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Krzysztof Połomski

**Tax Systems in the Selected Transition
Economies**

An overview

W a r s a w , 1 9 9 9

Materials published here have a working paper character. They can be subject to further publication. The views and opinions expressed here reflect Authors' point of view and not necessarily those of CASE.

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Abstract

The paper discusses the Value Added Tax, Personal Income Tax, Corporate Income Tax and excise tax in Poland, the Czech Republic, Hungary, Russia, Georgia, Ukraine, and the Kyrgyz Republic. It could be argued that the countries of Central Europe are more advanced in their reforms compared with the countries of the Former Soviet Union. In many cases the situation in the FSU still resembles the time of planned economy where enterprises function in an administratively regulated environment. It seems like a lot of political will is needed to overcome stagnancy and change the behavior of economic agents.

The paper will concentrate mainly on the so-called state taxes and will not cover local taxes such as real estate and land tax. It will not cover the social insurance contributions and other types of payroll taxes, as they are beyond the scope of this paper.

In the first part of the paper, I will try to compare the tax systems from the point of view of budget situation in the Czech Republic, Georgia, Hungary, the Kyrgyz Republic, Poland, Russia, Ukraine. In the second part of the paper, some legislative regulations will be presented.

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I. Introduction

The process of economic transformation has influenced the state of public finances in all post-socialist countries. Although there were many differences between the countries, one can name some similarities that were common for all these countries at the beginning of transformation to market economies. These were the following:

- poorly functioning tax administration,
- falling tax revenues to GDP ratios,
- highly differentiated rates,
- high effective tax rates,
- narrow tax base,
- huge number of taxes and different rates,
- extensive exemptions,
- compliance problems.

In order to balance a budget, government has either to reduce expenditures or increase revenues. It is obvious that improvement of tax collection takes time and the quicker way to balance a budget could be to cut government spending. However, this is not easy and as experience of the recent years has shown, it takes even more time than an improvement of revenues collection. It is a commonly known truth that privileges once granted are very difficult to be withdrawn. It needs a strong political will, which can challenge society's objections [1].

Growing budget deficits have forced authorities to undertake steps to overcome the crisis of public finances. In many instances, however, governments concentrated on ad-hoc measures (that were supposed to produce quick results) rather than on complex and comprehensive reforms of tax systems. Such an approach could be useful in the short run only but it usually cannot improve the situation in the longer run perspective. Moreover, politicians relying on ad-hoc measures may cause instability and create new distortions.

The better way to ensure the long lasting stability of the system is to undertake measures aimed at re-designing of the existing system. Such changes should try to reach the following goals, which are common for industrialized countries:

[1] All post socialist countries have experienced changes of governments and political forces being in power during the first few years of reforms.

- ensure sufficient level of revenues to enable the development of sound public finances,
- implement universal income taxation which would unify taxation of different sources of income,
- achieve equal treatment of different economic agents [2].

Apart from achieving these goals, a properly designed tax system should not disturb in optimal allocation of resources, should be transparent and not complicated, stable in time in order to ensure the taxpayers' certainty regarding their rights and obligations. Finally, the tax burden should be distributed fairly.

In the course of the last few years all transition countries tried to implement new tax laws and change their systems to reflect the Western standards. However, in many cases, especially in the Former Soviet Union, authorities were not able to introduce a whole package of tax reforms. Even if the new legislation was adopted, its enforcement remains very problematic, mostly due to the lack of executive acts, low qualifications of tax inspectors, and the lack of political determination to fight with tax avoidance.

2. Budget Revenues

The overall tax burden is usually measured by the ratio of budget revenues to GDP. Table I shows these ratios for the selected countries.

In all analyzed countries (except for Georgia) the ratio of budget revenues to GDP was smaller in 1997 than in 1994. This may be connected with a decreasing involvement of state in the economy and adjustment to the European Union standards in the case of Poland, Czech Republic, and Hungary. In other countries, we can observe a sudden fall of the ratios in 1995 and then a slight increasing tendency. Contrary to Poland, Czech Republic and Hungary, the fall of revenues to GDP ratios in the FSU countries was caused rather by the problems with tax collection and overall bad shape of their economies. A small increasing tendency is connected to introduction of non-tax revenues (e.g. customs duties). If one looks at tax revenues only, it appears that the ratios of tax revenues to GDP have fallen in all of the analyzed countries. An exception is Kyrgyzstan and Georgia where the ratio of tax revenues to GDP has been growing recently. This situation occurred mainly through an improvement of tax collection which was very poor in these countries (in Kyrgyzstan in 1995 only 74 percent of the planned revenues were collected).

[2] In many instances, especially in the Former Soviet Union, the achievement of this goal is very difficult, mostly due to strong rent-seeking.

Table 1. Total Budget Revenue as percentage of GDP

Country	1994	1995	1996	1997
Poland	47.5	45.7	45.1	44.1
Czech Republic	44.9	43.8	42.7	40.7
Hungary	51.4	48.1	46.8	44.9
Georgia	7.7	7.1	9.4	10.4
Kyrgyzstan	20.8	16.7	17.1	17.6
Ukraine	41.9	37.8	36.7	38.4
Russia	34.6	31.9	32.1	33.0

Source: IMF, World Economic Outlook 1998

3. Value Added Tax

Value Added Tax is a multistage tax on consumption. In the countries of Central and Eastern Europe as well as the ones of the Former Soviet Union, VAT replaced turnover and sales taxes. Before introduction of VAT, many turnover tax rates existed, which applied to different products. Some products were taxed very heavily while others were subsidized. Services in CEE and FSU were not taxed at all.

The logic behind the introduction of VAT was to achieve universal and equal tax treatment of different sectors of economy, different product, and forms of ownership. Only such a treatment could ensure the proper functioning of the market economy, that is adequate resource allocation driven by market forces.

Below you will find a description of budgetary revenues in the selected countries while in the second part of this chapter a comparison of legal solutions in these countries will be presented [3].

3.1. Statistical Analysis

Table 2 shows the share of VAT collection in GDP and total budget revenue.

[3] More detailed information about the legal framework you will find in chapter 6.

Table2. Share of VAT in GDP and in Government Revenue

	1994	1995	1996	1997
Poland				
VAT/GDP	7.1%	7.2%	7.2%	
VAT/Revenue	23.8%	24.7%	28.1%	30.8%
Czech Republic				
VAT/GDP		7.0%	7.1%	
VAT/Revenue	17.5%	17.1%	17.7%	18.1%
Hungary				
VAT/GDP	8.0%	7.9%	7.8%	8.3%
VAT/Revenue	22.2%	24.5%	23.3%	25.1%
Georgia				
VAT/GDP	1.2%	1.7%	2.4%	4.1%
VAT/Revenue	28.5%	28.9%	27.8%	42.2%
Kyrgyzstan**				
VAT/GDP	4.3	4.4	5.5	6.0
VAT/Revenue	20.7%	26.1%	32.3%	39.3
Ukraine				
VAT/GDP	11.4%	8.5%	7.8%	8%
VAT/Revenue	25.2%	21.5%	20.8%	21.5%
Russia				
VAT/GDP	5.9%	5.1%	5.7%	
VAT/Revenue*	24.5%	24%	25%	

* The ratios are shown for tax-only revenues

** Until the end of 1996 there was also a turnover tax in Kyrgyzstan which functioned together with VAT. If we combine these two taxes the ratios of VAT to GDP and VAT/Revenue will be the following: in 1994: 4.7 and 22.8; in 1995: 5.4 and 32.3; in 1996: 35.3 and 6.0

Source: IMF, Kyrgyz Republic: Recent Economic Developments, January 1998

Magdalena Tomczyńska: "Comparative Analyses of Direct Tax Systems..."

Jarosław Neneman: "The Reform of Indirect Taxation in Hungary..."

I. Sinicyna, "Fiskalnaya polityka i organizacija sfery gosudarstvennyh finansov v Gruziji"

It can be seen that in all analyzed countries (except for Ukraine) the importance of VAT in budget revenues has been growing during the recent years. This is connected with time that is needed for the completion of the tax reform and the adjustment of economic agents. For Poland, Czech Republic and Hungary the level of

VAT/GDP ratio and VAT/revenues ratio is quite stable while for Georgia and Kyrgyzstan it changes substantially. Georgia is an interesting example. After the collapse of the FSU and two civil wars, the state of public finances in this country was very bad. Even today, the total budget of Georgia stays close to the level of 10 percent of GDP. Revenues from VAT are the main source of the budget (42 percent in 1997 compared with 28 percent in 1994) and if we take only tax revenues the importance of VAT is even greater (about 60 percent of all tax revenues [4]). Kyrgyzstan also has a very big share of VAT in budgetary revenues. The reason is that VAT collection does not function properly in these two countries. In Georgia for example, VAT is often treated as a turnover (gross) tax (without effective tax credit mechanism) because there is lack of adequate executive acts.

The ratio of VAT collection to GDP in Georgia and Russia is very low compared with Poland, Czech Republic, Hungary, or Ukraine. It can be said that the tax base in these countries is quite narrow or (which is more probable) tax avoidance and abuse of the system is widespread.

Some goods (so called luxury goods) are taxed with higher rates than other goods. However, the number of these goods is limited and applying different VAT rates to them would distort the system of VAT collection. To avoid distortions, a special tax that accompanies VAT is introduced. This tax is an excise duty. In some countries, revenues from excise taxes are important budget item. In Kyrgyzstan, they amounted to 12.7 percent of budget revenues in 1995, while in 1996 to 8.6 percent. In Poland, Czech Republic and Hungary revenues from excise taxes range from 10 to 15 percent of total tax revenues, while in Ukraine and Georgia revenues from excise tax stay below the level of 5 or 6 percent.

3.2. Comparison of Legal Solutions

For the majority of industrialized countries, the basic rates of VAT range from 15 to 22 percent. The countries of CEE as well as FSU followed experiences of the Western countries and set the rates at 20 percent or a little bit higher.

In Russia, Kyrgyzstan, Ukraine and other CIS countries, the basic rate was set at 28 percent in the beginning of transition period (1992) and then reduced to 20 percent.

Below you will find the rates of VAT in selected countries (see Table 3).

The rules of VAT are almost the same everywhere. Different solutions may apply to exemptions, number of rates, tax base. The differences in basic rate of VAT are not big. Except for Czech Republic, in all countries there still exist preferential rates (zero

[4] Special funds (foreign grants or their equivalent) contain a big share of budget revenue.

Table 3. Rates of VAT (standard rate in bold)

Country	Rates in %
Poland	22 , 7, 0
Czech Republic	22 , 5, 0
Hungary	25 , 12, 0
Georgia	20 , 10, 0
Kyrgyzstan	20 , 0
Ukraine	20 , 0
Russia	20 , 10

Source: Tax codes of the selected countries

percent) [5]. However, the number of goods and services covered by this rate as well as the number of goods and services exempted from VAT is being reduced systematically.

4. Personal Income Tax

Introduction of PIT was the second crucial aspect of reform of state finances. From the social and political point of view, introduction of PIT is more important than changing from turnover tax to VAT. Apart from the fact that it regulates aspects connected with different sources of incomes, it also has a psychological and educational influence [6].

Table 4. PIT Revenues as percentage of GDP

Country	1994	1995	1996	1997
Poland	9.8	9.8	9.2	
Czech Republic	5.3	5.5	5.3	
Hungary	6.5	6.5	5.9	
Georgia	0.2	0.6	0.9	0.5
Kyrgyzstan	1.9	1.8	1.3	1.3
Ukraine	3.0	3.0	3.3	3.7
Russia	2.9	2.2	2.4	

Source: IMF Kyrgyz rep. recent economic developments. 1998; Magdalena Tomczyńska: "Comparative Analyses of Direct Tax Systems..."; Jarosław Neneman: "The Reform of Indirect Taxation in Hungary..."; I.Sinicyna, "Fiskalnaya polityka i organizacja sfery gosudarstvennyh finansov v Gruzji"; Ministry of Finance, Ukraine

[5] In Poland and Hungary it is planned to abolish them.

[6] People become interested how their money is spent and must learn how to deal with all tax forms, deductions etc

In Poland, Czech Republic and Hungary the revenues from PIT as percentage of GDP have declined (see Table 4). It is a result of overall decline of total budget revenues as percentage of GDP. The ratios in these countries are much higher than in Russia, Georgia or Ukraine. They are comparable to ratios in some of Western European countries (such as France or Spain). Very low ratios for Georgia, Russia, and Ukraine may result from the fact that majority of people does not pay taxes and there are many exemptions from PIT. Although the share of revenues from PIT has been rising, it is not stable. The reason for this is continuous changes in legislation, which are aimed at producing higher revenues when other sources of revenue do not give expected results.

PIT tax scales in the selected countries have similar, progressive structure. The differences refer to numbers of tax rates, exemptions, and marginal rates.

Tax rates range from 19 percent to 40 percent in Poland; 15 to 40 in Czech Republic; 20 to 42 in Hungary; 12 to 20 in Georgia; 10 to 40 in Ukraine; 5 to 45 in Kyrgyzstan, and 12 to 35 in Russia. In some countries, like Kyrgyzstan or Ukraine, the rates are linked to minimum annual wage while in the other the brackets are set in nominal terms of a country's currency.

An important issue from the point of view of simplicity of the system is the number of tax rates. In described countries, this ranges from 3 (for Poland) to 8 (in Kyrgyzstan). In the Czech Republic, there are 5 rates, in Hungary 6, and in Georgia 4 rates of PIT.

The main differences regarding PIT are connected with tax base and exemptions. Tax base should be designed in such a way to capture possibly all different sources of incomes. However, in each country some exemptions exist. A detailed information about legal solutions in selected countries are presented in chapter 6. Here I will mention only a few, most important ones. Poland is the only country where pensions and disability pensions are subject to PIT. In the rest of countries, they are free from PIT. In Kyrgyzstan, incomes of people working in the Ministry of Internal Affairs and Ministry of Defense are not included in the tax base. In Ukraine, miners pay PIT at a preferential, flat rate of 10 percent.

5. Corporate Income Tax

Looking at Table 5 one can notice a big difference between Poland, Czech Republic, Hungary on the one hand, and the countries of the former Soviet Union on the other. For Poland, Czech Republic and Hungary the ratios of corporate tax revenues to GDP are

below 4 percent while for Ukraine and Russia they are above 5–6 percent and 7 percent respectively. In the countries of the FSU, corporate tax was the main workhorse of budget revenues. In Western countries revenues from corporate tax account for about 10 percent of total tax revenues while in Russia they amounted to 30 percent of total tax revenues in 1994 and to 27 percent in 1995. Unfortunately, we do not have information for Kyrgyzstan but we can suspect that the situation is quite similar to Russia and Ukraine.

Table 5. Corporate Tax Revenue as percentage of GDP

Country	1994	1995	1996	1997
Poland	3.4	3.3	3.1	
Czech Republic	6.4	5.4	4.1	
Hungary	1.9	1.9	1.9	
Georgia	0.8	0.8	0.6	0.4
Kyrgyzstan	3.5	2.6	1.6	1.3
Ukraine	12.5	9.1	6.8	5.2
Russia	7.7	7.93		

Source: IMF Kyrgyz rep. recent economic developments. 1998; Magdalena Tomczyńska: "Comparative Analyses of Direct Tax Systems..."; Jarosław Neneman: "The Reform of Indirect Taxation in Hungary..."; I.Sinična, "Fiskalnaya polityka i organizacija sfery gosudarstvennyh finansov v Gruziji"; Ministry of Finance, Ukraine

In all countries, the ratios of corporate tax to GDP have been falling in the recent years but reasons differ between CEE and FSU countries. For Poland, Czech Republic and Hungary the reason is that the main tax burden was switched to consumption taxes (mainly VAT) and the rates of corporate taxes have been systematically reduced. For Russia and Ukraine the reason for a decline in revenues relatively to GDP is rather caused by poor financial standing of enterprises, ad-hoc adopted tax measures and changing economic environment (i.e. changing laws). The same reason holds for Georgia but here additionally the tax avoidance (connected with a big share of underground economy) plays a crucial role.

Needless to mention that in the FSU the behavior of authorities is ambiguous and depends on the budget situation. On one hand, many state-owned enterprises enjoy tax exemptions or forgiveness of debts while other enterprises (the ones with good financial standing) suffer from higher than average tax burdens. In the FSU the authorities tended not to look for additional sources of budget financing but rather tried to collect taxes in the easiest possible way, that is to execute taxes from enterprises controlled by the state. In many instances, such an approach caused even bankruptcy of enterprises.

6. Legal Systems

6.1. Value Added Tax

Georgia

Georgia implemented VAT in 1993 when it replaced the turnover tax and sales tax.

The base rate for VAT is 20 percent and it applies to each company with the annual turnover of 2000 Lari or more. For bread and flour, the rate is 10 percent. For goods produced outside CIS, which are to be re-exported, the rate is 0 percent. For imported goods the rate is 20 percent but food for children, and machinery for export oriented companies are exempted. Goods imported from CIS are also exempted, except for petrol.

During the years of 1996–1997, many exemptions from VAT were withdrawn and now they apply only to a limited range of activities [7]. However, the system of tax collection in Georgia is very weak and the abuse of the system is common.

Kyrgyzstan

The rate of VAT is 20 percent and applies to each legal entity with annual turnover above the level determined by the government. Some sorts of activities are free from the VAT. It relates, for example, to: lease of land (unless the land is used as a parking place), lease of real estate (unless the real estate is used as a hotel, motel or a parking place), agricultural production, financial services (like management of investment funds, foreign exchange operations, operation with securities and bonds, operations connected with transfer of money, life insurance and pension insurance [8]), transportation (except for taxi services), services provided by post-offices and municipal services (energy, water etc). In addition, services provided to and by non-commercial organizations are free from VAT [9].

There are also several exceptions connected with import of goods. This relates to humanitarian aid, imported goods, which are to be re-exported within 12 months, goods in transit, goods, which were earlier exported and now are imported by the same company, teaching aid, food for children, medicines.

[7] Among others: operations with deposits, provision of credits, operation with securities, re-export of goods, transit of goods, house rent, transportation (excluding taxi), food for children, insurance services, school books.

[8] However, services provided by financial consultants, lawyers etc. are not free from VAT.

[9] This applies to education, health, sport, science and culture.

Goods exported are taxed with zero rate unless they are exported to the member states of CIS.

Ukraine

VAT was introduced in Ukraine quite early, in 1992 but was not accompanied by the proper administrative preparation. VAT replaced a turnover tax and sales tax. Initially the rate was 28 percent and there were only few exemptions. However, a number of exemptions grew steadily. Imported goods were subject to VAT only if they were sold. In 1994, the rate of VAT was reduced to 20 percent but substantial exemptions were given to coal industry, energy sector, securities, and foreign exchange transactions, insurance premiums and other services.

Russia

The law on Value Added Tax was introduced in December 1991. All the legal entities and individuals running their own businesses were payers of the VAT [10]. The standard rate of VAT was 28 percent while the reduced rate was 15 percent. Financial, education and religious services were free from VAT. Apart from those, the following items were exempted: exported goods and services, city transportation, housing rents, research and development services ordered by state, production of some sorts of food, goods produced in enterprises in which more than 50 percent of the employed were disabled people.

In the end of 1992, new laws were adopted. From January 1, 1993, the rates were reduced: to 10 percent for goods for children and food, and to 20 percent for other goods. Starting from February 1993, imported goods (except for food, medical equipment and scientific equipment) were subject to VAT (VAT was calculated on the basis of the border value increased by customs duty and excise tax). A new list of goods and services exempted from VAT was created (the list remained unchanged until the beginning of 1995). It covered: exported goods and services, value of state owned enterprises' property, which was bought in the course of privatization, value of people's flats and houses, operations with foreign exchange and money (except for brokerage and intermediation services), services in housing construction, education and R&D sphere, sport, theater and entertainment events, turnover of casinos and slot machines, value of cultural and socially important property [11], medicines and medical services, goods and services produced in enterprises in which more than 50 percent of the employed were disabled people.

[10] In 1992 it applied to individuals running their own businesses and the turnover over 0,5 million RRb.

[11] Kindergardens, sports clubs, sanatoria etc.

In 1994, two main changes took place. Firstly, all the financial sources received from other enterprises (except for funds paid in as charter capital and funds for mutual activity) were subject to VAT. Secondly, individuals running their own businesses became exempted from VAT. In addition, from January 1, 1994 a special tax for financing different branches of the economy was introduced. The revenue from that tax was used according to government's decision. The rate of the tax was 3 percent [12].

In the beginning of 1995, the 3 percent tax was reduced to 1.5 percent and from 1996, it was supposed to be abolished. Some changes were made in VAT exemptions. Services in the sphere of housing construction were no longer free from VAT.

According to new Presidential Directives (from May 1997) the following goods are free from VAT: goods imported to Russia as input to charter capital of companies with foreign capital, technical equipment imported for the purposes of medical production, goods related to technical assistance, exported goods, services of transportation of foreign commodities through the territory of Russia, exported goods.

Poland

The law on VAT and excise tax was introduced in July 1993. It replaced the old laws from 1972 (law on turnover tax) and 1982 (law on taxation of state enterprises). The sale of goods and services on the territory of Poland is the base of taxation [13]. Enterprises and individuals running their own businesses are exempted from VAT if their annual turnover is smaller than 80 000 PLN (c.a. 23 000 USD). The rates of VAT are 22; 7; and 0 percent. The reduced rate (7 percent) applies to the following goods and services: equipment for disabled, medical equipment, goods for children, most of foodstuff, good connected with health protection, publishing of books and newspapers, construction, telecommunication, transport (except for public municipal transport and Taxi). The zero rate applies to inputs for agriculture, and to export. Exemptions cover: unprocessed agricultural products, handcraft, services in banking, insurance, postal services, TV, radio, public municipal transport, taxi, education, health and social care, water supply, services in R&D, services connected with culture, sport and recreation.

The list of goods that are subject to excise tax covers among others: crude oil and petrol, weapons, cars, alcohol, beer, wine, salt, jewelry, yachts, chewing gum, tobacco and cigarettes, fur-coats, electronic equipment and video cameras. The rates of excise tax may range from 25 percent to 95 percent for producers and from 40 percent to 1900 percent for importers [14].

[12] For many enterprises this tax meant an additional 3 percentage points higher VAT.

[13] The following items are also subject to VAT: barter of goods and services, provision of goods and services instead of money.

[14] The highest rates apply to alcohol and petrol.

Czech Republic

VAT was introduced in the Czech Republic in January 1993. There were three rates: 23, 5 and 0 percent. The rate of 23 percent was reduced to the level of 22 percent and nowadays there exist three rates: standard rate of 22 percent and two reduced rates (5 and 0 percent). There exist also some exemptions from VAT. The taxpayers of VAT are firms with annual turnover of more than CZK 750 000 which is a bit more than USD 22 000. Below you will find the break down of goods and services subject to different rates of VAT.

The following goods and services are taxed with the standard, 22 percent rate:

- all goods with only a few exceptions,
- services: wholesale and retail sale, accommodation and catering, road freight transport, commercial services.

The reduced, 5 percent rate applies to: live animals, meat, fish, milk and dairy products, oil, sugar, books, pharmaceuticals, newspapers, medical instruments, equipment for disabled, and other services not mentioned above.

The zero rate applies to export.

The following services are exempted from VAT: banking, insurance, postal services, radio and TV broadcasting, sale and lease of buildings (except for newly constructed), education, health and social care.

Hungary

Hungary introduced VAT very early – in January 1988. At the beginning there were three rates: a standard rate of 25 percent, and two reduced rates (15 and 0 percent). The reduced rate of 15 percent was then changed into 12 percent. The threshold for paying VAT is HUF 2 million (ca. USD 9000). As everywhere, there are some exemptions from VAT. These are: agriculture, education, postal services, radio, and TV broadcasting, culture.

Zero rate covers exports, pharmaceuticals and human nutrition products. The reduced rate of 12 percent applies to: electricity, gas, water, medical instruments, books, newspapers, dairy products, meat, vegetable oil, and accommodation services. The rest is subject to the standard rate of 25 percent.

6.2. Personal Income Tax

Georgia

Personal income tax is a weak component of the tax system in Georgia. Revenues from that tax accounted for 15.8 percent of the total budget revenues in 1995 and only around 8 percent in 1997. The tax base includes income received from permanent job,

income from contracted job, income from individual business activity. Tax inspection can determine the amount of tax due using three sources of information:

- declarations of individual people,
- materials from controls of individuals' activities,
- data about actually paid salaries received from enterprises, organizations and individuals.

During the years 1995–1997 the rates of personal income tax changed several times. In 1997, a new scheme was introduced. The rates range from 12 percent to 20 percent but the 12 percent rate applies only up to 200 Lari of annual income (see Table 6) [15].

The following items are not included in the income subject to taxation:

- state social benefits (e.g. disabled benefits, single mothers),
- pensions,
- per diems,
- unemployment benefits,
- income from Georgian or foreign state securities,
- interest from bank deposits,
- alimony,
- income from the sale of property unless it is a part of economic activity,
- income from the sale of agricultural products,
- grants and scholarships.

The rate for dividends is 10 percent.

Table 6. Rates of Personal Income Tax in Georgia

Annual income	Tax rate
up to 200 Lari	12%
201–350 Lari	24 Lari + 15% of income above 200 Lari
351–600 Lari	46.5 Lari + 17% of income above 350 Lari
above 601	89 Lari + 20% of income above 600 Lari

Source: I.Sinicyna, "Fiskalnaya polityka i organizacija sfery gosudarstvennyh finansov v Gruziji"

Although the system of individual declarations was introduced in 1993 the number of declarations received by the tax service is very low (in 1996 it was only 7 thousand declarations). Taking into account that most of revenues comes from enterprises employing workers we can say that actually it is a tax on salaries and not on income.

[15] It is about 25 percent of a minimum surviving level.

We must remember that according to official data, salaries account only for about 35 percent of people's income, which means that most of personal income stays untaxed.

Kyrgyzstan

Farmers for whom land is the main source of their income pay only a land tax. Others must pay personal income tax. One can deduct the amount equal to 4 minimum salaries from a gross income. The following incomes are free from PIT:

- alimony,
- insurance compensation,
- income from sale of fruits and vegetables coming from small plots of land,
- subsidies, pensions, social benefits, scholarships paid by the government,
- interest on bank deposits,
- income of disabled people and those who participated in WWII,
- per diems,
- income of people working for the Ministry of Internal Affairs, Ministry of Defense.

The rate of personal income tax range from 5 to 40 percent (see Table 7). The brackets are determined by the amount of minimum wage. The 5 percent tax is for incomes lower or equal to 5 times the minimal annual wage. The maximum, 40 percent tax is for incomes higher than 105 times the minimal annual wage.

Table 7. Rates of Personal Income Tax in Kyrgyzstan (1998)

Annual Income	Tax rate
up to 5 times minimum annual wage	5%
between 5 and 15 times minimum annual wage	tax from 5 times minimum wage + 10% of income above 5 times minimum wage
between 15 and 25 times minimum annual wage	tax from 15 times minimum wage + 15% of income above 15 times minimum wage
between 25 and 45 times minimum annual wage	tax from 25 times minimum wage + 20% of income above 25 times minimum wage
between 45 and 65 times minimum annual wage	tax from 45 times minimum wage + 25% of income above 45 times minimum wage
between 65 and 85 times minimum annual wage	tax from 65 times minimum wage + 30% of income above 65 times minimum wage
between 85 and 105 times minimum annual wage	tax from 85 times minimum wage + 35% of income above 85 times minimum wage
above 105 times minimum annual wage	tax from 105 times minimum wage + 40% of income above 105 times minimum wage

Source: Tax Code of the Kyrgyz Republic

Ukraine

Personal income tax was introduced in mid 1991. The tax has changed over the period of 1991–1996 several times and the rate ranged from 0 percent to 90 percent (see Table 8) depending on the level of income relative to minimum wage. In 1992 the rates ranged from 0 percent (for incomes below one minimum annual wage) to 30 percent, while in 1994 the top marginal rate was 90 percent (income above 50 times minimum annual wage) but in the end of 1994 was reduced to 40%. Several items are exempted from PIT. These are: social security benefits, pensions, social insurance, alimony, incomes of veterans, income from sale of property, income from private farm plots, gift and inheritances. Dividends are taxed at the rate of 15 percent. Miners are taxed at a flat rate of 10 percent.

Table 8. Rates of Personal Income Tax in Ukraine

Year	1993	1994	1995	1996 and 1997
Rates of PIT	0, 10, 20, 35, 50	0, 10, 20, 30, 40, 60, 90	0, 10, 20, 30, 40, 50	0, 10, 15, 20, 30, 40

Russia

A law on personal income tax was introduced in the USSR in 1990. It was based on information from enterprises and individual declarations on other sources of income. The base rate of tax was 12 percent and the upper rate was 30 percent. In 1992, a new law on PIT was implemented in Russia. The objective of the law was to cover as many sources of income as possible. Incomes included: salaries, value of gifts and prizes, value of property received by workers in the course of enterprise's liquidation and others. In 1992, the rates were changed twice. Till the middle of the year the rates ranged from 12 to 60 percent and from July 1992 from 12 to 40 percent [16]. In 1993, there were the following rates: 12, 20, and 30 percent depending on the income. The same rates stayed in 1994 and 1995, only income brackets changed [17]. In 1997 some changes were made. The number of rates was increased and the brackets changed. In 1998 the tax scheme was the following:

Annual income	Tax rate
up to 20 000 rubles	12 percent
from 20 001 to 40 000	2 400 rubles plus 15 percent of the amount above 20 000
from 40 001 to 60 000	5 400 plus 20 percent of the amount above 40 000
from 60 001 to 100 000	14 400 plus 30 percent of the amount above 60 000
from 100 001	20 400 plus 35 percent of the amount above 100 000 rubles.

[16] However, the new rates were valid from January 1, 1992.

[17] The upper limit was increased 5 times (to 50 million RRb).

Poland

The law on Personal Income Tax was approved by parliament in 1991, being effective from January 1, 1992. In 1992 and 1993 the rates of PIT were: 20, 30, and 40 percent. In the years 1994–1996 the rate changed to 21, 33, and 44 percent and in 1997 to: 20, 32, and 44 percent. From 1998, the rates amount to 19, 20, and 40 percent. The following source of income are included to the tax base: income from dependent activity (employment), pensions, income from entrepreneurial activity, independent activities and activities carried on personally, income from leasing (or rental income), income from capital and property rights, income from real estate or parts of real estate. Some items are subject to special rates and are not cumulated with other source of income. Income from interest on loans, dividends, and other revenue coming from share in the legal person's profits is taxed with proportional rate of 20%, winnings in competitions and games with rate of 10%, remuneration for providing assistance to the Police, and fiscal control authorities at 20%, income from the sale or exchange of real estate and property rights (10%). Income from unrevealed sources or not justified by the revealed sources is taxed with penalty rate of 75%. There are about 60 items that are exempted from PIT: social benefits (family allowances, childcare and maternity allowances, death benefit and funeral allowances), payments resulting from insurance claims, winnings from lotteries and games of chance operated on the basis of a granted license, interests and discounts on securities issued by the State Treasury, on bonds issued by local self-government units, interests on savings and deposits in bank accounts, except those kept in connection with non-agricultural economic activity, income from the sale of National Investment Fund shares, revenues from shares in trust or investment funds. There are also deductions from the taxable income (like disability pensions, social insurance premiums, donations) but the authorities tend to reduce the list of possible deductions and exemptions.

Czech Republic

There are five rates of PIT in the Czech Republic. These are: 15, 20, 25, 32, and 40 percent. The income that is free from taxation is c.a. USD 1000 and the highest marginal rate (40 percent) applies to incomes above c.a. USD 24 000.

The following types of income are subject to PIT:

- salary,
- income from independent activity,
- income from leasing, capital and property rights,
- income from real estate,
- income from agricultural production,
- income gained from the sale of real estate.

There are special categories of incomes that are taxed with different rates. Dividends are tax with 25 percent rate, winnings from lotteries with 20 percent, income from author's articles for newspapers – 10 percent.

Some items are exempted from PIT. These are:

- income from the sale of real estate providing that the period between the acquisition and sale is longer than five years,
- scholarships,
- income in the form of social benefits, pension insurance, unemployment benefits, health insurance,
- income from the sale of securities if the period between their acquisition and sale exceeds six months.

Hungary

In Hungary, there are six PIT rates: 20, 22, 31, 35, 39, 42 percent [18]. The amount of income that is free from tax is around USD 200. The top rate applies to income of more than USD 5000. The tax base consists of income from dependent activity (salaries) and independent activities (like agricultural production, income from running own business), and additionally from payments provided by private pension funds, voluntary mutual funds.

The following items are exempted from PIT:

- family allowance, maternity allowance, social aid, income earned in imprisonment,
- financial support for housing provided by local government,
- money received from foundation for the purposes of research or study,
- income of agricultural producers that do not exceed HUF 1 million (c.a. USD 5000).

Similar to Polish regulations, in Hungary there are items that are deductible from payable income. These are, among others:

- payments to private pension funds,
- payments to mutual funds (up to 50 percent of total payments to supplementary pension fund, 25 percent to supplementary health insurance fund),
- 30 percent of tuition fees of university students (but not exceeding HUF 60000 per year),
- HUF 1500 monthly for disabled people,
- 30 percent of donations for mutual insurance funds,
- 30 percent of donations for organization of public service.

[18] In 1998.

6.3. Corporate Income Tax (CIT)

Georgia

CIT was the most important tax in all socialist countries. Due to economic changes and a decline in output, the importance of this tax has fallen in the recent years. While in 1993 it accounted for 40 percent of budget revenues, in 1997 it was only 4 percent.

In the years 1995–1996 there were different rates for small firms (up to 20 sq. meters) and big companies. The latest had to pay a 20 percent rate while small firms paid quotas (156 Lari up to 12 sq. meters plus 12 Lari for each additional meter). It changed in 1997 when an obligation for a small business to keep accounting books and unified rate of 20 percent of corporate tax was introduced.

Newly established firms could also obtain tax vacations (exemption from VAT for the first year and only half of VAT obligations during the second year) but they were cancelled in 1996.

Kyrgyzstan

The standard rate of the CIT is 30 percent. Firms which employ 70 [19] or more percent of workers who are blind or deaf, and legal entities for which land is the main source of production are exempted from CIT (the latter pay only the land tax).

The CIT rate for dividends and interest earned is 5 percent. This however does not apply to interest paid by domestic banks or interest from state securities.

Different rates are envisaged for non-resident legal entities. They must pay: 15 percent on dividends and interest, 5 percent on incomes earned on telecommunication and transportation services, 30 percent on other incomes such as management and consulting services, lease of land.

Ukraine

Enterprise income tax was introduced in 1992 and the rates and system of calculating changed several times over the period of 1992–1996. In addition, the definition of tax base was subject of frequent changes. In 1992, the rate was 35 percent of profit. In 1993 the rate was 18 percent but was calculated on the basis of gross income that included the wage bill. In 1994, the rate was changed to 22 percent of gross profit. However, the managers of the companies tended to avoid taxes by increasing wages and salaries. In 1995 a new, 30 percent rate was adopted. This time wages were made deductible and the rate applied to net profits.

[19] According to the new project this will be changed to 50 percent.

Russia

The reform of corporate tax structure started in 1984. In 1990, a unified rate at the level of 45 percent for all enterprises was introduced. However, the rate of actually paid tax depended on the profitability of an enterprise. It was a progressive tax with marginal rate of 90 percent. In the end of 1991, a new rate of 32 percent was introduced and the progressive rates abolished [20]. The wage bill was restricted – wages higher than certain level (set in relation to minimum wage) could not be counted as costs of production (i.e. they were subjects of CIT). In 1994 the rate increased to 35 percent in the first quarter and to 38 percent in the second quarter (13 percent was transferred to the federal budget and 25 percent [21] to local budgets). At the same time new exemptions were introduced. For example, banks did not have to pay the tax on profit gained from long term (more than 3 years) credits. In addition, the list of enterprises exempted from paying the corporate income tax was broadened. In 1995 a maximum rate of tax owed to local budget was set at 22 percent for enterprises and 30 percent for exchanges, intermediaries, brokerage offices, banks and insurance companies.

In general, the CIT rate is of 35 percent, although it can be higher for some types of activities (e.g. 43 percent for banking). Since 1996, the tax consists of a 13 percent Federation tax and a tax up to 22 percent for regional authorities. The latter rate can be a subject to negotiation between the particular company and the regional authorities.

For some types of businesses there exists a two-year tax holiday (for small companies employing not more than 200 people). These apply mainly to construction of residential and industrial projects and public works.

For the following circumstances, the Law envisages profit tax exemptions:

- some transactions between parent company and subsidiaries,
- donations by foreign states or organizations for culture, education and science,
- funds transferred within a company for the development of infrastructure.

Poland

The Law on Income Tax of Legal Entities (Corporate Income Tax) was introduced first time in 1989. Until 1996, the rate of corporate tax was 40 percent. In 1997, it was lowered to 38 percent, in 1998 – to 36 percent. From 1999, the rate amounts to 34 percent and from the beginning of 2000 – 32 percent. Certain organizations are exempted from this tax. These are: the State Treasury, the National Bank of Poland, budgetary units, international organizations, the Agency for Restructuring of Agriculture, the Agency for Highways Construction, the Agency of Agricultural Market, investment funds, retirement pension

[20] The rate for intermediary operations, profits of exchanges and brokerage offices was 45 percent.

[21] For banks and insurance companies the rate was 30 percent.

funds. There are also some exemptions from this tax (income of taxpayers, co-operatives and companies whose statutory objects consist in scientific, technical research and educational activity, cultural activity, activity in the environment protection, charity, health protection and social aid, income of church legal persons, income of trade unions, organizations of employers and political parties – with the exclusion of economic activity, income received by taxpayers who employ disabled persons).

Czech Republic

In the Czech Republic, the CIT has been systematically reduced from the level of 45 percent in 1993 to 39 percent in 1997 and 35 percent in 1998. The following organizations do not have to pay CIT:

- the Czech National Bank,
- Deposit Insurance Fund,
- National Property Fund, Land Fund,
- Children's and Youth Fund,
- Agriculture and Forest Support Fund.

Some incomes are exempted from CIT. Among others: membership fees received by associations, trade unions, political parties, income from collection in churches, interest on mortgage bonds, income from the operation of small hydroelectric power plants, solar-powered facilities, income on savings and other yield on bank deposits.

From the tax base, a company can deduct the following items:

- 10 percent of input price of tangible assets,
- 15 percent of input price of agricultural and forestry machinery,
- some kind of donations.

Hungary

Hungary reduced the CIT rate to 18 percent in 1995 (from the level of 40 percent in 1993 and 36 percent in 1994). This rate still holds.

The CIT does not apply to the following organizations:

- the National Bank of Hungary,
- State Privatization and Property Holding Agency,
- public media companies (state-owned radio and TV),
- Hungarian News Agency,
- political parties,
- foundations, social organizations,
- voluntary mutual insurance funds if their revenue from supplementary (commercial) activity does not exceed 20 percent of their total revenue in a given year.

6.4. Excise Tax

Georgia

Revenues from excise tax grow very rapidly in Georgia. In 1997, they accounted for 12 percent of budget revenues while in 1995 for only 5 percent. This happened mostly due to tighter controls on the borders. Even though the rates for some goods have been reduced recently, the overall sum of tax collection is growing. The following goods are subject to excise taxes: alcoholic beverages, vodka, wine, champagne, beer, tea, chocolate, caviar, cigarettes, jewelry, carpets, leather clothes, cars, gasoline. The rates range from 15 to 100 percent (see Table 9). Goods imported from the CIS are free from excise tax except for gasoline.

Table 9. Rates of Customs duties and Excise Tax in Georgia

Goods	Customs duty in %	Excise Tax in %
Food for children	–	–
Grain	–	–
Wheel chairs	5	–
Machinery	5	–
Wheat	12	–
Beer	12	15
Cars	12	15
Tires	12	15
Petrol (including CIS)	12	15
Wine	12	20
Jewelry	12	35
Brandy, vodka	12	50
Tobacco (3rd and 4th class)	12	55
Tobacco (1st and 2nd class)	12	100
Cognac, whiskey	12	100
Rectified alcohol	12	100

Source: I.Sinicyna, "Fiskalnaya polityka i organizacija sfery gosudarstvennyh finansov v Gruzii"

Kyrgyzstan

The rates of excise tax and the list of goods are proposed every year by the Ministry of Finance and approved by the government. In 1996 the following goods were covered by the list:

- vodka, wine, liquor, cognac, beer, champagne,
- tobacco, cigarettes,
- jewelry,
- fur and leather clothes,
- goods made of crystal,
- weapons (except for those used by the state organs),
- carpets,
- crude oil and gasoline products.

The excise tax applies to goods produced in Kyrgyzstan (except for goods exported outside CIS) as well as to imported goods.

Ukraine

Excise tax was introduced in 1991 with 21 categories of goods that were considered as luxury goods. Alcoholic drinks, tobacco and cigarettes, jewelry, cars, carpets as well as sugar and chocolate were among them. The rates ranged from 10 to 85 percent.

Czech Republic

The main items covered by excise tax are the following:

- petrol (CZK 12 950 per tone),
- diesel oil (CZK 8 700 per tone),
- alcohol and spirit (CZK 234 per liter),
- beer (CZK 24 per hectoliter for each percent of original malt extract),
- wines (CZK 2,50 – 16,4 per liter),
- cigarettes (CZK 0.64 or 0.74 per unit depending on size).

Hungary

The list of goods subject to excise tax covers:

- jewellery and precious metals (excluding silver) (35 percent),
- coffee (12%),
- cars (10% and 20% for car with engines bigger than 1600 cc),
- wine (11%),
- mineral oil (including petrol and diesel): HUF 77–83 per liter,
- tobacco,
- beer (HUF 60 per hectoliter for each percent of original malt extract),
- alcohol (HUF 1270 per hectoliter).

Poland

The main items subject to excise tax are the following:

- mineral oils (including petrol and diesel) – PLN 664 – 1153 per tone,
- alcohol (PLN 5174 per hectoliter of 100% alcohol),
- cigarettes (PLN 50–76.5 per 1000),
- beer (PLN 5 per hectoliter for each percent of original malt extract),
- wine (PLN 100 per hectoliter),
- weapons (20%),
- salt (15%),
- jewellery (25%),
- yachts (20%),
- audio–video cameras (10%),
- fur coats (20%),
- perfumes and chewing gum (20%).

7. Conclusions

It seems that countries from Central and Eastern Europe are more advanced in their tax reforms than countries of the former Soviet Union. The first ones already have the structure of tax revenues similar to Western countries while in the latter a pattern of socialist budget still prevails. In the FSU, there is room for improvement but this can only take place when accompanied by structural adjustments, like liberalization and deregulation of economies that would enable equal treatment of all economic agents.

In all the countries, a lot can be done to increase budget revenues. First, through broadening of tax base and secondly, through abolishment of deductions and exemptions. However, both these tasks are very difficult to implement. The lack of structural reforms and restructuring of many enterprises hamper the broadening of the tax base because these enterprises still function according to the old rules, and thus, they are not profitable and do not produce revenues for the budget. On the other hand, enterprises do not want to restructure and give up their privileges. Instead of restructuring, they prefer political lobbying.

In the FSU, there is also an issue of enforcement of existing laws. Although the countries have bankruptcy laws, they are executed very seldom. The authorities use different kinds of measures (e.g. tax obligations are postponed or forgiven) to let enterprises survive. This causes distorted allocation of resources or even a lack of

allocation. Such an approach leads to nowhere and only worsens overall situation of these economies.

The final issue is a continued process of changing of tax systems. It is true that transformation from planned economy to market oriented one needs time and a perfect tax system does not exist but the majority of policymakers seems not to notice that the sooner stable rules are implemented, the quicker our countries can start to make up for the lost time.

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