

CHINA'S FOREIGN ECONOMIC LEGISLATION. Volume I. Translated and edited by the Foreign Languages Press with assistance from Jerome Cohen, Jamie Horsley, Yan Zekui, Wang Chanlun, and Anne Wang Pusey. [Beijing: Foreign Languages Press, 1982. 289 + vi pp. Yuan 1.45].

SINCE the end of the Cultural Revolution and the fall from power of the Gang of Four, China's leadership has taken pains to promote the development of a modern legal system. Immediate priorities in the late seventies concerned the reinstatement of the basic machinery of justice, devastated during the great upheavals of the late sixties. This entailed principally the promulgation of essential civil and criminal codes, which were largely in accordance with familiar socialist models but adapted to meet the needs and unique legal traditions of Chinese society.<sup>1</sup> At the same time, creation of a legal framework for foreign investment by non-socialist investors ranging from individual overseas Chinese to American, European and Japanese multinationals also received considerable attention. Although much remains to be done, progress in this latter realm has been extremely rapid, as publication last year of the first volume of *China's Foreign Economic Legislation* attests.

The importance of foreign investment to the present leadership's "Four Modernizations" development strategy is well-known abroad and has been aggressively promoted in China itself.<sup>2</sup> Ambitious targets

<sup>1</sup> See generally Chen, "China's Developing Legal System", 13 *Hongkong L.J.* 291 (1983). See also Chen, "China's Law of Civil Procedure", *Beijing Review* (16th August 1983); Leng, "Crime and Punishment in Post-Mao China", 2 *China L. Rep.* 5 (1982); Zhang, "Legislative and Judiciary Work in China", *Beijing Review* (15th August 1983); and Hsia, "Sources of Law in the People's Republic of China", 14 *Int'l. Law* 25 (1980).

Note also the commitment expressed in the Preamble to the 1982 Constitution, which, unlike its 1978 predecessor, states the improvement of the legal system to be part of the basic task of modernization. Article 5, also unprecedented, further declares that "the State upholds the uniformity and dignity of the socialist legal system" and proclaims the supremacy of the written constitution. *The Constitution of the People's Republic of China* [Beijing: Foreign Languages Press, 1983].

<sup>2</sup> For an example of one of many explanations of the foreign investment strategy to be found in the Chinese press see Meng, "Foreign Investments Benefit Construction", *China Daily* (20th April 1983).

for attracting foreign capital have been widely announced, with a goal of US\$20 billion for the five years beginning in 1979.<sup>3</sup> In furtherance of such objectives, investment protection agreements had by mid-1983 been reached with Sweden, Romania and West Germany and negotiations were proceeding with at least seven other capital-exporting nations, including, despite strains in relations over arms sales to Taiwan, the United States.<sup>4</sup>

The depth of the decision to promote foreign investment has recently been dramatically emphasized in the supreme law of the land, the 1982 Constitution. Article 18 thereof provides:

The People's Republic of China permits foreign enterprises, other foreign economic organizations and individual foreigners to invest in China and to enter into various forms of economic co-operation with Chinese enterprises and other economic organizations in accordance with the law of the People's Republic of China.

All foreign enterprises and other foreign economic organizations in China, as well as joint ventures with Chinese and foreign investment located in China, shall abide by the laws of the People's Republic of China. Their lawful rights and interests are protected by the law of the People's Republic of China.

Given China's unhappy experience with foreign investment in the century following the first Opium War and the deep hostility of the Communist Party's left wing to anything that smacks of a restoration of "capitalistic" economic incentives, the course now being followed by the regime is remarkable, if also highly pragmatic.<sup>5</sup>

Certainly pragmatism is reflected in the rapid development of legislation designed to facilitate the desired foreign direct investment. Since the promulgation of the cornerstone Chinese-Foreign Joint Venture Law in July 1979, China has constructed an estimable legal edifice, which consists of more than thirty major statutes and regulations with direct significance for foreign investors. Most of those enacted as of the end of 1981 can be found in the present volume. Despite the fact that most of the statutes and regulations reprinted have been revised or supplemented since their original promulgation,<sup>6</sup> the book is a wel-

<sup>3</sup> Fung, "China Clarifying Investment Rules for Foreigners", *The Asian Wall Street Journal* (31st May 1983).

<sup>4</sup> Statement of Wei Yuming, vice minister in the Ministry of Foreign Economic Relations and Trade ("MOFERT"), reported in "China Will Permit Foreigners to Start Their Own Firms", *The Asian Wall Street Journal* (13th October 1983).

<sup>5</sup> A very readable account of the struggles over economic policy which have rocked the People's Republic of China throughout its thirty-five years of existence can be found in Short, *The Dragon and the Bear: Inside China and Russia Today* [London: Abacus, 1982]. Particularly fascinating are the rationalizations offered for the rather abrupt reversal of course which followed the death of Mao Zedong and the defeat of his leftist successors by the present leadership. For example, Short quotes the economist Xue Muqiao, speaking in 1980: "We do not advocate the restoration of capitalism, yet we should not be overly afraid of it. It is all right to have a bit of capitalism since it is not time to exterminate capitalism yet."

<sup>6</sup> Among the most significant developments since the end of the period covered by the present volume are: (1) "Regulations for Implementation of the Law of the People's Republic of China on Joint Ventures Using Chinese and Foreign Investment", an English translation of which may be found in *Beijing Review* (10th October 1983); (2) "Rules for the Implementation of Exchange Control Regulations", an English translation of which may be found in *Beijing Review*

come addition to the scanty literature and one which allows an overall view of an important part of the legal structure so rapidly, by recent Chinese Standards, erected.

The statutes reprinted and translated range from the fairly well-known joint venture law through those dealing with export licenses, labour relations, taxation (of joint ventures, foreign enterprises and individuals), the establishment and regulation of special economic zone in Guangdong Province, foreign exchange controls, resident offices of foreign businesses, and even the Articles of Association of the Bank of China.<sup>7</sup> The book's compilers provide no information about the legislative history or genesis of the statutes reprinted and translated, nor is there commentary or analysis of any kind. This is unfortunate but not surprising. It must be due at least in part to the quasi-official nature of the publishers, although the book disclaims any authoritative status for its English translations. The reticence to comment is also understandable when one recalls that not so long ago all laws were considered state secrets in the People's Republic. Many are apparently still so considered today.<sup>8</sup>

Experience with these statutes has not measured up to expectations, Chinese or foreign. While assessments naturally vary, *The Economist* has gone so far as to describe the joint venture law as "a flop" and even Chinese officials have publicly expressed a certain disappointment with the quantity and quality of investment attracted by that much-vaunted vehicle. Far more investment has taken alternative and often rather less sophisticated channels, such as highly informal co-production

(22nd August 1983); (3) "Provisional Regulations Concerning the Reduction and Exemption of Income Tax Relating to Interest Earned by Foreign Business from China", which have apparently not yet been published in English but which are discussed in Reynolds, "New Rules May Ease Lending, Leasing to China", *The Asian Wall Street Journal* (8th June 1983); (4) "Measures of the State Administration of Industry and Commerce Regarding the Control of Registration of Long-term Representative Offices of Foreign Enterprises", of which an English translation by a foreign law firm may be found in *East Asian Exec. Rep.* (May 1983); (5) "Provisional Regulations for the Establishment of Representative Offices in China by Overseas Chinese and Foreign Financial Institutions", of which an English translation by a foreign law firm may be found in *East Asian Exec. Rep.* (May 1983); and (6) Regulations governing the registration of foreign oil companies and supply and service sub-contractors engaged in offshore exploration activities, which have apparently not yet been published but which are discussed in Moser, "China's Registration Rules for Foreign Oil Companies", *The Asian Wall Street Journal* (21st June 1983). This list is far from exhaustive, as informed sources suggest that as many as fifty laws and regulations with significance for foreign investors have been enacted — though not, alas, published — since the end of 1981. Presumably most of these will be made available in subsequent volumes.

<sup>7</sup> Interestingly, legislation does not yet exist in China to define the legal capacities of the multiplicity of entities which attempt to deal with foreign investors. As one Western lawyer has commented, establishment of the domestic entity's precise legal capacity has "undeniable relevance in the current Chinese legal environment, in which the lack of much basic legislation gives contracts an all-important role". Gelatt, "Foreigners Make Progress in China's Legal Maze", *The Asian Wall Street Journal* (10th August 1983). By all accounts the task is no easy one.

<sup>8</sup> The problem of actually getting a copy of the existing laws of the People's Republic is one which plagues all foreign investors and their lawyers. One experienced commentator recently reviewed the various legal problems facing foreign investors and suggested that "[p]romulgated laws or regulations have been, and probably still are, the tip of a much larger iceberg". Lubman, "China Should Make More Laws Public", *The Asian Wall Street Journal* (5-6th August 1983).

deals, one-off contract-based joint ventures, and compensation trade arrangements. Most of these have been small in scale and, as *The Economist* put it, are hardly "the stuff of a great leap into modernization."<sup>9</sup> Of course it is necessary to observe that the foreign investment policies themselves mark such a break with the preceding three decades as to make it remarkable that such changes could even begin to be implemented within only a few years. That the legal edifice established to facilitate that policy would have drawbacks is quite understandable, as the laws were put in place rapidly and statutes alone do not make a legal system where there was none before.

Most foreign investors have experienced their own particular problems with the legal structures for investment in China and have often recounted these in the press,<sup>10</sup> but one example which relates to the management of the Chinese-foreign joint venture vehicle illuminating perhaps a clash of legal cultures, might be worth recounting here. Control of these enterprises is not related to the equity shares of the participants and the law stipulates that the Chinese participant must occupy the chair of the board of directors even if, as is possible under the statutory scheme, the foreign participant has contributed 99% of the equity.<sup>11</sup> Composition of the board is, like much else, to be settled by "consultations". Investors have, predictably it must seem from a foreign perspective, found the resulting ambiguities deeply frustrating. Yet the problem seems to have been unanticipated on the Chinese side and, although it has been addressed to some extent in the 1983 implementing regulations, even those are still found ambiguous in this respect by Western lawyers.<sup>12</sup> It is desirable to avoid facile generalizations about legal traditions and supposed preferences for such things

<sup>9</sup> "Chinese Joint Ventures: Red Tape", *The Economist* (27th October 1983). On the reaction of foreign investors, and of Chinese officials, to experience with the joint venture law, *sec generally*, Stepanek, "Direct Investment in China", *The China Business Review* (September-October 1982). Chinese officials apparently hoped for literally thousands of joint ventures to be established in the first few years of the law. Yet in the three years following promulgation only 83 equity joint ventures were signed representing something less than US\$200 million in capital investment. Only ten were approved in the whole of 1982, although indications of improvement were clear in the first half of 1983, with the approval of 22 new joint ventures. Bennett, "China Spells Out Rules for Joint Ventures", *The Asian Wall Street Journal* (27th September 1983). Among the joint ventures approved in 1983 were several of the kind which the leadership has sought as part of its modernization plans, notably automotive works and machine building plants representing investment of more than US\$120 million. And in late 1983 it appears that an equity joint venture will be created to build the HK\$36 billion Daya Bay nuclear power station near the Shenzhen Special Economic Zone in Guangdong Province. Ma, "The Nuclear Family", *The Far Eastern Economic Review* (24th November 1983).

<sup>10</sup> *See, e.g.*, Cohen, "Equity Joint Ventures: 20 Potential Pitfalls That Every Company Should Know About", *The China Business Review* (November-December 1982).

<sup>11</sup> This problem was avoided in the statutes which served as models for the Chinese law, those of Hungary, Romania and Yugoslavia, by simply limiting foreign investors to a minority shareholding. Why this was not done in China is unclear. *See* Jaslow, "Practical Considerations in Drafting a Joint Venture Agreement with China", 31 *American J. Comp. L.* 209 (1983).

<sup>12</sup> *See* Gelatt, "China Sheds More Light on Foreign Investment Laws", *The Asian Wall Street Journal* (7-8th October 1983), highlighting as well other ambiguities in the joint venture law, *e.g.*, those relating to valuation of in-kind contributions to capital such as land, raw materials, plant and expertise; ability of joint ventures to sell products on the domestic market, which is left subject to MOFERT's more or less unfettered discretion; and the autonomy of the venture itself, which is directly linked to the availability of raw materials and other inputs in a socialist, centrally planned economy.

as negotiation or confrontation, specificity or generality. But clearly in China, as in other parts of the world, preconceptions and misguided expectations have hampered developments desired by both hosts and foreign investors.

Deficiencies in such a rapidly erected structure as that represented by China's foreign economic legislation are certainly not to be wondered at and expectations for foreign investment expressed in the late seventies were undoubtedly too high on both sides. To say this is not to excuse the fact that investors are still plagued by basic questions about law-making authority, the authoritative interpretation of statutes and regulations, resolution of conflicts resulting from the often overlapping and confused jurisdiction of state agencies, and the effect of subsequent rules on unrepealed but inconsistent legislation, all of which severely hinder the progress of foreign investment.<sup>13</sup> Technical problems and gaps in the legislation must be addressed if foreign investment is to reach anything like the levels hoped for.

Other, rather extra-legal, problems also exist. Chinese commentators have noted difficulties with the new legalism which cannot be resolved by legislative drafting, principally in the unwillingness of their socialist managers to adopt unfamiliar practices and procedures.<sup>14</sup> Ignorance of the law and a shortage of lawyers are also major hurdles to legal development. Finally, it must be recalled that foreign investment is still a deeply political issue in the People's Republic, and the current policies are undoubtedly constrained to some degree by the existence of powerful elements still unconvinced of the desirability of the tilt towards capitalism.

Recent statements from the highest levels of the leadership show that the regime is still committed to its foreign investment strategy and is aware of the need for further modification of the legal framework.<sup>15</sup> Draft laws are in some cases being circulated for comment among foreign investors and their lawyers in attempts to anticipate problems.<sup>16</sup> It is expected that the appearance of the present volume, which is printed in English and Chinese and contains extensive and very useful glossaries for the legal terminology employed, will facilitate development and improvement of the legal system in China as a whole. Certainly dissemination of the book abroad will extend opportunities

<sup>13</sup> The lack of clearly demarcated jurisdictions for the various state agencies dealing with foreign enterprises can create serious problems, witness the uncertainty which developed in mid-1983 concerning conflicting regulations issued by the People's Bank and by the Ministry of Finance dealing with the operation of foreign banks' representative offices, reported in Fung, "China Clarifies Rules on Foreign Banks", *The Asian Wall Street Journal* (29th June 1983).

<sup>14</sup> See, e.g., "Legal Procedures", a *Renmin Ribao* commentary reprinted in the English-language *China Daily* 20th April 1983.

<sup>15</sup> Towards the end of 1983, Premier Zhao Ziyang made noteworthy statements seeking to reassure foreign investors about China's political stability and commitment to present policies. See "China's Growing Economic Relations", *Beijing Review* (15th August 1983) and "China Honours Contracts, Promises", *Beijing Review* (19th December 1983). Regarding the legal framework, a number of high officials have made remarks similar to those of Yuan Mu, Assistant Secretary-General of the State Council: "Our laws are not perfect yet. After clarification of our laws, maybe there will be more investment" Quoted in Bennett, *supra* note 9.

<sup>16</sup> See Gelatt, "China Amplifies Laws on Foreign Investment", *The Asian Wall Street Journal* (30th August 1983), reporting that a draft of the new foreign exchange control rules was circulated among foreign oil companies in late 1982.

for study and analysis to foreign lawyers and potential investors who have had to rely, hitherto, on piecemeal publication of unofficial translations in a variety of periodicals. The compilers' meticulous translations and elaborate glossaries provide exactly the sort of foundations which will be required for more thoroughgoing analyses of the possibilities and prospects offered by China's new legal regime for foreign investment.

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