COMMENT

Joint Ventures in the Soviet Union:
Problems Emerge*

I. INTRODUCTION

On January 13, 1987, the Presidium1 of the USSR Supreme
Soviet and the Soviet Union’s Council of Ministers2 issued
laws3 that authorized the establishment of joint ventures4 in

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Harvard University.

1. According to the Soviet Constitution, the Presidium is the highest policy
making body of the Soviet Union. KONST. SSSR (Constitution) art. 118-20 (USSR).

2. “The Council of Ministers of the USSR, i.e., the Government of the USSR, is
the highest executive and administrative body of state authority of the USSR.”
KONST. SSSR (Constitution) art. 128 (USSR).

3. The initial laws consisted of an Edict and a Decree. The Presidium of the
USSR on January 13, 1987, passed the Edict On Questions Concerning the
Establishment in the Territory of the USSR and Operations of Joint Ventures,
International Amalgamations and Organizations with the Participation of Soviet and
Foreign Organizations, Firms and Management Bodies [hereinafter Edict] (the official
The USSR Council of Ministers on January 13, 1987, enacted the Decree On the
Establishment of the Territory of the USSR and Operation of Joint Ventures with the
Participation of Soviet Corporations and Firms from Capitalist and Developing
Countries [hereinafter Decree] (the official Russian text appears in the official gazette,
Sbornie Postanovlenii i Pravitelstva SSSR (1987), no. 9, item 40). The Edict
authorized the formation of joint ventures, while the Decree provided the basic
guidelines for their operation and establishment. Both laws were retroactive to

Many English translations of the laws are available. E.g., Pravda, Jan. 27, 1987, at
2, col. 1 (Eng. ed.); E. THEROUX & A. GEORGE, JOINT VENTURES IN THE SOVIET UNION:
Structure (available at Russian Research Center, Harvard University); The Soviet
Socialist Republics: Decree of Joint Enterprises with Western and Developing
Countries, 26 INT’L LEGAL MATERIALS 749 (1987) [hereinafter Joint Venture Decree];
Union of Soviet Socialist Republics: Edict Concerning Taxation of Joint Enterprises
in the Soviet Union and Dispute Settlement, 26 INT’L LEGAL MATERIALS 759 (1987)
[hereinafter Joint Enterprises].

4. The principle characteristics of a joint venture are the pooling of assets to

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the Soviet Union for the first time in nearly 60 years. The Soviets outlawed joint ventures in 1930 because "foreign control over any sector of the Soviet Union was ideologically unacceptable." However, the promulgation of the new Soviet laws, confirmed in the West in October 1986, was another important move in General Secretary Mikhail Gorbachev’s bold perestroika (restructuring). The main question for potential American investors is whether they can profit under the new joint venture laws, in an atmosphere of perestroika, knowing that such efforts failed in the past.

The primary purpose of this Comment is to examine the problems facing Americans who want to set up joint ventures in the Soviet Union. Before examining the challenges, the


8. Perestroika has three parts: economic reform, economic discipline, and industrial modernization. Though Gorbachev has implemented many plans under perestroika, all three parts must succeed for perestroika to work. Central Intelligence Agency and Defense Intelligence Agency, Report to the Subcommittee on National Security Economics of the Joint Economic Committee, 100th Cong., 2d Sess., Gorbachev’s Economic Program: Problems Emerge 6 (Comm. Print 1988) [hereinafter Gorbachev’s Program].


9. This Comment focuses on the American viewpoint and experiences in dealing with joint ventures in the Soviet Union.

According to Anatoly Belov, chief of the Department of Legal Protection of Foreign Economic Relations in the Soviet Ministry of Justice, two problems are holding up many joint ventures. One problem is the insistence that profits be transferable in hard currency, although made in rubles. A second problem is that the West wants all disputes between the Soviet partners and the foreign investors to be arbitrated by a third party. Trade Policy: Soviet Official Says Western Demands Impede Further Joint Venture Accords, DAILY REPORT FOR EXECUTIVES (BNA) July 21, 1988, No. 140, at 1 [hereinafter Trade Policy].

rationale for the decision to permit joint ventures and the objectives that the Soviets hope to achieve will be addressed. This Comment will then discuss the major provisions of the laws and the major problems these laws have caused for American investors. Finally, the major systemic and political problems confronting joint ventures will be examined.

II. JOINT VENTURES AND SOVIET GOALS

The Soviet decision to permit joint ventures in the Soviet Union is a vital part of *perestroika*. The success of joint ventures and of *perestroika* will depend somewhat on the success of the other. Consequently, one must have a basic understanding of *perestroika* and of Soviet economic problems to fully understand the role of joint ventures and the Soviet decision to permit them.

According to Gorbachev, *perestroika* is a result of Soviet dissatisfaction with the Soviet economy's poor growth rates, which have worsened in the last decade. *Perestroika* is necessary to help close the gap, especially in high technology products, between the Soviet and Western economies caused by this poor growth and development. Moreover, Gorbachev argues that *perestroika* must be implemented immediately. The delay or failure of *perestroika* could cause serious social, economic, and political problems. Thus, Gorbachev has proposed and implemented many economic reforms that are intended to aid the Soviet Union's transformation into an economic superpower.

To become an economic superpower, the Soviet Union must first become a major player in the world economy. Real-

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12. M. Gorbachev, *PERESTROIKA: NEW THINKING FOR OUR COUNTRY AND THE WORLD* (1987). Gorbachev argues that *perestroika* is necessary to bridge "the gap in the efficiency of production, quality of products, scientific and technological development, the production of advanced technology and the use of advanced techniques." *Id.* at 19.

13. *Id.* at 17.

izing this, the Soviets have taken several bold steps to integrate their economy into the world economy. One such move has been the discussion by leading Soviet economists of a freely convertible ruble,15 perhaps by the late 1990s.16 Unfortunately, most Western economists believe a freely convertible ruble is not possible within this century.17 Second, the Soviets applied for membership to the General Agreement on Tariffs and Trade (GATT)18 in October 1986, but were rejected.19 GATT membership would make Soviet goods eligible for tariff reductions and give the Soviets important international economic experience.20 The third and fourth steps were Soviet bids to join the World Bank21 and the International Monetary Fund (IMF).22

Many factors motivated the Soviet decision to permit joint ventures in the Soviet Union. The main factor was the poor

15. A freely convertible currency or hard currency is one that may be exchanged for gold or other currencies with no restrictions. Non-convertible or soft currencies, such as the ruble, are ones whose value is artificial and whose circulation is limited. N.Y. Times, Dec. 4, 1987, at A15, col. 1.
18. GATT is the principal multilateral organization that is designed to reduce barriers to international trade.
21. The International Bank for Reconstruction and Development (the World Bank) helps finance infrastructure development in developing countries.
22. See Jacoby with McCormick, Gorbachev's Prairie Pals, Newsweek, Apr. 6, 1987, at 31. But see Issue Brief, supra note 19, at 14 (reporting that the Soviets have not tried to join the IMF or the World Bank). The IMF was established to provide international exchange rate stability and to coordinate member state financial policies.
performance of the Soviet economy in recent years. This poor performance has exacerbated the Soviet lag in high technology products and has forced Gorbachev to develop a long-term strategy to make the Soviet economy competitive in such industries. A reduction in Soviet hard currency earnings and Soviet disdain for borrowing money from the West made it unlikely that the Soviets would rely on Western high technology imports to solve their problems. Moreover, high technology imports have not helped the Soviet economy become competitive.

A second factor that influenced the decision to allow joint ventures in the Soviet Union was the Soviet desire to avoid a return to the policies of detente. This desire stems from Gorbachev’s belief that detente hurt the Soviet economy. A third factor was that Soviet attempts at turnkey factories and licensing arrangements have not been successful. Finally, the Soviets could not rely on their Eastern European allies for economic assistance because the Eastern Europeans have their

23. Sherr, supra note 14, at 1. As of October 1988, the Soviets had more than 100 joint ventures with foreign partners and more than 500 additional projects were being negotiated. There were only 17 U.S. joint ventures operating at the time, while more than 50 letters of intent had been signed. Trade Policy: More than 300 Soviet Projects Planned to Include Foreign Input, Official Says, DAILY REPORT FOR EXECUTIVES (BNA) No. 193, at 1 (Oct. 5, 1988).

24. Gorbachev’s long-term challenge is to make the Soviet economy competitive in the high technology revolution. M. GORBACHEV, supra note 12, at 27; Goldman, Gorbachev and Economic Reform, FOREIGN AFF., Fall 1985, at 56, 58 [hereinafter Gorbachev and Economic Reform].


26. See McIntyre, supra note 19, at 496.

27. GORBACHEV’S CHALLENGE, supra note 11, at 120. Goldman argues that the Soviets inefficiently use the high technology products that they import from the West. Id.

28. Gorbachev argues that during detente the Soviets discontinued some of their research and development in high technology, naively relying on expanded economic and trade relations with the West to meet their needs. M. GORBACHEV, supra note 12, at 93-94. Moreover, the Soviets believe a vested interest in the Soviet economy by Western firms would reduce the risk of a sudden change in East-West economic relations. Sherr, supra note 14, at 7.

29. Turnkey projects are transactions in which “the contractor agrees to handle every detail of the project including the training of operations personnel. At the completion of the contract, the customer is handed the key to a completed plant that is fully ready for operations.” S. ROBOCK AND K. SIMMONDS, INTERNATIONAL BUSINESS AND MULTINATIONAL ENTERPRISES 468 (1983).

own economic and technological problems, as well as serious political problems. Given these constraints, the Soviets decided that allowing joint ventures in the Soviet Union would be an excellent way to help improve their economy.

Having decided to allow joint ventures, the Soviets have been direct about the place joint ventures will have in perestroika. Ideally, the Soviets want joint ventures to accomplish five goals. First, the Soviets want to gain access to Western high technology. As Marshall Goldman has pointed out, many high technology products have life cycles of only two to three years. Thus, Soviet imports of high technology products have actually worsened the Soviet position vis-a-vis Western economies in high technology industries. The Soviets believe that joint ventures are likely to have the latest technology because American companies, having a vested interest in the ventures' performance, will update the technology in their joint ventures.

Second, the Soviets expect joint ventures to help increase Soviet exports. Gorbachev believes that improving the export sector of the economy is necessary in order to obtain long-term economic improvement, and that joint ventures are crucial in this regard.

The third goal, which is closely related to the second, is import substitution. Import substitution is the reduction of

31. Id. at 3; Gorbachev's Program, supra note 8, at 39.
32. Gorbachev's Program, supra note 8, at 39; Gati, Gorbachev and Eastern Europe, FOREIGN AFF., Summer 1987, at 958 [hereinafter Gorbachev and Eastern Europe]. Gati argues that some leaders of Eastern Europe have taken a wait-and-see attitude toward Gorbachev's reforms, while others are outraged at the move toward capitalism. In either case, these leaders are skeptical about whether Gorbachev will succeed in his reforms. Gorbachev and Eastern Europe, supra, at 959-69.
33. Consistent with Gorbachev's belief that the Soviet Union was hurt by detente, he desires economic ties with the West but wants to avoid dependence. Sherr, supra note 14, at 5.
34. Dean, supra note 5, at 54.
35. Gorbachev and Economic Reform, supra note 24, at 58-59. The reliance on imports, instead of developing the high technology products at home, denies the Soviets valuable research and development. GORBACHEV'S CHALLENGE, supra note 11, at 120. Another drawback of imports is that the Soviets themselves must continually import the newest products, which will make the technological gap close more slowly.
36. Dean, supra note 5, at 54; Sherr, supra note 14, at 7.
37. Dean, supra note 5, at 54.
38. Gorbachev's Program, supra note 8, at 12.
39. The Soviets believe that Western technology will help improve the quality of Soviet goods, which will make them competitive on the world market. Zabijaka, supra note 19, at 7.
40. Dean, supra note 5, at 54; McIntyre, supra note 19, at 500. Stalin also used this
imports and the production at home of these previously imported products. In the long run, the Soviets want to reduce their reliance on imports and increase their exports by substituting products produced by the joint venture.41

The Soviets' fourth goal is for the joint ventures to earn hard currency.42 The Soviets need hard currency to buy goods in the world market because the ruble, the Soviet currency, is a soft currency and, therefore, is not freely exchangeable. The Soviets also must diversify their hard currency earnings because they are too dependent on unreliable sources, namely oil, gas, and weapons sales.43 For example, earnings from oil exports, the Soviets' largest source of hard currency, have been greatly reduced due to the drop in oil prices.44 Similarly, earnings from weapons sales, the Soviets' second largest source of hard currency, fell during the 1980s45 and are not expected to improve in the future.46

Finally, the Soviets hope the joint ventures will provide improved technical and managerial training.47 The Soviet Union has a shortage of competent managers and lacks the facilities to train managers in the newest management strategies. The Soviets believe that Western management expertise and training will help Soviet businesses become more competitive.48

In addition to specifying what they want the joint ventures to achieve, the Soviets have also been specific about the industries in which they want joint ventures to operate. The Soviets want joint ventures in chemical manufacturing, "wood processing, electronics, communications, computer-aided design, petroleum refining and petrochemical industries, construction

strategy as part of his economic development plan. GORBACHEV'S CHALLENGE, supra note 11, at 26-27.

41. McIntyre, supra note 25, at 479. The Soviets have cut back on machinery imports from the West, planning to substitute the products produced by the joint ventures. Id. at 485.

42. Zabijaka, supra note 19, at 7-8.


44. McIntyre, supra note 25, at 477.

45. Id. at 478.


47. Dean, supra note 5, at 54.

48. However, proper training of managers does not ensure that they will succeed in running businesses more effectively. GORBACHEV'S CHALLENGE, supra note 11, at 129.
materials, and light and food industries.  

III. THE JOINT VENTURE LAWS

This section will examine some of the major provisions of the Soviet joint venture laws.  The initial laws of January 1987, replaced the preliminary guidelines that had been issued by the Soviet government in 1986, but which had yet to take effect.  Many of the initial Soviet laws were considered vague and were not well received by many in the United States.  The Soviets sought to address these concerns by issuing, in September 1987, supplemental laws that clarified or modified the initial laws.

Current Soviet joint venture laws are governed by four sets of regulations. The first set of regulations is the Supreme Soviet's Edict of January 1987, which authorizes the establishment of joint ventures.  The second set of regulations is the Council of Ministers' Decree of January 1987 (Joint Venture Decree), which contains the basic framework for joint venture operations.  Third is the September 17, 1987, Supplemental Decree of the Central Committee of the Communist Party of the Soviet Union and the Council of Ministers.  Finally, the December 2, 1988, Council of Ministers' Resolution modifies

49. McIntyre, supra note 19, at 500. However, the Soviets do not want joint ventures in mining. Zabijaka, supra note 19, at 8.

50. Not every provision will be discussed, nor will the lengthy process of negotiating and establishing a joint venture be addressed. This process has been discussed in great depth elsewhere. E.g., LAW AND PRACTICE, supra note 3, at 9-18; Sherr, supra note 14, at 14-28.


51. The guidelines are republished in Dunn, supra note 7, at 182-186.

52. ISSUE BRIEF, supra note 19, at 10; Viehe, supra note 50, at 182; Wall Street J. Apr. 6, 1987, at 25, col. 4.

53. Viehe, supra note 50, at 192.

54. See Edict, supra note 3.

55. See Decree, supra note 3.

56. "On Additional Measures to Streamline Foreign Economic Activity In the New Conditions of Economic Management" (Supplemental Decree).
many of the earlier provisions. Before examining the application of the laws, the preliminary stages of negotiations will be examined.

A. Preliminaries and Documentation

The first document the American and Soviet negotiators will produce is a letter of intent. The letter of intent outlines the basic elements of the venture, but is not legally binding on the parties. The next task is to draft a feasibility study. The study has two purposes: 1) to persuade the Soviets that the proposed joint venture should be approved, and 2) to form a basis for agreement between the partners. In essence, the study contains the business projections and goals of the venture and should include the background of the project, projected sales and revenues, and the method of accounting to be used.

The Foundation Documents contain the venture’s basic documentation and consist of the joint venture agreement, its charter, and any other provisions that the partners want to include that are not contrary to Soviet law. The charter acts as the articles of incorporation and bylaws and must specify certain matters prescribed by the Joint Venture Decree such as the objectives and purposes of the venture.

B. Management and Personnel

Under the Joint Venture Decree, joint venture management is delegated to two bodies. The joint venture’s governing body is its Board of Directors. The parties will designate the members of the Board of Directors, whose Chairman may be a Soviet citizen. The Board’s specific responsibilities and activi-
ties shall be stated in the Foundation Documents.

The second body, the Directorate, is the venture’s management and is in charge of day to day operations of the venture. The Directorate’s Director General is the venture’s operating manager and also may be a Soviet citizen. The rest of management’s personnel will consist of Soviet and foreign citizens.

The American partner has several ways to maintain sufficient influence in management decisions. First, the parties may agree in the venture’s charter that some non-fundamental questions regarding the venture’s activities require unanimity for approval. Under the new Resolution, “[f]undamental questions of the activity of a joint venture are decided at board meetings on the basis of the unanimity of all board members.” This provision allows the American partner to protect its own agenda. According to Alan Sherr, “[e]ven the most sensitive and important issues—such as how quality control will be assured, how much of the venture’s product will be exported, or how hiring and firing decisions will be made—may be included in this list.”

Second, because the Joint Venture Decree does not require representation on the Board or Directorate to be in proportion to the partners’ shares, the partners may negotiate representation on these bodies between themselves. Moreover, the American party may designate its own representative to supervise specific areas of venture operations by so providing in the Foundation Documents. For example, the Soviets have allowed the foreign partner to appoint its own quality control representatives.

The personnel of the venture must consist primarily of Soviet citizens. Soviet law controls the salary, work schedule, leisure time, and social insurance of Soviet citizens who work at the joint venture. Though Soviet labor law will govern the appointment and dismissal of Soviet citizens who work at the joint venture, these decisions may be made by the joint ven-

63. Joint Venture Decree, supra note 3, at 753.
64. Resolution, supra note 57, at 67. Under the Decree, the Director General was a Soviet citizen. Joint Enterprises, supra note 3, at 753.
66. Id. at 751.
67. Sherr, supra note 14, at 29. There is even a list of the areas in which unanimity might be sought. LAW AND PRACTICE, supra note 3, at 19.
68. Joint Venture Decree, supra note 3, at 753.
69. Dean, supra note 5, at 56.
70. Joint Venture Decree, supra note 3, at 757.
tute. Likewise, Soviet law will govern "various aspects of the terms and conditions of work for foreign citizens employed by the joint venture." However, foreign personnel shall enter separate contracts regarding their salaries, vacations, and pension.

Though the Joint Venture Decree outlines the basic rules governing personnel, the American partner should try to negotiate key personnel issues to its benefit and include them in the Foundation Documents. For example, Richard Dean contends that American partners should try to negotiate arrangements that preclude the Soviets from unilaterally setting all personnel policies. Instead, personnel policies "would be matters for the mutual agreement of the foreign investor and its Soviet partner at either the Board or Directorate level." Further, the American partners must be adamant in negotiations regarding their intentions to attract and motivate the best Soviet workers. To meet these goals, the American partner should stress that it wants the freedom to pay workers more than the standard Soviet wages, a freedom the Soviets appear to have allowed. Finally, the American partner must insist that only competent Soviet managers with the necessary political clout and the ability to work well with Americans will be selected.

In general, most American partners have not had serious personnel-related problems. Soviet labor laws, in part, prevented ContiTrade Services from satisfactorily negotiating a joint venture. However, the ContiTrade experience has been

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72. Viehe, supra note 50, at 199.

73. Joint Venture Decree, supra note 3, at 757-58.

74. Dean, supra note 3, at 56.

75. Id. Under the Resolution, "the forms and size of remuneration, and material incentives in Soviet rubles with regard to personnel of the joint venture are decided by the joint venture." Resolution, supra note 57, at 67.

The American partner also might consider paying Soviet workers in hard-to-find products. Berman and Wechsler, The Five-Percenters, Moscow's Pet Capitalists, Forbes, Feb. 6, 1989, at 93, 97. However, incentive pay to help motivate workers and bonuses for others who excel are highly sensitive issues. Sherr, supra note 14, at 38; Laurita and McGloin, supra note 71, at 50.

76. Laurita and McGloin, supra note 71, at 48.

the exception.

C. Dispute Resolution

Dispute resolution mechanisms are vital to the success of joint ventures in the Soviet Union because they can offer an American partner assurances that disputes will be resolved fairly and objectively. Soviet law governs disputes between the joint venture and the Soviet authorities, between joint ventures, and between the joint venture participants themselves on issues related to joint venture operations. The parties may bring these disputes either to a Soviet court or, by agreement of the parties, to an arbitration tribunal for resolution in accordance with Soviet law. Additionally, by specifically providing in the Foundation Documents, the parties may agree to use the law of another country when interpreting the Foundation Documents. Although the Soviets have been flexible on dispute resolution issues, the American partner should include in the Foundation Documents specific provisions for dispute resolutions to eliminate problems regarding the dispute resolution process.

D. Duration and Termination of the Joint Venture

The partners may agree in the Foundation Documents, or in another agreement, on the venture's duration. The duration may be indefinite, and the Foundation Documents do not establish a minimum or maximum time requirement.

The Joint Venture Decree also allows the partners to establish the circumstances for terminating the joint venture. One commentator has written that the American partner should specify in the Foundation Documents the conditions for

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78. Joint Venture Decree, supra note 3, at 753. Dispute resolution is explained in detail in LAW AND PRACTICE, supra note 3, at 38-39.

79. Joint Venture Decree, supra note 3, at 753. The Soviets have allowed arbitration in London at the London Court of International Arbitration and in Stockholm at the Stockholm Chamber of Commerce. LAW AND PRACTICE, supra note 3, at 38-39.

80. LAW AND PRACTICE, supra note 3, at 38. The Soviets have limited this ability to a select number of internal, organizational matters. Soviet law will still govern most substantive questions arising out of the Foundation Documents. Letter from Bill Frenkel to the author (May 30, 1989) [hereinafter Letter] (on file at the University of Puget Sound Law Review).

81. LAW AND PRACTICE, supra note 3, at 38, 39; Dean, supra note 5, at 57.

82. Joint Venture Decree, supra note 3, at 751; see generally LAW AND PRACTICE, supra note 3, at 40; Sherr, supra note 14, at 27.

83. Joint Venture Decree, supra note 3, at 751.
termination "in the event that contingencies develop that prejudice its interests." Moreover, that commentator believes that the American partner should try to limit the conditions under which the Soviets could liquidate the venture.\footnote{Sherr, supra note 14, at 27. Some possible reasons for termination might include "the failure of Soviet agencies to supply promised credits, supplies, or insurance, [or] undue interference by state agencies." Id.}

The Joint Venture Decree contains a second provision for terminating the venture. This provision, which is perhaps the most disturbing provision in the Joint Venture Decree, grants the Council of Ministers power to liquidate the venture.\footnote{Id. at 28.} This "ominous provision [states] that the USSR Council of Ministers may [unilaterally] liquidate a joint venture if its activities are not consistent with its stated objectives\footnote{Joint Venture Decree, supra note 3, at 758.} as set out in the charter.\footnote{Dean, supra note 5, at 55.}

This provision has generated much concern and many questions. For example, American businessmen fear that the Council of Ministers may arbitrarily terminate the venture. Fortunately, such fear may be unwarranted. First, such action would thwart Soviet attempts to make the Soviet Union an attractive place for American investment and would seriously damage the Soviet Union's rating as an excellent credit risk.\footnote{Joint Venture Decree, supra note 3, at 751.} And second, the liquidation provision is at odds with another provision that provides security to the foreign investor by protecting the joint venture against expropriation by administrative order.\footnote{Gorbachev's Program, supra note 8, at 40.} A more palatable interpretation is that this provision applies to ultra vires actions and that a carefully drafted "objectives" clause in the venture's charter should assuage the American investors' concerns.\footnote{Joint Venture Decree, supra note 3, at 752.}

Though the Soviets probably would not invoke this provision, the American partner should specify in the Foundation Documents the grounds for termination by either side.\footnote{Letter, supra note 80.} This action would allow the American partner to minimize losses if
the venture works out poorly and could protect its investment against arbitrary action by the Soviets.

E. Funds and Credits

Joint ventures are required to allocate resources to several funds that they must establish. The Joint Venture Decree states that the Soviets must have at least fifty-one percent ownership of the joint venture's "charter fund." This provision has been drastically amended to allow the "partners' shares of the incorporation capital [charter fund] . . . [to be] determined by agreement between them." The charter fund is similar to a capital account, and the partners' contributions to it are directly proportionate to their percentage of ownership. The partners' contributions to the charter fund may take many forms, and profits from the venture and additional contributions can supplement the charter fund.

The Joint Venture Decree also requires the venture to contribute to "[a] reserve fund and other funds needed for the activities thereof and for the social development of the collective." The venture's contribution to these funds, unlike the partners' contributions to the charter fund, is not specified in the Joint Venture Decree. Instead, the parties must specify such contributions in the Foundation Documents.

Under the Joint Venture Decree, joint ventures may obtain credits, when necessary, from Soviet or foreign banks.

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93. Joint Venture Decree, supra note 3, at 751. The fund is also translated as an "authorized fund." LAW AND PRACTICE, supra note 3, at 20.

The initial requirement that the Soviets must have at least fifty-one percent ownership of the joint venture raised problems for some corporations. Many U.S. companies forbid investments in which they have minority ownership. Conference Board, supra note 17, at 3.

The Soviet's main purpose in requiring majority ownership was to control certain segments of the venture's operation. As long as the segments the Soviets want to control do not conflict with the segments the American partners want to control, the parties should be able to resolve the issue of control by specifying the duties of the officers and the manner of voting by the board.

94. Resolution, supra note 57, at 67. In practice, Soviet authorities probably would not approve a joint venture in which the Soviets had a minimal ownership interest, such as 20% or less. On the other hand, very few Americans would want 80% ownership because this would require investing large sums of capital in the uncertain Soviet economy.

95. See generally Sherr, supra note 14, at 36.
96. Joint Venture Decree, supra note 3, at 751-52.
97. Joint Venture Decree, supra note 3, at 755. These funds are also called reserve, operating, and social funds. Viehe, supra note 50, at 193.
98. Joint Venture Decree, supra note 3, at 755.
Foreign currency credits may be obtained from either the Soviet Foreign Trade Bank or from foreign banks, with the consent of the Soviet Foreign Trade Bank. Rubles may be obtained from the State Bank of the USSR or the Soviet Foreign Trade Bank. These banks have the power to ensure adequate security for the credits and their timely repayment.

F. Contributions and Valuation

The Joint Venture Decree does not provide a minimum capital contribution for the venture's charter fund. Each partner may contribute cash, assets, or a combination of each. Soviet contributions will usually consist of buildings, equipment, and natural resources. American contributions will usually include cash, technology, and know-how. The proportion of each partner's contribution determines the proportion of ownership and the distribution of profits.

The Joint Venture Decree stipulates that all contributions will be valued in rubles at the "official exchange rate of the State Bank of the USSR." If no world market price exists, the parties are to negotiate the value of the contributions. The Supplemental Decree modifies this requirement by also allowing the partners to value "their contributions in both Soviet and foreign currency." However, this modification has not eliminated serious valuation problems.

The parties must determine the value of contributions, considering the world market prices. This method has been problematic. First, problems tend to arise when determining the value of Soviet non-cash contributions. As one commentator noted, "[r]eal estate prices, the value of Soviet equipment, or the value of Soviet processes or know-how may on occasion be difficult to value by reference to world market prices." This is true because Soviet prices do not reflect a market price,
but represent what the Soviet government has decided the item should cost. This is also true because the ruble is overvalued by the Soviets.\textsuperscript{109} Although the Soviets have promulgated assessment guidelines to assist in determining the value of Soviet contributions,\textsuperscript{110} these guidelines are not useful in all cases. For example, when valuing Soviet contributions that are unique or have no precedent for comparison, these guidelines are of little help.\textsuperscript{111}

The American partners have four ways to value Soviet non-cash contributions when conventional guidelines are not useful. First, each party may separately negotiate the value of the Soviets' contributions, then negotiate an agreed price. Second, the parties may agree on an exchange rate for the ruble instead of using the official Soviet exchange rate. Third, the parties may agree to overvalue the American contribution to compensate for the overvaluation of the Soviet contribution.\textsuperscript{112} A final way American firms may mitigate this valuation problem is by minimizing their capital contributions. For example, the capital contributions of Combustion Engineering to its $6 billion oil refinery joint venture were less than $200 million.\textsuperscript{113}

A second valuation problem arises when trying to agree on prices for American non-cash contributions "which reflect fair market value."\textsuperscript{114} The problem is caused by Soviet hesitation in accepting the value the Americans place on their goods. This problem can be solved in several ways. First, the parties can negotiate the value of American non-cash contributions. Second, the parties may agree to determine the value of such contributions based on "the purchasing power of labor units."\textsuperscript{115} The third and probably best approach is for the Americans to present their Soviet partners with documentation indicating the value of their contributions. This value may be based on production costs or on market prices.\textsuperscript{116}

A final valuation problem, which affects the first two, is that the official Soviet ruble exchange rate significantly over-

\textsuperscript{109} LAW AND PRACTICE, \textit{supra} note 3, at 16.
\textsuperscript{110} These guidelines are reprinted in LAW AND PRACTICE, \textit{supra} note 3, at Appendix V.
\textsuperscript{111} Sherr, \textit{supra} note 14, at 25.
\textsuperscript{112} LAW AND PRACTICE, \textit{supra} note 3, at 17.
\textsuperscript{113} Laurita and McGloin, \textit{supra} note 71, at 46-47.
\textsuperscript{114} Viehe, \textit{supra} note 50, at 185.
\textsuperscript{115} Id.
\textsuperscript{116} LAW AND PRACTICE, \textit{supra} note 3, at 16.
estimates the ruble's true worth.\textsuperscript{117} This causes the value of American cash and non-cash contributions to be significantly discounted in favor of the Soviets. To solve this problem, the Soviets recently announced a massive overhaul of their currency system. The first step is the devaluation of the ruble by fifty percent as of January 1, 1990.\textsuperscript{118} Then, a new exchange rate will be implemented on January 1, 1991.\textsuperscript{119} If successfully implemented, the new currency system will solve many of the valuation problems the ruble causes American partners. In the meantime, the problem of the overvalued ruble can be resolved by the parties negotiating an exchange rate\textsuperscript{120} or by valuing American contributions at an exchange rate higher than the official Soviet rate.

\textbf{G. \textit{Joint Ventures and the Soviet Economy}}

The joint venture's relationship to the Soviet economy and the Soviet government is vital to the success of the venture and has changed several times since \textit{perestroika} began. The Joint Venture Decree allows the venture to directly contact local government authorities. It also requires the venture to establish relations with the proper central authorities of the Soviet government and the local governments of the Union Republics "superior to the Soviet participant."\textsuperscript{121} This requirement presumably means the Soviet partner must establish relations with the "ministry to which the Soviet partner is responsible."\textsuperscript{122}

The venture's relationship to the Soviet economy is broken into two parts. The first part is the relationship the venture has with Soviet central planning, which determines whether the venture will be supplied with the goods it needs. The second part is its relationship with the Soviet economy, which determines the process for buying its supplies and selling its products.

Because the Soviet joint venture is considered independent

\textsuperscript{117} Sherr, \textit{supra} note 14, at 25. Some have argued that the Soviet ruble exchange rate is four times its true value. Viehe, \textit{supra} note 50, at 185.

\textsuperscript{118} Resolution, \textit{supra} note 57, at 64.

\textsuperscript{119} The Resolution also directs Soviet authorities to complete, by the end of 1989, a study of specific proposals of the new exchange system. \textit{Id.}

\textsuperscript{120} Sherr, \textit{supra} note 14, at 26. In fact, one Soviet official stated that potential inequities resulting from the exchange rate problem could be solved by negotiation. \textit{Id.}

\textsuperscript{121} \textit{Joint Venture Decree, supra} note 3, at 753-54.

\textsuperscript{122} Viehe, \textit{supra} note 50, at 189.
of Soviet central economic planning, the joint venture may independently export and import products that are necessary to its operations.\textsuperscript{123} That is, the venture is allowed to trade directly with foreigners for these products using convertible currency.\textsuperscript{124} The venture is also free to determine its own economic operations and plans.\textsuperscript{125} This means that “Soviet authorities cannot dictate to the venture which suppliers it should deal with, how much it should buy and sell, and so on.”\textsuperscript{126} However, this exclusion from the Soviet 5-year plan raises a potential problem. A joint venture may need to purchase certain materials in the Soviet Union, but may not be able to do so because its operations are outside of the 5-year plan. Moreover, the Joint Venture Decree does not guarantee the venture access to these resources.\textsuperscript{127}

The Soviets have taken steps to calm American fears of being unable to buy supplies in the Soviet Union for the joint venture. Soviet authorities have privately said that joint venture demands for resources will take priority over the demands of other Soviet businesses.\textsuperscript{128} In addition to these Soviet guarantees, American businessmen should negotiate with the Soviets for assurances concerning venture supplies. These guarantees should be in the Foundation Documents and should take into consideration quality control, delivery dates, and payment schedules.\textsuperscript{129} If the supplies are vital to the venture’s operations, the American partner should also consider stipulating in the Foundation Documents that the Soviet failure to provide these supplies would be grounds for termination. Unfortunately, even these steps may not guarantee the availability of supplies because the supply system in the Soviet Union is generally inefficient and perestroika has done little to improve it.

The Soviets have also frequently changed the process by which the venture will buy supplies and sell products within the Soviet Union.\textsuperscript{130} The Joint Venture Decree requires that all joint venture purchases of equipment, raw materials, and

\textsuperscript{123} Joint Venture Decree, supra note 3, at 754.
\textsuperscript{124} LAW AND PRACTICE, supra note 3, at 23.
\textsuperscript{125} Joint Enterprises, supra note 3, at 754.
\textsuperscript{126} Sherr, supra note 14, at 32.
\textsuperscript{127} Carpenter and Smith, supra note 50, at 86.
\textsuperscript{128} Sherr, supra note 14, at 32.
\textsuperscript{129} LAW AND PRACTICE, supra note 3, at 23.
\textsuperscript{130} These changes are described in LAW AND PRACTICE, supra note 3, at 22-23.
other products on the Soviet market and all sales of its products on the Soviet market be conducted in rubles through a Soviet foreign trade organization (FTO), "taking into account world market prices."\textsuperscript{131} Though the Soviets may have wanted to take advantage of the FTOs' experience in dealing with foreigners by using them as intermediaries, subsequent laws have changed the role of the FTO.\textsuperscript{132} Joint ventures "may now buy and sell on the Soviet market either directly or through FTOs, using either rubles or foreign currency."\textsuperscript{133} Consequently, the venture's inability to sell directly on the Soviet market, which had been called "the single most dissuasive element in the joint-venture package,"\textsuperscript{134} has been reduced. Whether joint ventures will be successful in buying and selling in the Soviet Union will depend on the success of perestroika.

In sum, the joint venture's relationship to the Soviet economy should be understood in light of perestroika reforms that are designed to improve the Soviet economy's central planning system.\textsuperscript{135} The implementation of these reforms has caused short-term havoc in the Soviet economy. For example, many American business contacts in Soviet ministries have ended as the Soviet foreign trade apparatus has been reformed.\textsuperscript{136} Without the successful implementation of these reforms, joint ventures probably will not be successful over the long-term. After all, "[a]n autonomous capitalist joint venture is an anomaly in a state-directed economy."\textsuperscript{137}

\textbf{H. Hard Currency Issues}

A major concern for American businessmen interested in a joint venture in the Soviet Union is how to repatriate their Soviet market earnings in hard currency. Indeed, repatriation of earnings is considered the most troubling problem for joint ventures in the Soviet Union.\textsuperscript{138} The Soviets have guaranteed joint ventures the right to repatriate profits, which are distrib-

\textsuperscript{131} Joint Enterprises, supra note 3, at 754.
\textsuperscript{132} See generally Gardner, Restructuring the Soviet Foreign Trade Sector, 23 COLUM. J. WORLD BUS. 7 (1988).
\textsuperscript{133} LAW AND PRACTICE, supra note 3, at 23.
\textsuperscript{134} Viehe, supra note 50, at 202.
\textsuperscript{135} See generally M. GORBACHEV, supra note 12, at 112; Gorbachev and Economic Reform, supra note 24, at 56.
\textsuperscript{136} Dean, supra note 5, at 58.
\textsuperscript{137} Carpenter and Smith, supra note 50, at 84.
\textsuperscript{138} Dean, supra note 5, at 57.
uted to each partner in relation to their proportionate share in foreign exchange. Due to another Joint Venture Decree provision, however, this "guarantee" has not ended American concerns about being unable to repatriate profits in hard currency from the Soviet Union. This provision, which limits repatriation of profits, has been a stumbling block for many joint ventures. The provision provides that "[a]ll currency expenditures of a joint enterprise [venture], including the payment of profit and other amounts due foreign participants and specialists, must be ensured by the joint enterprise from receipts from the realization of its products on the foreign market." 

This provision has two main effects. First, it requires the joint venture to earn enough hard currency to cover its hard currency expenses or, in the alternative, it must be able to convert rubles into hard currency. The practical effect is to force the venture to be export oriented since the venture probably would not earn hard currency by selling in the Soviet Union. Perhaps the Soviets sought this effect because two Soviet goals for joint ventures are that they be export oriented and earn hard currency. The second effect of this provision is to force joint ventures that import a large amount of their products to have plenty of hard currency because payment for such imports "must also be covered by proceeds from the sales of the joint-venture's products on foreign markets." 

However, these effects conflict with the goals of many businesses that seek to set up ventures in the Soviet Union. The primary motivation for American companies to invest in joint ventures in the Soviet Union is the large, untapped domestic Soviet market. Most Americans investing in joint ventures in the Soviet Union want to sell their products in the Soviet market. One commentator noted that

[t]here is enormous pent up demand in the USSR, both in the production and retail sectors . . . . Retail customers have saved their rubles for years, waiting in vain for goods and

139. Joint Venture Decree, supra note 3, at 755.
140. Id.
141. Id. at 754.
142. Viehe, supra note 50, at 190; Carpenter and Smith, supra note 50, at 83-84.
143. Viehe, supra note 50, at 190. Of course, ventures that are not export-oriented may earn hard currency by import-substitution or by catering to foreign tourists through methods such as establishing hotels.
144. Sherr, supra note 14, at 8.
services on which it is worth spending their money. Many Soviet consumers consider Western styles and technology to be highly attractive.145

The Americans investing in these joint ventures do not want them to be export oriented for two reasons. First, many companies already sell extensively in foreign markets. These companies will not want to set up ventures in the Soviet Union that will compete with their already existing operations.146 Second, as with any new operation, there are risks that it will not be profitable or will be plagued with problems. Given the uncertain success of Soviet economic reforms and the mercurial nature of U.S.-Soviet economic relations, these risks will be increased.

Although the Joint Venture Decree creates problems for partners trying to repatriate hard currency, these problems can be avoided or minimized in five ways. The first and best way to avoid hard currency problems is to invest in joint ventures that would be able to earn enough hard currency for repatriation. The Soviets are helping in this regard by indicating that they will approve only joint ventures that have a good chance of earning enough hard currency for their operations. Additionally, the Soviets may approve certain high priority ventures regardless of their hard currency earnings potential, which could force the Soviets to commit their own hard currency reserves to the venture.147

Second, in response to foreign concerns, the Soviets promulgated foreign exchange clearing procedures.148 These procedures may permit a venture that is "short of hard currency to offset its shortage against surplus hard currency which may be available from other enterprises within the same ministry."149

A third way for a joint venture to minimize or avoid repatriation problems is for the joint venture to develop a strong export market. A strong export market should assure the joint venture that it will earn enough foreign exchange so as to meet its repatriation requirements. The success of this option

145. Id.
146. Carpenter and Smith, supra note 50, at 84. This was a major reason that Monsanto's negotiations with the Soviets failed. Dreyfus, Negotiating the Kremlin Maze, BUS. MONTH, Nov. 1988.
147. Dean, supra note 5, at 57.
148. Id.
149. Id.
may depend upon the type of product or service exported, labor costs, and the propinquity of the operation to its export market.\textsuperscript{150}

Fourth, the venture may try to set up countertrade arrangements.\textsuperscript{151} Combustion Engineering Corporation, the first U.S.-Soviet joint venture, is using one such method: "buy-back." Under the buy-back agreement, Combustion Engineering will make instruments for oil refineries. Instead of being paid in rubles or dollars, Combustion Engineering will be paid in refined products, which it then can sell for hard currency.\textsuperscript{152} Likewise, Pizza Hut plans to take out Russian-grown mushrooms as part of its profits.\textsuperscript{153} Countertrade arrangements will work only if the Soviet goods are exportable.

A fifth method to ensure repatriation of hard currency earnings is the consortium arrangement. In March 1989, Eastman Kodak, RJR Nabisco, Johnson & Johnson, Archer Daniels Midland, Mercator Corporation, and Chevron formed the American Trade Consortium (ATC). A Soviet counterpart was set up that consisted of the major Soviet economic ministries. Although the details of the arrangement are not fully known, the agreement may lead to the establishment of 25 joint ventures over the next 20 years. These ventures would primarily be in consumer and industrial goods. There is also speculation that ATC members would pool their hard currency earnings, which would allow an ATC member that does not earn enough foreign exchange to obtain hard currency from other ATC members.\textsuperscript{154}

Other approaches to dealing with the problem of repatriation—

\textsuperscript{150} Law and Practice, supra note 3, at 33.

\textsuperscript{151} Countertrade is the process by which the seller provides the buyer with products or services and agrees to buy other goods from the buyer.

\textsuperscript{152} Washington Post, Nov. 12, 1987, at E1, col. 4. However, two major problems exist with this type of arrangement. First, it is difficult to find Soviet-made products for which there is a demand outside the Soviet bloc. There are many reasons for this, including poor quality of the products. Second, the producers of the few Soviet products that are exported for hard currency probably would prefer to earn hard currency rather than rubles from such sales. Countertrade may still be a viable option if inexperienced Soviet producers can rely on the American partner's expertise in international business. Law and Practice, supra note 3, at 35.

\textsuperscript{153} Dreyfus, supra note 146.

tion of profits, such as import substitution\(^{155}\) and agreements whereby American partners keep a disproportionate share of hard currency profits,\(^{156}\) are less likely to be successful because they cut into the Soviet share of hard currency earnings. Nevertheless, the Soviets might disregard such a result and help a small company start its operations in the Soviet Union for export if the products are a high priority to the Soviets.\(^{157}\)

The Soviets realize that repatriation of hard currency profits is essential to attracting more American joint ventures. Accordingly, the Soviets have been flexible in allowing joint venture partners to find creative ways to do so. The partners may create new approaches to solve the problems of hard currency repatriation as long as their actions do not violate Soviet law.\(^{158}\) The Soviets must continue to be flexible on this issue or risk ruining the positive joint venture climate they have attempted to create.

I. Taxation and Accounting

As with hard currency issues, the Soviets have been quite flexible in working out potential taxation and accounting problems. The Joint Venture Decree requires the venture to keep its business, bookkeeping, and statistical records in the same manner as a Soviet State enterprise.\(^{159}\) This creates a problem because Soviet accounting principles and objectives are quite different from American accounting principles and objectives.\(^{160}\) Soviet accounting principles are intended to provide Soviet central planners with the statistical information that they require for state planning. American and Western accounting principles are designed to provide financial information and determine profits.\(^{161}\)

The Decree also requires the partners to provide a proce-

\(^{155}\) LAW AND PRACTICE, supra note 3, at 34.
\(^{156}\) Id. at 35.
\(^{157}\) Sherr, supra note 14, at 12.
\(^{158}\) Joint Venture Decree, supra note 3, at 751. Gorbachev has also stated this position. M. GORBACHEV, supra note 12, at 108.
\(^{159}\) Joint Venture Decree, supra note 3, at 757.
\(^{160}\) A good example of these differences is in the different depreciation rates. Depreciation rates in the Soviet Union are usually longer than in Western countries, which creates tax disadvantages. Soviet depreciation rates are longer because the Soviets usually replace older factories that wear out rather than upgrade them with new equipment. LAW AND PRACTICE, supra note 3, at 28.
dure whereby information affecting the joint venture’s operations would be furnished to the partners. To meet this requirement, the partners may set up internal auditing procedures. The Joint Venture Decree does not prohibit particular internal auditing procedures nor does it prescribe particular procedures. Consequently, the partners should be able to set up internal security procedures of their choice to protect the accuracy of the joint venture’s books. These procedures should be specified in the Foundation Documents to increase the probability that they will be followed.

Partners have chosen two ways to solve accounting related problems. First, the Soviets have been willing to allow the joint venture to maintain two sets of books and records. One set would be in accordance with established Soviet accounting principles, the other in accordance with the partner’s preferred accounting principles. The second approach, suggested by the Soviets, is for the partners to negotiate mutually acceptable accounting procedures. The joint venture partners would then seek separate official approval from the USSR Ministry of Finance and USSR Central Bureau of Statistics, which issues Soviet accounting principles, for the adoption and use of these principles.

A concern related to accounting is the method of taxing the joint venture. The basic problem is that the Joint Venture Decree provides a tax rate of thirty percent of profits but “provides no definitive statement of how the concept of profit is to be arrived at nor any accounting guidelines to determine profit.” The purpose here is not to examine how different accounting principles would yield different profits. Instead, the purpose is to provide the reader with a basic understanding of taxation on venture profits.

The Soviets have granted some tax breaks to joint ven-

162. Id. External auditing procedures are also governed by the Decree. Id.
163. LAW AND PRACTICE, supra note 3, at 29.
164. Dean, supra note 5, at 57.
165. Id.
166. This Comment discusses the taxation of the joint venture and does not discuss taxation of personal income of employees. The latter subject is dealt with in Maggs, supra note 161, at 21.
167. Viehe, supra note 50, at 194.
168. See generally LAW AND PRACTICE, supra note 3, at 30-31.
tures. The Joint Venture Decree provides joint ventures with a tax holiday on their profits during the first two years of operation.\textsuperscript{169} Unfortunately, most joint ventures would not have profits to exempt under this provision, which made the exemption a nullity.\textsuperscript{170} Thus, the Supplemental Decree was promulgated granting joint ventures a two year tax holiday starting from the first year the venture makes a profit.\textsuperscript{171} The tax holiday is extended to three years for ventures "in the far Eastern Economic Region."\textsuperscript{172} The Ministry of Finance also has the right to reduce a venture's tax rate or eliminate its tax\textsuperscript{173} and has extended the tax holiday to certain high priority ventures.\textsuperscript{174} Nonetheless, some have argued that the Soviets should have been more generous to the ventures by extending the tax holiday from four to ten years, as is the Western practice.\textsuperscript{175}

The tax rate on venture profits is thirty percent. The joint venture may repatriate its share of the profits only after paying an additional twenty percent withholding tax,\textsuperscript{176} making the effective tax rate for repatriated profits forty-four percent. Unfortunately, American businesses may be at a competitive disadvantage because "the U.S.-Soviet tax treaty does not contain a provision reducing Soviet withholding taxes on dividends paid on a Soviet business to a U.S. investor."\textsuperscript{177} However, the Soviets have tax treaties with many other countries that eliminate the twenty percent withholding tax.\textsuperscript{178} Thus, a U.S. partner might circumvent the tax disadvantage by investing in a joint venture through a third country that has a tax agreement with the Soviets that eliminates the twenty percent withholding tax.\textsuperscript{179}

\textsuperscript{169} Joint Venture Decree, supra note 3, at 755-56.
\textsuperscript{170} Maggs, supra note 161, at 19-20.
\textsuperscript{171} LAW AND PRACTICE, supra note 3, at app. X.
\textsuperscript{172} Resolution, supra note 57, at 67. The Resolution also states that the tax on joint venture profits in the region will be reduced to ten percent. \textit{Id}.
\textsuperscript{173} Joint Venture Decree, supra note 3, at 755-56.
\textsuperscript{174} Dean, supra note 3, at 757. Only six of thirty joint ventures have been given this special treatment. Sherr, supra note 14, at 35.
\textsuperscript{175} Viehe, supra note 50, at 195.
\textsuperscript{176} Joint Enterprises, supra note 3, at 756.
\textsuperscript{177} LAW AND PRACTICE, supra note 3, at 48. The U.S.-USSR tax treaty is explained in detail in M. NEWCITY, TAXATION IN THE SOVIET UNION, ch. 6 (1986).
\textsuperscript{178} The Soviet Union's other tax agreements are dealt with extensively in M. NEWCITY, supra note 177, at ch. 7.
\textsuperscript{179} LAW AND PRACTICE, supra note 3, at 49. There are several methods to circumvent the tax disadvantage created by the U.S.-Soviet treaty. \textit{Id} at 48-50.
In determining its taxable profits, the Joint Venture Decree allows the venture two types of deductions. First, the venture may deduct from income any transfers to the reserve funds or other funds "for the development of production, science, and technology." Deductions are allowed as long as the reserve fund does not fall below twenty-five percent of the charter fund.

The second type of deduction is for other business expenses, which will be determined by the accounting system the venture uses. Soviet accounting principles will usually yield larger taxable profits than American or Western principles because the Soviet principles "do not account for many items reflected as expenses under Western principles." Thus, the accounting system employed will have a noticeable effect on the amount of business expense deductions.

IV. SYSTEMIC PROBLEMS

The success of joint ventures in the Soviet Union will depend on more than just the laws. Indeed, even if the Soviet joint venture laws met every need of American business, the success of joint ventures in the Soviet Union could not be guaranteed. The reason is that perestroika has not solved the problems inherent in the Soviet system. Because many problems with the Soviet economic system have existed for nearly fifty years or more, their removal is difficult at best. Furthermore, economic reforms have been tried before in the Soviet Union without much success.

The major systemic problem confronting the success of joint ventures in the Soviet Union is the bureaucracy. The bureaucracy affects the successful implementation of perestroika and affects the ability of joint ventures to do business. Soviet bureaucrats depend upon the current economic

181. Id. at 755.
182. LAW AND PRACTICE, supra note 3, at 30.
183. Problems inherent in the Soviet system, such as central planning, and others created by the system will be examined as systemic problems.
184. The problems of the Soviet system and how they affect perestroika have been widely discussed. See generally GORBACHEV'S CHALLENGE, supra note 11, at 1-85; Gorbachev and Economic Reform, supra note 24, at 56.
185. GORBACHEV'S CHALLENGE, supra note 11, at 42-85.
186. William Zolner, who was part of Combustion Engineering's negotiating team, argued that bureaucracy causes everything to take "four times as long over there [in the Soviet Union]." Dreyfus, supra note 146, at 60.
system of central planning for their jobs. To fundamentally change the central planning system, which is a major goal of Gorbachev, would mean the end of many jobs. On the other hand, if the Soviets do not fundamentally change their central planning system, they risk falling further behind the West in the high technology revolution.\(^{187}\) Basically, Gorbachev's challenge is to win the support of the same people whose jobs are threatened by the success of perestroika and who defend the current central planning system.\(^{188}\) Many people have argued that the resistance of these entrenched bureaucrats will thwart the success of Gorbachev's reforms.\(^{189}\)

An excellent example of how bureaucratic resistance to a reform can hinder its implementation is the Enterprise Law.\(^{190}\) Passed on June 30, 1987, this law was designed to make enterprises eventually self-sufficient. Enterprises would become less dependent on Soviet ministries for their contracts and more dependent on direct contacts with customers. Because the ministries became concerned that they might lose control of enterprises if the law succeeded, they successfully opposed implementation of this law. "It has now been publicly acknowledged that the ministries have effectively sabotaged what was originally considered to be the key regulation of Gorbachev's reform process."\(^{191}\) The failure of such an important reform reveals how strong the bureaucratic resistance can be to reforms that may threaten job security or authority. One must wonder how successful Gorbachev will be with his other reforms if his attempt to implement the cornerstone of perestroika has been temporarily thwarted.\(^{192}\)

Likewise, the implementation of gospriyemka, a quality control program, has had mixed results.\(^{193}\) In fact, the quality controls were relaxed "[b]ecause many enterprises were unable

\(^{187}\) Gorbachev and Economic Reform, supra note 24, at 71.
\(^{188}\) Id. at 61.
\(^{189}\) Horvath, Soviet Economic Reforms are Destined to Fizzle, CHALLENGE, Mar.-Apr. 1988, at 50.
\(^{190}\) This example is taken from Perestroika in the Soviet Union, supra note 8, at 315.
\(^{191}\) Id. Goldman argues that a similar fate has befallen the Law on Cooperatives. Id.
\(^{192}\) One commentator has argued that many Soviet managers have a wait-and-see attitude during the early stages of perestroika because they "are skeptical about the changes of Gorbachev's reforms." Sherr, supra note 14, at 17.
\(^{193}\) Gorbachev's Program, supra note 8, at 7-18.
to deal with the tough quality standards. The successful implementation of gospriyemka is vital to the success of joint ventures because American businessmen are concerned that the low quality standards that plague Soviet products will plague products made by joint ventures. If these quality control concerns are not satisfactorily addressed, joint venture products will be uncompetitive with Western products. This will undermine a chief Soviet goal: increasing exports. Such poor results would discourage further joint venture investments in the Soviet Union.

Bureaucratic resistance to perestroika can be overcome, but Gorbachev must convince the Soviet bureaucrats that they will benefit by perestroika. To succeed, Gorbachev must convince them that whatever short-term inconveniences they might experience will be outweighed by long-term improvements in the quality of Soviet life. Unfortunately for Gorbachev, many Soviets remember sacrifices for other economic reforms that resulted in no improvement in their daily lives.

The second major systemic obstacle to successful joint ventures is the Soviet labor force. The success of joint ventures will depend in part on the quality of the Soviet work force. An unproductive or inefficient work force is an obstacle for joint venture investment because, among other things, it increases production costs. Compared with American standards, the Soviet labor force lacks creativity, is poorly disciplined, and is poorly motivated. The joint venture will also have difficulty in firing ineffective or lazy workers. Although one commentator admits that “[s]ome elements of the hiring and firing processes may be open to negotiation by the joint venture partners, [even if] others are likely to require clarification at high political levels.”

Improving the work force will not be easy, as Gorbachev has discovered. Helping Soviet workers become more creative or take initiative will take time because Soviet society sup-

194. Id. at 51.
195. Sherr, supra note 14, at 33.
196. Perestroika in the Soviet Union, supra note 8, at 341.
197. Id. at 313.
198. See generally GORBACHEV'S CHALLENGE, supra note 11; Gorbachev and Economic Reform, supra note 24.
199. Sherr, supra note 14, at 38.
200. Gorbachev's Program, supra note 8, at 17.
presses these traits. For example, central planning discouraged innovation and creativity because ministers and factory managers traditionally were "rewarded for producing more, rather than improved, products." Incentive pay to help motivate workers and bonuses for others who excel are also highly sensitive issues and could cause tensions between the American partner and Soviet workers. Pay disparities between Soviet and American managers might cause similar problems because Soviet managers would feel slighted even though they may lack the skill and training of the American managers.

A third systemic problem is the under-developed Soviet infrastructure. American businesses setting up joint ventures in the Soviet Union should be prepared for certain inconveniences in conducting business. First, the Soviet Union has no overnight mail service to the U.S. Second, the Soviet's tight control of the flow of information within Soviet society (for internal security reasons) might adversely affect joint venture operations. Even when equipment such as copying and fax machines is found, it usually is outdated and of poor quality. Further, this control over the flow of information has resulted in a Soviet phone system of extremely poor quality, which could frustrate communications. Finally, the Soviet Union has an inadequate supply of hotel, housing, and office space that meets Western standards. When adequate space is available, it is very expensive.

American companies with international business experience will find the systemic problems in the Soviet Union similar to the systemic problems in developing countries. As in those countries, American partners must adapt to the country's business culture and work within the existing framework.

201. GORBACHEV'S CHALLENGE, supra note 11, at 110-111.
202. Gorbachev and Economic Reform, supra note 24, at 60.
203. Berman and Wechsler, supra note 75.
204. Conference Board, supra note 17, at 8. Although there is no such service within the Soviet Union, there is overnight mail service to the Soviet Union. Sherr, supra note 14, at 42.
205. The strict control of access to copy machines, word processors, and computers could be burdensome to the venture's operations, especially if the American personnel are accustomed to such equipment and are denied its use.
207. GORBACHEV'S CHALLENGE, supra note 11, at 109-110.
208. Sherr, supra note 14, at 42.
With patience, perseverance, and the success of perestroika, American partners may find their hard work financially rewarding.

V. POLITICAL PROBLEMS

The success of Gorbachev's reforms in general and joint ventures in particular will also depend upon the political stability of the Soviet Union. Potential political problems that could threaten perestroika are three-fold: internal opposition, political unrest or instability, and U.S.-Soviet relations.

The first political problem is opposition to perestroika within the Soviet government and, more importantly, within the ruling Soviet Politburo. Gorbachev has tried to consolidate his power base by replacing people who do not support perestroika with people who do. The most recent example of this changing of the guard, and perhaps the most important in terms of securing Gorbachev's position, was the September 1988 purge in the Politburo. Gorbachev demoted three Politburo members who were either against perestroika or were against the pace at which it was moving. He also was elected president and chief of state, in addition to his existing position as general secretary of the Communist Party.

Gorbachev's moves have probably had three consequences. First, they have reduced the influence of top-level opposition to his reforms. Second, they have sent a warning to the bureaucracy that he will not allow anything or anyone to hinder the implementation of perestroika. And third, they have given Gorbachev the ability to circumvent the bureaucracy in order to implement his reforms. While Gorbachev's consolidation of power does not ensure the success of perestroika or joint ventures, it does improve the likelihood that his reforms will continue. However, his battles with internal opposition will also continue.

The second political problem facing perestroika is the political instability within the Soviet Union and Eastern Europe. Political unrest has been evident in many areas of the

210. Id. at 52. The article states that "[t]he new system was designed by Gorbachev as an end run on the party bureaucracy, which has stymied his reform efforts in order to protect its own power and perks. Last week's purge was a warning to the bureaucracy that Mikhail Gorbachev will not tolerate obstructionism." Id.
Soviet empire, including Eastern Europe, Estonia and Azerbaijan. Such unrest could force the Soviets to crack down on the demonstrators and suspend glasnost. Because glasnost is necessary for the success of perestroika, a Soviet crackdown could undermine perestroika and, consequently, reduce American investor confidence in the Soviet Union. On the other hand, Gorbachev cannot allow such unrest to get out of hand because of pressure from the Soviet military. The manner in which Gorbachev handles these politically sensitive regions and others will determine, in part, the success of joint ventures.

Finally, the U.S.-Soviet relationship is important to the success of joint ventures. Economic relations improve when U.S.-Soviet political relations improve. When political relations fizzle, so do economic relations. Although Soviet political relations with the U.S. should continue to improve over the next few years, obstacles still remain. The Soviets view the Jackson-Vanik Amendment, U.S. trade embargos and U.S. export restraints on strategic goods as major obstacles to improving economic relations with the U.S. Likewise, Americans view poor access to the Soviet ministries and the paucity of reliable information on the Soviet economy as major obstacles to improved economic relations. Other Americans argue that improved economic relations must not lead to the transfer of technology and management know-how that could assist the Soviet military.

216. Sherr, supra note 14, at 22. O.P.I.C. does not provide political risk insurance for businesses within the Soviet Union. However, private political risk insurance is available. See N.Y. Times, Mar. 14, 1988, at D4, col. 2.
217. ISSUE BRIEF, supra note 19, at 7. The amendment prevents the U.S. from granting most-favored status and government-backed credits to non-market economies unless they allow free emigration of Jews.
220. Trade Policy, supra note 9, at 1.
221. ISSUE BRIEF, supra note 19, at 5-6.
222. Pilon, A Yellow Light on U.S. Joint Ventures With the Soviets, No. 666 THE
To attract potential American investors, Gorbachev must convince them that the Soviet Union is a politically stable country in which to invest. His failure to do so could have dire consequences for the success of joint ventures in the Soviet Union and for perestroika.

VI. CONCLUSION

This Comment has addressed the major problems American partners face in establishing joint ventures in the Soviet Union. Many of these problems will remain at least through the mid-1990s while perestroika and new Soviet joint venture laws attempt to solve other problems.

The ultimate success of joint ventures in the Soviet Union depends on the Soviets. If they remain flexible and continue to address American concerns and fears, American investment in joint ventures should increase. However, if Gorbachev is unable to successfully implement perestroika or promulgate new Soviet joint venture laws that address the concerns examined in this Comment, joint ventures in the Soviet Union will be short-lived.

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