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Tax Considerations in Foreign Trade and Investment in the USSR

Michael Newcity

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I. INTRODUCTION

Prior to 1987, the Soviet tax system was of only passing concern to foreign companies doing business in the Union of Soviet Socialist Republics. Although the Supreme Soviet had adopted legislation in 1978 imposing a forty percent tax on income earned by foreign companies engaged in activities in the USSR,[1] it also had negotiated bilateral tax treaties with most of its capitalist trading partners, thereby reducing, and

* Associate Professor, University of Puget Sound School of Law. B.A., M.A., J.D., The George Washington University.

1. Decree of the Presidium of the Supreme Soviet of the USSR, May 12, 1978, *O podokhodnom naloge s inostrannykh iuridicheskikh i fizicheskikh lits* [On the Income Tax on Foreign Legal Entities and Individuals], Ved. Verkh. Sov. SSSR, No. 20, item 313 (May 17, 1978) [hereinafter Decree of the Presidium, May 12, 1978].

in some cases eliminating, the liability of these companies to pay taxes on most forms of income earned in the USSR.[2] Moreover, because of the limited opportunities to earn income in the USSR and a generally unsophisticated tax system that did not impose a heavy tax burden on foreign companies doing business there, tax considerations simply were not a major factor in shaping whether and how most foreign companies did business in the USSR.

The backwater status of Soviet tax law has changed dramatically during the past four years as a direct result of the decision of the Soviet government to permit foreign direct investment in the USSR. The USSR has permitted foreign ownership of interests in Soviet joint ventures since 1987,[3] and more recently, it was permitted foreigners to invest in Soviet limited liability companies.[4] The ability of foreign investors to make such equity investments in Soviet legal entities has raised many tax-related questions that were not previously pertinent.

The purpose of this Article is to provide a primer on the tax treatment accorded in the USSR to the various forms of income that foreign companies and individuals may earn in the course of doing business or otherwise investing there. This Article will not provide exhaustive answers to all questions arising in connection with the taxation of income earned by foreign businesses in the USSR. Such exhaustive answers are not cur-

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2. The USSR is a party to double taxation treaties with 19 free market and developing countries, representing most of its major trading partners. For a list of the USSR's tax treaties, see Newcity, *Tax Issues in Soviet Joint Ventures*, 25 TEX. INT'L L.J. 163, 188-89 (1990) [hereinafter Newcity, *Tax Issues*]; *see also* Newcity, *The Soviet Union's Other Tax Agreements* 18 N.Y.U. J. INT'L L. & POL. 833 (1986) [hereinafter Newcity, *Other Tax Agreements*].

3. *See* Decree of the Presidium of the Supreme Soviet of the USSR, Jan. 13, 1987, *O voprosakh sviazannykh s sozdaniem na territorii SSSR i deiatel'nost'iu sovmestnykh predpriiatii, mezhdunarodnykh ob"edinenii s uchastiem sovetskikh i inostrannykh organizatsii, firm i organov upravleniia* [On Questions Concerning the Creation Within the Territory of the USSR and the Activities of Joint Enterprises, International Associations and Organizations with the Participation of Soviet and Foreign Organizations, Firms and Management Bodies], Ved. Verkh. Sov. SSSR, No. 2, item 35 (Jan. 14, 1987). This decree was accompanied by regulations issued by the USSR Council of Ministers. *See* Decree of the Council of Ministers of the USSR, Jan. 13, 1987, *O poriadke sozdaniia na territorii SSSR i deiatel'nosti sovmestnykh predpriiatii s uchastiem sovetskikh organizatsii i firm kapitalisticheskikh i razvivaiushchikhsia stran* [On the Procedure for the Creation Within the Territory of the USSR and the Activities of Joint Enterprises with the Participation of Soviet Organizations and Firms of Capitalist and Developing Countries], SP SSSR, No. 9, item 40 (1987).

4. *See* Decree of the President of the USSR, Oct. 26, 1990, *Ob inostrannykh investitsiiakh v SSSR* [On Foreign Investment in the USSR], Izvestiia, Oct. 26, 1990, at 1, col. 4.

rently possible because of frequent changes in Soviet tax legislation and the lack of comprehensive and sophisticated regulations interpreting that legislation.

The Soviet Government, at both the union and republic levels, recently has adopted legislation that attempts to answer some of these tax-related questions. These laws are part of an ongoing effort to reform and modernize the Soviet system of taxation to accommodate a more market-oriented economy. The Soviet tax regime, as it applies to foreign investment-related income, must be viewed against these current reform efforts. Thus, before analyzing the specific tax provisions relating to foreign investment-related income in the USSR, this Article will discuss the reform process and the recent changes in Soviet taxation.

II. AN OUTLINE OF SOVIET TAX REFORM

As the Soviet Union moves slowly toward a market-oriented economy, a complete overhaul of the tax system is an indispensable element of any significant economic reform. The Soviet tax system as it stood in 1987 had remained relatively unchanged since the 1940s and was considerably better suited to a Stalinist command-model economy than to an emerging market-oriented economy. The pre-1987 tax system relied heavily on indirect taxation, principally the turnover tax and various payments into the state budgets by state enterprises,[5] with very little revenue generated by personal income taxation.[6] The administration of the personal income tax was relatively simple in that most citizens were employees of state enterprises and had their income tax deducted at their places of employment. The overwhelming majority of the Soviet population filed no tax returns, and the Soviet tax administrators had no concerns about securing voluntary compliance. In an economic system in which most enterprises were included in the state budget, a system of profit or income taxation comparable to those existing in capitalist countries was unnecessary. The system could employ more direct methods of distributing in-

5. In 1986, the turnover tax accounted for 91.5 billion rubles or 21.8% of the revenue in the Soviet state budget. An additional 129.8 billion rubles, 30.9% of total revenue, was derived from various payments by state enterprises into the budget. USSR STATE COMMITTEE ON STATISTICS, NARODNOE KHOZIAISTVO SSSR ZA 80 LET 628-30 (1987). For a discussion of the turnover tax, see *infra* notes 62-66 and accompanying text.

6. In 1986, the personal income tax and the bachelor's tax, which acts as a surtax on the personal income tax for some taxpayers, accounted for 31 billion rubles, or 7.4% of all Soviet state revenue. *Id.* at 628. In that same year, United States individual income taxes amounted to $349 billion, which represented 45.4% of total federal government revenues. U.S. DEP'T OF COMM., STATISTICAL ABSTRACT OF THE UNITED STATES—1990 at 310 (1990).

come and allocating resources.

Once President Gorbachev embarked on a program of reforming the Soviet economy to operate on more of a market basis, this command-economy model of taxation was no longer suitable. The need for a complete overhaul of the tax system became obvious as an increasing number of individuals were permitted to enter into private income-producing activities and as private enterprises, whether in the form of cooperatives, joint ventures, or privately-owned companies, began operations.

Several legislative and regulatory enactments adopted recently by the governments of the USSR and some of the union republics have attempted to modernize the Soviet tax system to accommodate it to a more market-oriented economy and, in so doing, to address some of the tax-related questions that are of greatest concern to potential foreign investors. The most important of these recent legislative enactments by the USSR are the Law on the Income Tax on Citizens of the USSR, Foreign Citizens and Stateless Persons (USSR Income Tax Law), adopted in April 1990,[7] and the Law on the Taxes on Enterprises, Associations and Organizations (USSR Enterprise Profits Tax Law), adopted in June 1990.[8] In addition, the Supreme Soviet of the Russian Republic (the Russian Soviet Federative Socialist Republic or RSFSR) has adopted laws purporting to implement both of these USSR tax laws within the RSFSR.[9]

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7. Law of the USSR, Apr. 23, 1990, *O podokhodnom naloge s grazhdan SSSR, inostrannykh grazhdan i lits bez grazhdanstva* [On the Income Tax on Citizens of the USSR, Foreign Citizens and Stateless Persons], Ved. Sezda Narod. Dep. SSSR, No. 19, item 320 (May 9, 1990) [hereinafter USSR Income Tax Law]. Most of the provisions of this law took effect as of July 1, 1991. Resolution of the USSR Supreme Soviet, Apr. 23, 1990, *O poriadke vvedeniia v deistvie Zakona SSSR "O podokhodnom naloge s grazhdan SSSR, inostrannykh grazhdan i lits bez grazhdanstva"* [On the Procedure for the Entry into Force of the Law of the USSR "On the Income Tax on Citizens of the USSR, Foreign Citizens and Stateless Persons"], Ved. S"ezda Narod. Dep. SSSR, No. 19, item 321 (May 9, 1990).

8. Law of the USSR, June 14, 1990, *O nalogakh s predpriiatii, obedinenii i organizatsii* [On the Taxes on Enterprises, Associations and Organizations], Ved. S"ezda Narod. Dep. SSSR, No. 27, item 522 (July 4, 1990) [hereinafter USSR Enterprise Profits Tax Law]. Most of the provisions of this law took effect as of January 1, 1991. Resolution of the USSR Supreme Soviet, June 14, 1990, *O poriadke vvedeniia v deistvie Zakona SSSR "O nalogakh s predpriiatii, obedinenii i organizatsii"* [On the Procedure for the Entry into Force of the Law of the USSR "On the Taxes on Enterprises, Associations and Organizations"], Ved. S"ezda Narod. Dep. SSSR, No. 27, item 523 (July 4, 1990).

9. Law of the RSFSR, Dec. 1, 1990 *O poriadke primeneniia na territorii RSFSR v 1991 godu Zakona SSSR "O nalogakh s predpriiatii, ob"edinenii i organizatsii"* [On the Procedure for the Application Within the Territory of the RSFSR in 1991 of the

These new laws contain several major changes. First, they have attempted to move toward a unitary system of taxation. Previously, profits and income were subject to very different tax treatment depending on the source. While state enterprise profits were taxed primarily through a variety of deductions from profits and mandatory payments into the state budget,[10] collective farms, and cooperatives were subject to a genuine income tax.[11] Similarly, personal income derived from state enterprises was subject to taxation at a maximum marginal rate of thirteen percent, while income derived from private income-producing activities was taxed at much higher rates, reaching a maximum marginal rate of ninety percent.[12] These differences in the tax treatment based on income source were premised on the assumption of socialist ideology that different categories of income should be treated differently depending on the "social value" of the income.[13] Under this earlier system, state enterprises and personal income earned at those state enterprises were treated differently, and more favorably, than income earned privately. Moreover, the integration of many Soviet state enterprises into the state budget made it inevitable that their profits would be subsumed into the state budget in a different way than the profits earned by nonstate enterprises, such as cooperatives and collective farms.

The thrust of the USSR Enterprise Profits Tax Law is to treat alike all enterprises, whether they are state-owned, cooperatives, joint ventures, or private companies. The USSR Income Tax Law also reduces the various categories of income and generally treats wage earners equally regardless of whether their wages are paid by state or private enterprises. Nevertheless, these laws have not been wholly successful in implementing a unitary system of taxation that treats all income alike. For example, the USSR Enterprise Profits Tax Law still provides dif-

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Law of the USSR "On the Taxes on Enterprises, Associations and Organizations"], Ekonomika i zhizn', Jan. 1991, No. 1, at 22; and Law of the RSFSR, Dec. 2, 1990 [hereinafter RSFSR Enterprise Profits Tax Law]. *O poriadke primeneniia na territorii RSFSR v 1991 godu Zakona SSSR "O podokhodnom naloge s grazhdan SSSR, inostrannykh grazhdan i lits bez grazhdanstva"* [On the Procedure for the Application Within the Territory of the RSFSR in 1991 of the Law of the USSR "On the Income Tax on Citizens of the USSR, Foreign Citizens and Stateless Persons"], Ekonomika i zhizn', Jan. 1991, No. 1, at 23 [hereinafter RSFSR Income Tax Law].

10. For a discussion of the taxes imposed on the profits of Soviet state enterprises, see M. NEWCITY, TAXATION IN THE SOVIET UNION 49-59 (1986).

11. *See id.* at 59-65.

12. *Id.* at 85-92, 96.

13. *See* Newcity, *Perestroika, Private Enterprise and Soviet Tax Policy*, 28 COLUM. J. TRANSNAT'L L. 225, 230-33 (1990) [hereinafter Newcity, *Perestroika*].

ferent rates for a few categories of enterprises,[14] and the USSR Income Tax Law still taxes some categories of income at different rates than others.[15]

A second major, and increasingly controversial, reform in the recent Soviet tax legislation concerns the role of the republic governments in establishing tax rates and other aspects of tax policy. Under the USSR Enterprise Profits Tax Law, each republic can decide for itself to impose a tax on enterprise profits of up to twenty-three percent, in addition to the twenty-two percent tax imposed on all enterprises by the national government.[16] Although provisions in the USSR Enterprise Profits Tax Law provide the republics with a greater measure of tax policy-making authority, the intention of the Gorbachev government is clearly to rest the principal responsibility for establishing tax policy on the union government.[17]

As part of the broader struggle over federalism in the USSR, some of the republic governments, most prominently the RSFSR, have not been satisfied with the tax authority granted to them by the union legislation and have asserted for themselves a greater power to determine tax policy and to retain tax revenues. In direct response to the USSR Enterprise Profits Tax Law and the USSR Income Tax Law, the RSFSR adopted legislation that, although purporting to implement those USSR laws within the territory of the RSFSR, modifies them in several significant ways.[18] The most important modification relates to the retention of tax

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14. Under the USSR Enterprise Profits Tax Law, the tax rate generally applicable to profits earned by Soviet enterprises is a maximum of 45%, for some banks and insurance organizations the applicable rate is 55%, for joint ventures the rate is 30%, and for certain other kinds of consumer and social organizations the rate is 30%. In addition, enterprises that earn profits exceeding a specified norm are liable for much higher tax on those excess profits. *See* USSR Enterprise Profits Tax Law, *supra* note 8, arts. 4-5.

15. Although personal income from both state enterprises and private sources generally is taxed at the same rates, which reach a maximum marginal rate of 60%, some income, such as royalty income paid to the heirs of the authors of works of literature, art, and science, is taxed at higher rates, with a maximum marginal rate of 90%. *See* USSR Income Tax Law, *supra* note 7, arts. 8, 17(2).

16. *See infra* note 100 and accompanying text.

17. *See* Law of the USSR, Apr. 10, 1990, *Ob osnovakh ekonomicheskikh otnoshenii Soiuza SSR, soiuznykh i avtonomnykh respublik* [On the Fundamental Economic Relations of the USSR, the Union and Autonomous Republics], Ved. Sezda Narod. Dep. SSSR, No. 16, item 270, art. 1(1) (Apr. 18, 1990) (providing that the "organization of the tax system in the USSR, and the establishment of federal taxes, charges and obligatory payments into the budget, and the maximum rates of taxation" are within the authority of the USSR government).

18. *See* RSFSR Enterprise Profits Tax Law, *supra* note 9; RSFSR Income Tax Law, *supra* note 9.

revenue by the republic and local governments. Under the USSR Enterprise Profits Tax Law, tax revenues are divided among the union, republic, and local budgets. Those revenues arising from the twenty-two percent tax imposed on enterprise profits are to be paid into the union budget, and the revenues arising from the additional tax on enterprise profits of up to twenty-three percent are to be paid into the republic and local budgets pursuant to legislation adopted in the republics.[19] Similar provisions are included throughout the USSR Enterprise Profits Tax Law with respect to revenues generated by the various taxes covered by that law. The RSFSR legislation implementing the USSR Enterprise Profits Tax Law, however, provides that all revenue arising from the taxation of enterprise profits will be paid into the republic and autonomous budgets, with none paid directly into the union budget.[20] The USSR Government, however, may have taken the position that this RSFSR legislation is unconstitutional. Therefore, the boundaries of the respective tax authority, and the rights to tax revenues, of the union, republic, and local governments remain unresolved and extremely controversial.

Although the Soviets have taken some affirmative steps in the direction of reforming their tax system to accommodate a market-oriented economy, these steps have been hesitant, and the process is far from complete. Many difficult hurdles will have to be surmounted before the tax system is stable, predictable, and well-managed. The ultimate uncertainty in the present Soviet tax system is whether the union or the republic governments will have primary responsibility for determining tax policy. The union government traditionally has exercised, and still claims, this role of determining tax policy. Until the conflict between the union and republic governments over the many aspects of federalism in the USSR—including whether there will be a USSR—is resolved, taxpayers, including foreign investors, will be faced with considerable volatility in tax policy and administration.

In addition to the uncertainties arising from constitutional conflicts, lack of experience with a market-oriented tax system likely will render the Soviet tax system uncertain and tentative for the foreseeable future. For example, the concept of "profit" in Soviet accounting previously bore little relationship to "profit" as it is understood in the capitalist world. The Soviets now are forced to adjust their understanding and their tax regulations to incorporate a more capitalistic concept of profit. Moreover, the Soviets have had very little experience with tax administration and

19. USSR Enterprise Profits Tax Law, *supra* note 8, art. 4(1)-(2).
20. RSFSR Enterprise Profits Tax Law, *supra* note 9, art. 3.

enforcement in a market-oriented economy. Their previous experience involved a tax system in which voluntary compliance was not especially important because most enterprises were state-owned and most individuals state-employed. As the ownership of enterprises and the employment of individuals shifts from predominantly state to predominantly private, Soviet tax administration will grow considerably more complex and difficult. The absence of a tax-paying culture—a culture in which there exists a tradition and general acceptance of voluntary compliance with tax laws—will force the Soviet authorities to develop new mechanisms and techniques for securing voluntary compliance with the tax laws.

Any assessment of Soviet tax reform as it now stands must conclude that, although the Soviet Government has taken some necessary steps to accommodate its tax system to a more market-oriented economy, many more steps will be necessary before the tax system is reliable, consistent, predictable, and efficient. Therefore, in evaluating the tax aspects of trading or investing in the USSR, foreign companies and individuals must recognize that further change in the system is inevitable.

III. The Taxation of Foreign Trade and Investment-Related Income

Some foreign businesses appear to have invested in the USSR unaware of the Soviet tax consequences. This attitude may be an understandable response to a Soviet tax system that is rather vague and that has emerged in a piecemeal, and occasionally contradictory, fashion. Moreover, most foreign investors participating in joint ventures do not expect short term profits. Therefore, how those profits will be taxed may not be a question of great importance. Despite these factors, foreign companies and individuals contemplating investing or otherwise doing business in the USSR should give serious pre-investment consideration to the tax consequences. Any assessment of the financial prudence of such an investment will be shaped largely by tax considerations, and during the negotiations preceding investment, foreign investors will be in the strongest bargaining position to obtain tax concessions, such as extended tax holidays, and to clarify the tax treatment of income and expenses with the tax authorities.

Currently, income earned by a foreign company from sources within the USSR will be subject to substantially different tax treatment depending on the nature and scope of the activities producing the income. There are essentially four categories of such income: (1) income earned by a company that directly engages in business in the USSR without a permanent establishment there; (2) income earned by a company that directly engages in business in the USSR through a permanent establish-

ment; (3) income earned by a company that owns an interest in a Soviet joint venture; and (4) income earned by a company that engages in business in the USSR through a wholly or partially owned Soviet limited-liability company or joint-stock association. In addition to these four categories of income that may be earned by foreign companies from sources in the USSR, a fifth category of income should also be considered in this connection: the personal income, principally wages, that a foreign individual may earn while working in the USSR or otherwise may receive from Soviet sources.

The tax treatment accorded to each of these categories of income is a function of Soviet tax laws and regulations and the provisions of applicable tax treaties. For purposes of the following discussion, this Article primarily will analyze the situation of United States companies and individuals doing business in the USSR and, therefore, will give greatest consideration to the Soviet Union's tax treaty with the United States.

A. *Income Earned by Companies that Do Not Maintain Permanent Establishments in the USSR*

The first two categories of income derived from doing business in the USSR do not relate to income earned from investments in the USSR, but rather relate to income earned by a foreign company from directly engaging in business activities in the USSR. These activities include companies trading or otherwise doing business in their own name and not through a joint venture or other Soviet juridical entity. The critical determinant of how such income will be taxed is whether that foreign company conducts its business activities in the USSR through a permanent establishment.[21]

The broad statutory definition of a permanent establishment includes not only the maintenance of an office or other such facility through which the foreign company engages in business activities, but also "organizations and citizens who represent the foreign juridical person within the territory of the USSR."[22] By including agents and representatives of

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21. For purposes of the USSR Enterprise Profits Tax Law, a permanent establishment is

> [A] bureau, office, agency, or any other place for engaging in activities (connected with the exploitation of natural resources, engaging in construction, installation, assembly, repair, maintenance of equipment, and other similar work), as well as organizations and citizens who represent the foreign juridical person within the territory of the USSR.

USSR Enterprise Profits Tax Law, *supra* note 8, art. 9.

22. *Id.*

foreign companies in this way, without any limitation or qualification, the definition of permanent establishment contained in the USSR Enterprise Profits Tax Law is much more inclusive than the tax treaties to which the Soviet Union is a party. For example, the definition of "representation" in the Convention Between the United States of America and the Union of Soviet Socialist Republic on Matters of Taxation (Convention on Matters of Taxation), does not include agents or representatives.[23] For purposes of this treaty, the term representation is the equivalent of permanent establishment. Many of the USSR's other early tax treaties did not include agents or representatives in their definitions of permanent establishment, although the more recent agreements have tended to include provisions that are comparable to the provisions contained in the Model Double Taxation Convention (OECD Model Convention).[24]

The OECD Model Convention provides that an agent, other than an agent of independent status, that acts on behalf of an enterprise and that has, and habitually exercises, authority to conclude contracts on behalf of an enterprise will be considered to constitute a permanent establishment for the enterprise on whose behalf it acts.[25] Thus, under prevailing international tax treaty practice, agents of independent status or agents that do not have the authority to contract for their foreign principals would not constitute permanent establishments for those foreign principals. No such limitations or qualifications, however, exist in the Soviet statutory definition of permanent establishment. Unless the Soviet tax authorities limit the breadth of this definition in the expected regulations,[26] the use

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23. Convention Between the United States of America and the Union of Soviet Socialist Republics on Matters of Taxation, June 20, 1973, United States-USSR, 27 U.S.T. 1, T.I.A..S. No. 8225, art. IV(2)(a) [hereinafter Convention on Matters of Taxation]. It should be noted that the United States and the Soviet Union are currently in the process of negotiating a new double taxation treaty to replace the 1973 U.S.-USSR Convention on Matters of Taxation. A draft of this new income tax treaty was initialed during the fall of 1990; some aspects of the treaty, however, are still being negotiated. *U.S. Tax Briefing: U.S.-Soviet Treaty Moves Ahead*, 18 TAX PLAN. INT'L REV., Mar. 1991, at 44.

24. COMMITTEE ON FISCAL AFFAIRS, ORGANISATION FOR ECONOMIC CO-OPERATION AND DEVELOPMENT, MODEL DOUBLE TAXATION CONVENTION ON INCOME AND ON CAPITAL, art. 5(5) (1977) [hereinafter OECD MODEL CONVENTION]. For a discussion of this Convention, see Newcity, *Other Tax Agreements*, *supra* note 2, at 856-57.

25. *See* OECD MODEL CONVENTION, *supra* note 24, art. 5(5).

26. The USSR Ministry of Finance adopted instructions concerning the implementation of the enterprise profits tax law in late December 1990. *See* Instructions of the USSR Ministry of Finance, Dec. 29, 1990, *Instruktsiia o poriadke ischisleniia i uplaty v biudzhet naloga na pribyl' i otdel'nye vidy dokhodov* [Instructions on the Procedure

of agents of independent status or of limited authority might be construed as creating a Soviet permanent establishment.

The statutory definition of permanent establishment is more inclusive than the comparable definition in the Convention on Matters of Taxation in another sense. This treaty defines a representation as "an office or representative bureau established in the USSR by a resident of the United States in accordance with the laws and regulations in force in the Soviet Union."[27] The definitions contained in several of the Soviet Union's other tax treaties contain similar language defining permanent establishment as an office established in accordance with the legislation in force.[28]

No similar qualification is contained in the statutory definition of permanent establishment. The apparent practical significance of this difference is that permanent establishment, as defined in the USSR Enterprise Profits Tax Law, is not congruent with an accredited representative office, which is "the only officially permitted means for a foreign company to establish a direct presence in the USSR"[29] and which involves registration with agencies of the Soviet government. Although the registration of an accredited office would certainly give rise to a permanent establishment as defined in the USSR Enterprise Profits Tax Law, a permanent establishment also would include the maintenance of agents within the USSR, which does not require registration as an accredited office.

The tax consequences of maintaining a permanent establishment in the USSR are significant. Under article 32 of the USSR Enterprise Profits Tax Law, and in the absence of an applicable tax treaty provi-

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for the Calculation and Payment into the Budget of the Tax on Profits and Other Forms of Income], Ekonomika i zhizn', Jan. 1991, No. 5, at 17. These instructions, however, specifically do not apply to joint ventures and foreign companies receiving profits from activities in the USSR. The application of the enterprise profits tax to those enterprises will be the subject of other regulations issued by the USSR Ministry of Finance. *Id.* preamble.

27. Convention on Matters of Taxation, *supra* note 23, art. IV(2)(a).

28. *See, e.g., Konventsiia mezhdu Pravitel'stvom SSSR i Pravitel'stvom Soedinennogo Sorolevstva Velikobritanii i Severnoi Irlandii ob ustranenii dvoinogo nalogooblozheniia v otnoshenii nalogov na dokhody i prirost stoimosti imushchestrva* [Convention between the Government of the USSR and the Government of the United Kingdom of Great Britain and Northern Ireland on the Avoidance of Double Taxation with respect to Taxes on Income and Capital Gains], July 31, 1985, Ved. Verkh. Sov. SSSR, No. 7, item 127, art. 5(1).

29. Sheedy & Dean, *Gaining a Foothold in the Soviet Market: How to Establish a Representative Office*, 25 INT'L LAW. 103 (1991). The authors characterize an accredited representative office as a direct presence in the USSR and distinguish it from an indirect presence such as a joint venture. *Id.* at 103 n.1.

sion, a company that does not maintain a permanent establishment in the USSR is subject to a twenty percent withholding tax on income earned from Soviet sources in the form of dividends, interest,[30] copyright and other license payments, freight, lease payments, and other income.[31] Income derived from the sale of goods or the provision of services to Soviet sources is not specifically mentioned in article 32. Whether this sales and services income would be considered "other income, the source of which is located in the USSR and that is not connected with engaging in activities in the USSR through a permanent establishment,"[32] and thus subject to this twenty percent withholding tax, remains unclear. The only other tax provisions that relate to income earned by foreign companies trading or otherwise doing business in the USSR apply to foreign companies engaging in activities through a permanent establishment. Therefore, sales and services income that is unrelated to a permanent establishment probably will be subject to the twenty percent withholding tax. A clarification, however, of this important question by the USSR Ministry of Finance certainly would be desirable.

The twenty percent tax will be withheld by the Soviet payor at the time of payment to the foreign company in the currency in which the transaction is effected.[33] Moreover, the USSR Enterprise Profits Tax Law includes a provision prohibiting the inclusion in foreign trade contracts of a clause requiring the Soviet payor to bear the expense of the applicable Soviet tax.[34] In addition to this twenty percent withholding tax, the USSR Enterprise Profits Tax Law contains a provision relating to income derived from concerts and other entertainment events that are staged in venues with seating capacities in excess of two thousand. This entertainment income[35] is subject to a seventy percent tax, which is not a withholding tax. Expenses incurred in connection with earning the income are deductible from receipts in determining the income subject to

30. Interest earned from loans to the USSR government, the USSR State Bank, or the USSR Bank of Foreign Economic Activity is exempt from taxation. USSR Enterprise Profits Tax Law, *supra* note 8, art. 32(3).

31. Although most of this income is subject to a 20% tax, income derived from the payment of freight is subject to a 6% tax. USSR Enterprise Profits Tax Law, *id.* art. 32(2).

32. *Id.* art. 32(1).

33. *Id.* art. 32(5).

34. *Id.* art. 34(3). This provision is applicable to all foreign companies that are subject to Soviet taxation, not just those that do not maintain a permanent establishment in the USSR.

35. These provisions also apply to income from casinos, video theaters, and the operation of gambling machines with monetary prizes. *Id.* art. 33(1).

taxation.[36]

All of the Soviet Union's double taxation treaties contain provisions that would eliminate liability for the payment of this tax by foreign companies that do not maintain permanent establishments in the USSR. The Convention on Matters of Taxation, for example, provides in article IV that "income from commercial activity derived in one Contracting State by a resident of the other Contracting State, shall be taxable in the first Contracting State only if it is derived by a representation."[37] Comparable provisions are found in all of the USSR's double taxation agreements.[38] Thus, a foreign company that is resident in one of the countries with which the USSR has a tax treaty and that does not maintain a permanent establishment in the USSR, as defined in the applicable treaty,[39] would be entitled to an exemption from payment of the twenty percent withholding tax on the commercial income derived from USSR sources. Such income will only be taxable in the recipient's resident country. These treaty exemptions, however, will not be applied automatically. If a foreign company is entitled to an exemption from the twenty percent withholding tax under an applicable treaty provision, it must

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36. *Id.*

37. Convention on Matters of Taxation, *supra* note 23, art. IV(1), at 7. Under the Convention, a company will be considered as a United States resident if it is "a corporation or any other organization treated in the United States as a corporation for tax purposes which is created or organized under the laws of the United States or any state thereof or of the District of Columbia." *Id.* art. II(4). The term "representation" as used in the Convention on Matters of Taxation is synonymous with "permanent establishment"; *see id.* art. IV(2).

38. *See, e.g., Soglashenie SSSR i Federativnoi Respubliki Germanii ob izbezhanii dvoinogo nalogooblozheniia dokhodov i imushchestva* [Agreement between the USSR and the Federal Republic of Germany on the Avoidance of Double Taxation of Income and Property], Nov. 24, 1981, Ved. Verkh. Sov. SSSR, No. 28, item 430, art. 5(1) (July 13, 1983); *Soglashenie mezhdu SSSR i Avstriiskoi Respublikoi ob ustranenii dvoinogo nalogooblozheniia dokhodov i imushchestva* [Agreement between the USSR and Austria on the Elimination of Double Taxation of Income and Property], Apr. 10, 1981, Ved. Verkh. Sov. SSSR (No. 50), item 945, art. 5(1) (Dec. 15, 1982); and *Soglashenie mezhdu Pravitel'stvom SSSR i Pravitel'stvom Korolevstva Shvetsii ob ustranenii dvoinogo naloogblozheniia dokhodov i imushchestva* [Agreement between the Government of the USSR and the Government of the Kingdom of Sweden on the Elimination of Double Taxation of Income and Property], Oct. 13, 1981, Ved. Verkh. Sov. SSSR, No. 2, item 8, art. 4(1) (Jan. 12, 1983). For a list of the Soviet Union's double taxation agreements, see Newcity, *Tax Issues*, *supra* note 2, at 188-89.

39. For purposes of these treaty exemptions, whether a foreign company maintains a permanent establishment in the USSR will be determined under the definition of permanent establishment contained in the applicable treaty, not the definition contained in article 32 of the USSR Enterprise Profits Tax Law.

submit an application for such an exemption to the USSR Ministry of Finance.[40]

B. *Income Earned by Companies that Do Maintain Permanent Establishments in the USSR*

Under the USSR Enterprise Profits Tax Law, a company that engages in commercial activities within the USSR[41] through a permanent establishment is subject to a thirty percent tax on the profits it earns thereby.[42] This law provides that the USSR Council of Ministers will issue regulations more completely defining profits and the business-related expenses that can be deducted in calculating taxable profits.[43] When the profits connected to the foreign taxpayer's Soviet activities are impossible to determine, taxable profits shall be determined on the basis of gross revenues and an assumed rate of profitability of fifteen percent.[44] Foreign companies that receive compensation in kind are obligated to pay the profits tax on the basis of their contract prices or prices for similar products offered by Soviet export organizations.[45]

A foreign company that engages in commercial activities in the USSR through a permanent establishment must register within one month of the commencement of its activities with the local tax authorities.[46] This registration process is apparently in addition to the registration procedure that a foreign company must follow in order to establish an accredited representative office in the USSR. To establish an accredited representative office, the foreign company must submit an application to one of the accrediting bodies within the Soviet Government, which include several USSR ministries and agencies and may include some republic ministries as well.[47] Only the tax officials in the local Ministry of Finance office, however, may register a foreign company for tax pur-

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40. USSR Enterprise Profits Tax Law, *supra* note 8, art. 32(4).

41. The activities include those "within the territory of the USSR, on the continental shelf and in the economic zone of the USSR." *Id.* art. 9.

42. *Id.* art. 11.

43. *Id.* art. 10. Article 12 of the USSR Enterprise Profits Tax Law provides that such foreign companies will be entitled to deduct from their taxable profits expenditures on environmental protection measures and for charitable purposes. *Id.* art. 12.

44. *Id.* art. 10. The Soviet tax authorities have previously calculated the tax liability of foreign companies on the basis of notional profits. This provision appears to give a statutory basis to this existing practice. *See* Sheedy & Dean, *supra* note 29, at 112-13.

45. Sheedy & Dean, *supra* note 29, at 112-13.

46. The local tax authorities include the USSR Ministry of Finance and its subsidiary departments at the republic and local levels.

47. *See* Sheedy & Dean, *supra* note 29, at 108, 115-16.

poses.[48] The company also must notify the tax authorities one month prior to the termination of commercial activities by its permanent establishment. Failure to register in this manner will be considered as the concealment of income that is subject to taxation.[49]

Prior to April 15 of each year, foreign companies that maintain permanent establishments in the USSR must submit tax returns with respect to the prior year's income. A company that has terminated its activities in the USSR prior to the end of the calendar year, however, must submit its tax return within one month of the termination of its activities.[50] The form of the tax return will be determined by the USSR Ministry of Finance in instructions expected to be issued in early 1991. Once submitted, the tax return is subject to audit by the Soviet audit organization. Once the amount of tax that is due is established, the USSR Ministry of Finance issues a notice of payment to the foreign company. Payment of this tax then must be effected through a bank transfer, either in rubles or foreign currency.[51]

Both the Convention on Matters of Taxation and other Soviet tax treaties contain provisions that should reduce or eliminate the tax liability of some foreign companies maintaining permanent establishments in the USSR. Article IV of the Convention provides that income earned by a resident of one state from commercial activity in the other state is taxable in that other state if it is derived through a permanent establishment.[52] Article III(1) of the Convention, on the other hand, provides that certain specific categories of income are exempted from taxation in the country from which the income is derived regardless of whether the recipient maintains a permanent establishment there.

The categories of income exempted from taxation under article III(1) are: rentals, royalties, or other license payments for intellectual or industrial property; gains from the sale of such property; gains from the sale of property received as a result of inheritance or gift; income derived from furnishing engineering, architectural, designing, and other technical services in connection with an installation contract, provided that these services are carried out within a thirty-six month period at one location; income derived from the sales of goods or the supplying of services through a broker or other independent agent; reinsurance premiums; and

48. USSR Enterprise Profits Tax Law, *supra* note 8, art. 8.

49. *Id.* Concealment of income, although not subject to criminal penalties, may entail the imposition of a fine equal to the amount of the concealed income. *Id.* art. 37(4).

50. *Id.* art. 13(2).

51. *Id.* art. 13(3).

52. Convention on Matters of Taxation, *supra* note 23, art. IV(1).

interest on loans connected with the financing of trade between the United States and the Soviet Union.[53] In addition, article III(2) provides that one state shall not attribute taxable income to the following activities when they are engaged in by a resident of another state: the purchase of goods or merchandise; use of facilities for storage or delivery of goods belonging to a resident of the other state; display of goods belonging to a resident of the other state; the sale of those goods upon the termination of the display; and advertising, collection or dissemination of information, research, or other activities of a preparatory or auxiliary character.[54]

The comparable provisions in the USSR's other tax agreements vary with respect to the specific categories of income and permanent establishment activities that are exempted from taxation in the state where the income arises, although broad similarities do exist. Most of the treaties contain provisions similar to those included in the Convention on Matters of Taxation that exclude storage, delivery, and display of goods and merchandise from the definition of permanent establishment.[55] Similarly, most of the treaties include provisions that eliminate the taxation of royalty income in the state in which the income arises.[56]

Thus far, the discussion of the tax liability of foreign companies that maintain permanent establishments in the USSR has referred only to the thirty percent tax on profits established by the USSR Enterprise Profits Tax Law. The USSR Enterprise Profits Tax Law also provides for several other taxes. These taxes include the turnover tax; the tax on export and import; the tax on income from securities; the twenty percent withholding tax imposed on foreign companies for income that is not connected to the conduct of activities in the USSR through a permanent establishment;[57] and the tax on income from casinos, gambling, video theaters, concerts, and other entertainment events.[58] In addition to these taxes provided for in the USSR Enterprise Profits Tax Law, recent decrees also have established a sales tax.[59] Foreign companies that main-

53. *Id.* art. III(1).
54. *Id.* art. III(2).
55. *See* Newcity, *Other Tax Agreements*, *supra* note 2, at 856.
56. *Id.* at 859.
57. *See supra* notes 30-34 and accompanying text.
58. *See supra* notes 35-36 and accompanying text.
59. *See* Decree of the President of the USSR, Dec. 29, 1990, *O vvedenii naloga s prodazh* [On the Introduction of the Tax on Sales], Izvestiia, Dec. 30, 1990, at 1, col. 5; *see also* Regulation of the Cabinet of Ministers of the USSR, Jan. 31, 1991, *Polozhenie o poriadke ischisleniia i uplaty naloga s prodazh* [Regulation on the Procedure for the Calculation and Payment of the Tax on Sales], Ekonomika i zhizn', Feb. 1991, No. 7,

tain permanent establishments in the USSR may be liable for the payment of some, but not all, of these taxes. Although clarification must await the issuance of definitive regulations by the Soviet authorities, foreign companies apparently will not be liable for payment of the turnover tax, the tax on export and import, or the tax on income from securities. They may be liable, however, for the twenty percent withholding tax; the tax on income from casinos, gambling, video theaters, concerts and other entertainment events; and the sales tax.

The turnover tax, which is a sales tax usually imposed on the difference between the wholesale and retail prices for a particular product,[60] is paid by enterprises that produce and sell goods for the Soviet domestic market. Although it has been suggested that foreign companies maintaining permanent establishments in the USSR may be liable for the payment of this tax,[61] the USSR Enterprise Profits Tax Law suggests otherwise. Article 14 states that the turnover tax will be paid by "enterprises, associations, and organizations (including production cooperatives, as well as joint enterprises with the participation of Soviet juridical persons and foreign juridical persons and citizens and their subsidiaries) that produce and sell goods (products) that are subject to the turnover tax."[62] Foreign companies engaged in activities in the USSR through a permanent establishment are not specifically mentioned in this section, nor are they mentioned in the two resolutions that have been promulgated by the USSR Council of Ministers to establish the turnover tax rates to be paid by joint ventures.[63] Moreover, it is highly doubtful that a foreign com-

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para. 1(c), at 17; Instructions of the Ministry of Finance of the USSR, Feb. 11, 1991, *Instruktsiia po primeneniiu Polozheniia o poriadke ischisleniia i uplaty naloga s prodazh* [Instructions on the Application of the Regulation on the Procedure for the Calculation and Payment of the Tax on Sales], Ekonomika i zhizn', Feb. 1991, No. 9, para. 2(c), at 19.

60. *See* de Jong, *Turnover Tax in the U.S.S.R.*, 31 BULL. INT'L FISC. DOC., Feb. 1977, at 69, 70-71.

61. *See* Sheedy & Dean, *supra* note 29, at 114.

62. USSR Enterprise Profits Tax Law, *supra* note 8, art. 14.

63. Resolution of the Council of Ministers of the USSR, Aug. 13, 1990, *Ob ustanovlenii stavok na 1990 god naloga na eksport i import, a takzhe naloga s oborota s sovmestnykh predpriiatii, sozdannykh na territorii SSSR s uchastiem sovetskikh iuridicheskikh lits i inostrannykh iuridicheskikh lits i grazhdan* [On the Establishment of Rates for 1990 for the Tax on Export and Import, as well as the Turnover Tax on Joint Enterprises Created within the Territory of the USSR with the Participation of Soviet Juridical Persons and Foreign Juridical Persons and Citizens], Pravitel'stvennyi Vestnik, No. 36, supp., at 5 (Sept. 1990) [hereinafter Resolution of the Council of Ministers, Aug. 13, 1990]; Resolution of the Council of Ministers of the USSR, Jan. 19, 1991, *O stavkakh naloga s oborota dlia sovmestnykh predpriiatii* [On the Rates of the

pany, operating in its own name in the USSR through an accredited representative office, would be permitted to produce and sell goods for the Soviet market.[64] Thus, the turnover tax would not apply.

The inclusion of foreign companies as one category of enterprises liable for payment of the five percent sales tax, which like the turnover tax is imposed in connection with the sale of goods in the Soviet domestic market, contradicts this argument.[65] The inclusion of foreign companies in this manner may suggest that Soviet tax officials are anticipating a future time when foreign companies, acting through branch offices, will be permitted to manufacture and sell goods directly in the USSR. If such a change in current legislation does occur, it might render foreign companies engaged in such activities liable for payment of the turnover tax. No evidence suggests, however, that foreign companies acting directly, rather than through joint ventures or Soviet companies, will be permitted to engage in such activities anytime soon.

Although the turnover tax has been the mainstay of the Soviet tax system since the 1930s, the USSR Enterprise Profits Tax Law is aimed at recapturing some of the profits earned by enterprises engaged in export and import operations within the USSR.[66] Substantial disparities between Soviet domestic prices and world market prices for some goods and commodities allow substantial profits to be made by enterprises that import foreign goods, especially consumer goods, and sell them at high prices in the unregulated domestic market in the USSR. The rates applicable to goods imported into the Soviet Union are expressed as a percentage of the contract price for the goods. These rates range from 20.9 percent for video and audio cassettes, to 1.2 percent for imported wool.[67]

Whether foreign companies with permanent establishments in the USSR will be liable for payment of the tax on export and import is not

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Turnover Tax for Joint Enterprises], Ekonomika i zhizn', Feb. 1991, No. 8, at 20.

64. The purposes for which accredited offices can be established include fulfilling commercial transactions, facilitating the performance of trade agreements, and other similar activities, but they do not include producing and selling goods for the Soviet market. *See* Sheedy & Dean, *supra* note 29, at 109-10.

65. *See* Instructions of the Ministry of Finance of the USSR, Feb. 11, 1991, *Instruktsiia po primeneniiu Polozheniia o poriadke ischisleniia i uplaty naloga s prodazh* [Instructions on the Application of the Regulation on the Procedure for the Calculation and Payment of the Tax on Sales], Ekonomika i zhizn', Feb. 1991, No. 9, para. 2(c), at 19.

66. The tax on export and import relates principally to export and import transactions not included in the state economic plan. *See* Resolution of the Council of Ministers, Aug. 13, 1990, *supra* note 63.

67. *Id.* at 6.

entirely clear. Article 17 of the USSR Enterprise Profits Tax Law states that the tax "shall be paid by all organizations listed in article 1 of this Law that are engaging in foreign trade operations."[68] Foreign companies are not mentioned in Article 1 of the law, nor are they referred to in the USSR Council of Ministers resolution that established rates for the tax on export and import.[69] Nevertheless, accredited representative offices of foreign companies are authorized to assist Soviet organizations in promoting the exportation of goods and services from the USSR and the importation of machinery and equipment by Soviet organizations.[70] Although these activities are not precisely the sort of export-import operations at which the tax is aimed,[71] some foreign companies with permanent establishments in the USSR may engage in export-import transactions that would bring them within the scope of the tax. Despite statutory language suggesting that foreign companies are not subject to the tax, it is not yet clear whether Soviet authorities will expect the foreign company to pay this tax. Greater clarification by the Soviet tax authorities on the application of this tax to foreign companies would be useful to foreign companies considering the tax consequences of their operations in the USSR.

The USSR Enterprise Profits Tax Law created a new tax on income derived from shares, debentures, and other securities, as well as interests in joint ventures.[72] This fifteen percent withholding tax applies to the income earned by foreign companies that own interests in Soviet joint ventures[73] and would certainly apply to any foreign company that maintains a permanent establishment in the USSR and owns an interest in a joint venture.[74] The tax, however, would not apply to a foreign company whose only involvement in the USSR is an accredited representative office or other permanent establishment.

In addition to this fifteen percent withholding tax on income from securities, there is also the twenty percent withholding tax applied to income received by foreign companies from sources such as dividends, in-

68. USSR Enterprise Profits Tax Law, *supra* note 8, art. 17.

69. Resolution of the Council of Ministers, Aug. 13, 1990, *supra* note 63, at 5.

70. *See* Sheedy & Dean, *supra* note 29, at 109.

71. The tax on export and import is aimed principally at the importation of consumer-oriented goods in transactions that are not included in the national economic plan. *See supra* note 66.

72. *See* USSR Enterprise Profits Tax Law, *supra* note 8, art. 31.

73. *Id.* art. 31(2).

74. For a fuller discussion of this 15% tax on the income earned by the foreign participant in a joint venture, see *infra* notes 85-91 and accompanying text.

terest, license fees, lease payments.[75] This tax applies to income that is unrelated to activities conducted in the USSR through a permanent establishment, but it is possible that a foreign company that maintains a permanent establishment in the USSR might also earn other income—interest or royalty payments, for example—that is unrelated to the activities it conducts through its permanent establishment. In that case, the foreign company apparently would be required to differentiate the income attributable to its permanent establishment from that attributable to Soviet sources unrelated to its permanent establishment. On the former, the company would pay the thirty percent profits tax, and on the latter, it would be required to pay the twenty percent withholding tax.

The final tax provided for in the USSR Enterprise Profits Tax Law that may have some relevance for foreign companies with permanent establishments is the tax on gambling, concerts, and entertainment events.[76] Under article 33 of the USSR Enterprise Profits Tax Law, a seventy percent tax will be imposed on income derived both from casinos, video theaters, the operation of gambling machines, and from the receipts of large-scale concerts and other entertainment events. Expenses incurred in connection with these income-producing operations are deductible from the amount of the receipts in determining the amount of taxable income.[77] Nothing in the language of article 33 suggests that foreign companies are not subject to this tax, and therefore, it must be assumed that they are.

The more difficult question relates to situations in which a foreign company with a permanent establishment in the USSR uses that permanent establishment to earn income from gambling, concerts, or other entertainment events. A foreign concert promoter likely will not have an accredited representative office in the USSR, because that is not one of the purposes for which such an office may be opened.[78] A foreign concert promoter, however, conceivably may be considered to have a permanent establishment within the USSR as defined in article 9 of the USSR Enterprise Profits Tax Law. If the foreign concert promoter has a relationship with a Soviet organization or individual who represents the promoter in the USSR, the promoter could be considered as maintaining a permanent establishment in the USSR.[79] This view would be advantageous for the promoter because arguably the income earned by the pro-

75. *See supra* notes 26-29 and accompanying text.
76. *See supra* notes 35-36 and accompanying text.
77. USSR Enterprise Profits Tax Law, *supra* note 8, art. 33.
78. *See* Sheedy & Dean, *supra* note 29, at 109.
79. *See supra* notes 23-26 and accompanying text.

moter is related to the permanent establishment and thus subject to the thirty percent profits tax, rather than the seventy percent tax on gambling, concert, and entertainment receipts. Whether the Soviet tax authorities would accept this argument remains unclear, and thus, the relationship between the thirty percent profits tax on foreign companies that maintain permanent establishments in the USSR and the seventy percent tax on receipts from gambling, concerts, and entertainment receipts is unresolved. As in several other areas of Soviet tax law and regulations, clarification will be necessary.

C. *Income Earned by Companies Owning an Interest in Soviet Joint Ventures*

The third and fourth categories of income that a foreign company may earn in the USSR do not arise from activities that the foreign company undertakes directly in the USSR, but rather arise from income generated by Soviet enterprises that the foreign company either partially or wholly owns. In recent years, the most significant such opportunity has involved the establishment of a joint venture.[80]

Income earned by Soviet joint ventures is subject to taxation at two different levels: when the joint venture itself earns profits and when those profits are remitted to its foreign participant. Profits earned by the joint venture itself are subject to a thirty percent profits tax, but if the joint venture was created in the Far Eastern Economic Region, the applicable profits tax rate is ten percent.[81] If the foreign participant's share is less than thirty percent, however, the tax rate is the same as the rate applicable to ordinary Soviet enterprises—a maximum of forty-five percent.[82]

In addition to this concessionary profits tax rate, which is fifty percent lower than the forty-five percent rate applicable to ordinary Soviet enterprises, Soviet legislation provides for a two-year tax holiday for most joint ventures. Joint ventures created in the Far Eastern Economic Region, however, are entitled to three-year holidays. Some joint ventures—those engaged in fishing and mineral extraction, those in which the foreign participant has an interest of less than thirty percent, and

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80. Joint ventures were first permitted pursuant to decrees originally adopted in January 1987. *See supra* note 3 and accompanying text. A substantial literature on Soviet joint ventures has been published in the four years since those enterprises were first permitted. *See, e.g.*, K. HOBER, JOINT VENTURES IN THE SOVIET UNION (1989); C. OSAKWE, JOINT VENTURES WITH THE SOVIET UNION: LAW AND PRACTICE (1990).

81. USSR Enterprise Profits Tax Law, *supra* note 8, art. 5(1)(b).

82. *Id.*

those that are not involved in material production—are not eligible for any tax holidays.[83]

In addition to the profits tax, dividends that are remitted by a joint venture to its foreign participant also are subject to taxation. Although the original Soviet joint venture decrees imposed a twenty percent withholding tax on profits remitted to a foreign participant,[84] the USSR Enterprise Profits Tax Law reduced this rate to fifteen percent.[85] This tax is withheld by the enterprise paying the dividend when the profits are to be transferred abroad. The foreign participant in the joint venture also is made responsible for its payment.[86]

The liability of foreign participants for payment of this withholding tax on remitted profits may be reduced or eliminated pursuant to the terms of an applicable tax treaty. Many of the Soviet Union's tax treaties include provisions relating to the taxation of such dividends,[87] and several of these treaties exempt the foreign participant from payment of any Soviet taxes on dividends.[88] The Convention on Matters of Taxation, however, contains no such provision.[89] Consequently, an American company that owns an interest in a Soviet joint venture will be obligated to pay the entire fifteen percent withholding tax on profits that are remitted in the form of dividends. If, however, these profits are remitted in the form of royalties, interest, or some other form of income that is exempt from Soviet taxation under article III of the Convention on Matters of Taxation,[90] the remitted profits also should be exempt from the Soviet withholding tax. A foreign participant in a Soviet joint venture that is entitled to an exemption from the withholding tax pursuant to one of the Soviet Union's tax treaties must submit an application according to procedures that are to be issued by the USSR Ministry of Finance.[91]

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83. *Id.* art. 6(6)(a).

84. Decree of Council of Ministers of the USSR, Jan. 13, 1987, *supra* note 3, para. 41.

85. USSR Enterprise Profits Tax Law, *supra* note 8, art. 31(2).

86. *Id.* art. 31(2)-(3).

87. *See* Newcity, *Tax Issues*, *supra* note 2, at 192-97.

88. The Soviet Union's treaties with Austria, Cyprus, Finland, and the United Kingdom grant a total exemption from payment of such taxes on dividends in the Soviet Union. *Id.* at 198-200.

89. *See supra* note 23.

90. *See supra* notes 52-54 and accompanying text; *see also*, Newcity, *Tax Issues*, *supra* note 2, at 189-92.

91. USSR Enterprise Profits Tax Law, *supra* note 8, art. 31(5). Joint ventures are also liable for payment of the turnover tax, the tax on export and import, and the sales tax. *See supra* notes 57-71 and accompanying text.

D. *Income Earned by Companies Doing Business in the USSR Through a Soviet Limited Liability Company or Joint-Stock Association*

The most important recent development in the law governing foreign investment in the USSR has been the adoption of legislation permitting the creation, for the first time in modern Soviet history, of limited liability and joint-stock companies and permitting foreigners to own some or all of the shares in such companies.[92] Many aspects of the legal nature, formation, rights, and obligations of these companies have not yet been fully resolved, and consequently, their utility as vehicles for foreign investment remains somewhat unknown. Inasmuch as the profits earned by these companies are subject to a different tax regime than the profits earned by joint ventures, tax considerations may be an important element in deciding whether a foreign direct investment in the USSR will take the form of a joint venture rather than a limited liability or joint-stock company.

The USSR Enterprise Profits Tax Law was adopted on June 14, 1990, five days before the USSR Council of Ministers adopted its decree on the creation of joint-stock and limited liability companies and four months before President Gorbachev adopted his decree permitting foreigners to own some or all of the shares of these companies. Consequently, the USSR Enterprise Profits Tax Law does not deal with the taxation of foreign-owned Soviet companies in any comprehensive fashion. Under this law, joint-stock and limited liability companies would be taxed under the provisions generally applicable to Soviet enterprises. They will be subject to a profits tax of up to forty-five percent, with possibly higher tax rates if the company's profitability level exceeds specified norms.[93] Additionally, these companies will be subject to the turnover tax, the tax on exports and imports, and the sales tax. In addition, income from the shares, bonds, or other securities issued by these companies would be subject to the fifteen percent withholding tax described above.[94]

When deciding whether their direct investments will take the form of

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92. Resolution of the Council of Ministers of the USSR, July 19, 1990, *Ob utverzhdenii polozheniia ob aktsionernykh obshchestvakh i obshchestvakh s ogranichennoi otvetstvennost'iu i polozheniia o tsennykh bumagakh* [On the Confirmation of Regulations on Joint-Stock Companies and Limited Liability Companies and Regulations on Securities], No. 590; *see also*, Decree of the President of the USSR, Oct. 26, 1990, *supra* note 4.

93. *See* USSR Enterprise Profits Tax Law, *supra* note 8, art. 4(3).

94. *See supra* note 74 and accompanying text.

a joint venture or a limited liability or joint-stock company, foreign companies must recognize that, under the USSR tax legislation, the difference in form will result in the application of different profits tax rates. As noted above, joint ventures are subject to a thirty percent tax on profits,[95] yet other enterprises, including Soviet companies, are subject to a maximum tax rate of forty-five percent. Although the Soviet authorities have little apparent reason to favor direct investments in the form of joint ventures, the tax legislation creates an incentive to invest in this form. Under the USSR Enterprise Profits Tax Law, a joint venture in which a foreign investor has a seventy percent interest will be subject to a thirty percent profits tax. Yet a Soviet company that is seventy percent owned by a foreign shareholder or shareholders will be taxed at a maximum rate of forty-five percent. No difference, however, exists in the tax rate imposed on profits that are remitted by these enterprises to their foreign participants. Profits remitted to the foreign participant in a joint venture, as well as dividends or interest on bonds that are paid to a foreign investor in a Soviet company, are subject to a fifteen percent withholding tax.

The greatest difficulty in assessing the tax liability of limited liability or joint-stock companies arises from conflicts between the tax legislation adopted at the national or union level by the USSR Government and the legislation adopted at the republic level. For example, under the USSR Enterprise Profits Tax Law, as adopted by the USSR Supreme Soviet, the rates for the tax on profits of Soviet enterprises such as limited liability and joint-stock companies are as follows: Most enterprises are subject to a profits tax of at least twenty-two percent; each union republic then is entitled to impose an additional tax of up to twenty-three percent of taxable profits, for a maximum total tax rate of forty-five percent of taxable profits;[96] and enterprises that earn profits in excess of a rate established by the USSR Council of Ministers are subject to a tax on the excess profits of eighty to ninety percent.[97]

Under legislation adopted by the RSFSR Supreme Soviet in December 1990, however, the tax rates applicable to enterprises in the Russian republic are somewhat different than under the USSR Enterprise Profits Tax Law.[98] This legislation, which purports to define how the USSR Enterprise Profits Tax Law will be implemented within the RSFSR, specifies that enterprises created under the authority of the USSR, pre-

95. *See supra* 81-82 and accompanying text.
96. USSR Enterprise Profits Tax Law, *supra* note 8, art. 4(1)-(2).
97. *Id.* art. 4(3).
98. RSFSR Enterprise Profits Tax Law, *supra* note 9.

sumably including limited liability and joint-stock companies created under the applicable USSR decrees, are subject to a profits tax of forty-five percent. Other enterprises are subject to a thirty-eight percent profits tax, although enterprises that are owned one hundred percent by foreigners are subject to a thirty percent tax rate.[99] This latter provision is interesting in that it provides comparable tax treatment to joint ventures and wholly-owned Soviet companies,[100] although it does nothing to resolve the disparity in treatment between joint ventures and partially-owned Soviet companies. Thus, under the RSFSR legislation, a joint venture in which foreign investors own a seventy percent share will still be subject to a thirty percent tax rate, while a Soviet company in which foreign investors own seventy percent of the shares will be subject to the forty-five percent or thirty-eight percent tax rates. Consequently, the Soviet tax legislation has created an incentive for foreign direct investments in the form of joint ventures, while the RSFSR legislation has created a tax incentive for either joint ventures, the taxation of which is unaffected by the RSFSR legislation, or wholly-owned joint-stock or limited liability companies.

Unlike the USSR Enterprise Profits Tax Law, the RSFSR Enterprise Profits Tax Implementing Law actually specifies the applicable profit margin for the excess profits tax. Article 2 of the RSFSR law states that the profits tax rates discussed above will apply to those enterprises that earn profit margins of up to fifty percent. Enterprises, including those wholly-owned by foreign investors, that earn profits in excess of fifty percent will be subject to the payment of a seventy-five percent tax on the excess profits.[101] Although the normal profits tax rates specified by the RSFSR Enterprise Profits Tax Implementing Law are within the discretion of the republic government as granted by the USSR Enterprise Profits Tax Law, the RSFSR Enterprise Profits Tax Implementing Law's provisions concerning the excess profits tax conflict with the provisions of the USSR Enterprise Profits Tax Law that specify an eighty percent tax on profits that are less than ten percent in excess of the officially-established norm and a ninety percent tax on profits that are more than ten percent in excess of that norm.[102]

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99. *Id.* art. 2.

100. In addition, this provision of the RSFSR law does not distinguish between companies established under the jurisdiction of the USSR from those established under RSFSR jurisdiction. It merely provides that the profits of enterprises that are 100% owned by foreign investment will be taxed at a 30% rate. *Id.* art. 2(b).

101. *Id.* art. 5.

102. USSR Enterprise Profits Tax Law, *supra* note 8, art. 4(3).

The principal conflict between the USSR and the RSFSR Profits Tax Laws relates less to tax rates or definitions of taxable profits than to where the tax revenues will be paid. The USSR Enterprise Profits Tax Law contains elaborate provisions specifying whether the revenues from particular taxes will be paid in whole or in part into the budgets of the union government, the republic governments, or the local governments.[103] The RSFSR Enterprise Profits Tax Implementing Law is in direct conflict with the USSR Enterprise Profits Tax Law because it uniformly provides that tax revenues will be paid into the republic and local budgets, with none of the revenue to be paid into the union budget of the national government. Even though this conflict has serious consequences for Soviet domestic fiscal policy and the relations between the national government and the republics, it has less significance to foreign investors, who, in general, probably will be unconcerned about which level of government receives the benefit of these taxes. Nevertheless, the differences between the union and republic governments over taxation indicate the potential for conflicting rules and procedures concerning the amount of tax that will be owed and the appropriate tax authorities to whom the tax payments should be made. Until these conflicts are resolved, presumably in the context of a new union treaty defining the respective roles of the union and republic governments, foreign investors and their Soviet companies possibly, or even likely, will be subject to conflicting and confusing instructions by the USSR and RSFSR tax authorities.

Another question of central importance to foreign investors contemplating the creation of a wholly or partially owned Soviet subsidiary is how the dividends on shares or the interest on bonds that is remitted by that company to its foreign parent will be taxed. Under the USSR Enterprise Profits Tax Law, income derived from shares and other securities is subject to a fifteen percent withholding tax, the same rate that is now applicable to profits remitted by a joint venture to its foreign participant.[104] Similarly, those Soviet tax treaties that include provisions reducing or eliminating Soviet taxes on dividends would apply to this tax, although the current Convention on Matters of Taxation includes no such provision.[105]

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103. Article 4(3), for example, provides that 50% of the tax on excess profits is to be included in the union budget and that the remaining 50% is to be included in the republic and local budgets in amounts to be determined by the republics. *Id.*

104. USSR Enterprise Profits Tax Law, *supra* note 8, art. 31(1).

105. Although there is an exemption for interest income in the Convention on Matters of Taxation, it applies only to interest on loans connected with the financing of

E. *Personal Income Earned in the USSR or from Soviet Sources*

Recent changes in the taxation of Soviet enterprises have stirred significant controversy,[106] yet changes in personal income tax legislation have precipitated even sharper debates. For example, an immediate, sustained, and intense outcry followed the Supreme Soviet's adoption of legislation in March 1988 that changed the tax rates applicable to cooperative members by increasing the maximum marginal rates applicable to their income from thirteen percent to ninety percent.[107] Ultimately, the criticism of this legislation by cooperative members and their supporters forced the Supreme Soviet to suspend the March 1988 tax law and adopt legislation providing that cooperative members would be taxed at the same rates as the employees of state enterprises.[108]

In one sense, the success of the "tax revolt"[109] by Soviet cooperative members and their supporters during the summer of 1988 was a pyrrhic victory. Although they won a commitment that cooperative members and other private entrepreneurs would be taxed on a par with state enterprise employees, they thereby insured that the tax rates ultimately to be imposed on all Soviet workers—state enterprise employees and cooperative members alike—would become considerably more progressive. A draft personal income tax law published in April 1989 retained the fea-

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United States-Soviet trade, not to interest on debt securities. *See supra* note 53 and accompanying text.

106. The principal controversy that arose during the public discussion of the reform of enterprise taxation related to the applicable tax rates: Should the rates be low to stimulate investment or production, or should they be higher to fund social programs? *See, e.g.*, Liubimtsev, *Nalogi: primerka zapadnoi modeli?* [Taxes: Trying Out the Western Model?], Ekonomika i zhizn', Apr. 1990, No. 15, at 10. This article introduced a new Russian word: *reiganomiki.*

107. Decree of the Presidium of the Supreme Soviet of the USSR, March 14, 1988, *O nalogooblozhenii grazhdan, rabotaiushchikh v kooperativnakh po proizbodstvu i realizatsii produktsii i okazaniiu uslug, a takzhe ob izmenenii poriadka vydachi patentov na zaniatie individual'noi trudovoi deiatel'nost'iu* [On the Taxation of Citizens Working in Cooperatives that Produce and Sell Goods and Provide Services, as well as on Amendments to the Procedure for the Issuance of Licenses to Engage in Individual Labor Activity], Ved. Verkh. Sov. SSSR, No. 11, item 174 (March 16, 1988).

108. *O poriadke nalogooblozheniia dokhodov chlenov kooperativov v sferakh proizvodstva i uslug, sel'skokhoziastvennykh kooperativov (krome kolkhozov) i lits rabotaiushchikh v nikh po trudovomu dogovorov* [On the Procedure for the Taxation of the Income of Members of Cooperatives in the Spheres of Goods and Services, Agricultural Cooperatives (Except Kolkhozes) and Individuals Working in them under Labor Agreements], Ved. Verkh. Sov. SSSR, No. 31, item 507 (Aug. 3, 1988).

109. *See* Keller, *Moscow Parliament Revolts: Tax on Business is Opposed*, N.Y. Times, May 26, 1988, at A1, col. 4; *see also* Newcity, *Perestroika, supra* note 13, at 240-44.

ture that individuals would be taxed at the same rates irrespective of whether they were employed by state or cooperative enterprises and included tax rates with a maximum marginal rate of fifty percent.[110] After a thorough debate, the Supreme Soviet adopted the USSR Income Tax Law in April 1990, which set the maximum marginal rate of taxation at sixty percent.[111]

Foreign citizens who are permanent residents of the USSR also are liable for payment of the income tax at these new and higher rates.[112] For these purposes, a permanent resident of the USSR is any individual who is located in the USSR for more than 183 days during a calendar year.[113] Under the USSR Income Tax Law, the Soviets have asserted taxing jurisdiction over the worldwide income of permanent residents of the USSR.[114] In addition, any individual who derives income from Soviet sources is liable for payment of tax on that income in the Soviet Union, even if that person is not a permanent resident of the USSR.[115] Thus, the principal effect of the USSR Income Tax Law on foreign companies and their employees in the USSR will, in the absence of an applicable treaty exemption, be to increase their tax liability.

As already stated, the USSR Income Tax Law has increased dramatically personal tax liability for individuals earning substantial incomes. For example, under the old rates that were applicable to employees of state enterprises as well as foreign employees in the USSR,[116] an individual earning 4000 rubles per month would have to pay 515 rubles, twenty kopecks in tax each month, excluding any personal or familial

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110. *Proekt: Zakon SSSR: Ob izmenenii poriadka i razmerov nalogooblozheniia naseleniia* [Draft Law of the USSR: On Changes in the Procedure and Rates of Taxing the Population], Pravda, Apr. 16, 1989, at 1, col. 5.

111. *See* USSR Income Tax Law, *supra* note 7. The 60% maximum marginal rate precipitated criticism such as the following:

> It takes incentives away from the diligent, the talented and the enterprising, and thereby robs society. From July 1, when the law comes into force, the standard-bearers of egalitarianism may sleep quietly: no official millionaires will turn up in the country. . . . How can we rebuild the economy by proclaiming the advance towards the market while backing farther and farther away from it?

Korshunov, *A Tax to Hit the Market*, Moscow News, June 10-17, 1990, at 10, col. 1.

112. USSR Income Tax Law, *supra* note 7, art. 1.

113. *Id.*

114. *Id.* art. 2(1).

115. *Id.*

116. Foreign individuals in the USSR were also subject to taxation at the same rates as the employees of Soviet state enterprises. *See* Decree of the Presidium, May 12, 1978, *supra* note 1, para. 6, at 278; *see also*, M. NEWCITY, *supra* note 10, at 215-21.

deductions.[117] The effective tax rate would be 12.9 percent. Under the USSR Income Tax Law, an individual earning this amount, which is within the highest tax bracket, would have to pay 1,646 rubles, twenty kopecks per month.[118] Under the new law, the effective tax rate would be 41.2 percent. For such a high-end taxpayer,[119] whether a successful cooperative member, an employee of a joint venture, or an employee of a foreign company who is working in the USSR, these changes in the applicable tax rates represent a tax increase of over two hundred percent.

One effect of this enormous increase in the Soviet tax liability for high-income individuals will be to increase the costs for foreign companies doing business in the USSR. Most of these companies offer their expatriate employees in the USSR benefits such as cost-of-living and tax equalization adjustments, as well as hardship allowances. Thus, a substantial portion of this personal income tax increase will be borne by the companies.[120] Nevertheless, because the income tax, including the tax on income that was received in foreign currency, can be paid in rubles or foreign currency,[121] this burden may be mitigated somewhat. For example, a foreign citizen who is a permanent resident of the USSR and who receives an annual income paid in United States dollars of 75,000 dollars would be liable, at the official exchange rate of 1.6 ruble per United States dollar, for the payment of taxes on 46,875 rubles, a monthly income of 3906 rubles, 25 kopecks. The tax on that amount of annual income would be 19,079 rubles, 40 kopecks.[122] The foreign executive, however, would be entitled to purchase rubles to pay this income tax liability at the tourist rate of six rubles to the dollar, with 19,079 rubles, 40 kopecks converting into 3179.90 dollars. Thus, if the tax liability is converted at one exchange rate and the purchase of rubles to pay that liability is effected at another rate, this foreign executive can achieve an

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117. The applicable tax rates are set out in Decree of the Presidium of the Supreme Soviet of the USSR, Oct. 20, 1983, *O vnesenii ijmenenii i dopolnenii v ukaj Prezidiuma Verkhovnogo Soveta SSSR "O podokhodnom naloge s naseleniia"* [On the Introduction of Changes and Amendments into the Decree of the Presidium of the Supreme Soviet of the USSR "On the Income Tax on the Population"], Ved. Verkh. Sov. SSSR, No. 43, item 653, art. 9 (Oct. 26, 1983).

118. For the applicable tax rates, see USSR Income Tax Law, *supra* note 7, art. 8.

119. The average monthly wages of Soviet factory and office workers in 1990 was 270 rubles. The average monthly wages for workers in cooperatives was 450 rubles. *Soobshchenie Gosudarstvennogo komiteta SSSR po statistike* [Report of the USSR State Committee on Statistics], Ekonomika i zhizn', Jan. 1991, No. 5, at 9.

120. *See* Sheedy & Dean, *supra* note 29, at 115.

121. *See* USSR Income Tax Law, *supra* note 7, art. 2(2).

122. At the official exchange rate of 1.6 rubles to the United States dollar, this sum would equal $30,527.04.

effective tenfold reduction in his or her Soviet income tax liability as measured in United States dollars.[123] "The effect of this tenfold decrease means that the personal tax rate becomes, in effect, 6 percent."[124]

There are no long-term guarantees to assure that this device will remain effective. The Soviet authorities could adopt regulations closing this loophole by stipulating that if the foreign executives opt to pay their tax in rubles, then the taxes must be paid in a noncash exchange transaction through a Soviet bank using the official Gosbank rate of 1.6 rubles to the dollar. Moreover, if the Soviet Union continues to move in the direction of a convertible currency, at some point the various exchange rates offered by the Soviet government will converge into a single rate, and this opportunity for minimizing tax liabilities by playing one exchange rate against another will end.

The USSR Income Tax Law includes provisions clarifying the definition of taxable income as it pertains to foreign individuals who are permanent residents of the USSR. Article 26 of the law defines the taxable income of foreign citizens as including allowances paid in connection with living in the USSR, presumably including both cost-of-living and hardship allowances, as well as allowances paid for the education of the individual's children, food for the individual's family, and transportation during holidays.[125] Amounts deducted by the foreign citizen's employer to pay to state social insurance and pension plans, lease payments for housing and job-related automobiles, and job-related expenses are not included in taxable income.[126]

For most Soviet citizens, the income tax is withheld at the individual's place of employment. Those individuals who receive income from sources outside the USSR are obligated to submit annual tax returns and make periodic tax payments based on projected income for the current year. Thus, foreigners who take up permanent residence in the USSR must submit declarations to the local tax authorities within one month of their arrival in the USSR, advising the authorities of that individual's projected income for the current year.[127] The taxpayer also must calculate an amount equal to seventy-five percent of the tax that would be owed on that projected income; this percentage then must be paid in three equal instalments on May 15, August 15, and November 15. At the end

123. This tenfold difference, of course, corresponds to the tenfold difference in the two exchange rates.

124. *See* Sheedy & Dean, *supra* note 29, at 115.

125. USSR Income Tax Law, *supra* note 7, art. 26(1).

126. *Id.* art. 2(2).

127. *Id.* art. 28(2).

of the year, any foreign citizen who is a permanent resident of the USSR and who received income from sources outside the Soviet Union must submit a tax return by March 1 showing the amount of income actually received during the preceding year.[128] These returns must be submitted to the tax authorities at the place where the individual lives, but if the individual lives in one place and works in another, the returns must be submitted to the tax authorities at the place of employment.[129] On the basis of the information contained in the tax return, the tax authorities will calculate the amount of tax that the taxpayer owed for the preceding year, compare it with the advance amount already paid, and issue a payment notice for any deficit. This deficit amount must then be paid within a month of the issuance of the payment notice by the tax authorities. If the taxpayer's advance payments have exceeded his or her actual tax liability, the authorities either will issue a refund of the excess or will credit it against future tax liabilities.[130] A foreign individual planning to discontinue working in the USSR must submit a declaration to that effect along with information concerning the individual's actual income no later than one month prior to his or her departure.[131]

In addition to these provisions relating to the taxation of foreign individuals who are considered to be permanent residents of the USSR, the USSR Income Tax Law also contains provisions relating to the taxation of foreigners who are not permanent residents of the USSR, but who receive income from Soviet sources. Such income is subject to a twenty percent tax, to be withheld at the source of payment in the USSR.[132]

As previously mentioned, the RSFSR has adopted legislation that purports to implement the USSR Income Tax Law.[133] The only provision in this republic legislation that materially would affect a foreign citizen working in the USSR is the section that introduces a different tax schedule for the taxation of the income of factory and office workers, for this is the tax schedule that applies to the salaries earned by foreign citizens in the USSR. Under the RSFSR legislation, the maximum marginal tax

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128. *Id.*

129. Instructions of the Ministry of Finance of the USSR, June 25, 1990, *Instruktsiia o poriadke primeneniia Zakona SSSR "O podokhodnom naloge s grazhdan SSSR, inostrannykh grazhdan i lits bez grazhdanstva"* [Instructions on the Procedure for the Application of the Law of the USSR "On the Income Tax on Citizens of the USSR, Foreign Citizens and Stateless Persons"], Biulleten' Normativnykh Aktov Ministerstv i Vedomstv SSSR, No. 12, para. 90, at 15 (1990).

130. USSR Income Tax Law, *supra* note 7, art. 28(3).

131. *Id.* art. 28(2).

132. *Id.* art. 29.

133. *See* RSFSR Income Tax Law, *supra* note 9.

rate on such income is fifty percent, instead of the sixty percent imposed by the USSR law. Under the modified tax schedule contained in the RSFSR law, a foreign employee who earns 4000 rubles per month would be liable to pay 1314 rubles in tax, 332 rubles, twenty kopecks less than the amount calculated according to the tax schedule contained in the USSR law.[134] Because the constitutionality of the RSFSR law is in serious doubt,[135] it is not clear whether it will be applied by the taxing authorities within the RSFSR.

The Convention on Matters of Taxation offers some limited assistance to United States citizens who are working in the USSR. Under article VI of the convention, a resident of the United States would not be liable for paying Soviet taxes on income received for the performance of personal services in the USSR, as long as they were not present in the USSR for more than 183 days during the tax year.[136] Thus, individuals who are not considered to be permanent residents of the USSR for purposes of Soviet tax legislation will be exempt from paying the twenty percent withholding tax on amounts earned for the rendering of personal services in the USSR. Individuals who are present in the USSR for more than 183 days during the calendar year, however, will not be exempted from the payment of Soviet taxes by the Convention on Matters of Taxation unless they fall into one of the categories of individuals that are accorded favorable treatment under the convention. Thus, residents of the United States who are government employees, participants in programs of intergovernmental cooperation, teachers and researchers temporarily present in the USSR, students, and trainees are exempt from taxation in the Soviet Union with respect to income they earn in these capacities, even if they are present in the USSR for more than 183 days

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134. *See* USSR Income Tax Law, *supra* note 7, art. 8.

135. This law and the RSFSR law that purports to apply the USSR Enterprise Profits Tax Law within the RSFSR state in their preambles that they were issued on the basis of the RSFSR Declaration on State Sovereignty. *See* RSFSR Income Tax Law, *supra* note 9, preamble; RSFSR Enterprise Profits Tax Law, *supra* note 9, preamble. Although the RSFSR Declaration of State Sovereignty does not specifically mention taxing authority, it does assert that the RSFSR is a sovereign state, with complete authority to decide "all questions of state and public life." Declaration on State Sovereignty of the RSFSR, Sovetskaia iustitsiia, No. 14, at 2 (1990). The USSR Constitution, however, vests the union government with the responsibility for "determination of the taxes and revenues forming the Budget of the USSR." KONST. SSSR art. 71(6). The author has been informed that the USSR government has taken the position that the two RSFSR laws applying the USSR tax legislation within the Russian republic are unconstitutional. Conversation with Christopher Osakwe in Nashville, Tennessee (March 15, 1991).

136. Convention on Matters of Taxation, *supra* note 23, art. VI(2).

during the calendar year.[137]

IV. CONCLUSION

The process of tax reform in the USSR is proceeding, and the principles and procedures by which the Soviet government taxes income earned by foreign companies and individuals in the USSR are developing and growing more sophisticated. As the Soviet tax authorities gain more experience in such matters, this process should only accelerate. The current lack of experience and conflicts within the Soviet Union over economic policy and relations between the national government and the republics suggest, however, that this tax system will be in a continuous state of flux and, regrettably, confusion for some years to come. Although uncertainties about the taxation of the income generated by investing or otherwise doing business in the USSR should not deter foreign companies, these uncertainties will make the decision to invest or do business less appealing.

137. *Id.* art. VI(1). The exemptions granted to participants in programs of intergovernmental cooperation, teachers and researchers, students, and trainees only extend for a period of time required to effectuate the purpose of the visit and, in any event, are subject to absolute time limits. *Id.* art. VI(1)(f).