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FOREIGN INVESTMENT IN YUGOSLAVIA — A REVIEW OF THE JOINT VENTURE LAW WITH AMENDMENTS AND PROPOSED CHANGES

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In the light of Yugoslavia's current economic crisis, Yugoslav officials have reiterated that joint venture investment with foreign partners provides an economically sound way of attracting foreign cooperation, needed foreign exchange and technology for the rehabilitation of Yugoslavia's economy. In support of this proposition, Yugoslavia considerably liberalized its Joint Venture Law[1] in 1984 and made several additional amendments in 1985, 1986 and 1987. Nevertheless, there still remains considerable confusion and controversy relating to several aspects of the Law. As a result, the Yugoslav Government is presently considering substantial revisions to the Joint Venture Law which, if adopted, would significantly liberalize foreign investment in Yugoslavia.

The purpose of this paper is to review and clarify the pivotal provisions of the Joint Venture Law, as well as proposed changes, and assess their applicability to foreign investors in Yugoslavia. In discussing the proposed changes, it should be noted that all changes are part of the proposed amendments introduced in the current Draft Law on joint ventures.[2] Although the proposed amendments represent substantial changes in the present Law, the changes must be in conformity with constitutional revisions. Consequently, the Federal Work-

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[1] The Law on Investment of Resources of Foreign Persons in Domestic Organizations of Associated Labour *(Official Gazette of the Socialist Federal Republic of Yugoslavia (SFRY)*, No. 18/78, No. 64/84, No. 5/85, and No. 38/86). (hereinafter cited as the »Joint Venture Law«).

[2] *See* The Second Draft Law of the Joint Venture Law, Federal Committee on Energy and Industry (FCEI), Working Group (Belgrade, September, 1987), (hereinafter cited as the »Second Draft Law«).

ing Committee for Social-Eeconomic Order[3] has recently proposed amending the Constitution in order to provide the necessary forum for adopting fundamental changes to the Joint Venture Law. The Constitutional changes would be in the form of Amendment 12, which would grant foreign investors unprecedented opportunities to formulate Western style joint ventures. Revising the Yugoslav Constitution, however, will take a minimum of one year. Thus, the proposed changes discussed in this paper are presented as a way of illustrating the current views of legislative committees and as a forum for discussing future changes in Yugoslavia's investment climate.

THE BASIS OF THE LAW

The primary objective of the Joint Venture Law is to attract foreign investment in a Yugoslav business organization[4] for the purpose of sharing the risk and income of joint business. Yugoslavia hopes the

[3] Skupština SFRJ Komisija za Ustavna Pitanja Koordinaciona Grupa — radna podgrupa za društveno-ekonomsko uređenje (May 26, 1988, Belgrade) (hereinafter cited as »Amendment 12«).

[4] In this paper, the term »Yugoslav business organization« denotes the different organizations of labour within Yugoslavia's unique »workers' self-management« system. Although a complete exposé of the various organizations is beyond the scope of this paper, it is important for the reader to have a general knowledge of the distinctions among the organizations. The Joint Venture Law stipulates that a joint venture contract may be concluded by a foreign investor with any of three organizations of associated labor: a basic organization of associated labor (BOAL), a work organization (WO), or a composite organization (CO). A BOAL is the basic form of associated labour in which workers directly exercise their self-management rights and decide on all questions concerning their work and status. A BOAL is formed for each unit of a work organization which makes a working unit or technological whole. For example, in an integrated cotton textile mill, there would exist BOAL's in the spinning process, weaving process, and continuing to the retail outlet. The combined working units (i. e., the mill itself) would be considered a work organization. A composite organization is a form of associated labor where work organizations merge. For instance, the cotton mill joined with a synthetic textile mill form a composite organization. If a joint venture contract is entered into by a work organization (WO) or a composite organization (CO), then one or more of the basic organizations (BOAL) must be designated by the contract and vested with the rights and obligations stemming from the contract and the rights and obligations of the WO or CO which formed the contract shall be defined by it. *See Joint Venture Law, supra* note 1, at art. 9. It is the Yugoslav business organization that has the status of a legal entity and makes use of the invested resources of the foreign partner. *See Joint Venture Law, Commentary, supra* note 1, at art. 8. All other organizations (i. e., the WO or CO) are acting as an agent on behalf of the disclosed BOAL. A joint venture can be concluded between a foreign partner and an existing WO or CO. In this situation, one of the existing BOAL's of the WO or CO is divided, thus creating a new BOAL which is vested with the contractual rights and obligations of the joint venture. If the joint venture contract is with a newly formed Yugoslav partner, then a WO must be created through an »act of foundation« which establishes the WO as a legal entity. Since a BOAL cannot exist seperately from a WO, it is the WO and not the BOAL which is created first.

Joint Venture Law will enable it to capitalize on its comparative advantage in the international division of labor, thereby increasing its exports, and to procure modern technology. The joint venture must be of a »long-term nature«, and its exact duration must be stipulated in the contract.[5] This is to assure that the Yugoslav business organization will benefit from an extended period of resource investment and technology transfer by the foreign partner. Nevertheless, the Joint Venture Law does not permit the foreign partner to extract a »permanent share« of the income generated through the joint venture.[6] Thus, the joint venture cannot be of indefinite duration.[7] Although the Joint Venture Law does not stipulate the upper and lower limits of a contract, practical experience shows that a duration of between 5 to 20 years is the acceptable norm.[8]

Among the more interesting proposals for liberalizing the Joint Venture Law is a provision which would permit the partners to form a joint venture contract for a »definite or indefinite period of time.«[9] So long as the partners did not object, a contract concluded for a definite period of time could be »automatically renewed« for a further defined period of time.[10]

In addition, there is a proposal to permit Yugoslav private firms to enter into joint ventures and to expand the definition of a foreign partner to include a Yugoslav citizen who has a registered business abroad.[11] Under the Second Draft Law, the Yugoslav investor may be an artisan cooperative or other cooperative, or a Yugoslav citizen who has at his disposal resources in conformity with the foreign exchange laws.[12]

One of the significant advantages of Yugoslavia's Joint Venture Law is the great flexibility afforded the parties in devising a contract that will realize their common objectives. The Joint Venture Law mandates only that certain broad parameters be included in the contract.[13]

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[5] *Joint Venture Law, supra* note 1, at art. 3.

[6] *Id.*, at art. 18.

[7] A joint venture contract must provide for the termination of the foreign partner's share in the income of the joint venture. *Id*, at art. 27.

[8] There are cases where the agreed upon period has exceeded 30 years. *See* Tešić, *The Yugoslav Model of International Transfer of Technology*, Exportpress (Belgrade, 1986) at 145.

[9] *See* »The Second Draft Law«, *supra* note 2, at art. 44.

[10] *Id.*, at sec. 2.

[11] *Id.*

[12] *Id.*, at sec. 3 and Amendment 12, *supra* note 3.

[13] The Joint Venture contract shall regulate in particular: (1) the subject matter of the joint venture, (2) the manner for determining the foreign partner's share in the income generated by the joint venture, (3) the terms, manner and time limits for paying the foreign partner's share of the income generated by the joint venture, (4) the terms, manner and time limits for returning to the foreign partner the remaining value of the resources invested, (5) the mutual obligations of the contracting parties in the event of business losses, and other obligations concerning risk bearing, (6) the composition and powers of the joint venture board, and mode of its election, and (7) the manner of settling mutual disputes. *Joint Venture Law, supra*, note 1, at art. 7.

It is advisable, however, to include in the contract the fullest possible provision for all issues involved in the joint venture, including an »article of definitions« to help clarify Yugoslav legal and economic terms. Direct discussions with foreign investors reveal that such meticulous preparation will greatly facilitate the operation of the joint venture. This includes stating what the »common goals« of the joint venture are to be. This is important because the failure to adhere to the predetermined goals of the joint venture is grounds for terminating the contract.

APPROVAL OF THE JOINT VENTURE CONTRACT

The approval of a joint venture contract is subject to only one Yugoslav federal agency: the Federal Secretariat on Foreign Economic Relations (FSFER)[14]. This amended provision is a significant simplification from the 1978 Joint Venture Law[15] which required the parties to obtain approval from various federal and republican agencies. The application for approval is accompanied only by the text of the

[14] This Secretariat was recently formed (May, 1988) through the reorganization of the Federal Committee on Energy and Industry (FCEI) and the Federal Secretariat of Foreign Trade. Although the 1984 Joint Venture Law virtually abrogates the authority of the various federal, republican and provincial agencies (Yugoslavia is divided into six republics and two autonomous provinces) in approving joint venture contracts, the law does require »opinions« and »comments« from several of these agencies. See *Joint Venture Law, supra* note 1, at art. 50. Once the contract is completed and approved by the workers' council of the Yugoslav business organization in which the resources are invested, the Joint Venture Law requires that prior to submitting the contract to the FCEI (i. e., now the FSFER), the Yugoslav partner must inform the Yugoslav Chamber of Economy of its intention to form a contract. *Id., supra* note 1, at art. 46. Since the Yugoslav Chamber of Economy is a nonprofit, »service« association of labor, organized to assist in the fomulation and cooperation of economic activities throughout Yugoslavia, its involvement in joint ventures is viewed primarily as an exercise in record keeping. Official interpretation, however, suggests that the Yugoslav Chamber of Economy may inform the Yugoslav partner of any possible problems that might arise in cooperation with the foreign partner. Although the legal consequences of such »suggestions« are not indicated in the Joint Venture Law, practical experience shows that the Yugoslav partner is expected to comply with changes to provisions of the contract which the Chamber finds to be contrary to the requirements of the law. In addition, the FCEI (i. e., the FSFER) is required to obtain an opinion by the Federal Office of Social Planning as to whether the provisions of the contract are contrary to the social plan of Yugoslavia. Another opinion is provided by the Yugoslav Chamber of Economy as to whether the provisions of the contract are contrary to the established strategy of Yugoslavia's technological development. The Committee may also seek the opinions of federal, republican and provincial authorities. *Id.*, at art. 50.

[15] The Law on Investment of Resources of Foreign Persons in Domestic Organizations of Associated Labor *(Official Gazette of the SFRY*, No. 18/78) (hereinafter cited as »the 1978 Joint Venture Law«).

joint venture contract[16] and a feasibility study.[17] Upon receipt of this information, the FSFER has 60 days to render a ruling on the application for approval of the joint venture contract.[18] If the application is not approved an appeal may be lodged with the Federal Executive Council[19] within 15 days from the date of service of the ruling.[20] The ruling of the Council is final and no administrative appeal is permitted.[21]

Although it is not uncommon for the approval process by the FSFER to exceed the legal 60 day limit,[22] the delay is more often caused by repeated requests by the FSFER for amendments to the contract.

Currently, there is discussion on changing the approval period from 60 to 30 days. This change would bring Yugoslavia in line with

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[16] If the joint venture involves technology transfer, long-term industrial coproduction or business and technical cooperation, then separate contracts for these areas are also included in the application for approval.

[17] The feasibility study is an economic and technical study which provides information on: (1) the sources of assets, (2) technological requirements for manufacturing products, (3) equipment, intermediate and raw materials to be imported, (4) the state of the professional staff to be employed, and (5) marketing. *See Joint Venture Law, supra* note 1, at art. 48. The preparation of the feasibility study may take from two to six months depending on the size of the joint venture. It is the responsibility of the Yugoslav partner to prepare the study which, of course, will be completed with the cooperation of the foreign partner. The importance of this study should not be underestimated. Not only is the study a basis for approval by the Yugoslav authorities but it represents the intentions of the parties to undertake contractual obligations based on its contents. Large size ventures will require the participation of various experts in the fields of law, accounting, marketing, engineering, etc. It may be appropriate for a small size venture, where the partners do not possess the experienced specialists, to contract with a qualified institution or company to formulate the feasibility study. Preparations can be costly. Discussions with foreign investors estimate that for a 1 million dollar contract, it will cost between 5 to 15 thousand dollars for the study, in addition to 10 to 20 thousand dollars for market research. Assistance is often available, without fee, through the Yugoslav bank which is participating in financing the joint venture. There also exists the International Investment Corporation of Yugoslavia (IICY) which can provide the foreign investor with assistance at a fee. The IICY is a consortium of 55 Yugoslav and major international banks established for the promotion of investments in Yugoslavia. In addition, there is the center for International Economic Cooperation which provides assistance to foreign investors. It is imperative that the foreign partner hire a Yugoslav attorney during the preliminary stages of the contract. The FCEI does not allow the foreign investor to be present during discussions. Only the Yugoslav partner may be present. The foreign investor, however, can be represented at the Committee discussions by a Yugoslav attorney.

[18] *Joint Venture Law, supra* note 1, at art. 50.

[19] The Federal Executive Council is the executive political body of the Yugoslav Assembly. The status and powers of the Council are similar to these of cabinets in other countries.

[20] *Joint Venture Law, supra* note 1, at art. 50. Since the Law does not state which party may appeal, the foreign party may lodge an appeal. *See* J. Barbić, M. Hanžeković, Z. Sakač, *Strana Ulaganja u Jugoslaviji,* (Informator, Zagreb, 1986).

[21] *Joint Venture Law, supra* note 1, at art. 50.

[22] Of the most recent 13 joint ventures in Yugoslavia, only 3 have been approved within one year. *See Politika,* 11 May 1987, p. 12.

other developing countries whose joint venture laws require a maximum of 30 days for approval. Notwithstanding, the proposed draft would retain the provision which permits the FSFER to wait 60 days from receipt of the application before rendering a decision as to the validity of the contract.[23]

There are essentially five areas where the FSFER will deny approval.[24] A joint venture contract will not be approved if the contract: (1) infringes upon the equality of the Yugoslav business organization and the foreign partner, i. e., the foreign partner cannot act in a multinational fashion and »control« the joint venture, (2) restricts exports of products manufactured by the Yugoslav business organization which are the subject matter of the contract and such restrictions are contrary to Yugoslavia's policy and system of foreign economic relations,[25] (3) incorporates provisions which are contrary to the social plan of Yugoslavia, (4) incorporates provisions which are contrary to the established strategy of technological development of Yugoslavia, and (5) incorporates provisions which are contrary to the defense and security interests of Yugoslavia.

There are also several »de facto« areas where joint ventures are not permitted.[26] They include insurance,[27] trade and social activities, i. e., education, cultural areas, social security, child care, etc.[28] A new exception to this provision is health and recreation related services. Thus, joint ventures are permitted in services involving outpatient and inpatient care, medical rehabilitation, dental care, pharmacies and recreational activities.[29]

Foreign investment in the banking and armaments sectors of the Yugoslav economy is regulated by separate laws.[30]

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[23] *See* Second Draft Law, *supra* note 2, at art. 52.

[24] *Joint Venture Law, supra* note 1, at art. 49.

[25] This provision does not preclude the foreign partner from restricting the sale of products to countries where it has existing production or exclusive licensing arrangements.

[26] *Joint Venture Law, supra* note 1, at art. 11.

[27] This restriction could be amended depending on the outcome of the GATT discussions regarding restrictions of insurance services. Nevertheless, discussions with Zlatko Mandžuka, Secretary for Relations with OECD Countries in the Yugoslav Chamber of Economy, reveal that Yugaslavia is not presently contemplating changes in the law which would permit joint ventures in the insurance sector.

[28] The Federal Executive Council can grant an exemption to this provision and permit joint ventures in certain social activities if this will contribute to the development of the activities concerned. *Joint Venture Law, supra* note 1, at art. 11.

[29] The inclusion of recreational activities corresponds to article 33 of the Joint Venture Law which permits the foreign partner to contribute services to the joint venture in lieu of income. These provisions are intended to attract foreign investors to Yugoslav tourist projects.

[30] For banking: The Law on the Yugoslav Bank for International Economic Cooperation and on Joint Financial Organizations *(Official Gazette of the SFRY*, No. 55/78) and the Law on Joint Banks *(Official Gazette of the SFRY*, No. 32/87). For armaments: Regulation on the Investment of Resources of Foreign Legal Entities and Physical Persons in Domestic Organizations of Associated Labor Manufacturing Armaments and Military Equipment *(Official Gazette of the SFRY*, No. 65/84).

Upon approval by the FSFER, the contract must be registered in accordance with the Joint Venture Law within 15 days of the date of approval.[31] The FSFER will then notify the authorities of the republic or autonomous province where the Yugoslav business organization is located.[32]

The Yugoslav partner is responsible for forwarding to the FSFER, the Yugoslav Chamber of Economy and the appropriate republican or provincial authorities annual reports on the achievements of the joint venture with respect to the success of the business, imports, exports, technical equipment, technology applied and other relevant data pertaining to the operation of the joint venture.[33] The annual report must be submitted by April 30 of the current year for the previous year.[34]

THE VALUE AND FORM OF INVESTMENTS BY THE FOREIGN PARTNER

The capital invested by the foreign partner may be in the form of foreign exchange, tangible assets and »rights which constitute instruments and objects of labor« (i. e., intangible assets and labor).[35] The most common arrangement is where the foreign partner contributes intangible assets and cash[36] and the Yugoslav partner contributes fixed assets.[37] Intangible assets include patent rights, trademark and brand rights, rights to production and technical documentation, and know-how.[38] Investment of intangible assets must also adhere to

[31] Article 51 of the Joint Venture Law lists the information required for registration.

[32] *Joint Venture Law, supra* note 1, at art. 51.

[33] *Id.*, at art. 56.

[34] Detailed regulations of the report is set by the FSFER in cooperation with the Public Accounting Office.

[35] *Joint Venture Law, supra note* 1. Since foreigners cannot own property in Yugoslavia, the invested capital cannot be in the form of land or buildings.

[36] Prior to 1984, the investment had to be in a convertible currency. New changes in the law, however, now permit investment in any foreign currency. The investment cannot be in the form of dinars unless the foreign partner is reinvesting into the joint venture.

[37] The latest figures from the Yugoslav Federal Office of Statistics show that in 1983, total foreign resources invested through joint ventures comprised 82% cash, 11% equipment and 7% intangible assets. Other studies have shown a somewhat smaller proportional representation with 57% investment in cash, 24% in intangible assets and 19% in equipment. *See* P. Artisien, *Joint Ventures in Yugoslav Industry,* (Grower Press, 1985), at 124. The differential may be explained by the percent of the foreign partner's investment share. When the share is relatively large (i. e., above 25%), cash contribution is significantly higher than other forms. When the investment share is less than 25% (usually denoting a smaller foreign firm with less cash) contribution through intangible assets becomes increasingly more important. *See* Artisien, *Id.* The Yugoslav partner, however, is permitted to invest intangible rights and labor.

[38] Under previous joint venture laws, the foreign partner could not contribute know-how without allowing the Yugoslav partner to use the technological improvement brought about during the duration of the con-

the requirements of the relevant laws.[39] For this reason, it is important to survey and clarify the relationship among the particular laws which are included in the joint venture contract. For instance, if the joint venture contract includes a licensing agreement, then that agreement will also be subject to different regulations other than the Joint Venture Law. Thus, it is important to stipulate which laws will have priority in case of conflict. Furthermore, there should be a clause in the joint venture contract which addresses the consequences of changing one of the incorporated agreements in relation to the joint venture contract as a whole.

In addition, the foreign partner may invest equipment and intermediate or raw materials. This is permissible, however, only when the goods are not produced in Yugoslavia in appropriate quality and quantities and at appropriate prices.[40]

The total value of the resources necessary for the joint venture is freely determined by the partners in accordance with the specific conditions and requirements of their project. An important change already adopted in the existing Joint Venture Law, which could greatly enhance the partners' ability to structure a flexible investment, pertains to the maximum level of investment for the foreign partner. The previous joint venture laws required the foreign partner to maintain a minority investment position in the joint venture. Thus, the foreign partner's share of the invested capital in the joint venture had to be less than 50%.[41] The present Joint Venture Law permits the foreign partner's investment share to exceed the parity level and thus the foreign partner may now hold a majority »equity« position. The Law also abolishes the lower investment requirement limit for the foreign partner.[42] The removal of the lower limit requirement is an attempt

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tract. This is no longer a requirement under the current Joint Venture Law. Intangible assets may also include the value of human capital in the form of management and manpower.

[39] In the areas of patent, trademark and brand rights, the applicable law is The Law on the Protection of Inventions, Technical Improvements and Trademarks *(Official Gazette of the SFRY,* No. 34/81). If the joint venture provides for the investment or procurement of technology, then the applicable law is the Law on Long-term Coproduction, Business and Technical Cooperation and Acquisition and Assignment of Material Rights to Technology between Organizations of Associated Labor and Foreign Persons *(Official Gazette of the SFRY,* No. 30/83) (hereinafter cited as the »Law on Long-term Cooperation«).

[40] The opinion as to the »appropriate quality and quantities« and »appropriate prices« is rendered by the Yugoslav Chamber of Economy. *See Joint Venture Law, supra,* note 1, at art. 12.

[41] The 1967 Joint Venture Law (which was actually a combination of four different laws) provided for a maximum foreign investment of 49%. *See* The 1967 Joint Venture Law *(Official Gazette of the SFRY,* No. 31/67). The 1978 Joint Venture Law also provided for a maximum of 49%. *See* The 1978 Joint Venture Law, *supra* note 15.

[42] In accordance with the Decree on the Minimal Amount of Resources which a Foreign Person Must Invest into the Domestic Organization of Associated Labor *(Official Gazette of the SFRY,* No. 45/78), the minimum investment was the lesser of either 10% of the »total value of the joint project« or five million dinars.

by Yugoslav authorities to attract smaller investors into Yugoslavia.[43]

It is important to note, however, that the ability of the foreign partner to acquire a majority investment share in the joint venture does not imply an interest in property rights. The total value of each partner's investment share denotes only a contractual right and acts as the basis for determining each partner's share in the income generated by the joint venture.[44]

Furthermore, the foreign partner's status as the majority investor in the joint venture does not include operational control over the joint venture. The responsibility of managing the joint venture is the function of a joint business board which will be discussed in a separate section of this article.

These limitations may change with the adoption of Amendment 12 to the Constitution. Provisions in that Amendment would allow the joint venture partners to determine their respective rights and obligations through collective agreement.[45] Theoretically, the foreign partner could gain significant control over the operation of the joint venture. The proposed Amendment, however, does state that these freely defined rights and obligations could not be in conflict with federal law.[46] Consequently, there is sufficient opportunity for the Yugoslav government to restrict the perceived liberalization.

Finally, the ability of the foreign partner to acquire a majority investment share in the joint venture does not abrogate the obligation of the Yugoslav business organization to share the risks of the joint venture. In fact, a joint venture is illegal unless it provides for the sharing of business risks.[47] The very nature of joint ventures in Yugoslavia is »joint risk sharing«, not nomination by multinationals.[48] Thus, the Yugoslav business organization must contribute to the investment into the joint venture.

The exact share of each partner's investment, however, is determined by the contracting parties. Consequently, whereas a 100% majority investment share by the foreign partner would not be permitted, there is no legal impediment to the foreign partner acquiring a 99% investment share.[49] Although such a high porportional investment share by the foreign partner is legally permissible, the practical concern is whether the Yugoslav authorities would grant approval to the contract.

This aspect of the Joint Venture Law would also change with the adoption of Amendment 12. The provisions of the Amendment

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[43] There is some confusion as to whether a minimum investment would be required under the new Joint Venture Law. The Second Draft Law states that the share of foreign capital invested in the joint venture »shall not amount to less than 20%« of the total investment.

[44] *See Joint Venture Law, supra* note 1, at art. 18.

[45] Amendment 12, *supra* note 3, at sec. 3.

[46] *Id.*

[47] *Joint Venture Law, supra* note 1, at art. 27.

[48] *See* Orbe, »The Multinational in Yugoslavia«, 19 *The International Lawyer* 632 (1985).

[49] This view was supported by members of the Yugoslav Government during the U.S. Overseas Private Investment Corporation (OPIC) mission, held in Belgrade, May 26, 1987 (hereinafter cited as the »OPIC meeting«).

would allow for the creation of »mixed companies« and »wholly-owned« foreign companies within certain designated »free trade zones.«[50]

It is common that the joint venture contract evokes the principle of limited liability for the foreign partner. In this way, the foreign partner is liable only for the amount of his initial capital investment.[51] Thus, the contract should also stipulate that any losses[52] incurred through the joint venture will be covered by the partners in proportion to their invested shares. If the foreign partner fails to cover his proportion of losses with additional resources, then his initial resources will be reduced by the corresponding amount.[53] Since, however, the foreign partner is entitled to the »premature« termination of the contract after two consecutive years of losses,[54] it is unlikely that all of his resources invested in the joint venture would be used to cover the losses.

LOANS

Because of changes incorporated in the Joint Venture Law, the resources required to finance the joint venture can now be obtained from a credit or loan.[55] This is an important amendment because it eliminates the necessity of the partners to secure 100% of their required contributions to the joint venture in the form of equity. Still, a major drawback to this provision is that the amount of the loan cannot exceed the amount of equity invested by the contracting parties. Thus, the debt: equity ratio cannot exceed 1:1. The debt: equity ratio, however, applies only to »joint loans.« It does not apply to credits taken independently by the foreign partner or the Yugoslav business organization.[56] When the joint venture does obtain a »joint

[50] Amendment 12, *supra* note 3, at sec. 3.

[51] *Joint Venture Law, supra* note 1, at art. 28. Article 28 reads: »Foreign persons shall be liable for obligations arising from joint ventures to the extent of the resources they have invested, *unless they have assumed greater liability under the joint venture contract*« (emphasis added).

[52] Losses occur when the income generated by the joint venture is smaller than the agreed upon amount for workers income or smaller than the amount of personal income guaranteed by the law for the period for which the workers have not been paid. In addition, losses occur when the income is smaller than the amount of liabilities to be met under law out of the income of the joint venture. *See Joint Venture Law, supra* note 1, at art. 29.

[53] During the year where losses are recorded, the foreign partner cannot share in the income generated by the joint venture. It is important to note that other than when the joint venture records a loss, the foreign partner cannot be compelled to invest additional resources into the joint venture.

[54] *Joint Venture Law, supra* note 1, at art. 13.

[55] *Id.*, at. 8.

[56] Either party may obtain financing for its own invested share. Consequently, the repayment of the loan comes from the partner's share of income (or other sources) after distribution of the joint venture income. For instance, the Yugoslav partner may obtain its share of assets from three sources: (1) his own accumulated funds, (2) a contract with another Yugoslav business organization to supply assets, or (3) a loan from a Yu-

loan«,[57] the ultimate user is the Yugoslav business organization (i. e., the BOAL). Although there is a legal distinction between the joint venture entity and the participating BOAL as to their respective capacity to acquire a joint loan, the practical effect is the same.[58]

The »joint loan« must be repaid from the income generated by the joint venture and prior to its distribution between the partners. Assuming it is stipulated in the contract, each partner's share in the repayment of the loan principle is determined by their proportional investment share. The interest payments, however, are deducted prior to reaching the net income (i. e., as an expense) and, therefore, are not proportionally allocated between the partners.[59] Prior to a 1986 amendment,[60] the emphasis was on the ability of the joint venture to generate sufficient funds for the repayment of the loan. If the income generated by the joint venture was not sufficient for repaying the loan, the partners were obligated to repay the loan »proportionally to the stipulated risk of the joint venture«.[61] At present, if there does not exist sufficient income for repayment, the necessary funds can be obtained by »other means«, in conformity with the contractual provisions. Since the amended law permits the partners to define the term »other means«, it is likely that the proportional risk sharing aspect of »joint loans« would still apply since it is an important reaffirmation of the foreign partner's limited liability.

goslav bank. The foreign partner may also independently take loans to finance operations which contribute to the aims of the joint venture. For instance, the foreign partner may, through credit, supply the equipment for the construction of the plant which is the subject matter of the joint venture. *See* Commentary *Joint Venture Law, supra* note 1, at art. 8.

[57] There has arisen a problem with securing a joint loan through the joint venture itself. Since funds invested in the joint venture are always vested with the Yugoslav business organization, only the Yugoslav business organization has the legal status to make use of the joint loan. The credit user is always the Yugoslav business organization and thus is responsible for repaying the credit from the income generated by the joint venture before it is distributed between the parties. However, if the Yugoslav business organization is a newly formed entity, it does not have any legal status until the act of foundation and does not become effective until that date. Consequently, the Yugoslav banks will not approve any loans until such time of foundation. For further discussion on this matter, *see Industrial Cooperation and Investment in Yugoslavia*, (Office for Official Publications of the European Communities no. CB. 46-86-630-EN.C, Luxembourg, 1986) (hereinafter cited as »Investment in Yugoslavia«).

[58] A joint venture must be registered as an Organization of Associated Labor with a share of foreign capital. For an excellent discussion on this point *see* Vukmir, »Recent Development in Joint Venture Legislation in Yugoslavia«, *ICSID Review*, (Spring, 1986) at 73.

[59] *See* Kovačević and Bilušić, *Razmatranja o Potrebi Poboljšenja Načina i Uvjeta Realizacije Zajedničkih Ulaganja*, discussion paper, International Investment Corporation for Yugoslavia (1987).

[60] *See Official Gazette of the SFRY*, No. 38/86, at art. 1.

[61] *Joint Venture Law, supra* note 1, at art. 8.

DECISION-MAKING

Under the Joint Venture Law, decisions relating to the business activity of a joint venture can be decided either directly by the parties or through a joint business board within the framework of the joint venture contract.[62] To date, nearly all of the joint venture contracts concluded have established such a board.[63] In 1976, a change in the law clearly eliminated the past »de facto« advisory function of the foreign partner and introduced the concept of »joint management«. Consequently, the board will decide on all matters relating to the joint venture which have been designated by the foreign partner.[64] Essentially, this provision pertains to all decisions relating directly to the joint venture, including the use of joint venture assets.

At first glance, the newly amended provision provides considerable latitude in the foreign partner's participation in the joint venture. There are, however, several important impediments to the foreign partner's role in decision-making.

First, there exists a substantial limitation on the foreign partner's ability to regulate the labor components of the joint venture. Although the joint venture law provides that the partners »may establish standards ... for current labor«,[65] this does not necessarily imply that the partners may set forth an exact criterion for the number of workers and their income. It would be difficult for the foreign partner to precisely define these variables because they encompass part of the inalienable rights of the workers and thus must be determined in strict accordance with the Yugoslav Constitution[66] and the Associated Labor Act.[67] Nevertheless, there is precedence for stipulating the exact number of workers. Several joint ventures have predetermined the number of workers and have agreed that the Yugoslav partner will absorb all costs related to the hiring of additional workers. In addition, it is quite clear that the foreign partner does maintain the right to require that personal incomes do not exceed the stipulated standards of »current labor« (i. e., that only a certain amount of funds will be allocated to personal income). Accordingly, if the amount paid

[62] *Id.*, at art. 15.

[63] The joint business board is set up within the work organization in which a foreign investor's resources are invested or in the work organization in which the joint venture is a member (i. e., if the joint venture is on the level of a BOAL. *See supra* note 4.

[64] *Joint Venture Law, supra* note 1, at art. 17.

[65] *Id.*, at art. 7.

[66] The Constitution of the Socialist Federal Republic of Yugoslavia, *(Official Gazette of the SFRY*, No. 9/74). The foreign partner must cede certain rights vested to the workers. Article 27 of the Constitution states, in part: »Workers in organizations of associated labor which make use of resources invested by foreign persons *shall have the same socio-economic and other self-management rights as workers in the organizations of associated labor* ...« (emphasis added).

[67] The Associated Labor Act, *(Official Gazette of the SFRY*, No. 53/76 and No. 57/83).

for personal income does exceed the stipulated limit,[68] then the excess payments will not be deducted from the foreign partner's profit but will be covered entirely by the Yugoslav partner.[69]

Second, the joint business board is required to »hear the views« of the managing bodies (i. e., workers' council[70]) of the Yugoslav business organization concerning the operation of the joint venture.[71] The main purpose of this provision is to ensure that the joint business board does not encroach upon the self-management rights of the workers. The Joint Venture Law, however, does not indicate how disputes between the two bodies are to be resolved nor does it state the consequences for the failure of the joint business board to either obtain or adhere to the views of the workers' council. Although problems of this nature would most probably be an internal matter for the Yugoslav partner to address,[72] the practical consequences for the foreign partner would most likely be internal dissension within the joint venture[73] or even possible disruption in the business activity of the joint venture.[74] The potential serious nature of dissension emphasizes the importance of maintaining a stable and beneficial relationship between the joint business board and the management and working bodies of the Yugoslav business organization.

Several joint ventures have lessened the possibility of strife by consulting the workers' council of the Yugoslav business organization before the joint venture is signed. In this way, the issues to be decided with input by the workers' council will be settled prior to the time

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[68] Because of Yugoslavia's high inflation rate, the »stipulated limit« is calculated in a »hard currency« which will reflect the devaluation of the dinar.

[69] For further discussion, *see* the section on Income Sharing, *supra.*

[70] For discussion on the workers' council, *see* the section on Management, *supra.*

[71] *Joint Venture Law, supra* note 1, at art. 7.

[72] *See* Vukmir, *supra,* note 58, at 71.

[73] An illustration of this problem is seen within a recently formed joint venture. The foreign partner wanted one of the Yugoslav members of the joint business board to attend a management workshop outside Yugoslavia. The workers' council, however, refused to fund the trip and after much confusion, the foreign partner was forced to pay for the trip.

[74] For one joint venture presently existing in Yugoslavia, the interference from the workers' council is to such a degree that all major decisions must have the council's approval prior to the subsequent approval of the joint business board. The result has been substantial delays in carrying out the joint business. This view, however, is in contrast to a study by Patrick Artisien, *supra* note 37, in which it was concluded that the overall majority of joint venture firms which were interviewed responded that in times of disagreement, the workers' council followed the recommendations of the manager. Only 3 firms (out of 42) indicated that the workers' council utilized its legal prerogative to »veto« the decisions of the joint board. Nevertheless, a majority of the firms interviewed did indicate that the decision-making process, with its lengthy debates and bureaucratic drawbacks, hindered the operation of the joint venture. If the foreign partner is not satisfied with the council's decision, he may request a reconsideration but cannot demand a reversal of the decision. If problems with the council persists, the foreign partner can terminate the contract so long as this was foreseen in the contract.

of signing. This approach, however, will not work if the Yugoslav business organization is a newly formed entity. Since the workers' council of the Yugoslav business organization does not become effective until the act of foundation, the council does not legally exist.

In order to alleviate this problem, the proposed new Joint Venture Law would allow the partners to regulate their rights, duties and liabilities during the formation of the joint venture within a newly formed Yugoslav business organization.[75]

If the joint venture is established from an existing Yugoslav business organization then the partners may envisage changes under the joint venture contract which shall be carried out within the context of the Yugoslav business organization's statute and other self-management acts.[76] The changes may relate to (1) the joint venture's obligations towards other organizations with which it is associated (i. e., its relationship with BOALs) and (2) the powers of the management to introduce more efficient management and organization of work in order to improve the quality of products and services, and to structure the rights and duties between management and labor.

Finally, the Joint Venture Law stipulates that the decisions to be made by the joint business board are to be by »mutual agreement«.[77] This provision supports Yugoslavia's desire to have both parties on equal footing, thus avoiding exploitation by the foreign party. To assure this status, the Joint Venture Law mandates that the foreign partner's representation on the joint business board cannot exceed the number of representatives from the Yugoslav business organization, irrespective of the partners' proportional capital investment.[78] Thus, in this context, the term »mutual agreement« means equal representation on the joint business board and does not mean unanimity in decision-making. Considering the make-up of the board,[79] unanimity in all matters related to the joint venture would be highly burdensome.

There are, however, some issues which must be resolved by mutual agreement, regardless of the number of representatives on the joint venture board.[80] In this context, the term »mutual agreement« denotes unanimous decision-making. Thus, even in circumstances where the Yugoslav business organization has a majority of representatives on the joint venture board, certain designated issues require unanimity. Although the Joint Venture Law mandates that certain issues will be decided by a unanimous vote, the law neither states the number nor the subject matter of the pertinent issues. The issues which are

[75] Second Draft Law, *supra* note 2, at art. 21.

[76] This provision is consistent with a newly formed Yugoslav business organization which must maintain its statute and self-management acts in conformity with the newly formed joint venture agreement.

[77] *Joint Venture Law, supra* note 1, at arts. 15 and 16.

[78] *Id.*, at art. 16.

[79] It is common for the joint business board to consist of 4 or 5 members designated by the contracting parties: 2 by the foreign partner; 2 by the Yugoslav partner and, if 5 members, 1 by the BOAL of the joint venture.

[80] *Joint Venture Law, supra* note 1, at art. 16.

usually reserved for a unanimous vote include: the organization of production, purchase and sales, the rate of productivity, material and energy inputs, the reconstruction of facilities and modernization of production, joint credit borrowing, and the replacement of fixed assets.[81] In order to assure that the joint venture will not be hampered because of problems with obtaining unanimous consent, joint ventures resort to the arbitration or opinions of outside specialists to resolve disputes on an issue requiring unanimity.[82] More common, however, is the reliance on »boardroom tactics« to reach an agreement. Although this approach is time consuming and often leads to confrontations among the board members, it seems to be the preferred management technique among joint ventures in Yugoslavia.

In practice, there tends to be a natural inclination towards allocating decisions-making authority to the partner which has the comparative advantage. Thus, the foreign partner has a *de facto* right to decide on matters concerning the quality of products, whereas the Yugoslav partner has authority over the setting of prices (in the domestic economy), the number of workers, and the purchasing of raw materials.[83] Decisions concerning marketing, labor training and costs, and product selection tend to be truly »joint decisions«.

As a consequence of the practical decision-making process within the joint business board, current discussions on revising the Joint Venture Law include provisions which would greatly enhance the foreign partner's role on the joint business board. Presently, there is a proposal which would permit the parties to the joint venture to determine the composition, election and work method of the joint venture board which, as a rule, would be related to each partner's invested share and »the amount of labor invested« (i. e., number of employees).[84] Thus, a foreign partner who contributed 70% of the total investment could retain a majority voting position on the joint venture board.[85]

The proposed Amendment 12 to the Constitution goes even further. It would permit all decisions relating to decision-making to be determined by the terms of the contract.[86] Nevertheless, since federal law would supplement these provisions, it is likely that the requirement of a joint business board would be retained in the Joint Venture Law.

In addition, the proposed changes would permit the partners to specify their responsibilities in planning and conducting business, and

[81] *See* Commentary, *Id.*
[82] *See* Milošević, *Investing in Yugoslavia,* (Exportpress, Belgrade, 1985).
[83] *See* Artisien, *supra* note 37, at 142.
[84] There may, however, exist a problem concerning the term »invested labor«. Since it is unlikely that the largest number of employees will be from the Yugoslav side, determining the quota of representatives on the joint business board by the variable »invested labor« will automatically favor the Yugoslav partner.
[85] *See* Second Draft Law, *supra* note 2, at art. 23.
[86] Amendment 12, *supra* note 3, at sec. 3.

in managing the operations of the joint venture. The duties of the joint business board with respect to these same issues could also be determined in the contract.[87]

MANAGEMENT

By all accounts, one of the most important elements in a successful Yugoslav joint venture is the relationship between the joint business board and the workers' council[88] of the Yugoslav business organization. This relationship is considerably enhanced by an effective manager. Whereas the business board acts as a management council, with certain fundamental responsibilities, the day to day operation of the joint venture is carried out by either a management board or, as it is more common, by a senior individual manager.[89] The manager runs the commercial operations of the organization, proposes business policy, organizes the activities and working process within the organization, and executes the decisions of the joint business board.

In practice, the managing director of a joint venture is a Yugoslav national. The law, however, does not preclude the foreign partner's representative from being appointed as the managing director.[90] The foreign person would have to be employed in the Yugoslav business organization on a full-time basis and possess the appropriate work permit, which means that the foreign national would possess skills and experience not normally available in Yugoslavia.[91] In addition, the management board or manager is elected through the same legal procedure as in Yugoslav business organizations,[92] and thus the manager or management board must be approved by the workers' council. The manager cannot be »appointed« by the joint venture partners. The foreign partner participates in »suggesting« a manager through his position on the joint business board.

[87] *See* Second Draft Law, *supra* note 2, at art. 22 and Amendment 12, *supra* note 3, at sec. 3.

[88] The workers' council is an elected body consisting of representatives of workers from all departments in the Yugoslav organization.

[89] This was not always the case. In June 1976, The Decree on Foreign Investment (*Official Gazette of the SFRY*, No 26/76) transferred the management responsibilities from the joint business board to the workers' council. This decree was subsequently repealed by the 1978 Joint Venture Law, *supra* note 14.

[90] The Joint Venture Law does not prohibit such an arrangement. The controlling law is the Law on the Conditions Necessary for the Employment of Foreign Nationals (*Official Gazette of SFRY*, No. 11/78). This arrangement is consistent with Yugoslav joint banks where foreign citizens are permitted to act as president of the bank.

[91] *See* Milošević, *supra* note 82, at 31.

[92] The manager or management board of all Yugoslav business organizations is elected by the workers' assembly through the workers' council. When the Yugoslav business organization consists of less than 30 workers, there is no elected workers' council and the whole working assembly acts as a council.

Although it is legally permissible to elect a foreign national as the manager of the joint venture, the political influence of the local community (i. e., the commune[93]) could prevent such an occurrence.[94] Consequently, it is more common that the foreign partner occupies senior management positions within the structure of the joint venture (e. g., a management accountant).[95]

In addition, it is possible for a foreign worker to be represented on the workers' council or any other body of management[96] of the Yugoslav business organization. In this case, the worker would be selected in the same way as any Yugoslav worker on the workers' council. The worker would have to be elected through the workers' assembly. It is important to note, however, that the foreign worker would be a representative of the workers and not the joint venture. The foreign partner cannot have a voting representative on the workers' council. The joint venture contract, however, may provide for a nonvoting foreign representative on the council.[97]

The exact format for the management structure is left entirely to the discretion and imagination of the partners. Current management structures in Yugoslav joint ventures include: »project leaders« from both sides who share day-to-day management responsibilities, an »advisor« from the foreign partner who has »residency« at the plant but does not share in day-to-day operation responsibilities, and an arrangement where the foreign partner has no representative at the plant nor in Yugoslavia, but conducts business from its European office.[98] Direct discussions with several U.S. joint venture partners, however, reveal that it is imperative, as a practical matter, to have a permanent

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[93] The commune is the basic socio-political community. There are 512 communes throughout Yugoslavia. Their sizes differ according to the number of inhabitants, from 10,000 to over 100,000, and in area, from 50 sq. km. to over 1,000 sq. km.

[94] Prior to 1984 and on the basis of the Social Compact on Personnel Policy, the workers' council would have to »consult« with the local commission for the Coordination of Personnel Policy, which was responsible for giving an opinion aimed at protecting »the common social interest«. Although this law is no longer in effect, most communes are still represented on selection committees for directors of Yugoslav business organizations and, depending on the size of the local community, can wield considerable influence over the selection process.

[95] Foreign persons who join the staff of the joint venture must also adhere to the same requirements necessary for employing a foreign manager, i. e., they must become full-time employees of the Yugoslav business organization and qualify for work permits. Practical experience shows that there is little problem in employing foreign persons on the joint venture staff.

[96] Organs of management are bodies elected on a self-managing basis, i. e., workers' council, and should be distinguished from business-managing organs, such as directors.

[97] For an excellent discussion, *see* Barbić, *supra* note 20.

[98] According to a recent study, this arrangement is not uncommon. Over 64% of the firms sampled said they had no managerial staff working in the joint venture. An even larger percentage of firms (83%) said they had no technicians employed with the joint venture. Apparently, once the initial operational stages were completed, the foreign partner relinquished the day-to-day operations. *See* Artisien, *supra* note 37, at 167.

»resident« at the plant to assure that the crucial issues of the joint venture operation are addressed on a daily basis.

As a result of the constraints on the management aspect of joint ventures, Yugoslav officials are presently discussing changes in the Joint Venture Law which would greatly liberalize the partners' ability to appoint a manager. Essentially, this would involve limiting the workers' council's right to participate in the selection of the manager.[99] The Second Draft Law on amending the Joint Venture Law, however, advocates only that the business board should »propose« to the workers' council the appointment and removal from office the manager and other executives of the joint venture.[100] The proposed Amendment 12, however, makes no such limitation.[101]

EVIDENCE ACCOUNT

For the purpose of monitoring the investment shares of the partners' invested capital, the partners may maintain a separate evidence account as a record of the foreign partner's liabilities and claims against the Yugoslav partner.[102] The evidence account can be considered an »extended« nominal capital account. The only difference is that the evidence account shows all the claims of the foreign partner as well as the date when the claims mature or must be settled.[103] The evidence account can be kept either in dinars[104] or in a foreign currency.[105]

Since the accounting aspect of a joint venture can be exceedingly difficult to comprehend, Yugoslavia provides assistance through the Social Accounting Service (SDK).[106] The SDK is an independent organ-

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[99] These views were stated by Yugoslav officials during the OPIC mission, *supra* note 49, and the US—Yugoslav Economic Council meeting in Cavtat (June 1—3, 1987).

[100] Second Draft Law, *supra* note 2, at art. 24.

[101] Amendment 12, *supra* note 3, at sec. 2.

[102] *Joint Venture Law*, *supra* note 1, at art. 26.

[103] The account may include: (1) the original investment and additional investment paid to the Yugoslav partner, (2) any reinvested capital which the foreign partner has paid from his profits, (3) unpaid profits due to the foreign partner, (4) the repayment of any portion of the foreign partner's invested capital, and (5) any losses of the joint venture. For instance, changes in the status of the foreign partner's investment account could occur upon subsequent investments made by the partner or the coverage of losses from the joint venture operation.

[104] If the account is kept in dinars, then the conversions of the contributions made by the parties will be made at the official rate of exchange in effect on the date of the contribution. Any subsequent devaluation of the dinar would not affect the value of the contributions already recorded.

[105] By maintaining the account in a foreign currency, the foreign partner can more effectively protect himself from Yugoslavia's high rate of inflation. As was pointed out by Vukmir, *supra* note 54, at 75, the Joint Venture Law does not mention foreign currency as a mode for accounting, but in practice it is a widely accepted method.

[106] In Serbo-Croatian, the Social Accounting Service is called Služba Društvenog Knjigovodstva (SDK).

ization, acting on federal and republic levels, which reviews all internal payments among Yugoslav business organizations.[107] The SDK monitors the transactions of the joint venture.[108] In addition, the foreign partner may seek assistance from the Financial Revision Department of the SDK which will transpose accounts and balance sheets of the joint venture into the western accounting model.

INCOME SHARING

Because the notion of income in Yugoslavia is so different from that of the West, the provisions of the Joint Venture Law which regulate the partners' rights and obligations stemming from invested resources are the most difficult for foreign investors to understand.[109] The present Joint Venture Law attempts to clarify the notion of income within the Yugoslav system as it pertains to joint ventures.[110]

Prior to the new Law, there were serious problems as to whether the foreign partner had to cover the obligations of the Yugoslav business organization outside those stipulated in the joint venture contract. The major impediment was the definition of »joint venture income« and the right to expend that income for obligations which were outside the confines of the joint venture. Since, in most cases, the Yugoslav business organization in which resources from a foreign partner were invested was also engaged in its own business operation, the two incomes were merged. As a result, the new Joint Venture Law includes provisions which require the Yugoslav business organization to keep records which separate its own generated income from the

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[107] In Yugoslavia, banks, government agencies and all Yugoslav business organizations do not make direct payments to each other. Every organization instructs SDK to make the payment against the amount transferred to the SDK. The SDK possesses the right to inspect the account of any Yugoslav enterprise.

[108] Under the Decision on Records for Organizations of Associated Labor in which Foreign Persons have invested Resources are Bound to Provide in their Business Books *(Official Gazette of the SFRY,* No. 34/81), the Yugoslav business organization is required to submit annual reports about the operations of the joint venture to the SDK. Similar annual reports are also required under the Law on Rules on the Contents and Submission of Annual Reports on the Implementation of Contracts on the Investment of Foreign Persons' Resources in the Domestic Organization of Associated Labor *(Official Gazette of SFRY,* No. 11/80).

[109] Self-management in the socialist market economy of Yugoslavia means that workers employ socially-owned resources in order to generate income. The income earned by the workers is distributed along agreed upon criteria as stipulated in: (1) inter or intra self-management agreements, (2) social compacts (which are agreements which regulate relations of collective interest and the general concerns of the community, i. e., principles of income distribution, general price formation, etc.), and (3) the applicable law and taxes. Through these agreements, funds are channeled to »social« sectors of the society such as education, health, recreation, etc. These funds are referred to as »contributions« rather than taxes, although the effect is the same.

[110] *Joint Venture Law, supra* note 1, at arts. 18—29.

income generated through the joint venture.[111] In this way, the part of the joint venture income belonging to the foreign partner may not be used to cover obligations and expenses which are not related to the joint venture. Consequently, the foreign partner is now exempt from certain taxes and obligations which are considered to be outside the parameters of the contract. Thus, as shown in chart 1, income (net) is determined by deducting material and depreciation costs[112] and does not include the statutory obligations and expenses of the Yugoslav business organization.[113] After deducting expenditures for personal incomes[114] and funds for common consumption,[115] from the net income, the »residual net income« (i. e., profit) is obtained. It is from the residual net income that profits are distributed to the foreign partner in accordance with its respective share of investment capital into the joint venture.[116]

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[111] *Id.*, at art. 19. The Yugoslav business organization is required to maintain separate accounts in order to distinguish the use of the foreign partner's resources. The records must be kept in accordance with the Law on the Determination and Distribution of Gross Income *(Official Gazette of SFRY*, No. 56/84), articles 53 to 56 and article 58. These articles primarily deal with the relationship between two or more basic organizations of associated labor and the income earned from the joint venture. Further regulations on business records is found in the Decision on Records that Organizations of Associated Labor in which Foreign Persons who have Invested Resources are Bound to Provide in their Business Books (Official Gazette of the SFRY, No. 34/81) which was enacted by the Federal Executive Council in conformity with Article 56 of the Law on Bookkeeping (Official Gazette of the SFRY, No. 25/81).

[112] The Joint Venture Law permits the partners to set standards for material costs and the criteria for determining depreciation rates. Minimum depreciation rates are fixed by the Law on Changes and Amendments of the Law of Depreciation of Assets of BOALs and Other Users of Social Needs *(Official Gazette of the SFRY*, No. 65/84). When the partners agree to apply an increased rate of depreciation on fixed assets in excess of the compulsory minimum, the difference in the depreciation rates above the minimum must be covered prior to arriving at net income.

[113] These obligations are: (1) national and civil defense, (2) depreciation charge in excess of the minimum stipulated by law, (3) fines not incurred by the joint venture, and (4) insurance premiums for resources of the Yugoslav partner. *See Joint Venture Law, supra* note 1, at art. 21.

[114] In practice, the partners may determine the personal incomes of the workers (i. e., current labor) through limiting the percentage of the net income allocated for salaries. In this way, if the salaries exceed the agreed upon standards, the Yugoslav partner will pay the difference from his share of the joint income. The excess costs fall exclusively on the Yugoslav partner and conversely the realized savings also go to Yugoslav partner. For further discussion, *see* Vukmir, *supra* note 58, at 77; Čičinšain and Ellis, ed. *Doing Business with Yugoslavia — Economic and Legal Aspects*, RCCDC (Ljubljana, 1986) at 156; Milošević, *supra* note 82, at 36.

[115] Funds for common consumption denote welfare and social and fringe benefits, i. e., funds for the operation of workers' restaurants, housing, vacations and contributions to local self-managing communities for education, health, social security, culture, recreation, etc. This collective common fund is actually an indirect tax prior to the distribution of profit.

[116] *Joint Venture Law, supra* note 1, at art. 22. Under article 19 of the 1978 Joint Venture Law, *supra* note 15, the joint venture contract had to state the maximum amount of profit the foreign partner could earn. Any

Under current consideration is an amendment to the Joint Venture Law which would permit the contracting parties to stipulate the amount of taxes and contributions (i. e., common consumption fund) which would be borne by the foreign partner.[117] If adopted, this provision could significantly enhance the foreign partner's ability to limit his contributions to benefits (other than wages) accorded to Yugoslav workers.[118]

PROFITS OF THE FOREIGN PARTNER

Once the residual net income (i. e., profit) has been determined, a tax is levied on the foreign partner's profit.[119] In the past, taxation has varied among the various republics and autonomous provinces, with the economically less developed regions enacting lower tax rates.[120] The tax differential, however, had very little, if any, influence on foreign investors[121] and thus a new tax policy was recently adopted which replaced the varying tax rates with a flat tax rate of 10% for all republics and autonomous provinces.[122]

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excess profits had to be reinvested or substracted from the foreign partner's investment share. The present Joint Venture Law has deleted this provision and thus there is no limitation on profit.

[117] *See* Second Draft Law, *supra* note 2, at art. 37 and Amendment 12, *supra* note 3, at sec. 3.

[118] For an excellent discussion on income sharing between Yugoslav joint venture partners, *see* Kovačević, Milan, *Finansiranje Domaćih Organizacija Stranim Ulaganjem*, Institute for Industrial Economics (Belgrade, 1987).

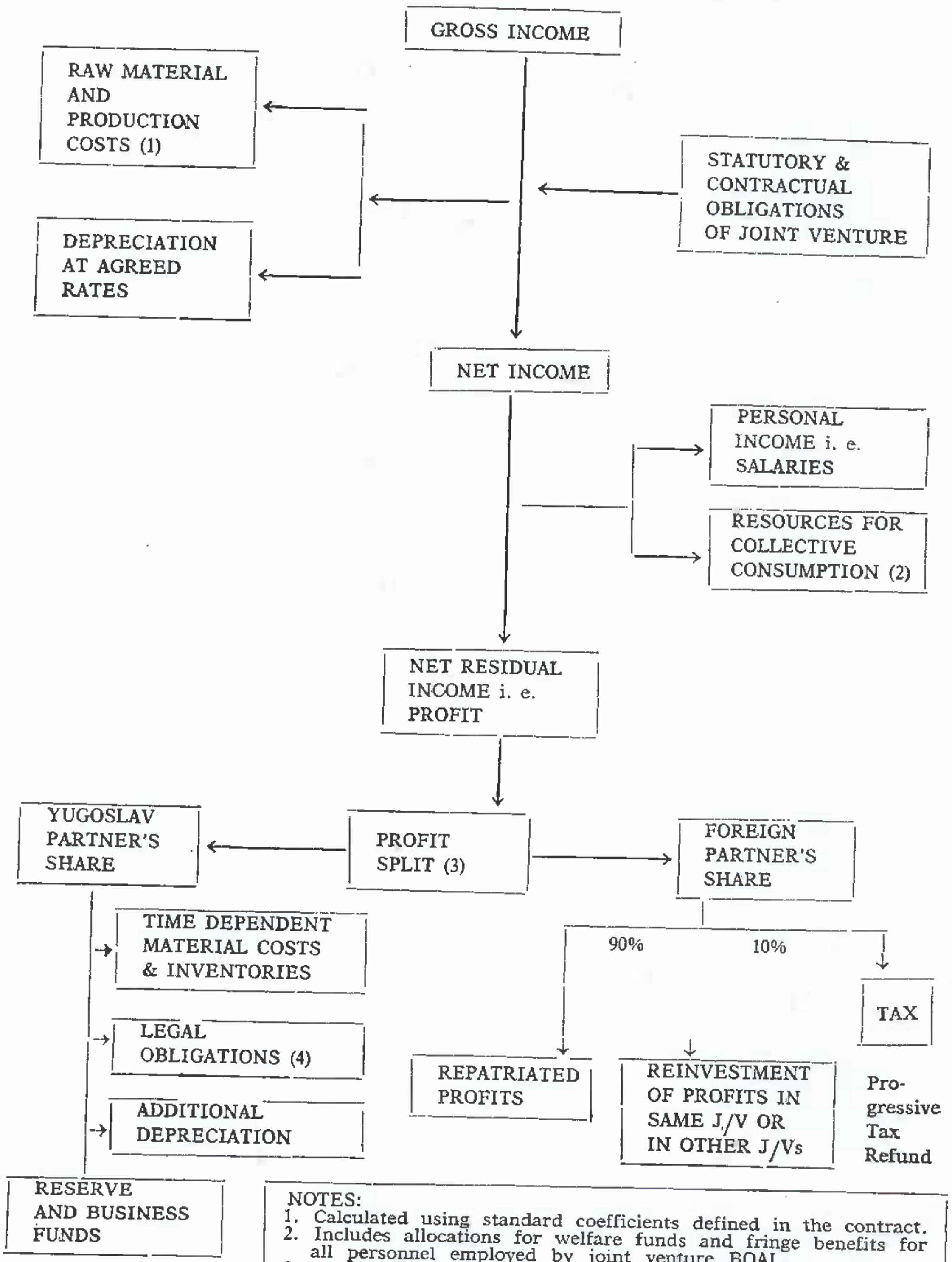
[119] *See* The Law on the Taxation of Foreign Persons and The Law on Taxing Income of Yugoslav Business Organizations, which were enacted by the relevant republican and provincial governments. Yugoslavia has, to date, concluded numerous conventions on the avoidance of double taxation with respect to taxes on income and capital: Austria (1975), France (1976), Sweden (1981), Denmark (1982), The Netherlands (1984), Czechoslovakia (1984), Italy (1984), Norway (1985) and Sri Lanka (1986). Yugoslavia and the United States are presently negotiating a tax treaty. The first round of talks occurred in Washington during March 1987, and further talks are expected to be held in Belgrade later this year (1988). The conventions which have been concluded are in accordance with the OECD draft convention of 1963 and the revised draft convention of 1977. The conventions cover both taxes and contributions of Yugoslav business organizations and taxes and contributions on personal income derived from dependent personal services.

[120] Slovenia had a 35% rate; Croatia, 35%; Bosnia and Herzegovina, 20%; Montenegro, 15%; Serbia, 15%; Macedonia, 15% Vojvodina, 10%; and Kosovo, 10%.

[121] Between 1968—1980 there was a negative correlation between lower rates and joint venture investments. The republics with the highest tax rates also attracted the largest number of investors: Slovenia, with a 35% rate, had 39 joint ventures; Croatia, with a 35% rate, had 31; Bosnia-Herzegovina, with a 20% rate, had 28%; and Serbia, with a 15% rate, had 42. Kosovo, which had the lowest rate of 10%, had only 2 joint ventures. *See* Artisien *supra* note 37, at 62.

[122] *See* The Compact on the Foundation of Taxation Policy (*Official Gazette of the SFRY*, No. 61/81). All republics and autonomous provinces have signed the unified tax compact but since the compact is not obligatory, Croatia and Serbia have not yet implemented it but are expected to do so by the end of 1988.

PROFIT SHARING AND TAXATION OF FOREIGN PARTNER'S EARNINGS ACCORDING TO 1984 JOINT VENTURE LAW



NOTES:
1. Calculated using standard coefficients defined in the contract.
2. Includes allocations for welfare funds and fringe benefits for all personnel employed by joint venture BOAL.
3. Split is according to the investment participation of the partners on following agreed formula specified in the contract.
4. Legal obligations include:
   — National and civil defence.
   — Depreciation charges in excess of minimum laid down by law.
   — Fines not incurred by joint venture.
   — Insurance premius for resource of Yugoslav partner.

Source: Investment in Yugoslavia, supra note 57 at 91.

There also exists a progressive tax »refund« to encourage reinvestment of the foreign partner's profit. Thus, if a foreign partner reinvests a portion of his profits in the joint venture[123] or deposits the proceeds in a Yugoslav bank, the tax is reduced according to the percentage of the reinvested or deposited profit.[124] This tax relief, however, is granted only if the reinvestment or deposit is made for a duration of at least five years. If the reinvestment or deposit is withdrawn prior to the five year period, then the profit will be taxed at the original rate.

The only indirect taxes paid in Yugoslavia are sales taxes and customs duties. Products sold on the domestic market are subject to a one-phase tax paid at the retail level. The tax includes a basic sales tax levied by the federal government and republican or provincial government, as well as a communal sales tax.

Custom duties are in accordance with Yugoslavia's adherence to the General Agreement on Tariffs and Trade (GATT) and are based on the principle or most-favored-nation treatment. Recently, Yugoslavia adopted new legislation on custom-free trade zones,[125] thus permitting joint ventures to freely import and export machinery, instruments, raw materials and intermediate products used in joint venture activities carried out in the zones.[126]

TRANSFER OF PROFITS

The Joint Venture Law provides for the transfer of the foreign partner's profit in four different ways.[127] The profit can be transferred

[123] The profits can also be reinvested into another Yugoslav investment project. *See Joint Venture Law, supra* note 1, at art. 30.

[124] A minimum of 25% of the profits must be reinvested or deposited. A 25% reinvestment provides for a 15% reduction. The subsequent 25% receives a 30% reduction. The final 50% receives a 50% reduction. For example, for the first 25% reinvestment, the tax rate would be 8.5% ($10 \times .15 = 1.5$); between 25% and 50% reinvestment, the tax rate would be 7% ($10 \times .30 = 3.0$); above 50%, the tax rate would be 5% ($10 \times .50 = 5.0$).

[125] Free trade zones in Yugoslavia are governed by the Law on Free Trade Zones *(Official Gazette of the SFRY*, No. 58/85); The law on Special Conditions for the Performance of Foreign Trade Operations in Customs Free Zones *(Official Gazette of the SFRY*, No. 59/85); and The Decree on Additional Customs Control Measures and Records in Free Trade Zones *(Official Gazette of the SFRY*, No. 60/85).

[126] The Draft Law on amending the Joint Venture Law states that a joint venture in a duty-free zone which manufactures for export may, for the purpose of carrying out contractual business, and on the basis of appropriate papers, temporarily take specified capital assets and its products out of the duty-free zone and bring them back into the zone. Second Draft Law, *supra* note 2, at art. 50.

[127] The contract should provide for the transfer of profits to occur no less than 30 days from the date of approval of the annual balance sheet. During the U.S.—Yugoslav Economic Council Meeting in Cavtat *(supra,* note 99) a Yugoslav organization revealed that it gained permission from the Yugoslav Government to transfer profits to its foreign partner twice a year.

in the form of dinars,[128] through deliveries of products manufactured by the joint venture,[129] through rendering certain services which are the subject matter of the joint venture,[130] or in a foreign currency.[131]

The transfer of profits in dinars is more attractive for the foreign investor since the 1987 revision in the law.[132] Prior to this change, profit transfers in the form of dinars were severely restricted.[133] As a result of the new provision, the foreign partner can now use the earned dinars to purchase and re-export any goods and to make payment for services which are not prohibited from being exported (e. g., military products).[134]

The most common avenue of transferring profits to the foreign partner is by way of foreign exchange.[135] The transfer of profits in a foreign currency is regulated by the Law on Foreign Exchange Operations.[136] Earlier laws limited the transfer of profits to 50% of the

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[128] *Joint Venture Law, supra* note 1, at art. 31.

[129] *Id.*, at art. 32. Profits can be transferred to the foreign partner through the delivery of goods manufactured by the joint venture, but only if the joint venture involves: (1) the exploration, exploatation and primary processing of crude oil, gas, ores and other minerals or (2) the production and processing of agricultural products, raising and fattening of livestock, fish farming, processing meat, fish and other livestock products, plantings of single species forests or laying out of other kinds of plantation or processing. The Yugoslav Executive Council may denote additional economic activities where the delivery of goods is permissible. The proposed changes to the Joint Venture Law include a provision which would repeal the present limitations on receiving goods produced by the joint venture. *See* Second Draft Law, *supra* note 2, at sec. 3.14.

[130] *See Joint Venture Law, supra* note 1, at art. 33. The Joint Venture Law does not define what services are included and thus there exist an array of possibilities, so long as the services are defined as the subject matter of the joint venture. For example, if the joint venture involves the manufacturing of equipment, the Yugoslav party could render its obligation to the foreign partner by constructing the equipment for the buyer.

[131] *Id.*, at art. 30 and the Law on Foreign Exchange Operations, *(Official Gazette of the SFRY*, No. 66/85) (hereinafter cited as the »Foreign Exchange Law«).

[132] *See* Resolution on Modifying Dinar Payments *(Official Gazette of the SFRY*, No. 37/87).

[133] Prior to the changes in the law, the transfer of profits, in the form of dinars, could occur only when the joint venture produced products which were prohibited from being exported or, by their nature, could not be exported (e.g., public utility service, bridge maintenance). The foreign partner could then use the dinars to purchase goods in Yugoslavia and re-export them, to transfer the dinars to another foreign person, or invest them in Yugoslavia. In addition, if the products of the joint venture were not subject to restrictions, the transferred dinars could only be used for non-merchandise payments and personal expenses in Yugoslavia or kept in a non-interest bearing account with a Yugoslav bank. *See Joint Venture Law, supra* note 1, at art. 31.

[134] The export of goods, however, still must be done through a Yugoslav business organization registered for export operation.

[135] The foreign exchange must be in the currency in which the foreign partner has invested resources in the joint venture. Other currencies may be transferred only upon approval of the National Bank of Yugoslavia.

foreign exchange earnings from the export of goods and services. The present Joint Venture Law allows the Yugoslav partner to utilize 100% of the foreign exchange receipts earned from the joint venture for transfer to the foreign partner. If the joint venture does not generate sufficient foreign exchange earnings to cover the foreign partner's profit, the Yugoslav partner is entitled to purchase the needed foreign exchange on the Yugoslav foreign exchange market. This remains one of the most controversial aspects of joint ventures in Yugoslavia.

Because of Yugoslavia's present balance-of-payments deficit, there remains an excess demand for foreign exchange in Yugoslavia. The 1986 Foreign Exchange Law abolished foreign exchange accounts of Yugoslav business organizations. They are bound to convert their foreign exchange earnings through commercial banks into dinars within 48 hours of receipt.[137] In times of foreign exchange shortage, which has existed since the enactment of the Law, external payments of foreign exchange were recently allocated according to priorities set forth in Article 110 of the Foreign Exchange Law. According to this article, the repayment of Yugoslavia's foreign debt had first priority while the import of consumer goods had last priority. Although the Foreign Exchange Law did not explicitly place the transfer of profits to the foreign partner as a first priority payment, the Yugoslav Government stated that such payments were to be treated in the same way as foreign debt and thus given first priority treatment.[138]

In order to alleviate the many problems associated with foreign exchange allocation, the Yugoslav government, pursuant to the IMF Standby Agreement, has abolished Article 110 of the Foreign Exchange Law.[139] In its place, Yugoslavia has introduced a »quasi« free-floating exchange rate. Foreign exchange will be »freely« sold on the exchange market at a rate that will more accurately reflect supply

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[136] The Foreign Exchange Law, *supra* note 130.

[137] Payment is made in such a manner that the Yugoslav business organization gives dinar payment orders to its bank. The commercial bank then debits either the firm's foreign exchange account or purchases foreign exchange on the foreign exchange market.

[138] This view has been expressed on numerous occasions, particularly at the U.S.—Yugoslav Economic Council meetings held in Cavtat in June 1986 and 1987. The basis for this position is founded in the Foreign Exchange Law, *supra* note 131, at art. 110 which reads in part: »... the Federal executive Council may lay down other purposes and *different rankings for outward payments*...« (emphasis added). To strengthen this position, the proposed changes in the Joint Venture Law include a provision which explicitly states that profit transfers and the repatriation of invested assets will be considered first priority payments. *See* Second Draft Law, *supra* note 2, at art. 34. If changes to the Joint Venture Law are adopted then the problem associated with the transfer of profits and the repatriation of invested resources will affect only those joint ventures which sell products and services on the domestic market or collect payments for exported goods and services according to the clearing system. The joint ventures which export and thus earn foreign exchange will not be affected by the priority system because they will be permitted to retain a proportion of their foreign exchange earnings (*see* section on Importation Rights, *supra*).

[139] This occurred at the end of May, 1988.

and demand. Nevertheless, since Yugoslavia is presently not willing to float its currency, the »market rate« will not be an auction rate. The rate will, however, be considerably closer to a true equilibrium exchange rate than was possible under the previous system.[140]

Presently, the major concern of foreign investors is with the practical consequences of the transfer of profits. Legally the transfer of profits should occur no less than 30 days from the date of approval of the annual income statement.

Foreign investors, however, indicate that a three to five month delay in the transfer of profits is not unusual. There also exists a provision in the Foreign Exchange Law that permits the Federal Executive Council to implement temporary measures of restriction on international payments.[141] Although this provision is not often noticed, during a recent period of balance of payments disequilibrium, foreign »assets,« including rights to profit transfers, were actually frozen.[142] Although no legal foundation is given for the action, it is the author's opinion that the »temporary restriction« provision of the Foreign Exchange Law provides the necessary legal foundation.

An additional problem concerns the transfer of convertible currency to the joint venture account in a Yugoslav bank. In order to meet its obligations to internal payments (i. e., rent, salaries, etc.), the foreign partner often transfers funds (i. e., cash calls) into the joint venture account. During the 1—2 months needed to complete these internal payment transactions, no interest is paid on the account.[143]

IMPORTATION RIGHTS

Another major problem caused by Yugoslavia's balance-of-payments crisis has been in the area of importation rights for the equipment, raw materials and intermediate goods needed for the joint venture. Under the Joint Venture Law, if the foreign partner invests equipment, intermediate goods or raw materials whose imports are regulated or, in the case of equipment, if it is purchased from the foreign partner's invested share, then the Yugoslav business organization may import such equipment on the basis of consent by the

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[140] Discussions on this issue were held at the annual U.S.—Yugoslav Economic Council Meeting held in Split, June 4—8, 1988.

[141] Article 144 of the Foreign Exchange Law, *supra* note 131, states, in part, that the Federal Executive Council may »...order a decrease in import rights for individual forms of imports and in *payments rights concerning visible and invisible trade*« (emphasis added).

[142] In mid 1987, the Yugoslav Government froze the assets of all joint ventures in Yugoslavia. The action, which was not well publicized, was admittedly short. However, foreign partners reported that they were unable to gain access to their funds, including earned income, because then Yugoslav National Bank had designated joint venture payments as second priority payments.

[143] Provisions regulating the payment of interest on foreign exchange account are found in The Foreign Exchange Law, *supra* note 131, at arts. 73—75.

FSFER and the Foreign Trade Office, »in conformity with law«.[144] This consent, if given, lasts during the entire duration in which the foreign partner invests resources.[145]

The weakness in this provision is two-fold. First, it pertains only to the foreign partner's invested share. It does not address the situation where the joint venture imports additional equipment, intermediate goods or raw materials throughout the duration of the contract. Only if the foreign partner *invests* equipment, intermediate goods or raw materials into the joint venture would they be allowed to be »freely« imported with the consent of the authorities.[146] Second, the importation of equipment, intermediate goods and raw materials must still be »in conformity with law«. Although not directly stated, it is most probable that this provision includes conformity with the foreign exchange laws and thus in addition to obtaining »rights to foreign exchange« through the priority allocation system of article 110 of the Foreign Exchange Law,[147] the joint venture operation must also obtain »import rights« pursuant to articles 113 to 135 of the Law on Exports and Imports of Goods and Services.[148] The import rights are established under certain import regimes which determine which imported products are restricted.[149] The crucial regime for joint ventures is the »conditionally free import« (LBO) regime which controls the importation of most raw materials, intermediary goods and equipment.

Raw materials and intermediate goods falling within the LBO regime are paid for according to the joint venture's (i. e., the Yugoslav business organization's[150]) »right to import«. This right is calculated

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[144] *Joint Venture Law, supra* note 1, at art. 53.

[145] *Id.*

[146] A crucial question is whether the funds invested by the foreign partner under article 100 of the Foreign Exchange Law are to be considered the foreign partner's funds or the Yugoslav business organization's funds. If considered the latter, then the funds would not be eligible for the »free« importation of equipment.

[147] Foreign Exchange Law, *supra* note 131.

[148] The Law on Exports and Imports, *(Official Gazette of the SFRY*, No. 00/00). (hereinafter cited as the »Law on Export and Imports«).

[149] Imports are structured within the framework of the following regimes: liberalized »free« imports (LB), conditionally liberalized imports (LBO), imports and exports subject to quotas (K), and imports (and exports) subject to permit (D). The »LB« regime covers goods which are not produced in Yugoslavia in sufficient quantities such as medical equipment, spare parts, energy products and some consumer goods such as foreign publications. The »LBO« regime is discussed in the above text. The »K« regime is designed to protect domestic production and limit the demand for foreign exchange. It primarily covers certain raw materials, crude oil and many capital goods. The Federal Executive Council fixes the volume of imports and exports subject to quotas. The quotas are then allocated to Yugoslav business organizations through the Yugoslav Chamber of Economy. The »D« regime is structured to ensure effective control over trade in goods subject to international treaties (i. e., coffee, cocoa, narcotics, etc.) as well as military equipment, historical and artistic work and precious metals.

[150] Since a joint venture must be registered as an Organization of Associated Labor (i. e., a BOAL, a work organization, or a composite organization), with a share of foreign capital, regulations aimed at controlling imports are directed at the Yugoslav business organization.

through an elaborate procedure which determines the firm's »socially-recognized production needs«.[151] Essentially, the »right to import« is given priority to the firms which realize greater exports and foreign exchange inflow than imports and those which implement programs for »joint development«[152] and »joint exports«[153]

The right to import equipment is determined within the formula of the computed depreciation of equipment, export earnings, »the need to modernize the production which replaces imports of specific raw materials«, and the need to develop joint investments.[154]

Although the Yugoslav government has stated that the importation of inputs for joint ventures would not be hindered, the practical experience of joint ventures has indicated problems with acquiring both »import rights« and the needed foreign exchange for the importation of equipment, raw materials and intermediate goods. This problem even occurs for those joint ventures which are foreign exchange earners. Since all foreign exchange must be converted into dinars through Yugoslav commercial banks, these joint ventures must also obtain import and foreign exchange rights from the bank in order to receive foreign exchange to import needed equipment, raw materials, and intermediate goods.

Considering that foreign investors tend to view joint ventures as an avenue for gaining access to the Yugoslav market rather than for export-oriented production,[155] less emphasis is being placed on the

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[151] *See* the Foreign Exchange Law, *supra* note 131, at art. 114 and the Law on Exports and Imports, *supra* note 148, at art. 116.

[152] Joint development programs are a new approach to social planning in Yugoslavia and the basis for such programs are found in the Law on the Foundations of the System of Social Planning (Official Gazette of the SFRY, No. 00/00) and the Social Plan of Yugoslavia for the Period 1986—1990. Joint development programs are agreements by which Yugoslav business organizations mutually undertake obligations towards export-oriented programs, programs in the energy sector and programs aimed at import substitution. Joint development programs are assessed and approved by the Yugoslav Chamber of Economy. Recently, the Chamber designated export-oriented joint development programs (i. e., programs with net foreign exchange earnings of at least 50 million dollars a year) as having priority over all other joint development programs. The special measures for joint development programs include: (1) a reduction in or exemption from customs duties and other import dues levied on imports of equipment and spare parts not produced in Yugoslavia, (2) the granting of importation and payment rights for participating Yugoslav business organizations and (3) the use of funds from commercial banks at more favorable interest rates. Examples of export-oriented joint development programs include: Jugo-Zastava cars, metal and wood working machine tools, domestic appliances, and prefabricated houses.

[153] *See* the Foreign Exchange Law, *supra* note 131, at art. 125.

[154] The Law on Exports and Imports, *supra* note 148, at arts. 116 and 124.

[155] This view is supported by direct discussions with joint venture partners and Artisien's study which shows that joint venture production predominantely serves the Yugoslav market. *See* Artisien, *supra,* note 37, at 157. Study by M. Svetličič, *Skupna Vlaganja S Tujimi Partnerji,* (paper presented at the Slovenian Economic Association meeting, Portorož, March 9—11, 1988) confirmed this finding.

export capabilities of joint ventures. Since the Joint Venture Law no longer obligates the joint venture to earn foreign exchange through exports,[156] this trend will likely continue,[157] unless the current problems of obtaining import rights and foreign exchange persist in which case joint ventures will be forced to export. It is certain, however, that joint ventures can expect to face further difficulties in obtaining both »import rights« and foreign exchange.

Consequently, foreign investors are looking for ways to circumvent the current foreign exchange shortage. Recently, the trend has been away from joint venture contracts[158] and towards a greater reliance on long-term coproduction agreements,[159] which are not subject to limitations of the foreign exchange laws,[160] and towards straight compensation transactions.[161]

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[156] Under earlier laws, the amount of foreign exchange that could be used for transferring profits or repatriating capital was 7% of total export earnings. In addition, the foreign partner was required to reinvest 20% of his profits or deposit the amount with a Yugoslav bank. *See* The 1967 Joint Venture Law, *supra* note 37. In 1971, the repatriation quota was increased to 33% of total export earning. *See* The 1971 Amendments *(Official Gazette of the SFRY*, No. 34/71). In 1978, the quota for profit transfers was increased to 50%, except in Kosovo where all of the profits could be transferred through acquired foreign exchange. *See* The 1978 Joint Venture Law, *supra* note 15.

[157] Because of Yugoslavia's inflation rate (presently at 150%), the monopolistic and oligopolistic status of most Yugoslav firms, and the existing disincentive to export, the Yugoslav domestic market represents a highly attractive and lucrative alternative to exporting. For these reasons, foreign partners are pressing for exemptions on price controls over their products. In fact, in the proposed draft joint venture law there is a provision which states that »prices of joint venture products and services may not be regulated«. Second Draft Law, *supra* note 2, at art. 12.

[158] In the Republic of Croatia, the number of newly signed joint ventures declined from 30 in 1979 to 18 in 1985. *Source:* The Chamber of Commerce of Croatia.

[159] In the Republic of Croatia, the number of newly signed long-term coproduction agreements, increased from 42 in 1980 to 120 in June of 1986. *Source: Id.* For the complete text of the law *see* The Long-term Coproduction Law, *supra*, note 39.

[160] Long-term coproduction agreements are also exempt from the requirements of obtaining import rights. Thus, it is common to find a long-term coproduction agreement incorporated into the joint venture contract.

[161] The term »compensation transaction« is used to denote the exchange of goods and services without foreign exchange transfer (i. e., countertrade transactions, barter transactions, counterdelivery transactions). Compensation transactions are regulated by the Law on the Exchange of Goods and Services with Foreign Countries *(Official Gazette of the SFRY*, No. 66/85, article 31); The Foreign Exchange Law, *supra* note 130, at articles 52, 39 and 135); The Decree on Compensation Transactions *(Official Gazette of the SFRY*, No. 73/85); and the Decree on Conditions under which the Export of Goods and Services can be Negotiated with Payments in Goods *(Official Gazette of the SFRY*, No. 73/85). An example of the use of countertrade operations is the U.S. company Combustion Engineering Co. (CE). CE has a countertrade obligation of 180 million dollars as a result of its participation in the Kolubara power station. The countertrade obligation is over a 10—15 year period and involves a four stage approach. First, CE is working to offset its obligation by finding buyers for Yugoslav commodities. Second, CE will be purchasing goods for its own use. Third, CE will

As a result of the detrimental effects of the foreign exchange regulations on joint ventures, Yugoslav officials are contemplating changes in both the Foreign Exchange Law and the Joint Venture Law which would permit joint ventures to use part of their foreign exchange inflow for their own needs. Foreign exchange earned from a joint venture in the field of »industry and mining« could be maintained in a Yugoslav bank account[162] and up to 70% of the foreign exchange could be freely expended for the needs of the joint venture. For other sectors of the economy, 30% of the earned foreign exchange could be maintained in the account. In accordance with the proposed changes to the Foreign Exchange Law and the Joint Venture Law, the funds held in this type of an account would not be included in Yugoslavia's central bank's calculation of Yugoslavia's total foreign exchange holdings. Thus, the joint venture could freely use these funds and would not be required to obtain foreign exchange rights. If the firm needed additional foreign exchange, then it would be required to follow the existing system for the allocation of foreign exchange. The firm's remaining foreign exchange earnings would be sold on the Yugoslav foreign exchange market.[163] It has been proposed that the sale would take place within a »two-tier« exchange rate system whereby the present »official« exchange rate market would be accompanied by a parallel »free« market in which the price for the sold foreign exchange would be determined by supply and demand.[164]

Even more significant is the proposed amendment which would permit the joint venture to maintain these funds in a foreign bank account and, therefore, outside the regulatory perimeters of the Yugoslav Central Bank.[165] In addition, the foreign partner's initial investment, if it exceeds one-fourth of the total joint venture investment, could be kept in a foreign bank.[166]

Nevertheless, even with the liberalized provisions regulating the possession of foreign exchange, the joint venture would still be impeded by the necessity to obtain import rights. There were earlier discussions about revising the present law to allow the joint venture

locate foreign firms who will purchase and/or market the engineering products of its Yugoslav partner. Finally, CE has entered into a joint venture to produce engineering products which will be marketed to third countries. It should be noted, however, that »compensation transactions« must adhere to the prescribed regimes governing imports and exports.

[162] Interest on this account would be paid in a foreign currency.

[163] *See* Second Draft Law, *supra* note 2, at 31.

[164] *See Politika*, 30 August 1987, p. 7., and G. Nikić, *Structural Adjustment and Exchange Rate Policies*, paper presented at the International Conference on the World Debt, Zagreb, Yugoslavia, September, 8—11, 1987. These changes are being proposed by the republics of Croatia and Slovenia, which stand to gain a great deal by a more liberalized foreign exchange system because of their prominence in earning foreign exchange. Notwithstanding, the political division between Yugoslavia's »North« and »South« is so embedded that any substantial change in the allocation of foreign exchange between the different republics of Yugoslavia will be very difficult to accomplish.

[165] *See* Second Draft Law, *supra* note 2, at sec. 3.

[166] *Id.*, at art. 33.

to freely utilize its own foreign exchange earnings to import the equipment, raw materials and intermediate goods needed for the operation of the joint venture.[167] This provision, however, does not seem to be acceptable because only joint ventures would be accorded this privilege. Yugoslav firms would still be obligated to obtain the necessary »import rights«.[168] Consequently, the proposed changes to the Foreign Exchange Law by the Yugoslav Government envision only an increase in import rights (i. e., »socially recognized production needs« as described in article 97 of the Foreign Exchange Law) and a greater access to foreign exchange, *when available.* The Government proposes to fix a percentage of the projected foreign exchange proceeds which would be reserved for priority payments in accordance with the »socially recognized production needs« of the firm. Although the reserve would be greater for net exporters than for net importers, the amounts of foreign exchange sought by the firm could not exceed the actual inflow of foreign exchange by the firm. In addition, both the right to import and the priority in foreign exchange payments would still be contingent on the amount of projected foreign exchange proceeds for Yugoslavia as a whole.

There is also a proposed provision which would permit the joint venture to import equipment without paying customs duty or other import taxes, so long as the joint venture is for a minimum of 7 years and the foreign partner's share of the total investment in the joint venture exceeds one-fourth.[169]

REPATRIATION OF RESOURCES

The foreign partner is entitled to repatriate the remaining value of his invested resources.[170] The Joint Venture Law permits the contracting parties to decide on the mode and value of the returned resources. Repatriation may occur upon the expiration or termination of the contract,[171] or successively during the validity of the contract.[172]

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[167] Under the current law, there is a provision which would allow the importation of needed material rights, equipment, raw materials and intermediate goods to be paid for with foreign exchange earned from the joint venture's current business. There exists confusion as to whether the joint venture would still be obligated to obtain import rights. The First Draft Law on Joint Ventures, (FCEI, working group, Belgrade, July, 1987), did not mention the requirement. The Second Draft Law, *supra* note 2, at art. 33, states that the importation of these goods would be »subject to a Yugoslav import regime«.

[168] This concern may be alleviated if the new Joint Venture Law requires joint ventures to obtain the necessary import rights. On the other hand, such a provision would seriously undermine Yugoslavia's desire to attract foreign partners into joint ventures.

[169] Second Draft Law, *supra* note 2, at art. 36. In case of the premature cancellation of the joint venture, the joint venture would be obligated to pay customs duty and other import taxes.

[170] *Joint Venture Law, supra* note 1, at arts. 25, 28 and 40.

[171] *Id.,* at arts. 39 and 40. Usually upon termination of the contract, the total assets of the joint venture are converted into a loan. Repayment occurs over an agreed period with interest.

Of two ways in which the value of the foreign partner's investment can be determined, the first approach involves income generation. The evaluation of resources invested by the foreign partner in relation to the resources' nominal value is determined by the income generated through the joint venture. The generated income of the joint venture is partially result of contributions by the foreign partner in the form of increased productivity through technical advancement, increased production efficiency, greater involvement in international markets, etc., all of which add to the income of the joint venture.[173] Thus, the foreign partner's contribution towards the generated income of the joint venture becomes the basis for evaluating the foreign partner's invested resources in the joint venture.[174] The foreign partner's share would be calculated through the use of a multiplier, reflecting the foreign partner's contributions to the average profits for the joint venture over the relevant number of years. The foreign partner then has the right to withdraw the invested resources in the amount remaining, if the value has been refunded in part, or at a higher (lower) amount depending on the success of the joint venture.

The parties may also determine the value by maintaining a separate account statement (i. e., evidence account).[175] The account will show the final result of the full depreciation and the value of the assets not written off. This account also makes possible the revaluation of the foreign partner's nominal share. The nominal value of the foreign partner's assets must be agreed upon in advance. The value can be designated in dinars. To date, however, nearly all of the joint ventures which maintain an evidence account designate the value of the invested assets in either a foreign currency or a dinar/foreign currency valuation which is periodically (usually every 3 months) revalued to account for exchange rate fluctuations.[176] It is this calculation, however, that accounts for considerable difficulties for the foreign partner. Both Yugoslav and foreign officials have indicated that there is little problem in calculating the »book value« or »replacement value« of the foreign partner's invested resources. The major problem is with determining the proper method of obtaining the present »mar-

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[172] *Id.*, at art. 40. This approach takes place over stages with complete repatriation occurring on or after the effective date of termination. For instance, the contract may provide for full payment to occur within three years, payable in six equal and consecutive semi-annual installments at the interest rate of x%.

[173] *See* Milošević, *supra* note 82, at 42.

[174] Article 39 sec. 3 of the Joint Venture Law states that »the foreign person shall be entitled to the return of the resources invested... in an increased or decreased amount depending on the income generated by the joint venture and exports«.

[175] *See* Section on Evidence Accounts, *supra*.

[176] The GM joint venture signed in 1977 still maintains the value of the invested assets at 18 dinars to 1 dollar. The Yugoslav government, however, has assured the company that a realistic revaluation of the assets will be allowed under the current provisions of the Joint Venture Law. *Source:* OPIC meeting, *supra*, note 49.

ket value« of the assets.[177] Yugoslav officials, however, have recently stated that any reasonable formulation of the present value of the assets would be acceptable.[178]

The foreign partner's share of resources is refunded in the amount equal to »the value of invested resources up to the level of claims in the evidence account«.[179] This provision does not restrict the method of revaluation and seems to provide considerable latitude in negotiating the conditions for establishing the final value of the foreign partner's share. It is the opinion of the author that the partners are able to agree on any method of valuation which would account for the fluctuation in the market value of the foreign partner's share. Thus, if the business venture is successful, repatriation will include the »increased« value of the nominal investment. On the contrary, a poor performance will lead to a »reduced« value.

A clarification of this point is presented in the Draft proposal for amending the Joint Venture Law.[180] If adopted, the amendment would allow the joint venture partners to determine the »final result« of the joint venture operation through international accounting standards.[181] The investors would gain the right to share in the »real net value of the joint venture's assets«.[182] Thus, relying on a »market value« criterion (including the concept of »goodwill«) for determining the value of the foreign partner's repatriated assets would most likely become the accepted accounting method.

The return of the value of resources invested by the foreign partner may be affected in four ways. First, the contract may provide for repatriation in the form of dinars.[183] These funds can be used for purchasing goods in Yugoslavia,[184] for investing in Yugoslavia, for payment of services rendered, for transfer to other foreigners, or for any internal payments in Yugoslavia.

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177 An example would be if the foreign partner's initial investment was 100 dollars with an annual depreciation rate of 10%. Thus, after 5 years the replacement value of the asset would be 50 dollars. If there was an additional investment in the asset of 10 dollars, then the replacement value would be 60 dollars. However, the fluctuation of the market value of the asset will result in a different »final« valuation of the asset.

178 The Yugoslav officials, however, did not confirm that the western accounting method of »goodwill« in a tourist project would be acceptable. *Source:* OPIC meeting, *supra* note 49. There is another opinion which holds that pursuant to article 39 of the Joint Venture Law, the partners can formulate a method for including the concept of »goodwill«, so long as the term »goodwill« is not used. *See* Barbić, *supra* note 20.

179 *Joint Venture Law, supra* note 1, at art.

180 *See* Second Draft Law, *supra* note 2, at sec. 3.10.

181 If the parties to the agreement stipulate that profit and loss shall be calculated according to international accounting standards, they shall provide within the agreement sources for covering any loss arising as a result of applying those standards. *See* Second Draft Law, *supra* note 2, at art. 29.

182 *Id.*, at art. 47.

183 *Id.*, at art. 41.

184 Products may be exported by the foreign partner through a Yugoslav business organization registered for export operations and in conformity with regulations pertaining to exports from Yugoslavia.

Secondly, repatriation may be in the form of a delivery of products that have been the subject matter of the joint venture, if the joint venture is involved in specific areas of processing.[185]

Thirdly, the joint venture contract may permit the foreign partner to repatriate his invested resources through the performance of services which are the subject matter of the joint venture.[186]

The final and most frequently provided method for returning invested resources involves the transfer of the value of resources through a convertible currency. As with the transfer of profits, The Foreign Exchange Law governs the repatriation of invested resources.[187] The law explicitly allows for the »free« transfer of the respective dinar resources into a convertible currency.[188]

Individual items of movable property »invested« by the foreign partner may be repatriated as well. The property may either be valued, as any other invested asset would be, and included in the total share of the joint venture or the right of ownership and the property itself may be returned. The former option may cause difficulties for the foreign partner if, at the expiration or termination of the joint venture, there are insufficient funds to cover the joint venture's commitments. In that case, the value of the foreign partner's invested property can be reduced by a porportional amount of the debt. Nevertheless, since the Joint Venture Law allows for the premature termination of the contract if losses occur over two consecutive years,[189] it is unlikely that the foreign partner's entire investment would be used to cover the losses. The latter option, however, would provide protection to the foreign partner since the property would not be considered part of the foreign partner's investment in the joint venture.

There is also a provision in the Law which allows the foreign partner's invested equipment, even when included as part of his invested share, to be repatriated in kind rather than in value. Article 38 of the Joint Venture Law states that the contract may provide for the right of the return of the »specific things« invested by the foreign partner. This would include tangible assets such as equipment.

CONCLUSION

In light of Yugoslavia's current debt crisis and its growing technological gap, joint ventures must play an increasingly important role in the acquisition of needed foreign exchange and modern technology.

[185] *Joint Venture Law, supra* note 1, at art. 42. The areas of processing are identical to those areas which pertain to the transfer of profits. *See supra* note 129.

[186] *Joint Venture Law, supra* note 1, at art. 42. This provision, which has been recently incorporated into the Joint Venture Law, has been made along the same lines as the provisions of the newly introduced article 33 of the same law. *See supra* note 130.

[187] The Foreign Exchange Law, *supra* note 131.

[188] *Id.*, at art. 139.

[189] *Joint Venture Law, supra* note 1, at art. 13.

Although the continuing liberalization of the Joint Venture Law has been a welcome development, the changes have been slow in execution and relatively inconsequential, particularly when compared with joint venture opportunities in other developing and socialist countries.

Foreign investment in Yugoslavia through joint ventures has always been modest. During the past 18 years, only $1 billion has been invested in Yugoslav joint ventures by foreign investors, in approximately 340 joint ventures. In comparison, during the past four years, China has concluded over 3,200 joint ventures.

The somberness of both the foreign investor's reluctance to participate in Yugoslav joint ventures and Yugoslavia's present economic crisis should be persuasive reasoning for a significant liberalization of the present Joint Venture Law. In fact, from a preliminary view, the current proposed amendments to the Joint Venture Law, the Constitution and the Associated Labor Act envision some important changes in relation to foreign investment in Yugoslavia. The pivotal point, however, is to what degree will these proposed changes be incorporated into law.

Unfortunately, one cannot be too optimistic about the amendment process. Already, the Federal Committee on Legislation has rejected the proposed changes in the Joint Venture Draft as being unconstitutional. The Committee based its decision on article 27 of the Yugoslav Constitution which guarantees Yugoslav workers in a joint venture the same »socio-economic and other self-management rights« as Yugoslav workers in domestic firms. Thus, the Committee held that the proposed changes governing the workers of the joint venture would infringe upon the constitutional rights of the workers. The Committee's position is that the Constitution must first be amended, followed by changes in the Joint Venture Law.

Notwithstanding, even with the adoption of all the proposed changes, Yugoslavia's investment climate would still be sufficiently encumbered in relation to the relatively unrestricted foreign investment environment in other developing and socialist countries. Nevertheless, the ratification and full implementation of all the proposed amendments would represent a significant step in Yugoslavia's desire to attract foreign investment.

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STRANA ULAGANJA U JUGOSLAVIJI — PRIKAZ ZAKONA O ZAJEDNIČKOM ULAGANJU SA AMANDMANIMA I PREDLOŽENIM IZMENAMA

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Rezime

U kontekstu tekuće dužničke krize i rastućeg tehnološkog jaza, zajednička ulaganja mogu biti od izuzetnog značaja u obezbeđivanju neophodnih deviznih sredstava i moderne tehnologije. Mada se liberalizacija Zakona o zajedničkim ulaganjima povoljno razvijala, promene su bile spore i nekonzistentne, posebno u poređenju s praksom u ostalim socijalističkim zemljama u razvoju.

Strane investicije u Jugoslaviji putem zajedničkih ulaganja oduvek su bile skromne. Tokom proteklih 18 godina strani ulagači investirali su samo jednu milijardu dolara kroz oko 340 zajedničkih ulaganja. Poređenja radi, u proteklih pet godina Kina je zaključila preko 3.200 ugovora o zajedničkom ulaganju.

Odsustvo interesa stranih investitora za zajednička ulaganja, kao i tekuća ekonomska kriza, ubedljivi su razlozi za značajnu liberalizaciju Zakona o zajedničkim ulaganjima. U stvari, sa preliminarnog stanovišta predloženi amandmani na Zakon o zajedničkim ulaganjima, Ustav i Zakon o udruženom radu, predviđaju neke značajne promene na planu stranog investiranja u Jugoslaviju. Najznačajnije je, ipak, u kom stepenu će predložene promene biti inkorporirane u zakon.

Na žalost, ne može se suviše biti optimista oko čitavog procesa uvođenja amandmana. Savezni komitet za pravosuđe već je odbacio kao neustavne predložene promene u Nacrtu zakona o zajedničkim ulaganjima. Komitet je odluku doneo na osnovu člana 27. Ustava, koji jugoslovenskim radnicima u zajedničkom ulaganju garantuje jednaka »društveno-dužnička i ostala samoupravna prava« kao i korisnicima u domaćim preduzećima. Na taj način, Komitet je bio mišljenja da predložene promene zadiru u ustavna prava radnika angažovanih u zajedničkim ulaganjima. Stav Komiteta je da promene Zakona o zajedničkim ulaganjima mogu uslediti tek nakon ustavnih promena.

Čak i ako sve predložene promene budu usvojene, investiciona klima u Jugoslaviji još uvek će biti nepovoljna u poređenju sa slobodnim okruženjem za strana ulaganja u ostalim socijalističkim i zemljama u razvoju. Ipak, ratifikacija i puna implementacija svih predloženih amandmana predstavljaće značajan korak u privlačenju stranih investicija.