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Western Investment in State-Controlled Economies: Establishment of Joint Ventures in Eastern European Countries

The steady growth of East-West business transactions has culminated within the past decade in the establishment of joint ventures by Western companies in Eastern Europe. Although cooperation agreements, generally involving sales of capital equipment and technology, currently represent the most popular form of long-term investment by Western firms in socialist countries, the international joint venture, a merger of representatives of the two divergent economic and political philosophies into one commercial enterprise, has recently emerged as a viable, albeit challenging, alternative.

Cooperation agreements in Eastern Europe usually take one of four forms: (1) co-production and specialization agreements with both partners producing components for a final product to be assembled by one partner, (2) subcontracting whereby the socialist partner produces the product in accordance with designs and specifications supplied by its Western partner and delivers an agreed-upon quantity of the product to the Western partner, (3) licensing agreements in which the Western firm licenses technology to the socialist partner and payment is made in products or components resulting from the use of the license rather than in the ordinary form of hard currency royalties, and (4) turnkey plants involving the sale of a complete plant or production line with at least partial payment in the resulting product. These agreements (under which the transacting partners keep their separate identities) form a bond between the parties greater than that created by a simple sales contract, but generally less than that created by a joint venture. See M. Sukijasovic, Joint Business Ventures in Yugoslavia Between Domestic and Foreign Firms 31 (1973).

A licensing agreement may be an integral part of a joint venture association if the Western licensor agrees to accept some equity share in the licensed firm as partial or full payment for his contribution of patents, trademarks and/or know-how to the socialist partner. Travaglini, Foreign Licensing and Joint Venture Arrangements, 4 N.C. J. INT'L. L. & COM. REG. 159, 167 (1979).

Pederson, Joint Ventures in the Soviet Union: A Legal and Economic Perspective, 16 HARV. INT'L. J. 390, 390 (1975). E.g., Poland's agreement with Honeywell concluded in 1973 for the production of Honeywell-designed automation equipment. Honeywell agreed to provide equipment, materials and know-how and to accept payment in the form of the equipment produced. While the Polish party apparently has sales rights anywhere in COMECON, Honeywell acts as exclusive distributor in the West. The agreement also makes provision for detailed quality control standards and extensive training of personnel. Grzybowski, The Polish People's Republic, in EAST-WEST BUSINESS TRANSACTIONS 263-63 (R. Starr ed. 1974).

Typically, an international joint venture arises by an agreement between at least two parties from different countries to pool their assets to form a new and distinct economic entity, to share profits and losses, and to jointly manage the enterprise which is located in the country of one of the parties or in a third state. Pederson, supra note 2, at 390. See generally G. Friedman & G. Kalmanoff, Joint International Business Ventures (1961).

According to Dr. Miodrag Sukijasovic, joint venture contracts are controlled by four legal orders: the national order of the host country which governs questions of business organization, property ownership, taxation, customs, foreign exchange and labor, etc.; the national order of the investor's country which imposes limits on or grants incentives to the foreign investments of
Joint Venture Investment in General

Despite potential difficulties arising from joint management,4 East-West joint ventures afford advantages to both parties. The socialist country not only acquires tangibles, such as cash, machinery and intermediate goods, but also intangibles in the form of property rights, good will and services furnished by the Western firm.5 Continued access to the Western partner’s technical know-how6 and the utilization of Western managerial expertise are of particular importance to the Eastern Europeans.7 Generally the foreign investor is interested in entering a new market, reaching third markets through a new base, and/or transferring production to a place where costs are lower. Often lured to Eastern Europe by the availability of necessary natural resources and a less costly and more stable labor supply, some Western firms favor joint ventures to achieve their goals. The Western company has a large measure of control over production through its participation in management and may thereby receive a higher return on investment than a cooperation agreement involving straight licensing or a sale of technology would yield. Western firms also find that the joint venture association facilitates relations with the local government and believe that the fact that the venture is jointly owned may serve to deter expropriation.8

Joint ventures constitute the most complex form of business endeavor that can be established in member-countries of the Council for Mutual Economic Assistance (COMECON) or the Socialist Federal Republic of Yugoslavia [hereinafter Yugoslavia]. Proposals for joint ventures are generally scrutinized by the socialist country to determine its citizens; the international order, including public and private international law and the international law of investment, which prescribes legal principles protecting foreign investment property; and transnational law which is an attempt to isolate international economic development agreements and joint venture contracts from national laws and international law. M. SUKIJAŠOVIĆ, supra note 1, at 57-58.

4 Many Western firms still hold the conservative view that joint ventures are “fraught with risks.” Most companies attempting this form of investment have previously engaged in straight sales transactions, followed by licensing or production cooperation. Business International S.A., Joint Ventures: Rush or Wait, 8 BUS. EASTERN EUROPE 332, 333 (1979).

U.S. firms generally have not been eager to establish joint ventures in Eastern Europe since major U.S. corporations favor wholly owned subsidiaries which are not permitted in European socialist countries. P. JONAS, TAXATION OF MULTINATIONALS IN COMMUNIST COUNTRIES 16 (1978).

5 P. JONAS, supra note 4, at 15.

6 From the socialist perspective, cooperation agreements have sometimes been used by Western firms to unload out-dated technology. Even if the technology has been current at the inception of the agreement, by the time the East European partner has mastered it, the foreign partner has gone beyond it. In addition, some turnkey cooperation agreements have allegedly not been fully or properly implemented. Pederson, supra note 2, at 396 n.24.

7 See id. at 396. The Western company directly participates in marketing and other operations of the joint company whereas cooperation agreements do not incorporate such ongoing managerial participation. Starr, The Potential for Joint Ventures in Eastern Europe, 10 INT’L L. 35, 35 (1976).

8 See P. JONAS, supra note 4, at 14-15; Pederson, supra note 2, at 396; Starr, supra note 7, at 35; Travaglini, supra note 1, at 172.

9 Business International S.A., Joint Ventures: Rush or Wait?, supra note 4, at 333.
whether the activities of the enterprise will advance the economic goals of the country, especially the development of production for export purposes. In 1967 Yugoslavia became the first socialist country to allow foreign capital investment. Although Yugoslavia has been the leader in attracting joint ventures with Western firms, the Socialist Republic of Romania, the Hungarian People’s Republic, and mostly recently the Polish People’s Republic [hereinafter Romania, Hungary and Poland] have also passed legislation specifically permitting international joint ventures within their borders.

In all four countries it is now possible to establish joint ventures that have legal characteristics similar to joint ventures in market economy nations, with the proviso that the Western partner’s equity share may as a general rule not exceed forty-nine percent. This legislation provides the legal framework for joint ventures and guarantees the property and management rights of foreign investors, thus protecting the Western firm from the power of the state to “dispose of the property rights of individual enterprises” and to “merge, divide, regroup, and rearrange industrial branches in accordance with the economic plan or current line of economic policy.” In the absence of such protective legislation, the Western investor has no assurance of its legal position in a socialist regime.

10 P. Jonas, supra note 4, at 23.
11 Id.
12 M. Sukijasovic, supra note 1, at 7.
13 The most recent joint venture legislation of these countries, i.e., Yugoslavia (1978), Romania (1972), Hungary (1977) and Poland (1979), will be discussed. There are a number of basic similarities in the foreign investment laws of these countries, but substantial differences exist as to the legal status, scope of activities and organizational structure of a joint venture in each country. See National Legislation and Regulations Relating to Transnational Corporations, U.N. Doc. ST/CTC/6.15 (1978) [hereinafter cited as National Legislation].
14 Starr, supra note 7, at 35-36. Unlike transacting with independent private entities in market economies, state control of economic activity in socialist countries requires that the Western company exercise care in identifying the appropriate Eastern partner. Although the Eastern party may be a producing enterprise, it more likely will be a foreign trade organization (FTO) or a governmental body. The structure of the governmental organization of the country, coupled with the form of the agreement and the field in which cooperation is anticipated, determines which socialist entity will have authority to deal with the Western firm. See Starr, Evolving Patterns of East-West Business Transactions: Introductory Note on Cooperation Agreements, in EAST-WEST BUSINESS TRANSACTIONS 490-91 (R. Starr ed. 1974).
15 While preserving socialist ownership of the means of production, this limitation ensures that the Western partner will not have voting control in the joint company. However, it is possible to include mechanisms in the contract to provide the Western firm with a substantial measure of control in key areas and to prevent important decisions from being taken without its consent. Starr, supra note 7, at 38. Also, exceptions to the forty-nine percent limitation may be permitted by the government if in the national interest. See National Legislation, supra note 13, at 15.

Usually the capital is provided according to a ratio determined by the contract establishing the joint venture association. P. Jonas, supra note 4, at 15.
16 Grzybowski, supra note 2, at 263.
17 In socialist regimes of the Soviet type, such as Poland, the ownership of land and the
This legislation has not only a protective effect, but also a regulatory function. As compared with market economies, the more centralized political and economic systems of these socialist countries permit greater supervision and control of foreign investment. Thus, the Eastern European governments are able to enforce the detailed requirements set out in their respective laws and decrees much more effectively than countries operating under a market system.  

Yugoslavia

Yugoslavia’s 1967 legislation permitting foreign investment in domestic enterprises was followed in 1973 and 1975 by subsequent codifications of the law. In 1978 the Yugoslav Federal Assembly completed the latest revision of the country’s legislation on this subject by enacting a new law covering joint ventures within Yugoslavia. In general, two changes appear to favor Western investment. This new legislation provides for greater flexibility in regard to capitalization of equipment and know-how and permissibility of profit transfer either in dinars or products. On the other hand, the law establishes profit ceilings for the first time, stipulating that the foreign partner’s share is to be determined by the proportionate value of its investment. Moreover, all proposals will be

means of production are vested exclusively in the state. The state thus has powers over the management of industry and commerce which must be restricted in order to encourage foreign investment. Joint venture legislation provides a legal basis for the formation of joint venture enterprises and guarantees property and management rights of investors. Id.

The remaining European socialist states follow the policy of the U.S.S.R. and do not permit Western capital investment in their economies. P. JONAS, supra note 4, at 74. Czechoslovakia is expected to solicit more co-production and licensing agreements in 1979 and thereafter, but no mention has been made of joint ventures. Bulgaria issued new regulations on the subject of industrial cooperation with Western firms in 1974 but refrained from approving joint venture agreements. See Business International S.A., Eastern Europe in Brief, 8 BUS. EASTERN EUROPE 62 (1979). Likewise, East Germany and the Soviet Union have no joint venture legislation. Starr, supra note 7, at 37.

18 National Legislation, supra note 13, at 17.
20 Law on Investment of Resources of Foreign Persons in Domestic Organizations of Associated Labor, Official Gazette of the SFRY No. 22/73. See Conner, Joint Ventures in Yugoslavia, 10 INT’L L. & COM. REG. 45, 47-52 (1976) for a summary of this legislation and the formation of joint ventures under its provisions.

In 1975 Yugoslavia issued another law of the same title, Official Gazette of the SFRY No. 12/75, and in 1976 a Decree Specifying the Conditions for the Investment of Resources of Foreign Persons into Domestic Organizations of Associated Labor, Official Gazette of the SFRY No. 26/76.


These two laws, enacted in 1978, were intended “to improve the climate for foreign technology and capital,” and “to curtail certain practices of foreign licensors and investors that the Yugoslavs find objectionable.” Conner, Introductory Note, 18 INT’L LEGAL MATERIALS 229 (1979).
subjected to tight screening by Yugoslav officials.\textsuperscript{22}

Yugoslavia’s interests in joint venture investment are described in Article 1 to include acquiring modern technology and increasing exports and the supply of goods on the domestic market.\textsuperscript{23} The country still adheres to the general rule limiting the foreign partner’s equity share to a maximum of forty-nine percent;\textsuperscript{24} but provides in the same article:

> Exceptionally, if the investment of resources of foreign persons is of special interest for the development of a particular branch of the economy, or of a particular activity, the existence of such interest . . . being established by an act of the Federal Assembly, the joint venture agreement can provide that the total value of resources which foreign persons invest in a DOAL [organization of associated labor] exceed the total value of resources which are invested by DOAL’s.\textsuperscript{25}

Article 8 lists ten areas which the joint venture agreement itself regulates, including the amount of total resources invested by the DOAL and the foreign person respectively, the procedure for establishing the amount of the income of the DOAL in which the foreign person participates, obligations concerning the sharing of risks, and the procedure for settling disputes.\textsuperscript{26} The law also permits the joint venture agreement to

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\item \textsuperscript{22} Business International S.A., \textit{Green Light for More Yugoslav Joint Ventures}, 7 BUS. EASTERN EUROPE 121, 121-22 (1978). Provisions apparently favorable to the West include the elimination of upper limits on the value of imported equipment, previously limited to one-third of the foreign partner’s total investment; a broader range of permitted activities excluding only commerce, insurance and public services; and removal of the requirement that Western firms supply the joint venture with all modifications and improvements in any patents and know-how. Business International S.A., \textit{Yugoslavia’s New JV Law: The Positive Provisions}, 7 BUS. EASTERN EUROPE 356-57 (1978).
\item \textsuperscript{23} In contrast, maximum profit levels must now be specified in the joint venture contract, and any excess profits must “either be reinvested or taken out as a reduction of the foreign partner’s invested capital.” Business International S.A., \textit{Yugoslavia’s New JV Law: Some Provisions Under Fire}, 7 BUS. EASTERN EUROPE 362, 362-63 (1978) [hereinafter cited to reprint as \textit{Yugoslavia’s New JV Law}]. On this subject the law states, \textit{inter alia}:

> The foreign person participates in the income realized by the joint venture in proportion to the contribution which he has made to the realization of that income on the basis of the invested resources. Art. 17, ¶ 1. The [organization of associated labor] and the foreign person establish in the joint venture agreement the maximum amount of compensation for use of the invested resources in economic activities as the part of the foreign person’s participation in the income realized by the joint venture. Art. 19, ¶ 1. [Any excess] is deducted from the amount of resources in the joint venture unless this is provided for differently in the joint venture agreement. Art. 19, ¶ 3.

Law on Investment of Resources of Foreign Persons in Domestic (Yugoslav) Organizations of Associated Labor, 18 INT’L LEGAL MATERIALS 230, 234-35 (1979) (emphasis added) [hereinafter cited to reprint as \textit{Law on Joint Ventures}].
\item \textsuperscript{24} Law on Joint Ventures, \textit{supra} note 22, at 230.
\item \textsuperscript{25} Article 11 states: “The total value of resources which foreign persons on the basis of a joint venture agreement invest in a given DOAL cannot exceed the total value of the resources which DOAL’s invest, nor can it be equal to the total value of these resources.” \textit{Id.} at 232.
\item \textsuperscript{26} \textit{Id.} at 231-32. The term “total resources” refers to capital, equipment and know-how, etc., thereby excluding pure financial investments. National Legislation, \textit{supra} note 13, at 16-17. Note, however, that the Federal Executive Council “shall prescribe the lowest amount, or percentage of the total value of the joint venture, which the foreign person must invest . . . .” art. 11, ¶ 3, and the joint venture will not be approved unless this minimum amount is invested, art. 42. Law on Joint Ventures, \textit{supra} note 22, at 233, 242.
establish a joint business board to carry out the provisions of the joint venture agreement but imposes restrictions and obligations upon this board once formed.\(^{27}\)

Articles 40 through 51 delineate the extensive procedures required for approval and registration of joint venture agreements.\(^{28}\) Within this section, article 42 provides guidelines as to the circumstances which will prompt approval or disapproval.\(^{29}\) The last section prescribes penalties for various violations of the law or of the obligations assumed by the foreign investor, described in articles 53 through 56.\(^{30}\)

The law addresses termination of the joint ventures in two separate articles. The foreign investor’s right to participate in the income realized by the joint venture expires upon the happening of either of two events: when the value of the invested resources (capital) is returned to him along with compensation for the use of the resources in economic activities (profits, etc.) or when the period specified in the joint venture agreement expires regardless of whether the return of the value of the invested resources has been realized.\(^{31}\) The joint venture agreement may specify the value to be returned to the foreign partner, but the value is to be "reduced in proportion to the amount of uncovered losses which represents the share of the foreign person."\(^{32}\)

Unlike the state-controlled corporations of many socialist countries, Yugoslavia’s commercial enterprises operate under a unique self-management system.

Standing ideologically . . . between the centrally managed, state-enterprise communist countries of Eastern Europe and the basically free-market economies of Western Europe, Yugoslavia has a substantially market-oriented economy in which the various levels of local and federal government provide . . . guidance for the so-called ‘self-managed’ business enterprises that hold and manage the country’s productive assets . . . . It is these autonomous entities which enter into . . . joint ventures with foreign companies.\(^{33}\)

\(^{27}\) See id. at 233-34, arts. 14-16.

\(^{28}\) Id. at 240-46.

\(^{29}\) E.g., for approval, \textit{inter alia}, the joint venture must comply with the provisions of this law and with other regulations, the foreign partner’s share (patent rights, license, technology, etc.) must be realistically valued, and the total amount of resources invested must ensure the realization of certain goals, such as an increase in production, exports, or the construction of new capacities on the basis of modern technology. \textit{Id.} at 242-43.

\(^{30}\) Id. at 246-47.

\(^{31}\) Id. at 234, art. 17, ¶ 2. The following paragraph prohibits the joint venture agreement from providing for a joint venture association for an indefinite period of time. \textit{Id.} at 234, art. 17, ¶ 3.

\(^{32}\) Id. at 239, art. 32.

\(^{33}\) Conner, \textit{supra} note 21, at 229. "Under this system, the workers of every business enterprise manage their affairs in small ‘basic organizations of associated labor’ (BOALs) that are united with other BOALs in a larger domestic ‘organization of associated labor’ (DOAL or OAL) . . . . Foreign joint venture partners normally invest their capital and technology in a single BOAL pursuant to a joint venture agreement with the overall DOAL of which the joint venture unit is a part." \textit{Id.} at 230. Thus, the foreign firm invests in an existing unit of a Yugoslav enterprise rather than creating a new company. National Legislation, \textit{supra} note 13, at 15.
The plants and their assets belong to all the people of Yugoslavia in conformity with the social ownership concept. In lieu of direct government supervision, all workers of a given enterprise have a voice in the operation and management of the factory through a Worker's Council comprised of fifteen or more members. Also, individual enterprises and the commercial banks which supply them with much of their financing are not subject to the restraints of the Yugoslav five-year plans. Yugoslavia has concluded some 165 joint venture agreements with Western enterprises, a substantial aggregate investment greatly exceeding similar Western investment in other Eastern European countries.

Romania

Realizing its need for hard currency in order to promote industrial development, Romania in the early 1970s embarked on a program to encourage direct foreign private investment in the form of joint ventures. According to Decree No. 424 issued in 1972, joint ventures may be formed in areas of industry, agriculture, construction, tourism, transportation, and scientific and technical research.

The foreign company, as discussed above, can own only up to forty-nine percent of the equity. The Romanian Bank of Foreign Trade guarantees not only the Romanian partner's financial contribution to the joint venture, but also the repatriation of profits and other sums due the Western company in hard currency. Although the joint venture must

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34 The workers not only decide what products to produce, the rate of production, selling prices and marketing strategy, but also determine within limits the distribution and reinvestment of profits. Conner, Joint Ventures in Yugoslavia, 10 INT'L LAW. 45, 46 (1976).

35 Id. See generally E. Lamers, Joint Ventures Between Yugoslavia and Foreign Enterprises (1976).

36 Business International S.A., Joint Ventures: Rush or Wait?, supra note 4, at 332. One example of these agreements is the joint venture between Gillette and Yugoslav Commerce to produce Gillette razor blades. Gillette's apprehension that Yugoslavia would curtail the import of razor blades and substitute its own production in order to reduce the flow of hard currency out of the country motivated the joint venture initiative. The joint company began production in 1973 and has maintained and even expanded its share of the razor blade market, although sales to COMECON countries have not been as great as expected. Company officials are satisfied with operating in Yugoslavia, but acknowledge that "some of the more complex processes of decision-making have proved to be a 'time-consuming novelty'." Business International S.A., Pointers from Gillette's Yugoslav Joint Venture, 8 Bus. Eastern Europe 26, 26-27 (1979). See also Business International S.A., Some Ongoing Problems in Yugoslav Joint Ventures, 7 Bus. Eastern Europe 371 (1978).

37 Pederson, supra note 2, at 406.


40 Burgess, supra note 38, at 291.
focus on expanding markets and diversifying products in order to increase exports.\footnote{Rohlik, Trading with Socialist Partners, 4 Ga. J. Int'لم L. & Comp. L. 362, 384 (1974).} Products manufactured by the joint company may be traded in Romania.\footnote{Id.; Burgess, supra note 38, at 295.}

As with the joint venture legislation and decrees of other East European countries, the Romanian government places several restrictions on joint enterprises within its borders. At the outset there is an elaborate procedure for initial approval of the venture and any subsequent changes in its operation.\footnote{After conducting an initial feasibility study, the partners must draft a memorandum of association specifying their intent to enter into the joint venture, its economic justification, and its objectives and purposes. A contract of association and statutes of the joint venture generally provide for the duration of the joint venture, the capital and procedures for subscription, the rights and obligations of the partners, and other details of operation of the joint business. Before execution of these documents, the Romanian partner must obtain approval from the State Planning Committee, the Ministry of Finance, the Ministry of Labor and the Bank of Foreign Trade. The Ministry of Foreign Trade then reviews the proposal to ensure compliance with Romanian law before submitting it to the Council of Ministers. After obtaining approval of the Council of State, the Council of Ministers, upon its acceptance of the proposal, drafts special legislation incorporating the joint venture into local law. Finally, registration of the joint venture with the Ministry of Finance and the Ministry of Foreign Trade brings it into formal existence. Burgess, supra note 38, at 292-94.} The joint company must contribute to a social insurance fund for all Romanian employees and satisfy other financial obligations imposed under Romanian law. These commitments must be met before the joint venture can distribute any profits. Profits are taxed, accompanied by a reinvestment incentive in the form of a deduction. At the operational level, the Romanian partner retains the power to hire and fire both Romanian and foreign personnel.\footnote{Id. at 291-92; Pederson, supra note 2, at 406.}

On the other hand, although the joint venture must develop its own five-year plan with annual updates which may be integrated into the national plan, the business of the company is not subject to the national plan. The mechanism for the settlement of disputes between the parties is left to the agreement of the partners, and Decree 424 contains a provision allowing the use of foreign arbitration tribunals.\footnote{Decree 424, supra note 39, at 656, art. 38.} Foreign firms may deal directly with Romanian enterprises rather than through foreign trade organizations (FTOs) or other government agencies; the decree also permits the direct sale abroad of joint venture production rather than use of the FTO as an intermediary.\footnote{Burgess, supra note 38, at 291, 300.} These concessions to Western market investors initially appeared to illustrate the willingness of the Romanian government to compromise the traditional principle of a state monopoly of foreign trade in order to develop commercial relations with the West.

Despite this auspicious legislation, however, only a few Western firms have established joint companies in Romania.\footnote{Western investors include firms in West Germany, Italy, Austria, France and the
est on the part of Western investors may be attributed to several factors. Domestically Romania maintains one of the strictest centrally-planned systems in Eastern Europe, although foreign relations are generally conducted independently of the Soviet Union and other COMECON countries.\(^{48}\) One joint venture agreement concluded in 1974 encountered unforeseen delays which the foreign investor attributed in part to competition with other enterprises for supplies and construction labor which have priority under the national five-year plan, and to its inability to grant incentives to Romanian workers to complete the plant on schedule since the workers are paid at set rates in Romanian currency (lei).\(^{49}\) As an additional complication, Romanian joint ventures sell exclusively in hard currency, even to domestic buyers. This stymies sales to other COMECON countries, since the FTOs of COMECON members are reluctant to import goods for hard currency from a joint venture in another COMECON country if the same goods can be purchased directly from Western suppliers.\(^{50}\) Romania thus has not presented the most attractive environment for Western firms considering capital investment in Eastern Europe.

**Hungary**

The Hungarian Decree on Economic Associations with Foreign Participation issued in 1977 permits production joint ventures in Hungary for the first time.\(^{51}\) Specified Hungarian economic organizations and foreign enterprises may establish economic associations, subject to the approval of the Minister of Finance. Approval depends upon whether the parties exhibit "mutual interests for producing, trading and servicing activities aiming at the profitable development of the level of technology," and the ability of the association to realize its goals.\(^{52}\)


Control Data Corporation and Romania in 1973 created the joint company Rom Control Data SRL to produce computer printers, card readers and card punch systems. See Donaghue, *Control Data's Joint Venture in Romania*, 8 COLUM. J. WORLD BUS. 83 (1973).

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\(^{48}\) P. Jonas, supra note 4, at 40.


The original Hungarian decree on this subject was issued by the Minister of Finance in 1972. Decree. No. 28/72, Official Gazette of the PRH No. 76, Oct. 3, 1972. This decree did not permit direct Western participation in production. *Hungary: New Decree*, supra note 50, at 290.

\(^{52}\) Hungarian People's Republic: Decree on Economic Associations with Foreign Participation, 17 INT'L LEGAL MATERIALS 1451, 1453, §§ 2(1), 3(3) (1978) [hereinafter cited to reprint as Hungarian Decree].
may be waived by the Minister of Finance in the field of finances (banks) and services. Section 7 of the decree deals with taxes, and section 11 adds that "[w]hile implementing international agreements on double taxation, the standpoint of the Minister of Finance is decisive in the question of reciprocity." In case of dissolution of the association, the foreign company's share remaining after liabilities of the association have been settled may be transferred abroad tax-free.

Foreign employees may transfer abroad fifty percent of their after-tax salaries in a currency stipulated by the association. The National Bank of Hungary agrees to transfer the foreign partner's profits abroad to the extent of the sum paid up to the Bank. The Hungarian National Bank may also issue a guarantee to the Western investor to reimburse it for "damages resulting from acts of the State," up to the amount of the foreign partner's contribution. Section 14 specifies other laws with which the association must comply and adds that the decree does not apply to matters settled by international agreements.

In response to criticism that the 1977 decree was too vague, the Hungarian Ministry of Finance in July 1979 issued a decree "explaining" the law. This explanatory decree clarifies several troublesome points, including accounting practices, taxation, profit transfer, and sales restrictions. Moreover, several substantive provisions favor Western investment: the decree, inter alia, waives the 1977 requirement that joint ventures must be created in new premises separate from existing production facilities, the application and approval procedures are simplified, and the Hungarian National Bank will guarantee fulfillment of all obligations of the Hungarian partner to the joint venture.

Since promulgation of the 1977 decree, approximately thirty companies from five countries have engaged in negotiations with Hungarian officials for the establishment of joint ventures. The Hungarian govern-

53 Id. at 1452, § 4.
54 Id. at 1455, § 13.
55 Id. at 1453, § 8.
56 Id. at 1454, § 11(1).
57 Id. at 1454, § 11(2).
58 Hungarian Decree, supra note 52, at 1451. An Agreement on Trade Relations was concluded in Budapest between Hungary and the United States on March 17, 1978. The agreement contains specific provisions for the entry, exit and stay of foreign employees of joint ventures. In addition, article V states that each party adheres to the Paris Convention for the Protection of Industrial Property, as revised at Stockholm on July 14, 1967, 21 U.S.T. 1583, T.I.A.S. No. 6923, 7727. Both parties also endorse the adoption of arbitration for the settlement of disputes not otherwise amicably resolved. Hungarian People's Republic—U.S.: Agreements on Trade Relations, 17 INT'L LEGAL MATERIALS 1475, 1478-80 (1978).
59 Decree No. 5/1979/PK 10/pm.
60 Hungary: New Decree, supra note 50, at 290.
61 For a description of these and other substantive provisions of the decree, see id. at 291.
ment issued its explanatory decree of 1979 to break a deadlock in negotiations by fostering confidence in Western negotiators so that final agreements could be reached. A major breakthrough occurred in late 1979 when the first banking joint venture is Eastern Europe was established in Budapest. The bank is expected to be instrumental in financing Hungarian investment projects, a factor which may provide additional incentive for Western firms to establish production joint enterprises within the country.

**Poland**

After deliberating over the passage of joint venture legislation for several years, the Polish Council of Ministers issued a decree on February 7, 1979, to promote joint ventures with Western manufacturing enterprises for the production of goods for domestic use and for export. The decree contains the typical limitation of forty-nine percent on the Western partner's equity contribution, and the Western partner will be able to repatriate net profits only to the extent of its equity share in the venture. Western companies must negotiate directly with the Polish industrial enterprise or with the cooperative union that is to become the majority equity holder of the joint company.

Although industrial manufacturing and processing joint ventures are permitted, the Polish enactment precludes the exploitation of raw materials and the development of heavy industry, both key industries that are centrally administered. Foreign personnel must be paid in Polish currency (zlotys), but they can repatriate up to fifty percent of their salaries if the hard-currency funds are made available by the joint venture.

The decree assigns priority to ventures introducing advanced technology and know-how. The joint companies are exempt from the Polish planning system, but all their contracts with Polish State enterprises are subject to the planning regulations that apply to those enterprises. A fifteen-year maximum duration is imposed on the joint venture license;

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62 Id. at 290.
63 Initial capital is subscribed sixty percent by Western banks and forty percent by the Hungarian National Bank and other local banks. While the bank's managing director will be a Hungarian, its president will be a representative of one of the Western banks. Business International S.A., Hungarian-Western Bank Launched in Budapest, 8 BUS. EASTERN EUROPE 324 (1979).
64 Id.
65 Business International S.A., Poland Liberalizes Laws on Manufacturing JVs, 8 BUS. EASTERN EUROPE 81, 82 (1979) [hereinafter cited as Poland].
66 Id. at 81, 82. Methods exist to evade the requirement that the Western partner's right to share in the joint venture profits must be limited to its share of equity capital. The contract may include a clause for the payment of profit-management fees or royalties, and the pricing of supplies sold to the enterprise and of purchases from it by the Western firm at a level advantageous to the Western company offer opportunities to increase the Western firm's income. Starr, supra note 7, at 38.
67 Poland, supra note 65, at 81.
68 Id. at 81, 82.
after that time the Western share of the equity passes to the Polish partner unless an extension is granted. The decree does not elaborate as to the circumstances which would prompt approval of such extension. If the venture is dissolved at any time, even after expiration of the fifteen-year period in the absence of an extension, the Western partner is entitled to a refund of capital in proportion to its equity share.\(^69\)

On March 28, 1979, Polish authorities issued two decrees supplementing the February legislation. In general, these decrees “define the financial transactions that joint ventures in the services sector may undertake” and detail “procedures for import, export and domestic retail trade activity by Polish firms with Western equity.”\(^70\) With regard to the latter, all exports and services abroad must be handled through a specified FTO or state agency. Likewise, imports of raw materials, components and other goods needed for operation of the joint venture must be made by one of the two specified enterprises.\(^71\) Kore International Trade and Investment Company has already built a 600-bed hotel in the center of Warsaw under the Polish joint venture legislation.\(^72\)

Poland’s large debt to the West may prompt Polish officials to encourage joint venture investment in order to increase hard currency earnings through the export of venture-manufactured products.\(^73\) Poland may be especially interested in joint venture associations with Western firms which can supply the necessary mineral-related technology to manufacture industrial products from abundant Polish resources of copper and silver.\(^74\)

**Dispute Settlement**

In general, dispute settlement has not presented extraordinary problems for Western joint venture partners, but express arbitration provisions should be included in the contract in the event that informal negotiations fail to resolve any difficulties. The Eastern European countries permitting joint ventures generally stipulate that investment disputes involving foreign investors are to be settled by domestic courts, but

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\(^69\) Id. Eastern European legislation generally contains such a provision. However, in order for the Western partner to receive a share in the accumulated value of the joint venture upon liquidation, a clause to that effect must be included in the contract. Yugoslavia’s New JV Law, supra note 22, at 363.

\(^70\) Business International S.A., Polish JV Legislation Revised by New Decrees, 8 BUS. EASTERN EUROPE 137 (1979). The decrees consist of an order issued by the Minister of Finance with regard to bank accounts and a joint order of the Ministers of Finance and Foreign Trade & Maritime Economy regulating foreign trade rights. Id.

\(^71\) Id. at 138.

\(^72\) The company is a Chicago-based firm specializing in trade with Poland. Business International S.A., Kore Sees Opportunities for U.S. Firms in Poland, 8 BUS. EASTERN EUROPE 345 (1979) [hereinafter cited as Kore].


\(^74\) Kore, supra note 72, at 346.
disputes may be submitted to arbitration if the contract so provides.\textsuperscript{75} The parties may select an arbitration court in the Eastern European country, in the country of the Western company or in a third state.\textsuperscript{76} Yugoslavia’s 1978 legislation requires that disputes be heard by the authorized court of law in Yugoslavia, unless the joint venture agreement provides for settlement by the Foreign Trade Arbitration at the Yugoslav Chamber of Economy or by some other domestic or foreign arbitration.\textsuperscript{77}

Under Romanian law, the joint venture agreement can provide for the method to be used to resolve disputes between the parties,\textsuperscript{78} such as a provision for settlement at a foreign arbitration tribunal like the Arbitration Court of the International Chamber of Commerce in Paris.\textsuperscript{79} Disputes between the joint venture and Romanian national enterprises or natural persons are subject to the jurisdiction of the courts,\textsuperscript{80} but with the consent of the other party, the dispute may be settled by the Arbitration Commission at the Romanian Chamber of Commerce.\textsuperscript{81} Similarly, Hungary recognizes settlement of disputes by foreign arbitration tribunals and accepts the position of the International Chamber of Commerce on disputes between joint venture partners.\textsuperscript{82} Once the tribunal has rendered a decision, the Eastern Europeans can be relied upon to honor the terms of the arbitration award.\textsuperscript{83}

Conclusion

International joint ventures have become a feasible alternative to other forms of East-West cooperation only during the past decade. Recent legal developments indicate that joint ventures will constitute a more viable form of international economic collaboration in the future. The close working relationship of the East European and Western representatives in the joint company may produce not only commercial success, but also more comprehensive economic cooperation between peoples of divergent political philosophies.

Of the four Eastern European countries which have issued special legislation permitting the establishment of joint ventures with foreign

\begin{footnotesize}
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\item \textsuperscript{75} National Legislation, supra note 13, at 16.
\item \textsuperscript{76} See Business International S.A., EE Gets Tough in Court—Arbitration Cases Rising, 7 BUS. EASTERN EUROPE 361 (1978). One of four alternative sets of rules may generally be elected to govern the arbitration: the Regulations of the International Chamber of Commerce in Paris, the arbitration rules of the U.N. Economic Commission for Europe, the U.N. Commission on International Trade Law (UNCITRAL) arbitration rules, or the COMECON regulations of February 1974. \textit{Id.} at 362.
\item \textsuperscript{77} Law on Joint Ventures, supra note 22, at 246.
\item \textsuperscript{78} Decree No. 424, supra note 39, at 656.
\item \textsuperscript{79} See Business International S.A., Snags in Romanian JV Show Need to Protect Knowhow, 8 BUS. EASTERN EUROPE 41-42 (1979).
\item \textsuperscript{80} Rohlik, supra note 41, at 384-85.
\item \textsuperscript{81} P. JONAS, supra note 4, at 21.
\item \textsuperscript{82} \textit{Id.} at 62.
\item \textsuperscript{83} Van der Huevel, Russel & Winter, Practical Difficulties of Transactions with State Controlled Economies, 4 GA. J. INT’L & COMP. L. 26, 35 (1974).
\end{itemize}
\end{footnotesize}
firms, only Yugoslavia has attracted substantial Western investment through this means. Yugoslavia, the first Eastern European country to allow foreign capital investment in the form of joint ventures, operates its economy under a self-management system which departs from the typical state-controlled systems of other Eastern European countries. It thus may lure businesses which otherwise might consider investment in Romania, Hungary or Poland. However, in 1979 Poland indicated its encouragement of this mode of investment by adopting legislation authorizing joint ventures within its borders, and Hungary reaffirmed its commitment to joint venture associations by issuing a decree liberally interpreting and clarifying its 1977 law. In the future, foreign firms interested in establishing joint ventures in Eastern Europe may seriously consider these other Eastern European countries as an alternative to investment in Yugoslavia.

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