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## An Introduction to Foreign Investment Laws in the People's Republic of China, 28 J. Marshall L. Rev. 471 (1995)

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# ARTICLES

## AN INTRODUCTION TO FOREIGN INVESTMENT LAWS IN THE PEOPLE'S REPUBLIC OF CHINA

JOHN ZHENG DONG HUANG\*

### INTRODUCTION

China's policy of enlivening its domestic economy and opening to the outside world has achieved success in encouraging foreign investment. In the past sixteen years, China has maintained the annual economic growth at the average rate of 9.3%.<sup>1</sup> China has established economic and trade relationships with over 220 countries and regions.<sup>2</sup> Realizing that China is a large and fast growing market, foreign investors have poured into China for business opportunities in recent years. From 1979 to 1994, China has approved over 200,000 foreign investment enterprises, which consist of the Chinese-foreign equity joint ventures, foreign capital enterprises, and Chinese-foreign contractual joint ventures. In 1994 alone, China approved 41,000 foreign investment projects with the committed capital of \$68.1 billion, and actual invested capital of \$27.7 billion.<sup>3</sup> In 1978, China's foreign trade only ranked thirty-second in the world, yet in 1994, China jumped to eleventh place with a total trade volume of \$236.7 billion, with an annual increase of 20.9%.<sup>4</sup> Of the \$236.7 billion, the import and export transactions performed by the foreign investment enterprises totalled \$87.6 billion, equivalent to 34.3%.<sup>5</sup>

In 1979, in order to attract foreign capital, and promote economic cooperation and technical exchanges with foreign companies, China delineated four cities as special economic zones: Shenzhen, Zhuhai, Shantou, and Xiamen. These special economic

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1. Xu Zheng Zhong, *Deng Shang Shi Jie Jing Ji Da Wu Tai (Stepping on the Grand Global Economic Stage)*, RENMIN RIBAO (PEOPLE'S DAILY), Dec. 16, 1994, at 1.

2. *Id.*

3. Article, RENMIN RIBAO (PEOPLE'S DAILY), Jan. 9, 1995, at 1.

4. *Wo Wai Mo Jing Chu Kou Zai Chuan Jia Ji, Our Foreign Trade, Imports, and Exports Have Made New Achievements*, RENMIN RIBAO (PEOPLE'S DAILY), Jan. 14, 1995, at 1.

5. *Id.*

zones provide investors with a wide scope of favorable operating conditions and preferential treatment. In 1984, China further opened fourteen coast cities, Dalian, Qinhuangdao, Tianjin, Yantai, Qingdao, Lianyungang, Nantong, Shanghai, Ningbo, Wenzhou, Fuzhou, Guangzhou, Zhanjiang and Beihai. These open coast cities enjoy wide autonomy in foreign economic activities, and provide preferential treatment to foreign companies. In 1988, China founded a new province, Hainan Province, and delineated the whole Hainan Island as China's largest special economic zone. Shortly thereafter, China decided to open and develop the Pudong New Area of Shanghai, China's largest and most powerful city.<sup>6</sup>

With the expansion of foreign investment, China felt the urgent need to establish and improve the legal system to alleviate foreign investors' concerns for legal protection. On July 1, 1979, the Fifth National People's Congress of China adopted its first statute governing foreign investment; this was titled the Law of the People's Republic of China on Chinese-Foreign Equity Joint Ventures.<sup>7</sup> Since then, China has enacted over 200 foreign economic laws and statutes which have constituted a legal framework for foreign investors.

The major laws and statutes governing foreign investment can be broken into the following five areas:

(1) Foreign investment entities: Law of the People's Republic of China on Chinese-Foreign Equity Joint Venture (1979); Law of the People's Republic of China on Economic Contracts Involving Foreign Interest (1985); Law of the People's Republic of China on Foreign-Capital Enterprises (1986); Law of the People's Republic of China on Chinese-Foreign Contractual Joint Ventures, Regulations of the People's Republic of China on the Exploitation of Off-shore Petroleum Resources in Cooperation with Foreign Enterprises (1982); Regulations of the People's Republic of China on Administration of Technology-Introduction Contracts (1985); and Interim Provisions for the Administration of Foreign Chambers of Commerce in China (1980);

(2) Taxation: Income Tax Law of the People's Republic of China on Enterprises with Foreign Investment and Foreign Enterprises (1991); Interim Provisions of the State Council Concerning the Reduction of and Exemption from Enterprise Income Tax and Consolidated Industrial and Commercial Tax in the Special Eco-

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6. See generally ZHONG HUA REN MIN GONG HE GUO SHANG MO TOU ZHI ZHI NAN, A GUIDEBOOK TO COMMERCIAL AND TRADE INVESTMENT IN THE PEOPLE'S REPUBLIC OF CHINA, 14-15 (Jingji Kexue Pub. House 1992).

7. *Id.* at 15. This law was revised in accordance with the Decision of the National People's Congress Regarding the Revision of the Law of the People's Republic of China on Sino-foreign Joint Equity Enterprises adopted at the Third Session of the Seventh National People's Congress on April 4, 1990.

conomic Zones and the Fourteen Coastal Port Cities (1984); and Individual Income Tax Law of the People's Republic of China (1980);

(3) Finance and loans: Measures of the Bank of China Concerning the Granting of Loans to Enterprises with Foreign Investment (1987); Measures for Providing Short-Term Loans in Foreign Currency by the Bank of China (1980); Interim Regulations on Foreign Exchange Control of the People's Republic of China (1980); Rules for the Implementation of Foreign Exchange Control Regulations Relating to Enterprises with Overseas Chinese Capital, Foreign-Capital Enterprises and Chinese-Foreign Equity Joint Ventures (1986); Regulations of the People's Republic of China for the Administration of Foreign Banks and Chinese Foreign Joint Banks in the Special Economic Zones (1985); Measures for the Administration of Foreign-Capital Financial Institutions and Chinese-Foreign Equity Joint Financial Institutions in the Shanghai Municipality (1990); The General Rules Governing Enterprise Financial Affairs (1992); Accounting Criteria for Enterprises (1992); and Interim Measures for the Participation in Swap of the Foreign Exchange Held by Residents in China or to be Used by Residents Going Abroad for Private Business (1991);

(4) Land use: Interim Regulations of the People's Republic of China Concerning the Assignment and Transfer of the Right to the Use of the State-owned Land in the Urban Areas (1990); Interim Measures for the Administration of the Foreign-Invested Development and Management of Tracts of Land (1990); and

(5) Dispute settlement: Civil Procedure Law of the People's Republic of China (1991); Interim Rules for General Average Adjustment of the China Council for the Promotion of International Trade (1975); Arbitration Rules of the China International Economic and Trade Arbitration Commission, and Arbitration Rules of the China Maritime Arbitration Commission.

The National People's Congress and its Standing Committee promulgate all the laws. The State Council proposes and oversees the legislative process. The State Council, its ministries, and various government departments also promulgate legislation, regulations, and rules governing foreign investment. This Article will provide an overview of the legal framework regulating the foreign investment in China.

## I. FOREIGN INVESTMENT ENTERPRISES

There are three types of foreign investment entities in China: Chinese-foreign equity joint ventures, Chinese-foreign contractual joint ventures, and foreign-capital enterprises. Foreign companies are also permitted to establish branch offices and representative offices under limited conditions. This Section will summarize the three types of foreign investment enterprises, branch offices, and

representative offices, and focus on the rules and procedures for setting up such entities.

### A. *Equity Joint Ventures*

Of the various forms of investment in China, equity joint ventures have attracted the most attention from both foreign investors and the Chinese authorities. An equity joint venture is a separate limited liability legal entity registered in China, formed between the foreign entity and a Chinese partner. China has published a substantial body of laws governing equity joint ventures. These include the Law on Chinese-Foreign Equity Joint Ventures and the Regulations for the Implementation of the Law on Chinese-Foreign Equity Joint Ventures.

#### 1. *Framework*

An equity joint venture must take the form of a limited liability company.<sup>8</sup> Parties to the joint venture may include Chinese corporations, enterprises or other entities, and one or more foreign companies, enterprises or individuals. In the registered capital of an equity joint venture, the proportion of the investment contributed by the foreign enterprise shall not be less than twenty-five percent.<sup>9</sup> The most common contributions from Chinese partners are land, labor, factory buildings, and raw materials. The profits, risks, and losses of a joint venture are shared by the parties to the venture in proportion to their contributions to the registered capital. The transfer of one party's share in the registered capital shall be effected only with the consent of the other parties to the venture. Each party to an equity joint venture may contribute cash, capital goods, or industrial property rights as its investment in the venture.<sup>10</sup> The technology or equipment contributed by foreign enterprises as investment shall be truly advanced and appropriate to China's needs. A joint venture shall open an account with the Bank of China or a bank approved by the Bank of China.<sup>11</sup>

Equity joint ventures are required to promote the development of China's economy and to comply with at least one of the following four conditions: (1) adopt advanced technical equipment

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8. Law on the People's Republic of China on Sino-foreign Joint Equity Enterprises, Act of Apr. 4, 1990, art. 4, 1 CHINA L. FOR FOREIGN BUS. REG. (CCH) ¶ 6-500, at 7,803 [hereinafter *Joint Equity Enterprise Law*].

9. *Id.*

10. Regulations for the Implementation of the Law of the People's Republic of China on Joint Ventures Using Chinese and Foreign Investment, Act of Sept. 20, 1983, art. 25, 1 CHINA L. FOR FOREIGN BUS. REG. (CCH) ¶ 6-550, at 7,927.

11. *Id.* at 7,953.

and scientific management; (2) promote the technical renovation of enterprises; (3) produce export-oriented products; or (4) enable the training of technical and managerial personnel.<sup>12</sup>

## 2. *Procedures for Establishing An Equity Joint Venture*

Equity joint ventures shall be approved by the Ministry of Foreign Trade and Economic Cooperation (MOFTEC) or local authorities.<sup>13</sup> Each administrative level of government authority (i.e., province, county, and township) has the power to approve foreign-investment projects, depending on the size of the investment. The examining and approval authorities decide whether or not to approve an equity joint venture application within ninety days.<sup>14</sup>

When applying for approval of a joint venture, the Chinese party is required to submit the following documents to the approval authority: (1) application for the establishment of a joint venture; (2) a feasibility study report, jointly prepared by the parties to the venture; (3) joint venture agreement and articles of association signed by representatives authorized by the parties to the venture; (4) list of candidates for chairman, vice-chairman, and director appointed by the parties to the venture; (5) written opinions of relevant local government agencies with regard to the establishment of the joint venture. The aforesaid documents must be written in Chinese, and documents (2), (3), and (4) may also be translated into a non-Chinese language.<sup>15</sup> Within three months from the date of receipt of these documents, the approval authority must notify the parties of its decision whether to approve or disapprove them.

Within one month after receipt of the certificate of approval, a joint venture is required to register with the local bureau of the State Administration for Industry and Commerce (SAIC) at the place where its head office is located.<sup>16</sup> When applying for registration, a joint venture should provide the following documents to the registration authority: (1) the document of approval; (2) copies of the Chinese and foreign-language texts of the joint venture agreement, the joint venture contract, and the company charter; (3) a copy of the foreign party's business license or other similar documents issued by the authorities of the foreign party's home country; (4) a completed registration form, in triplicate, containing such items as the name of the venture, its address, the scope of

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12. *Id.* at 7,913.

13. *Id.* at 7,915.

14. *Id.* at 7,917.

15. *Id.* at 7,915-17.

16. *Id.* at 7,917.

production and business, forms of production and business, registered capital of the parties concerned, names of the chairman and vice-chairman of the board of directors, general manager and deputy general managers or general director and deputy general managers or general director and deputy directors of the plant, the number and date of approval on the document, the size of the entire staff, and the number of foreign workers and staff members. Upon registration, the joint venture becomes a legal entity and is issued a registration certificate and a business license that is valid for the duration of the joint venture contract. The time required to set up an equity joint venture is not fixed; the process generally requires six to twelve months.<sup>17</sup>

Fees for the registration of joint ventures are levied in accordance with the Provisional Regulations on the Standards of Registration Fees. Joint ventures with a registered capital below RMB 10 million are required to pay a fee equal to 0.1% of the registered capital. If the registered capital exceeds RMB 10 million, but is below RMB 100 million, the required registration fees is assessed at a rate of 0.1% up to RMB 10 million and 0.05% of the excess.<sup>18</sup> No fees are payable for the portion exceeding RMB 100 million.

### *B. Contractual Joint Ventures*

A contractual joint venture, also referred to as a cooperative joint venture, is a common form of cooperative investment arrangement. China adopted the Law on Chinese-Foreign Co-operative Enterprises in 1988.

#### *1. Framework*

Compared with equity joint ventures, contractual joint ventures offer greater flexibility in structure and investment because the terms, conditions, contributions and profit sharing can be contractually agreed between the parties. The parties to the joint venture may determine the distribution of earnings of the venture as they choose,<sup>19</sup> rather than in proportion to specific ownership

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17. WANG HE ET AL., *ZHONG GUO SHE WAI JING JI MOU YI FA ZHI GUAN LI*, LEGAL ADMINISTRATION OF FOREIGN ECONOMICS AND TRADE IN CHINA 113 (Pub. House of Law 1991).

18. The official exchange rate for RMB in January of 1995 was \$100 = 844.37 RMB. *Ren Min Bi Shi Chang Hui Jia*, *RMB Market Exchange Rate*, REN MIN RE BAO (PEOPLE'S DAILY), Jan. 6, 1995, at 2.

19. Article 2 of the law on Chinese-Foreign Contractual Joint Ventures stipulates that the joint venture parties should prescribe in the contractual joint venture contract such matters as the investment or conditions for cooperation, the distribution of earnings or products, the sharing of risks and losses, the manner of operation and management, and the ownership of the property. Law of the People's

shares as required under the equity joint venture law. Also, unlike the equity joint venture law, which generally sets a twenty-five percent minimum for the foreign party's contribution to registered capital, contractual joint ventures are neither subject to the same capital investment requirements as equity joint ventures, nor are they restricted to a range of economic activities or objectives. Contractual joint ventures may use buildings, equipment, land use rights, intellectual property and other investments without having to express these contributions in monetary terms. Moreover, the contractual joint venture law places no requirements on the posts of key management personnel. It does not even require that there be a general manager. In addition, the contractual joint venture law permits the investors to entrust a third party with the management and operations of the venture. The investment contributed by the Chinese and foreign parties may be provided in cash, or may include the right to the use of land, industrial property rights, non-patent technology, or other property rights.<sup>20</sup>

## *2. Procedures for Establishing Contractual Joint Ventures*

The procedures for establishing both equity and contractual joint ventures are generally similar. Separate implementation regulations governing contractual joint ventures are not yet issued. To apply for the establishment of a contractual joint venture, the parties are required to submit such documents as the agreement, the contract, and the articles of association. These documents must be signed by the Chinese and foreign parties for examination and approval by the department in charge of foreign economic relations and trade under the State Council or local government authorities. The government agencies shall decide whether or not to grant approval within forty-five days from the date of receipt of the application.<sup>21</sup>

Upon the approval of the application, the parties to the contractual joint venture shall, within thirty days of receiving the certificate of approval, apply to SAIC for registration and obtain a business license.<sup>22</sup> The date of the license issuance shall be the date of its establishment. A contractual joint venture shall, within thirty days of its establishment, carry out tax registration with the tax authorities.<sup>23</sup>

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Republic of China on Sino-foreign Co-operative Enterprises, Act of Apr. 13, 1988, art. 2, 1 CHINA L. FOR FOREIGN BUS. REG. (CCH) ¶ 6-100, at 7,551.

20. *Id.* at 7,553.

21. *Id.* at 7,551-53.

22. *Id.* at 7,553.

23. *Id.*



### C. Foreign-Capital Enterprises

A foreign company can set up a wholly owned business enterprise with limited liability in China. Such enterprises are limited to industries that can benefit the national economic development of China, adopt advanced technology and facilities, or export more than fifty percent of its products.<sup>24</sup> The capital contribution can be in the form of convertible foreign currency, machinery and equipment, industrial property rights, or proprietary technology.<sup>25</sup>

#### 1. Framework

The Law of the People's Republic of China on Wholly Foreign-Owned Enterprises was promulgated in 1986. Although joint ventures are the most common form of foreign investment in China, investments in wholly foreign-owned enterprises have increased substantially in recent years. China may not nationalize or requisition foreign capital enterprises.<sup>26</sup> The law also forbids any interference in the legitimate operations and management of the foreign capital enterprises.<sup>27</sup>

Like equity joint ventures, foreign capital enterprises must adopt advanced technology, develop new products, or achieve a foreign-exchange balance or surplus. In general, a wholly foreign-owned enterprise is formed as a limited liability company, but it may be established as another form of entity upon government approval. Wholly foreign-owned enterprises enjoy the advantages of full control over business operations, maintenance of better confidentiality of technology and trade secrets, and availability of tax incentives such as, exemption custom duties on imported equipment, component parts and production facilities, and import of raw materials for production of export products.

#### 2. Procedures for Establishing a Wholly Foreign-Owned Enterprise

The approval and registration process for establishing a wholly foreign-owned enterprise is similar to that for joint ventures. Foreign companies are required to submit an application to

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24. Detailed Rules for the Implementation of the Law of the People's Republic of China on Sole Foreign Investment Enterprises, Act of Oct. 28, 1990, art. 3, 2 CHINA L. FOR FOREIGN BUS. REG. (CCH) ¶ 13-507, at 16,659 [hereinafter *Implementation of Foreign Investment Law*].

25. *Id.* art. 26, ¶ 13-507, at 16,671.

26. Law of the People's Republic of China Concerning Enterprises with Sole Foreign Investment, Act of Apr. 12, 1986, art. 5, 2 CHINA L. FOR FOREIGN BUS. REG. (CCH) ¶ 13-506, at 16,651.

27. *Id.* at 16,653.

the relevant authorities, together with the following documents: (1) a feasibility study; (2) articles of association of the enterprise; (3) a list of legal representatives or candidates for the board of directors; (4) evidence of the foreign investor's legal certification and credit standing; (5) the written response of the local government, at county level or above, in the locality of the proposed enterprise; (6) a detailed list of goods and materials needed to be imported; and (7) other necessary documents.<sup>28</sup> The application must be examined and approved by the department in charge of foreign economic relations and trade of the central or the authorized local governments. The examination and approval authority should decide whether to approve or disapprove an application within ninety days from the date of receipt.<sup>29</sup>

Upon the approval of the application, the foreign applicant should file a written application for registration with SAIC within thirty days of the receipt of the certificate of approval and obtain a business license.<sup>30</sup> The foreign investor should propose the term of operations of the enterprise in the application. The term of operations is then subject to government approval. No minimum capital requirements are imposed. The amount of registered capital of the enterprise should correspond to its scale of operations and requirements.

#### *D. Branch Offices*

Under the new Company Law of China, a foreign company may establish branches in China and engage in production and operational activities.<sup>31</sup> A foreign company seeking to establish a branch office should submit the company's articles of association and a copy of the applicant's business license or certificate of incorporation issued in the applicant's country or place of origin.<sup>32</sup> Upon approval, the company must register with SAIC to obtain a business license. The foreign company must appoint a representative in charge of the branch and allocate operating funds to the branch. Branches of foreign companies in China do not have the status of Chinese legal persons; this means that the foreign company assumes civil liability for the operational activities of its branches in China.<sup>33</sup>

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28. *Implementation of Foreign Investment Law*, *supra* note 24, art. 11, ¶ 13-507, at 16,663.

29. *Id.* art. 12, ¶ 13-507, at 16,665.

30. *Id.* art. 13, ¶ 13-507, at 16,665.

31. Company Law of the People's Republic of China, Act of Dec. 29, 1993, art. 119, 2 CHINA L. FOR FOREIGN BUS. REG. (CCH) ¶ 13-518, at 16,787-89.

32. *Id.* art. 200, ¶ 13-518, at 16,831.

33. *Id.* art. 204, ¶ 13-518, at 16,833.

### *E. Representative Offices of Foreign Enterprises*

A representative office of a foreign enterprise refers to a resident representative office engaged in indirect business operations, marketing, promotion, equipment service, and business communication. A foreign enterprise must register with SAIC and its provincial and city branches. No initial capital requirement is required to establish a representative office.

A foreign company wishing to establish a representative office in China must first obtain appropriate sponsorship from a Chinese enterprise for the establishment of such an office. Normally, the sponsoring organization is the organization with jurisdiction over the company's business: (1) a trader, manufacturer or shipping agent should apply to MOFTEC; (2) a banking or insurance institution should apply to the People's Bank of China; (3) a maritime shipping operator or agent should apply to the Ministry of Communications; (4) an accounting enterprise should apply to the Ministry of Finance; and (5) an air transport enterprise should apply to the General Administration of Civil Aviation of China.<sup>34</sup> After sponsorship is obtained, the foreign enterprise must undergo formal registration procedures with the local bureau of SAIC.

To obtain approval, a foreign enterprise must submit the following documents, in both Chinese and English: (1) an application letter signed by the chairman of the board of directors or the general manager of the applicant company;<sup>35</sup> (2) a certified copy of the company's business registration/certificate of incorporation issued by the authorities of the country or region in which the company operates or is incorporated; (3) a letter of good credit standing issued by a banking institution that has business dealings with the company; and (4) letter(s) of appointment of the office representative(s) together with their credentials and brief biographies.<sup>36</sup>

After obtaining approval of its application to establish a resident representative office, a foreign enterprise must register with the local bureau of SAIC, autonomous region, or municipalities directly under the central government within thirty days of the date of approval.<sup>37</sup> After examining the required documents, the

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34. Interim Regulations of the State Council of the People's Republic of China Concerning the Control of Resident Representative Offices of Foreign Enterprises, Act of Oct. 30, 1980, art. 4, 1 CHINA L. FOR FOREIGN BUS. REG. (CCH) ¶ 7-500, at 9,051 [hereinafter *Interim Regulations*].

35. The content of the application letter should include the following: the name of the representative office, the name(s) of its designated representative(s), the scope of its activity, its duration, and its location.

36. *Interim Regulations*, *supra* note 34, art. 3, ¶ 7-500, at 9,051.

37. *Id.* art. 5, ¶ 7-500, at 9,053.

registration agency grants registration approval, collects a registration fee, and issues a registration certificate and a representative certificate.<sup>38</sup> The registration certificate is issued after the registration formalities are completed.<sup>39</sup> Therefore, registration with the local tax bureau is also required.

## II. TAXATION AND TAX INCENTIVES

Compared with western countries, China's tax system is relatively simple. Until China opened its door to foreign investors in 1978, it did not have any tax statute governing foreign operations. In 1980 and 1982, China enacted tax laws concerning equity joint ventures and wholly foreign-owned enterprises, respectively. In 1991, those statutes were replaced by the Income Tax Law of the People's Republic of China on Enterprises with Foreign Investment and Foreign Enterprises (the Foreign Enterprise Tax Law). Today, foreign investment enterprises are all subject to this statute.

In 1993, China extensively reformed its tax system for the purpose of setting up a modern tax system that conforms with the internationally recognized rules, and fits the needs of transforming China's planning economy into market economy. Although the reforms of the tax system involved China's domestic corporations, the reforms had some impact on foreign investors. Beginning in January, 1994, China implemented a new tax system. The new tax system repealed the Consolidated Industrial and Commercial Tax. Under the new tax system, both foreign companies and Chinese domestic enterprises are subject to three turnover taxes: value added tax, business tax, and consumption tax.

### A. Foreign Entities Subject to Income Tax

Under the Foreign Enterprises Tax Law, two types of foreign entities are obligated to pay income tax: enterprises with foreign investment and foreign enterprises.<sup>40</sup> Enterprises with foreign investment include Chinese-foreign equity joint ventures, Chinese-foreign contractual joint ventures, and wholly foreign-owned enterprises established in China. Foreign enterprises include: (1) foreign companies and other economic organizations which are established in China and engage in production or business operations; or (2) foreign companies and other economic organizations which have income from sources within China, but are not estab-

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38. *Id.*

39. *Id.*

40. Income Tax Law of the People's Republic of China for Enterprises with Foreign Investment and Foreign Enterprises, Act of Apr. 9, 1991, art. 2, 3 CHINA L. FOR FOREIGN BUS. REG. (CCH) ¶ 32-505, at 40,309 [hereinafter *Income Tax Law*].

lished in China.

An enterprise with foreign investment which establishes its head office in China pays income tax on income derived from sources inside and outside China. By contrast, a foreign enterprise pays income tax on income derived from sources within China.<sup>41</sup> Taxable income is income remaining in a tax year after deducting costs, expenses, and losses.<sup>42</sup> The tax year is usually the calendar year. However, a foreign enterprise may use its own fiscal year as the calendar year if it gets approval from the local tax authorities.<sup>43</sup> Enterprises with foreign investment and foreign enterprises that are organized in China to engage in production or business operations are subject to a tax at the rate of thirty percent plus a local income tax of three percent.<sup>44</sup> Furthermore, an enterprise with foreign investment that liquidates must pay income tax on the amount of its net assets that exceeds its paid-in capital after liquidation.<sup>45</sup> A foreign enterprise with no establishment in China which derives profits, interest, rent, royalties or other income pays an income tax of twenty percent.<sup>46</sup>

#### B. Tax on Associated Enterprises

An associated enterprise refers to an enterprise that has the following: (1) relationships with respect to existing direct or indirect ownership of matters such as finances, business operations, or purchases and sales; (2) direct or indirect ownership by a third party; or (3) any other relationship with respect to an association of reciprocal interests.<sup>47</sup> Under the Chinese tax laws, the payment or fees in business dealings between a company with foreign investment and its associated enterprises are treated as the payment or fees in business transactions between independent enterprises.<sup>48</sup> Foreign business entities have a duty to provide to the local tax authorities relevant materials, such as standard prices and charges in respect of business dealings with their associated enterprises.<sup>49</sup> If the prices of transactions between an enterprise and its associated enterprises are not based on independent business dealing, local tax authorities may make adjust-

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41. *Id.* art. 3, ¶ 32-505, at 40,309.

42. *Id.* art. 4, ¶ 32-505, at 40,309.

43. *Id.* art. 8, ¶ 32-505, at 40,311-13.

44. *Id.* art. 5, ¶ 32-505, at 40,309.

45. *Id.* art. 18, ¶ 32-505, at 40,315.

46. *Id.* art. 19, ¶ 32-505, at 40,335-37.

47. Detailed Rules for the Implementation of the Income Tax Law of the People's Republic of China for Foreign Investment Enterprises and Foreign Enterprises, Act of June 30, 1991, art. 52, 3 CHINA L. FOR FOREIGN BUS. REG. (CCH) ¶ 32-507, at 40,397-99 [hereinafter *Tax Law Implementation*].

48. *Income Tax Law*, *supra* note 40, art. 13, ¶ 32-505, at 40,313-15.

49. *Tax Law Implementation*, *supra* note 47, art. 53, ¶ 32-507, at 40,399.

ments.<sup>50</sup>

### C. Tax Incentives Offered to Foreign Investors

China offers preferential treatment to foreign investors to encourage investment in China. Foreign investment enterprises enjoy greater tax benefits if they are located in the special economic zones, coast open cities, or economic and technological development zones. This preferential tax treatment particularly encourages establishment of foreign investment enterprises with advanced technology and equipment.

China reduces the income tax rate to fifteen percent for foreign investment enterprises established in the special economic zones or economic and technological development zones.<sup>51</sup> China reduces the income tax rate to twenty-four percent for foreign investment enterprises located in coastal economic open zones, or in urban districts containing special economic zones, or economic and technological development zones.<sup>52</sup>

A foreign investment enterprise scheduled to operate for a period of ten years or more, which is engaged in manufacturing and production, is exempted from taxation for its first two profit making years, and is granted a fifty percent tax rate reduction for the following three years.<sup>53</sup> Any such enterprise engaged in agriculture, forestry, animal husbandry, or located in China's remote underdeveloped areas may be allowed a fifteen percent to thirty percent reduction in the amount of income tax payable for another ten years following the expiration of the period for tax exemption or reduction.<sup>54</sup> Provincial-level local governments may, at their discretion, determine exemption or reduction of local tax on foreign investment enterprises with advanced technology or equipment, or in an industry encouraged by China.<sup>55</sup>

Foreign investment enterprise may apply losses to the following tax year.<sup>56</sup> If the income of the following tax year would be insufficient to make up for the losses, the balance may be made up by its income of the further subsequent year, and may continue over a period of not more than five years.<sup>57</sup>

A foreign investment enterprise may reinvest the profits obtained from the enterprise or use the profits as capital investment to establish other enterprises to operate for a period of five

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50. *Id.* art. 54, ¶ 32-507, at 40,399.

51. *Income Tax Law*, *supra* note 40, art. 7, ¶ 32-505, at 40,311.

52. *Id.*

53. *Id.* art. 8, ¶ 32-505, at 40,311-13.

54. *Id.*

55. *Id.* art. 9, ¶ 32-505, at 40,313.

56. *Id.* art. 11, ¶ 32-505, at 40,313.

57. *Id.*

years or more. It may also be refunded forty percent of the income tax already paid.<sup>58</sup> The tax refund may be increased to 100% if the reinvestment pertains to an enterprise engaged in infrastructure or agricultural development projects in the Hainan Special Economic Zone.<sup>59</sup>

Foreign investors engaged in infrastructure-development projects in the Hainan Special Economic Zone and the Shanghai Pudong New Development Zone, and Chinese-foreign equity joint ventures engaged in port development in China with an operating period of fifteen years or longer, may be entitled to a five year tax exemption and a five year fifty percent tax rate reduction beginning in the enterprise's first profit-making year.<sup>60</sup> Profit remitted abroad by foreign investors is exempt from withholding tax.<sup>61</sup>

### III. THE RIGHT TO USE LAND AND THE RIGHT TO TRANSFER THE USE OF THE LAND

Since 1949, the state has firmly controlled the ownership of all of the land in China. No organizations or individuals were allowed to appropriate, buy, sell, transfer, or lease land. However, with the deepening of the economic reforms, China felt strong pressure from the business sectors to relax the rigid restriction on land use and transfer. In 1979, China enacted the Law on Chinese Foreign Equity Joint Venture. The law provided that:

[a] Chinese joint venturer's investment may include the right to the use of a site provided for the equity joint venture during the period of its operation. If the right to the use of the site is not taken as a part of the Chinese joint venturer's investment, the equity joint venture shall pay the Chinese Government for its use.<sup>62</sup>

For the first time, China allowed foreign funded enterprises to acquire the right to the use of the land for value. Thereafter, China's special economic zones and coast open cities respectively adopted local regulations on land use and management.<sup>63</sup>

On April 12, 1988, the National People's Congress of China

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58. *Id.* art. 10, ¶ 32-505, at 40,313.

59. ERNST & YOUNG, *DOING BUSINESS IN CHINA* 28 (1994).

60. *Id.* at 27.

61. *Id.* at 28.

62. *Joint Equity Enterprise Law*, *supra* note 8, art. 5, ¶ 6-500, at 7,803.

63. *Id.* For instance, Hainan Province promulgated the Measures on Land Use Management and the Regulations on the Right to the Use of the Land and Assignment of the Right to the Use of the Land for Value, which constituted the first local land use for value system. Article 4 of the Measures on Land Use Management stipulates: "The system of land use for compensation is hereby instituted. The right to the use of the land may be assigned, transferred and mortgaged. Foreign and Hong Kong, Macao, Taiwan companies, enterprises or individuals are allowed to participate in land development, management or contract for land use."

amended Article 10 of the Constitution.<sup>64</sup> Although the amended Constitution still prohibits any organization or individual from appropriating, buying, selling, or engaging in the transfer of land by unlawful means, it permits the transfer of the use of land. Thereafter, China adopted the Interim Regulations Concerning the Assignment and Transfer of the Right to the Use of the State-Owned Land in the Urban Areas (Interim Urban Land Use Regulations), and the Interim Measures for the Administration of the Foreign-Invested Development and Management of Tracts of Land (Interim Measures of Tracts of Land) on May 19, 1990.

Accordingly, China has separated the right to own land, which may be exercised only by the State, from the right to use the land, which may be assigned and transferred.<sup>65</sup> China also distinguishes between the right to use land, which requires the land user to pay certain compensation, and the allocated right to use the land, which does not require the land user to pay compensation.<sup>66</sup> The allocated right to use the land may not be transferred, leased, or mortgaged.<sup>67</sup>

#### A. Three Ways to Acquire the Right to the Use of the Land

A foreign investor interested in acquiring the right to the use of the land may achieve the goal through one of the three methods: (1) assignment; (2) transfer; and (3) lease.

##### 1. Assignment

The state, as the sole owner of the land, assigns the right to use the land for a fee.<sup>68</sup> This is the first level where land use is treated as a kind of market commodity; thus, it is called the "first level real property market."<sup>69</sup> The assignment may be carried out by reaching an agreement, by invitation to bid, or by auction.<sup>70</sup> The term of the assignment is limited to a maximum of seventy years for residential uses; fifty years for industrial uses, educa-

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64. Article 10 of the Constitution of the People's Republic of China, as amended, reads as: "No organization or individual may appropriate, buy, sell or other wise engage in the transfer of land by unlawful means. The right to the use of land may be transferred according to law." XIANFA art. 10 (1988).

65. Provisional Regulations of the People's Republic of China Concerning the Grant and Assignment of the Right to Use State Land in Urban Areas, Act of May 24, 1990, art. 2, 2 CHINA L. FOR FOREIGN BUS. REG. (CCH) ¶ 14-716, at 18,647 [hereinafter *Urban Land Use Regulations*].

66. *Id.* art. 43, ¶ 14-716, at 18,659.

67. *Id.* art. 44, ¶ 14-716, at 18,659.

68. *Id.* art. 8, ¶ 14-716, at 18,649.

69. CAO JIANMING ET AL., SHE WAI JING JI FA LU HE ZHENG CHE, FOREIGN ECONOMIC LAW AND POLICIES 146 (Shanghai Ke Xie Pu Ji Pub. House 1993).

70. *Urban Land Use Regulations*, *supra* note 65, art. 13, ¶ 14-716, at 18,651.



tional, scientific, cultural, public health uses; and forty years for commercial, tourist and recreational uses.<sup>71</sup>

After a land user pays the fee for the assignment, he or she should register and obtain the certificate for land use.<sup>72</sup> Within sixty days of the signing of the contract, the land user must pay the total amount of the assignment fee. If the land user fails to pay the assignment fee, the assigning party may terminate the contract and claim compensation for breach of contract.<sup>73</sup>

## 2. *Transfer*

Transfer means that the land user reassigns the right to the use of the land, including its sale, exchange, and donation.<sup>74</sup> In China, this is called the "second level real property market."<sup>75</sup> The land user and the transferee are required to sign a transfer contract.<sup>76</sup> The rights and duties specified in the contract for assigning the right to the use of the land shall be transferred.<sup>77</sup> The ownership of the above-ground buildings and other attached objects shall also be transferred.<sup>78</sup>

## 3. *Lease*

A foreign investor may acquire the right to the use of the land by entering into a lease with the lessor. The lessor may lease the right to the use of the land, together with the above-ground buildings and other attached objects, to the lessee.<sup>79</sup> The lessor and the lessee are required to sign a lease contract.<sup>80</sup> The lessee is obligated to perform the contract for assigning the right to the use of the land.

### *B. Mortgage of the Right to the Use of the Land*

For the first time, Chinese law permits mortgage of the land use right. The new regulations have features similar to the western mortgage system. Above-ground buildings and other attached objects can be mortgaged.<sup>81</sup> If the mortgagor cannot fulfill its liabilities or declares dissolution, the mortgagee may dispose of

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71. *Id.* art. 12, ¶ 14-716, at 18,651.

72. *Id.* art. 16, ¶ 14-716, at 18,651.

73. *Id.* art. 14, ¶ 14-716, at 18,651.

74. *Id.* art. 19, ¶ 14-716, at 18,653.

75. JIANMING ET AL., *supra* note 69, at 146.

76. *Urban Land Use Regulations*, *supra* note 65, art. 20, ¶ 14-716, at 18,653.

77. *Id.* art. 21, ¶ 14-716, at 18,653.

78. *Id.* art. 23, ¶ 14-716, at 18,653.

79. *Id.* art. 28, ¶ 14-716, at 18,655.

80. *Id.* art. 29, ¶ 14-716, at 18,655.

81. *Id.* art. 33, ¶ 14-716, at 18,657.

the mortgaged property in accordance with the laws.<sup>82</sup> The mortgagee has priority over other creditors to the proceeds of the sale of the property.<sup>83</sup>

### *C. Obtaining the Right to the Use of the Land by a Joint Venture*

If a Chinese-foreign joint venture needs land for project development, it has to obtain the right to the use of the land. It should submit an application to the land administration departments and the housing administration departments under the local governments at the municipal and county levels. Upon the approval of the application, the joint venture will sign a contract and then acquire the right to the use of the land. The contract shall list the size and location, the purpose, the term, the land use fee, the rights and duties of the two parties, and the penalties for contract violation. If a Chinese partner to the joint venture has acquired the right to the use of the targeted land, the joint venture may provide it as part or all of its capital contributions to the joint venture.

### *D. Foreign Investor's Development of Tracts of Land*

In order to stimulate the construction of public works, improve the environment for investment, and introduce foreign-invested technically advanced enterprises and export-oriented enterprises, China encourages foreign investment for the development and management of tracts of land. "Tract development" refers to development which occurs after the foreign investors acquire the right to the use of the land. At this point, foreign investors should implement comprehensive development and construction on the land. This includes levelling the ground and constructing such public works as water supply and drainage systems, power and heat supply systems, roads and communications networks, and communications facilities.<sup>84</sup>

A foreign company intending to invest in tract development should set up development enterprises in the forms of equity joint ventures, contractual joint ventures, or foreign capital enterprises. Then, the development enterprises must acquire the right to the use of the land from the local governments.<sup>85</sup> However, the state continues to own the resources and objects buried under the assigned land. The development enterprises are required to draft a

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82. *Id.* art. 36, ¶ 14-716, at 18,657.

83. *Id.* art. 37, ¶ 14-716, at 18,657.

84. Provisional Administrative Measures Governing Commercial Land Development and Management by Foreign Investors, Act of May 19, 1990, art. 2, 2 CHINA L. FOR FOREIGN BUS. REG. (CCH) ¶ 14-723, at 18,735.

85. *Id.* art. 5, ¶ 14-723, at 18,737.

tract development plan which specifies the overall targets and respective targets for different stages. The enterprises must then submit the draft plan to the provincial level government for examination and approval.<sup>86</sup> The development enterprises are permitted to transfer the right to the use of the land only after they have completed the tract development plans and have satisfied all the conditions in the contract.<sup>87</sup> The development enterprises may call on investors to make investment in the development areas, accept the transferred right to the use of the land, and set up enterprises.<sup>88</sup>

#### IV. ADMINISTRATION OF FOREIGN EXCHANGE AND LOANS

Since 1980, China has adopted a series of statutes and regulations on foreign exchange control. In December 1980, the State Council promulgated the Interim Regulations on Foreign Exchange Control of the People's Republic of China, (Rules on Foreign Exchange Control), effective on March 1, 1981. In order to implement this statute, the State General Administration of Exchange Control (SGAEC) formulated specific rules, such as the Rules for the Implementation of Foreign Exchange Control Relating to Individuals (1981); Rules for the Implementation of the Examination and Approval of Applications by Individuals for Foreign Exchange (1981); Rules for the Implementation of Foreign Exchange Control Regulations Relating to Enterprises with Overseas Chinese Capital, Foreign-Capital Enterprises and Chinese-Foreign Equity Joint Ventures (1983); and Implementing Rules on Punishment of Violation of Foreign Exchange Control (1985). In January of 1986, China further promulgated the Provisions of the State Council Concerning the Issue of Balance of Income and Expenditure in Foreign Exchange of Chinese-Foreign Equity Joint Ventures (Provisions on Balance of Income and Expenditure of Equity Joint Ventures). In April of 1987, the Bank of China promulgated the Measures Concerning the Granting of Loans to Enterprises with Foreign Investment (Measures Concerning the Granting of Loans). These statutes and regulations constitute the initial legal structure in foreign exchange control.

##### *A. Foreign Exchange Control Relating to Foreign Investors*

Foreign exchange refers to foreign currencies, securities in foreign currencies, instruments payable in foreign currency, and other foreign exchange funds.<sup>89</sup> All foreign exchange receipts of

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86. *Id.* art. 7, ¶ 14-723, at 18,739.

87. *Id.* art. 9, ¶ 14-723, at 18,739.

88. *Id.* art. 10, ¶ 14-723, at 18,739.

89. Provisional Regulations for Foreign Exchange Control of the People's Re-

foreign-capital enterprises and Chinese-foreign equity joint ventures must be deposited with the Bank of China and disbursed from the deposit accounts.<sup>90</sup> Without the approval of SAEGC, foreign-capital enterprises and equity joint ventures must use Renminbi, the Chinese currency, in the settlements of accounts between them and other enterprises or individuals.<sup>91</sup> Foreign-capital enterprises and foreign joint venturers may apply to the Bank of China for remitting abroad their profits or other legitimate earnings. However, they should first apply to SAEGC or its branch offices for the transfer.<sup>92</sup>

*B. Balance of Income and Expenditure of Equity Joint Ventures*

China has created channels for Chinese-foreign equity joint ventures to achieve the balance of income and expenditure in foreign exchange. The equity joint ventures are encouraged to increase export of products and generate more foreign exchange.<sup>93</sup> If there is a need to regulate income and expenditure in foreign exchange of the equity joint ventures, the authorities at different levels may administer and affect such regulation.<sup>94</sup> Advanced technology products, key technology, or China's urgently needed products provided by foreign joint venturers may be granted preferential treatment by the Chinese authorities by placing them on China's domestic market.<sup>95</sup> The equity joint venture contract should specify such products. Moreover, if foreign joint venturers fail to achieve a balance in foreign exchange, they may, upon the approval of the Chinese authorities, reinvest the share of profit in Renminbi in Chinese enterprises that are capable of bringing in foreign exchange earnings.<sup>96</sup> In addition, they are refunded any income tax paid, and they may obtain foreign exchange from the newly increased foreign exchange revenues of the enterprises.<sup>97</sup>

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public of China, Act of Dec. 18, 1980, art. 2, 1 CHINA L. FOR FOREIGN BUS. REG. (CCH) ¶ 8-550, at 10,353.

90. *Id.* art. 22, ¶ 8-550, at 10,363.

91. *Id.* art. 24, ¶ 8-550, at 10,365.

92. *Id.*

93. Regulations of the State Council Concerning the Balance of Foreign Exchange Income and Expenditure by Sino-Foreign Joint Equity Ventures, Act of Jan. 15, 1986, art. 2, 1 CHINA L. FOR FOREIGN BUS. REG. (CCH) ¶ 6-590, at 8,031.

94. *Id.* art. 3, ¶ 6-590, at 8,031.

95. *Id.* arts. 4-5, ¶ 6-590, at 8,031-33.

96. *Id.* art. 10, ¶ 6-590, at 8,035.

97. *Id.*

### *C. Granting of Loans to Foreign Investors*

To support the business development of enterprises with foreign investment, the Bank of China may grant loans to enterprises with foreign investment, giving priority to export oriented and advanced technology enterprises.<sup>98</sup> Foreign investment enterprises must meet the following requirements: they must have obtained a business license; they must have fully paid the registered capital; the board of directors must have made the decision on the borrowing; the planning department must have approved the program of investment; and the applying enterprise must have the ability to repay the loan.<sup>99</sup> The Bank of China may grant fixed asset loans, working capital loans, loans on spot exchange mortgage, and stand-by loans.<sup>100</sup> Applying enterprises should submit an application to the Bank of China; upon approval, the lender and the borrower sign a loan contract.<sup>101</sup> The Bank of China may require applying enterprises to submit a credit guarantee or mortgage guarantee for the repayment of the principal and interest of the loan.<sup>102</sup> The enterprises must use the loans in accordance with the terms of the loan contract.<sup>103</sup>

### V. DISPUTES SETTLEMENT

With the advent of foreign investors pouring into China, disputes involving foreign investment have increased. Disputes generally arise out of the interpretation and enforcement of economic contracts between Chinese enterprises and foreign investors. The Law of the People's Republic of China on Economic Contracts Involving Foreign Interest (Foreign Economic Contract Law) defines foreign economic contracts as those concluded between enterprises or other economic organizations of China and foreign enterprises, other economic organizations, or individuals.<sup>104</sup> Disputes involving foreign investment may be settled by the arbitration institutions or the people's courts.

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98. Measures of the Bank of China on Loans for Foreign Investment Enterprises, Act of Apr. 24, 1987, art. 1, 1 CHINA L. FOR FOREIGN BUS. REG. (CCH) ¶ 8-702, at 10,809.

99. *Id.* art. 7, ¶ 8-702, at 10,811.

100. *Id.* art. 5, ¶ 8-702, at 10,809-11.

101. *Id.* art. 13, ¶ 8-702, at 10,813.

102. *Id.* arts. 15-16, ¶ 8-702, at 10,813-15.

103. *Id.* art. 14, ¶ 8-702, at 10,813.

104. Foreign Economic Contract Law of the People's Republic of China, Act of Mar. 21, 1985, art. 2, 1 CHINA L. FOR FOREIGN BUS. REG. (CCH) ¶ 5-550, at 6,621.

### A. Arbitration of Foreign Related Matters

China's new Civil Procedure Law<sup>105</sup> contains a special section specifying the legal status of arbitration foreign business persons. In disputes arising from foreign economic or trade activities in China, if the parties have adopted an arbitration clause in the contract, they may not bring an action in court.<sup>106</sup> This section confirms the legal status of the arbitration clause in foreign economic contracts and agreements and excludes the jurisdiction of the courts in such disputes. Moreover, in cases where a Chinese arbitral organ has made an award, the parties may not bring an action in a court in China.<sup>107</sup> However, if the losing party to an arbitration furnishes proof that the parties have not made an arbitration clause in the contract, or the award was made not through proper arbitration proceedings, or the enforcement of the award shall harm the social and public interest of the country, the court may make a written order to prohibit the enforcement of the award.<sup>108</sup>

China now has two arbitral organs: the Foreign Trade Arbitration Commission within the China Council for the Promotion of International Trade<sup>109</sup> and the Maritime Arbitration Commission within the China Council for the Promotion of International Trade.<sup>110</sup> The Foreign Trade Arbitration Commission was renamed as the China International Economic and Trade Arbitration Commission (The Arbitration Commission)<sup>111</sup> while the Maritime Arbitration Commission was renamed as the China Maritime Arbitration Commission (The Maritime Arbitration Commission) in 1988.<sup>112</sup> The Arbitration Commission hears dis-

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105. China adopted the Civil Procedure Law (For Trial Implementation) in March 1982. This statute was repealed and replaced by the new Civil Procedure Law on April 9, 1991 at the Fourth Session of the Seventh National People's Congress.

106. Civil Procedure Code of the People's Republic of China, Act of Apr. 9, 1991, art. 257, 3 CHINA L. FOR FOREIGN BUS. REG. (CCH) ¶ 19-201, at 24,001-03 [hereinafter *Civil Procedure Code*].

107. *Id.* art. 259, ¶ 19-201, at 24,003.

108. *Id.* art. 260, ¶ 19-201, at 24,003.

109. Provisional Rules of Procedure of the Foreign Trade Arbitration Commission of the China Council for the Promotion of International Trade, Act of Mar. 21, 1956, art. 2, 2 CHINA L. FOR FOREIGN BUS. REG. (CCH) ¶ 10-500, at 12,801.

110. Provisional Rules of Procedure of the Maritime Arbitration Commission of the China Council for the Promotion of International Trade, Act of Jan. 8, 1959, art. 1, 2 CHINA L. FOR FOREIGN BUS. REG. (CCH) ¶ 10-540, at 12, 863.

111. *The State Council's Official Reply Concerning the Renaming of the Foreign Economic and Trade Arbitration Commission as the China International Economic and Trade Arbitration Commission and the Amendment of its Arbitration Rules*, June 21, 1988, available in WESTLAW, Chinalaw Database, File No. 481.

112. *The State Council's Official Reply Concerning the Renaming of the Maritime*

putes arising from international economic and trade transactions in accordance with arbitration agreements. This includes disputes in finance and loans involving equity joint ventures, and contractual joint venture and foreign capital enterprises. The Maritime Arbitration Commission hears disputes involving remuneration for: (1) salvage services; (2) collisions; (3) chartering, agency, towage, raising, sale, repairing and building of sea-going vessels; and (4) pollution damages to marine environment.<sup>113</sup>

Disputes involving economic contracts are governed by the China International Economic and Trade Arbitration Commission Arbitration Rules (The Arbitration Commission Rules). The Arbitration Commission is composed of a chairman, a vice-chairman, and commission members.<sup>114</sup> A claimant must submit his written application for arbitration to the Arbitration Commission specifying the claim, facts, and evidence. The claimant should appoint an arbitrator from among the panel of arbitrators.<sup>115</sup> Then, the Arbitration Commission immediately mails a copy of the application to the respondent. The respondent should appoint an arbitrator within twenty days and file his defense and evidence within forty-five days.<sup>116</sup>

The Chairman of the Arbitration Commission appoints a third arbitrator as the presiding arbitrator to form an arbitration tribunal to hear the case.<sup>117</sup> Alternatively, a sole arbitrator may form the arbitration tribunal.<sup>118</sup> The arbitration tribunal may hold oral hearings for the case. The tribunal generally does not hear cases in open sessions.<sup>119</sup> However, at the request of the disputing parties, the tribunal may examine the case and make an award on document evidence only.<sup>120</sup> The arbitration tribunal should make an award within forty-five days after the closing of the examination and hearing.<sup>121</sup> The arbitral award is final; no party may appeal to a court.<sup>122</sup> If one party fails to execute the award, the other party may apply to the Chinese court for enforcement of the award, or apply to the foreign court which has juris-

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*Arbitration Commission as the China Maritime Arbitration Commission and the Amendment of its Arbitration Rules*, June 21, 1988, available in WESTLAW, Chinalaw Database, File No. 480.

113. *Arbitration Rules of the China Maritime Arbitration Commission*, Sept. 12, 1988, art. 2, available in WESTLAW, Chinalaw Database, File No. 482.

114. *Id.* art. 3.

115. *Id.* art. 6.

116. *Id.* art. 8.

117. *Id.* art. 14.

118. *Id.* art. 15.

119. *Id.* art. 25.

120. *Id.* art. 22.

121. *Id.* art. 32.

122. *Id.* art. 36.

diction for enforcing the award under the 1958 Convention on the Recognition and Enforcement of Foreign Arbitral Awards (New York Convention).<sup>123</sup>

In June of 1989, the Hong Kong Supreme Court ordered enforcement of an arbitration award made by the Arbitration Commission tribunal in favor of a Chinese trade company against a Hong Kong business corporation.<sup>124</sup> This was the first time that an arbitration award of the Chinese arbitral tribunal was enforced by a foreign court since China joined the New York Convention.<sup>125</sup> Since then, more foreign courts have recognized and enforced the Chinese arbitration awards.

### *B. Foreign-Related Matters in Courts*

China's 1979 Organic Law of the People's Courts created the current structure of the court system.<sup>126</sup> China now has four tiers of courts: the Regional Court, the Intermediate Courts, the High Courts, and the Supreme People's Court. In addition, there are specialty courts handling maritime, military, railroad, traffic, and forestry matters. Intermediate courts have original and appellate jurisdiction over civil, criminal, economic, and administrative matters. Most litigation involving foreign-related matters is brought in the intermediate courts.<sup>127</sup>

The Chinese courts exercise jurisdiction over the following foreign-related cases: (1) contract disputes over property rights brought against non-resident defendants if the contract is signed or performed in China, or if the defendant has its representative office in China, or the object of the action is located in China; (2) disputing parties, through a written agreement, choosing the proper Chinese court; and (3) disputes arising from the performance of contracts for equity joint ventures, or contractual joint ventures, or cooperative exploration and development of natural resources in China.<sup>128</sup> The Chinese courts also have jurisdiction over foreign-related lawsuits in real estate where the estate is located in China, or in harbor operations where the harbor is located in China, or in succession where the decedent's domicile and

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123. *Id.* art. 38. China became a member state of the New York Convention on April 22, 1987.

124. WANG CHANGYIN, *ZHONG GUO GUO JI SHI FA LI LUN YU SHI JIAN, THE CHINESE THEORY AND PRACTICE OF INTERNATIONAL PRIVATE LAW* 452 (People's Court Pub. House 1993).

125. *Id.*

126. RALPH H. FOLSOM ET AL., *LAW AND POLITICS IN THE PEOPLE'S REPUBLIC OF CHINA* 124 (West Pub. Co. 1992).

127. *Id.* at 126.

128. *Civil Procedure Code*, *supra* note 106, art. 25, ¶ 19-201, at 23,903.



the principal part of estate is located in China.<sup>129</sup>

### CONCLUSION

In conclusion, China's economic reforms and legal system have dramatically improved. The country has enacted a large number of laws and gradually filled in the details. Investors are more comfortable now that they can rely on Chinese law and economic infrastructure for protection. The Chinese government has realized the advantages of establishing a more sophisticated legal system in order to attract foreign investment. The central and local governments have promulgated statutes to provide extensive preferential treatment and tax incentives, and have gradually eliminated tariff barriers in some areas. China has set up special economic zones, economic development zones, high-tech industrial development zones, and coastal open cities. It has also created securities and futures markets to encourage foreign investment.

However, Chinese economic changes have moved more rapidly than the legal system, and problems still exist in the legal environment. Foreign investors often complain about the enforceability and implementation of the laws. Some government officials still regard themselves as standing above the law. China's sophisticated "Guanxiwang" (personal relationship network) also hinders the effective implementation of laws. A few Chinese partners to joint ventures are ignorant of laws and have triggered disputes in enterprise operations and management.<sup>130</sup> Nevertheless, investors should be encouraged by the positive trends in China as it progresses toward a market economy and more accessible markets ruled by the law.

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129. *Id.* art. 34, ¶ 19-201, at 23,905.

130. For instance, in 1986, a local government agency decided to remove the general manager and the vice-general manager of a Chinese-U.S. joint venture without any board meeting. The American partner indicated that they could not accept the removal decision. Only after the central government agency and the provincial government intervened, the local government agency repealed its removal decision. Such interference of management of a joint venture violated the Chinese laws on joint ventures. ZHANG PEITIAN ET AL., JIE JUE SHE WAI JING JI MIN SHI JIU FENG FA LU ZHI NAN, LEGAL GUIDEBOOK OF RESOLVING FOREIGN ECONOMIC CIVIL DISPUTES 169-70 (Chinese Univ. of Pol. & L. Pub. House 1993).