set low targets in order to receive bonuses for "plan overfulfillment." Even so, payments into the fund depended on the simultaneous achievement of a large number of specified targets, and failure to achieve even one of them reduced, or even completely removed, the prospects for a bonus. Finally, the fact that diverse purposes such as financing investment not provided for in the plan and expenditures for collective staff benefits, were met from the enterprise fund reduced its effectiveness as an incentive to increase production.[13] Prior to the Reform, depending on the industry, 1 to 6 percent of any additional profits were available for this fund.

Two of the new incentive funds initiated under the Reform are designed to distribute additional monetary rewards to management and workers either (a) on the basis of a specified formula, or (b) as a reward for exceptional performance entitling winners in "socialist competition" to receive additional rewards (see Table 5.2). The distribution formula is set by each individual enterprise and may vary from department to department. In some cases, special criteria, different from those applied for the fulfillment of plan targets, are used in determining an individual department's claim for bonus payments, and shadow prices rather than official prices may be used.[14] Such bonus payments may, in certain cases, result in significant additions to basic wages and salaries. Moreover, the new arrangements also widen the distribution of

[13] See Alexandrov [4], pp. 44–45.
[14] [4], p. 48.

such additional compensation to benefit the entire work force, not only management and the professional staff, which had been largely the case under the old system. Another fund provides for fringe benefits in the form of staff facilities like factory housing, kindergartens, children's camps, and vacations for workers at nominal cost.

The third "development fund" can be used by the enterprise itself for research expenditures, some limited product development activities, and certain specified types of investment not provided for in the plan.

Finally, enterprises are encouraged to make the widest possible use of remainders and by-products that are likely to help overcome shortages and that can be disposed of locally. The additional profits resulting from such operations are treated in a way to stimulate their production further. The use of incentives is discussed in more detail in a following section of this chapter.

The order in which profits are distributed among the budget, the various funds, and the other recipients continues to be determined by administratively set priorities and allocation formulas. The differentiations between the rules applying to planned profits and those governing additional profits, as well as the special procedures set up for enterprises requiring subsidies since their plans anticipate losses rather than profits, were unaffected by the Reform.

PAYMENTS TO THE BUDGET

As illustrated in Table 5.2, a portion of enterprise profits goes to the budget as interest payments. Interest, under the name of "charge on capital," is now charged on both fixed and working capital. To equalize the cost of new and existing fixed capital originally supplied on a grant basis, a charge has been inposed on the depreciated value of capital assets in use at the time the new system became applicable to an industry following the 1965 Reform. Enterprises that require subsidies ("planned deficit units") are exempt from the capital use charge. The ancestry of this charge can be traced to discussions during the NEP period. In 1922–1923 a proposal was made by the Commissariat (now Ministry of Finance) to introduce a capital use tax for all state-owned enterprises as a means of improving the use of fixed and working capital. A rate of 4 to 5 percent was discussed at the time.[15] While the charge on capital is applied to gross profits, it is a cost factor in setting prices. It may be regarded as a property tax, or, alternatively, as the minimum socially acceptable rate of return on productive assets (capital use tax), or as the minimum share of government in enterprise profits.[16] Its introduction affected the rate of profits in individual industries and for the economy as a whole.

The question of what the proper level and structure of charges on invested funds should be is far from resolved. In the first full year of the Reform rates were set uniformly at 6 percent, but in the following year (1967) they varied within a range of 3 to 10 percent for individual industries.[17] The whole problem of the proper charge for capital, its relation to planned profits, and the disposition of such profits, including the determination of the share to be retained for the "funds for stimulation," is still being hotly debated, and competing schemes are being put forward,[18] including proposals for differential rates between branches of the same industry and even between individual enterprises.

The existence of quasi rents is recognized by the introduction of a rental ("fixed") payment with a rate set for fairly long periods in advance in each case when it is levied. Given the divergence of profit rates in individual industries, the ratio of this rental payment to total costs varies widely. Differential rents are fixed either as a percentage of sales or as a fixed amount per unit of output, and tend to equalize the production cost of each enterprise.

In effect, these fixed rents are akin to the turnover tax, except that they are imposed on an enterprise (or entire industry or industry branch) rather than on a product basis. They tend to equalize net profits among individual units within the same industry, where otherwise, with pricing on the basis of average industry costs, enterprises enjoying natural, locational, or technological advantages would obtain a higher profit rate and therefore retain a greater share of profits.

The introduction of the capital use and rental charges, while reducing the amount collected under the heading of "remaining

[15]See Mitel'man [194] and Decaillot [228].
[16]Ipatov [41], p. 20.
[17]Tulebaev [88], p. 13.
[18]See, for instance, Brazovskaya [170] and the literature quoted therein.

profit,'' has not changed the total share of profits in the economy going to the budget. Payments for capital use and quasi rents are a relatively small part of profits as calculated prior to the Reform. They do not depend on changes in sales or profitability which affect ''remaining profits'' only. The share of profits retained by the enterprise is determined under the new system by the net profits, defined as profits measured by ''accounting profitability,'' from which fixed rental payments and capital use payments are deducted.

The Reform had only a very slight overall effect on the sources of budgetary income and on the structure of expenditures. In 1971 the share of national income channeled into the budget was essentially the same (52.7 percent) as in the year the Reform was initiated (52.9 percent in 1965). The budgetary receipts derived from payments by the socialized sector of the economy remained very close to the old level (91.1 percent, compared with 91.8 percent in 1965); and the expenditures for the economy, overwhelmingly for investment purposes, rose (from 45.7 percent in 1965 to 48.9 percent in 1971), in spite of all the emphasis on decentralized investments from profits retained by individual enterprises.[19]

FINANCING FIXED CAPITAL INVESTMENT

Financing fixed capital investment from budgetary resources on a nonreturnable grant basis under the standard system had involved considerable misallocation of resources and costly delays in the completion of construction projects. Since the Reform, the financing of fixed investment has been gradually shifting toward a combination of retained enterprise profits, depreciation reserves and bank loans. If and when this process is accelerated, the proportion of national income redistributed through the budget will tend to decline, and that of self-investment and bank loans, to increase.

The ultimate objective of the new arrangement is to achieve a more rational pattern of investment in productive capital and a reduction in investment in relation to output. If the Reform is to be more than a substitution of control mechanisms, financial

[19]Vinokur [209]; for 197, computed from [86], 1972, p. 481.

processes must acquire new functions. The significant question is, therefore, whether the functional relationship of the financial system to resource allocation and profit maximization is being changed. Thus far, central accumulation and allocation of investment resources has remained largely unimpaired, though implementation is shifted to a multichannel system of fund flows which, among other things, reduces the circuitous flow of resources between the units that generate them.

Changes in the flow of investment funds (including depreciation reserves) and credit are bound to have some effect on patterns of real investment, inventory behavior, and the producers' price structure, and thus on consumer welfare. The broad question is, therefore, whether reforms in the area of financing will tend to raise efficiency of investment, accelerate the rate of real output growth, and improve the relative apportionment of the increased output between consumers and the state.

One change that received considerable publicity when the Reform was announced involved (a) shifting fixed investment financing from grants to repayable loans,[20] and (b) permitting individual enterprises to retain a greater share of profits and depreciation reserves in a move toward greater decentralization of investment. However, greater decentralization of investment funds does not necessarily mean greater decentralization of decision making. Investment decisions remain largely centralized in the bureaucratic hands of the planning agencies, industrial ministries, and the *glavks* and their organizational successors. Even most of the resources of the decentralized enterprise funds must still be spent on centrally planned investment.[21] The state continues to control the level and the broad distribution of investments. (Since 1971, the upper limit of investment is set by the relevant ministries of the various republics, depending on who supervises the individual enterprise. In the new scheme of things, there is no more room than under the old system for anything even remotely resembling a capital market. The principal channel for enterprise initiative is "arguing it out" with the supervisory and planning

[20]Partial shifting to loan financing of investment in fixed capital had been under discussion since at least 1957.

[21]In 1965, for instance, 38.7 percent of all centrally planned investment was financed from enterprise resources. See Poskonov [70]. For a detailed discussion of the various kinds of enterprise funds which, under the standard system, could be used to finance decentralized investments, see [93], pp. 37–41.

authorities. The bulk of investment designed to increase existing plant capacity and investments involving a variety of minor projects remain centrally planned but no longer necessarily grant-financed. Loan financing of part of all such projects by the state and by the Investment Bank will gradually lead to the formation of revolving loan funds by the latter and reduce the need for giving them additional resources from the national budget.

Grants from the budget continue to be made not only for social overhead investments like schools and hospitals, but also for such priority projects as new industries, large plants (such as those in the automotive industry), and major programs for the development of national resources. In principle, they are to be limited to large *de novo* projects, designed to change the structure of production and the geographic distribution of industry, to introduce new technology, to open up major new sources of raw materials, and to construct important hydro-electrical projects. Needless to say, all defense-related investments, as well as those connected with atomic energy and space programs, continue to be budget-financed. While these expenditures are never mentioned in Soviet literature, they are no doubt subject to rules different from those applying to other investments, and what changes, if any, the Reform has brought.

The change in the channeling of investment funds between 1965 and 1971 can only be described as modest. In 1971, 59 percent of total profits in all branches of the economy still went to the Treasury, as against 70 percent in 1965 (and only 64 percent in 1960). During the same period, the percentage retained for investment purposes rose from 10 to 13 percent—not much above the 1960 level of 12 percent. In money terms, the increase amounted to about 8 billion rubles. Depreciation allowances rose from 18.8 billion rubles to 32.1 billion, of which half were retained by enterprises each year for plant maintenance. Thus, the total fund for investments available internally rose. Some part of retained profits had to be invested in centrally planned projects, however. As a result, the amount that individual enterprises can expend independently for capital projects, including those required to upgrade technology, and even for maintenance and repairs has not been significantly increased. It remains to be seen whether profits put at the disposal of the newly created associations of enterprises *(ob'edineniye)*, in fact, horizontal or vertical combinations of enterprises which retain a large amount of independence, will contribute to greater decentralization of fixed investment decisions.

Long-term loans (outstanding at year's end) for investment purposes in the six-year period rose only by 6.3 billion rubles despite their tenfold increase from the 0.7 billion level at the end of 1965.[22] This roughly 21 billion expansion in retained profits, depreciation allowances, and loans compared with an increase by 35.5 billion in budgetary expenditures for the economy, overwhelmingly for fixed investment purposes. Thus, so far, the gap between announced objective and actual performance remains very wide; the share of centrally directed investments may have actually increased rather than decreased since the Reform was launched.

During the last ten years prior to the Reform, retained profits available for "decentralized investments" amounted to only about 2 percent of total new investments in the Soviet economy.

While the Reform undoubtedly gave enterprises greater financial control over their own capital investment, it did so without simultaneously improving the availability of real resources to implement this more decentralized investment. This fact constitutes one of the principal limitations of the Reform. For it is clear that the one major reason for changes in investment financing had been to help solve one of the main problems of capital formation in the Soviet Union—the chronic immobilization of resources in uncompleted construction projects and hoarded building supplies[23] and the lack of pressure to complete individual projects as rapidly as possible.

[22]Computed from [86], 1972, pp. 465, 466, 480, and 486. These figures relate to the entire economy, excluding *kolkhozes*, and thus include state farms, municipal enterprises, et cetera. Separate data for manufacturing are not available.

[23]In many cases, plant managers have been unable to find contractors willing to take on additional jobs since their resources were already fully committed to major projects approved by central authorities and were included in lists of eligible projects. See Petrakov [197], p. 181. Thus, in the third full year after the initiation of the Reform, enterprises which had switched to the "new system of economic steering" were able to spend only 47 percent of the funds earmarked for housing and the construction of social and cultural facilities such as clubs and movie theatres. Only 58 percent of their *total* "funds for economic stimulation" were spent in that year. In 1969, only 85 percent of all construction scheduled to be completed was actually finished. Lack of funds and other shortcomings in planning and execution account for the shortfall. See Kartashova [179]. At the beginning of 1971 incompleted construction of retail stores in rural areas exceeded the value of a full year's investment. See Sotnikov [205].

Project completion was delayed by many factors prior to the Reform. Since performance was measured in terms of gross value of work performed (construction put in place) rather than value added, subcontracting construction firms tended to give preference to those operations that yielded the largest "work performed" figures, with the result that the flow of many projects was much delayed.[24] Another factor was poor coordination between construction and equipment delivery schedules, as well as the tendency to place contracts for equipment in excess of financial resources available.[25]

To remedy this situation, the Reform has instituted moves designed to increase financial incentives for the completion of projects. Prior to 1965, payments were made as a rule for each individual job (in 1954, for instance, to the extent of 95 percent of all disbursements) irrespective of whether it resulted in additional operating capacity. One of the ways in which the Reform began to use financial levers was to make partial progress payments dependent on the percentage of scheduled operating capacity completed. In a more radical step, in some cases progress payments on each phase of a construction job completed have been replaced by a system under which the Investment Bank pays the contracting firm only after the completed plant is ready for delivery, but by 1972 only a small part of all projects financed was subject to this procedure.

Other shortcomings of the standard system, such as interruption of construction because of inadequate financial planning, [26] are to be remedied in a variety of ways. Projects requiring bank financing must now submit flow-of-funds projections to document availability of funds over the entire period of construction and loan amortization and penalty rates are charged when loans are not amortized on schedule.

Despite these measures, there is little evidence that the Reform

[24]Belkin and Inventor [13] have estimated that projects in process of completion absorb 50 percent more resources than would be required if their average time of construction was comparable to average U.S. performance.

[25]For a fairly candid discussion of reasons behind the inefficiency of the construction industry and of the attempts of the Investment and State Banks to foster improvements, see Yunik [91], pp. 13ff. and pp. 133–135.

[26]Poskonov [70], p. 260. Immediately prior to the Reform (1964–1965), the average cost of projects sponsored by local Soviets exceeded estimates by 18.9 percent. Alexandrov [4], p. 89.

has succeeded in improving the chronic problem of failure of investment projects to be completed on time.

ENTERPRISE FINANCES AND THE REFORM

Has the enterprise made real strides toward greater autonomy under the Reform? There are no easy answers to this question. It is not clear to what extent any of the moves toward autonomy have been actually implemented in various industries. The creation of associations of enterprises (*ob'edineniye*) [27] represents a substitution of administrative authorities interposed between the enterprise and the industrial ministry (such as *glavk*). Their creation does not necessarily mean more autonomy for the enterprise, since they can possibly also result in the transfer to the association of some decisions previously left with the enterprise manager. It is not clear as yet whether enterprises have, on balance, won at the expense of the top and intermediate levels of the economic hierarchy.

Reducing circuitous channeling of investment funds means an increase in funds retained by enterprises, and a shift to credit on turnover simplifies their short-term credit relations with the State Bank. It must be kept in mind, however, that the financial flexibility of managers in dealing with the funds retained by the enterprise has been increased only within narrow limits.[28] Furthermore, retained enterprise funds can still be transfered to other enterprises (decree of February 12, 1966) under ill-defined conditions at the discretion of higher-level economic administrations.[29] Nevertheless, funds subject to management control are normally accumulated in segregated bank accounts pending disbursement, and enough of these temporary accumulations seep into the gen-

[27] *Ob'edineniye* is an association of enterprises, usually within the same industry and region. It represents a standard administrative level between the *glavk* and an individual enterprise. (It corresponds to the "trust" in earlier periods of administrative organization.) On the arrangements for the extension of credit to associations, see Stundyuk [206].

[28] For example, with trade union approval, up to 20 percent of funds allocated to the bonus fund can be used for fringe benefits (such as factory housing construction), and vice versa. See Chistyakov, "The New System of Stimulation Funds and their Role in Increasing Efficiency of Production." in Alexandrov [4], p. 56.

[29] Eidonova, "Profits, Rentability, and Their Role in Increasing Efficiency of Production," in Alexandrov [4], p. 36. Examples are given where profits were transferred in their entirety to other enterprises supervised by the same ministry.

eral cash balances of the enterprise to offer various possibilities for escaping constraints imposed by planners and controllers.

Moreover, ministries and other economic authorities (such as *glavks*) can act as intermediaries, borrowing from the Bank and making credit available to individual enterprises for the purpose of retiring funds borrowed to bring working capital up to required levels. The same authorities can also remove the need for borrowing either by replenishing working capital through transfers from other enterprises under their supervision or by simply lowering the working capital requirements (norms) they impose.[30]

As a result of the Reform, funds of enterprises designated as "internal resources" have increased in relation to their working capital. Such "temporarily available funds," which are not considered part of the "owned working capital," include, in addition to retained profits earmarked for various specific purposes but not as yet actually expended, also (a) profits payable into the budget but not yet actually transferred (these transfers, as well as those to the Investment Bank for the financing of centrally planned investments, are being currently made only three times a month, at roughly ten day intervals), as well as (b) a large part of accounts payable. It was estimated at the beginning of 1971 that such "internal resources" constituted about one-fifth of the *total* working capital of state enterprises; less than one-third of these internal resources were at that time actually taken into account in financial planning (as *ustoichivye passivy*—"stable liabilities"), so that the individual enterprises had a certain flexibility in using the remainder. A special investigation conducted by the Central Statistical Office (TsSU) as of January 1, 1971, revealed that 70 percent of these "unplanned internal financial resources" were actually used for bridging various shortages in funds resulting from situations not foreseen in financial plans, thus obviating the need for unplanned bank loans or other outside assistance. Typical uses of such resources included financing of inventories not eligible for bank loans, meeting expenditures for which resources provided in the enterprise's financial plan did not actually materialize, and reducing accounts payable.[31]

[30]See Kartashova [43].

[31]See Agraponov [160] and Shermenev [75].

Enterprise balance sheets also show a certain amount of resources provided by creditors even though inter-enterprise lending is prohibited. Some of the amounts shown in this

Greater profit retention and the extension of credit on turnover have increased average cash balances of enterprises with the State Bank (which prior to the Reform averaged 4 to 5 percent of working capital). They have somewhat reduced the need for short-term credit, and have provided enterprises more opportunity for maneuvering in spite of the existing safeguards against the use of funds accumulated for purposes other than those specified. The level and structure of bank interest rates apparently do not encourage loan repayment before maturity, while abolition of the payment of interest on free balances encourages their use for unauthorized purposes if the vigilance of the controllers of the State Bank can be circumvented.[32]

FINANCIAL INCENTIVES

Before the Reform, enterprises had very limited opportunities for technical modernization, and few incentives existed to stimulate efforts in that direction. The Reform recognizes that financial incentives on an individual as well as on a group (team or enterprise) basis are indispensable for increasing efficiency and stimulating initiative leading to cost reductions and generally improved performance.

Bonuses can be paid for a variety of reasons. The precise basis on which such payments are made is fixed by the director of the enterprise, ostensibly with the participation of the trade union committee. The premium schemes of individual enterprises may cover individual workers and members of the technical and managerial staff as well as groups of workers, such as departments or teams ("brigades"), including premiums for winners of intrafactory competition for superior performance, known as "socialist competition." The resources for such premiums are derived from savings achieved in "planned" payrolls as well as from the various premium funds (see section above, "Profits Since the

---

category are float (bills in the process of collection), contested bills, as well as bills due for which settlement credit was not available to the buyer and which may be considered as trade credit. The percentage of total amounts due from creditors (including drafts in the process of collection) in total working capital varies by industry, over time and for individual enterprises within an industry, but usually averages between 8 and 12 percent.

[32] This is shown by Lisitsian [188] and [189] on the basis of several sample surveys. One survey of machine building enterprises shows that the special funds for the stimulation of the staff and for decentralized investment accounted for 15 percent of total "nonplanned expenditures" on January 1, 1966, but for as much as 47.3 percent on October 1, 1969.

Reform"). All premium schemes require approval by the supervising economic administration and must be within the limits set by the Council of Ministers for each industry.[33]

To increase the effectiveness of incentives, the profit funds earmarked for additional employee compensation are made available, although in reduced amounts, even if individual plan targets are not achieved, while under the old system no premiums were payable unless all targets were met.[34]

There is little evidence to indicate that the main objective of the new financial incentives has been achieved. After nearly a decade of discussion and considerable experimentation, no satisfactory way has been found to find a workable bonus system that would heighten the staff's interest in raising productivity and introducing new technology. The new system of determining bonuses retains the earlier procedures. No mechanism has emerged that would automatically make factory workers and various levels of technical, managerial, and administrative personnel strive for more efficient use of existing equipment, the introduction of superior technology, and for the elimination of bottlenecks due to resources immobilized in construction or the distribution process. Instead, a new, rigid system of bonuses has been combined with the previous one. Moreover, neither the bureaucracy of the higher-level economic administrations (*glavks,* for example), on whose initiative, or at least approval, technological and managerial progress depends, nor the staff of the State Bank and the Investment Bank participate in the new system of incentives. These groups may derive some satisfaction from the fact that the targets they set, the norms they determine, and the repayment schedules they impose are possibly met with greater regularity than before. But their interest remains in playing safe by setting targets low enough to show "overfulfillment," and by refraining from innovations that contain the risk of something going wrong.

One of the generally recognized effects of the Reform has been a greater seepage of profits into labor compensation. With profit-related bonuses becoming a significant part of money income,

[33]Up to 20 percent of the resources accruing to the three individual funds for stimulation can be reallocated during the year. See Belobzhetsky [169]. See also Leeman [243].

[34]Slavnyi [79], p. 35. On the rules governing the formation of funds for stimulation in enterprises with planned losses, see Tarsov and Utkin [208].

control of payroll disbursement has proved an insufficient means of planning and balancing real flows of consumer goods and of money incomes. As a result of the broader use of bonuses and other changes introduced by the Reform, in some industries labor income has increased more rapidly than productivity. To counteract the resulting inflationary pressures, measures have been taken to transfer to the "fund for social and cultural purposes" at least part of the funds that should have automatically become available for individual bonus payments under the Reform, or, alternatively, to postpone their disbursement to the following year.[35]

By 1971, manufacturing enterprises were distributing more than 4.1 billion rubles in bonuses, and, if the "funds for stimulation" were distributed proportionately in the other branches of the economy, the total disbursed by all state enterprises must have been near 5.4 billion rubles. Interestingly enough, the amount accumulated for this purpose but not yet disbursed at the end of 1971 in manufacturing alone amounted to nearly two-thirds of the sum actually paid out. By comparison, the two funds carried over from pre-Reform years (premiums for "socialist competition" and for creating and introducing new technology) yielded only 36 million and 586 million rubles, respectively, in all state enterprises.[36] Once the provisions of the Reform are fully and generally implemented and the financial incentives have had their full effect on productivity, as much as one-fifth of the total compensation of employees is expected to come from the incentive fund, with perhaps a more than proportionate share going to the engineering and management group.[37]

[35]There are indications that, despite the new emphasis on consumer goods, their output has been lagging behind effective household demand, and shortages for specific geographic areas persist. This was particularly true in 1968 and 1969, when payrolls increased at a more rapid rate than productivity, partly as a result of a general upward revision of wage scales. The various old and new problems slowing down expansion of services to consumers also revealed themselves again. See Smirnov [81], p. 84 and Zverev [93]. While during the three years preceding the Reform (1963–1965) annual increases in consumer services exceeded that in consumer goods by about 15 percent, in 1967–1969 the value of services grew less than that of goods available to consumers. See Slavnyi [203].

[36][86], 1972, pp. 478 and 479.

[37]The new provisions for worker compensation affect almost exclusively production workers, whose share in the labor force has been declining mainly as a result of the growth of nonmanufacturing industries. The percentage of nonproduction workers in the labor force, only 11.7 percent in 1940, had risen to 20 percent by 1965 and has doubtless increased since. Slavnyi [79], p. 15.