

DRAFT

March 29, 1997

MEMORANDUM FOR

Mr. Egor Timurovich Gaidar

cc: Professor Michael Alexeev
Mr. Joel McDonald
Professor Andrei Shleifer

From: Bob Conrad

Subject: Completing the Tax Code

I understand you had some productive meetings with Professors Alexeev and Shleifer. In particular, I understand that the deadline for completing the current exercise is April 18, 1997. There are a number of things to clarify in order to complete this effort. Some of these items are discussed below and some questions are raised about planning.

A. What Will Be Delivered

Attached to this document is the current work program developed by our group. I propose that we continue to draft according to this schedule and that we will deliver the parts of the code promised by April 18. Neither a general nor technical explanation of the law will be completed by that date. General and technical explanations will be completed in due course.

There is a risk that the code will not move forward because of lack of understanding. It will be difficult to explain the provisions and technical detail without reference documents. Consideration should be given to redrafting your working group's report as a substitute for, and a bridge to, a general and technical explanation for the code sections. This document can serve a statement of government policy intentions reflected in the code and can serve as a discussion document. The particular code sections can then be judged relative to this document until a technical and general explanation can be developed. Our group is willing to work on this policy statement. I can work on the effort from the United States and am making arrangements to return to Moscow as soon as possible to work on completing the project.

A number of modifications to the original work program are necessary in order to meet the new deadlines. We believe the new deadline can be satisfied if we can agree on a number of points.

1. A new tax administration law has been drafted by our group which we believe is superior to the provisions contained in the code. We

propose to substitute our law for the existing code sections. A copy of this law will be provided to you this week.

2. We want to substitute the expense section of the profits tax in the current code with rules contained in Presidential Decree 685. We worked with Mr. Orekhov and others to develop Decree 685 and believe the expense rules are better than those found in the existing code. In addition, the statutory language is nearly complete. Finally, the code will reflect the President's explicit policy guidance as reflected in Decree 685.
3. We will not provide any statutory rules for mineral taxes at this time. Mining taxes will be one project to begin after April 18. Revenue implications are significant. In addition, a number of lobby groups plus technical assistance providers are planning to make proposals for significant change in both the tax and production sharing laws. It will be imperative to move in this area quickly in order to stabilize the rules for this sector.

I believe a satisfactory document can be developed on time if these conditions are satisfied.

B. Delivery Date

Drafts will be provided to you and your group for review as completed. I understand that the completed draft will be provided to your group by April 18 for consideration by others. We will continue to work on other sections and explanations after that date.

C. Relationship to Ministry of Finance Draft

I want to clarify the relationship between this exercise and the work being completed by Mr. Shatalov. Mr. Shatalov has publicly stated that the code will be sent to the government by the end of March. Thus, is our joint effort with you a competing version of the code, a substitute for the Shatalov code or a version which will be supported by Mr. Shatalov? In addition, if our effort is either a substitute or one supported by Mr. Shatalov, will the Ministry of Finance be involved in the reviewing the draft and will we work with Ministry of Finance to complete the work?

D. How Will the Remainder of the Code Be Completed and Submitted to the Government?

Parts 3 and 4 of the Code have not been reviewed and will not be revised in the near future. In addition, a number of sections in Part 1 will not be revised prior to April 18. Finally, some sections of Part 2 (mining taxes and customs for instance) will not be revised by the deadline. Given the

incomplete nature of the redrafting, it is important to know what strategy will be developed to move the code through the Duma. Questions include:

1. Will the entire code go forward regardless of the amount of review and redrafting?
2. If the answer to Question 1 is yes, then how can further amendments supported by the government be introduced? A significant number of changes will be necessary and it will be important to know how the government will be able to substitute language and policy for the draft submitted to the Duma, if this option is selected.
3. If the answer to Question 1 is no, then how will further sections be submitted for consideration and what time schedule should be employed?
4. What will be the timetable to get sections of the code (or the entire code) passed? I understand the Duma will recess for the summer at the end of June and that any changes for the next budget must be made by that time.

E. Other Issues

1. I understand that you will be contacting Mr. Orekhov about participating in this process. I am pleased to hear this and look forward to working with him.
2. Professor Shleifer informed me that you would like some lawyers on your staff to be paid by our project. Please provide details to our Moscow office and we will arrange contracts.
3. I am trying to rearrange my schedule and will return to Moscow as soon as possible.

Finally, many policy decisions are being made other than those proposed in your group's working document and during our discussions. For instance, source rules, the treatment of foreign exchange gains and losses, residence rules, and issues like reverse charging are examples of the numerous decisions that must be reflected in the law. It will not be possible to discuss every detail given time constraints. A compilation of policy decisions will be prepared as we proceed and will be provided to you on a timely basis. These decisions should be reviewed by your group and discussed with us as needed.

I hope this is helpful and I look forward to your response. Please contact me should you need anything.

Thank you for your consideration of these matters.

PROPOSED WORK PROGRAM FOR REVISION OF DRAFT RUSSIAN TAX CODE
March 24, 1997

Subject	Tax Code Articles ¹	Statutory Language		Technical Explanation	
		Resp. Person(s)	Deadline	Resp. Person(s)	Deadline
1. Tax administration					
a. Collection, penalties, appeals, assessment, etc.	Part 1- Articles 61-68, 111-172, 192-416	Chewning, Haberly	April 4	Hook	April 18
b. Transfer pricing	Part 1 - Articles 93, 99-100	Short	April 4	Summers	April 18
2. VAT	Part 1 - Articles 93-98, 107 Part 2 - Articles 425-450	Summers	April 4	Chewning, Haberly	April 18
3. Excise taxes	Part 2 - Articles 462-485	Summers	April 4	Chewning, Haberly	April 18
4. Personal income tax	Part 1 - Article 76 Part 2 - Articles 606-632	Hussey, Schmalbeck	April 18	Himes	May 2
5. Social taxes	Part 2 - Articles 636-644	Ross	April 18	Himes	May 2
6. Profits tax					
a. Accrual/cash	Part 1 - Articles 181-189, 191	Hussey	April 18	Trinklein	May 2
b. Estimated payments	Part 2 - Articles 588-589	Hussey	April 18	Haberly	May 2
c. Inventories	Part 1 - Article 190	Short	April 25	Degler	May 9
d. Small business tax	Part 1 - Articles 40-41 Part 2 - Articles 578-584	Himes	April 25	Trinklein	May 9
e. Income/gain determination	Part 1 - Articles 95, 101 Part 2 - Article 513	Stephan	May 2	Haberly	May 16

¹ Except where indicated, "Part 1" refers to the January 1996 version of part 1 of the draft tax code that was submitted by the Government to the Duma, and "Part 2" refers to the February 1997 version of part 2 of the draft tax code that was prepared by the Ministry of Finance.

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f. Expenses/exemptions	Part 2 - Articles 518-546, 586	Chewning	May 2	Summers	May 16
g. International	Part 1 - Articles 5, 32-35, 74, 102-105 Part 2 - Articles 516, 574-577, 594	Rosenbloom	May 2	Stephan	May 16
h. Consolidation, contributions, distributions, reorgs, trusts	Part 1 - Articles 31, 36-37, 81-87, 95, 106 Part 2 - Articles 517, 549, 563-573	Klayman	May 2	Avi-Yonah	May 16
i. Non-profits	Part 1 - Articles 21, 25-26, 51-54 Part 2 - Articles 543, 547, 596	Cerny	May 2	Klayman	May 16
j. Financial intermediaries/securities operations	Part 2: Banks - Articles 514, 532, 540, 585 Ins. cos. - Articles 515, 533, 585 Tax pships - Article 548 Securities operations - Articles 534, 552-562	Degler, Morris	May 2	Short	May 16
7. Taxes on income from capital	Part 1 - Article 106 Part 2 - Articles 593-602	Degler	April 18	Stephan	May 2
8. Mineral taxes	Part 2 - Articles 491-500, 528, 550, 726-764	Smith	April 18	Summers	May 2