

PEOPLE'S REPUBLIC OF CHINA—1983 JOINT VENTURE
IMPLEMENTING REGULATIONS—THE SUPPLEMENT OF DETAIL,
IN AN ATTEMPT TO ATTRACT FOREIGN INVESTMENT*

The People's Republic of China's (PRC) revitalization of international relations in 1976 led to many changes in Chinese law, including the issuance of the 1979 Joint Venture Law.¹ The purpose of the 1979 Joint Venture Law was first to facilitate a level of industrial development in China on par with the industrial world,²

*Although the 1983 Joint Venture Implementing Regulations are not that recent of a development, the *Journal* recognizes the value of publishing substantial portions the telegrams quoted and cited throughout the piece.

¹ Law of the People's Republic of China on Joint Ventures Using Chinese and Foreign Investment, July 8, 1979, unofficial translation printed in 125 CONG. REC. 7793 (1979), reprinted in 18 *I.L.M.* 1041 (1979) [hereinafter cited as Joint Venture Law]. Interaction between East and West through this 1979 law is especially important because joint ventures are one of the most integrated forms of international cooperation. "The joint venture not only places responsibility upon each of the investing parties but also provides the means to bridge a vast cultural and economic gulf between societies." Klingenberg & Pattison, *Joint Ventures in the People's Republic of China: The New Legal Environment*, 19 VA. J. INT'L L. 807, 814 (1979). Certain features are common to all joint ventures: pooled assets, shared profits, shared losses, and joint management. *Id.* In a Chinese joint venture the foreign investor must invest at least 25% of the original joint venture investment and afford limited liability to investors. Ultimate control of the joint venture will apparently rest in the hands of the Chinese government, an arrangement that is not the standard international practice but is common in China. Finally, a transfer of interest in the enterprise requires unanimous consent by the parties. Bosco, *The Law of the People's Republic of China on Joint Ventures Using Chinese and Foreign Investment*, 6 BROOKLYN J. INT'L L. 217, 223 (1980). The 1979 Joint Venture Law provided a broad framework, but since its enactment both Chinese and foreign investors have sought a more formal system for negotiating and enforcing joint venture contracts. Note, *Joint Ventures in the People's Republic of China*, 14 J. INT'L L. & ECON. 133, 144-45 (1979). This desire for more formalities in negotiations stems from the lack of detail in the 1979 Joint Venture Law, a flaw that caused delays in assessing and processing foreign investment. The 1983 Implementing Regulations should remedy that defect. See INT'L. TRADE AD., U.S. DEPT. OF COMMERCE, *Joint Venture Agreement in the People's Republic of China*, app. A, art. 1 (1982) [hereinafter cited as Trade Report].

Since the "Four Modernizations Movement" in 1980, the PRC has emphasized reform, coordination, and promotion of new technology to achieve balanced economic growth. A. HO, *DEVELOPING THE ECONOMY OF THE PEOPLE'S REPUBLIC OF CHINA* 63-65 (1982). Ideally, joint venture participants will primarily be in the technology field. Trade Report, *supra* at app. A.

² For a general review of Chinese law and business, see Note, *An Analysis of Chinese Contractual Policy and Practice*, 27 WAYNE L. REV. 1229 (1981). The People's Republic of China (PRC) believes that the most practical approach to modernization is by acquiring technology directly from the western industrial states. *Id.* at 1229-30.

The terms "industrial world," "industrial nation," and "Western" refer to ideological ten-

and second, to remedy China's foreign currency imbalance.³ Foreign investors received the 1979 Joint Venture Law with great expectations, but because of significant ambiguities and restraints on foreign investment, enthusiasm waned and the expected investment failed to materialize.⁴ The Chinese response to this lack of investment came on September 26, 1983, when the Chinese Ministry of Foreign Economic Relations on Trade (MOFERT) released Regulations for the Implementation of the Law of the People's Re-

dencies rather than strict geographical location. Generally, they are used in reference to "capitalist" economies such as those in Japan, the European Economic Community, and the United States.

The movement toward greater industrial development was a portion of the "Four Modernizations" campaign, in which the PRC emphasized economic modernization of industry, agriculture, defense and science and technology. See *New Economic Laws and Regulations*, BEIJING REV., Nov. 23, 1981, at 6. *Supra* note 2, at 1229.

³ China has an excellent payment record and has followed accepted international payment practices, but if its trade activity expands as it hopes, China will need increasing foreign currency reserves to maintain steady growth. Shaney, *Selected Legal Aspects of China's Conduct of Foreign Trade*, 11 INT'L LAW. 641, 650-52 (1977).

From the perspective of the PRC, the purpose of the 1979 Joint Venture Law was fourfold: (1) to attract advanced foreign capital and equipment needed in the PRC's modernization plan, (2) to begin balancing imports and exports, (3) to save PRC capital for its own investments, and (4) to provide training needed for management skills. Note, *China's New Joint Venture Law: Analysis and Economic Overview*, 4 B.C. INT'L COMP. L.J. 115, 127 (1981).

⁴ Since China relaxed its restrictions against foreign intercourse in 1976, trade has increased dramatically. The past few years have witnessed substantial expansion, especially in the area of Chinese purchases of foreign made goods. Klingenberg & Pattison, *supra* note 1, at 811. Due to the ambiguity that surrounds the law, however, the "utilization of joint ventures in the economy has been conspicuously absent." *Id.* Not only has it been absent, but also joint venture activity actually has been decreasing. For example, in 1980, 20 joint ventures were approved, representing a market value of investments of \$177 million. In 1981, the total number of approved joint ventures dropped to 19, but the market value of investments plummeted to \$20 million. See Trade Report, *supra* note 1, at 3; see also Dept. of Commerce, Incoming Telegram 1 (Sept. 8, 1983) [hereinafter cited as Incoming Telegram/Implementing Regulations].

Perhaps the details regarding joint ventures were omitted deliberately. The Chinese may have intended that the detailed terms of the agreements "be spelled out by the parties in their contract association." See Trade Report, *supra* note 1, at 12. The Chinese may have assumed the eventual existence of a Chinese civil commercial code, as well as patent, banking, insurance, and other legislation, and believed it preferable to have separate detailed laws in these areas instead of burdening the Joint Venture Law with such details. *Id.* One other alternative is that the Chinese merely omitted the details of operation to maintain a firm grip over joint venture activities. Finally, it may be that since this style of law and business structure was so new to the Chinese drafters that they simply did not know what details to include.

The lack of detail may also simply be due to strict central government control. If the communist government proposes one economic state plan, alternatives in reaching it are limited. Since there may be only one way to reach such a goal, there is no danger of departing from that one established procedure, and, therefore, there is no need for details.

public of China on Joint Ventures Using Chinese and Foreign Investment.⁵ The two objectives of the Implementing Regulations are to clarify the nebulous characteristics of the 1979 Joint Venture Law⁶ and to stimulate foreign investment by providing new legal materials.⁷ In light of the purposes behind these new regulations,

⁵ Regulations for the Implementation of the Law of the People's Republic of China on Joint Ventures Using Chinese and Foreign Investment, Sept. 20, 1983, official translation printed in BEIJING REV., Oct. 10, 1983, supplement [hereinafter cited as Implementing Regulations]. According to Chinese figures, 188 joint ventures between foreign companies and Chinese enterprises were operating in China at the end of 1983, attracting \$348 million of foreign investment. Dept. of Commerce, Incoming Telegram, Subject: Japanese Investment in China 1 (Aug. 1984) [hereinafter cited as Incoming Telegram/Japan].

Generally, the Japanese and Chinese are heavy trade associates. The type of investment in China attracting the most attention and concern in Japan is the equity joint venture. Yet surprisingly, Japan has captured only a small part of this market by participating in only 14 of the 188 joint ventures that were operating by the end of 1983, according to Chinese figures. (The Japanese count only nine ventures; the discrepancy arises because the Chinese total includes Japanese companies operating through Hong Kong subsidiaries). This level of Japanese activity lags behind both Hong Kong, which leads the field by far, and the United States, which had 21 joint ventures by the Chinese count. The American edge is even more significant in dollar amount since Japanese joint ventures tend to be smaller operations than United States enterprises. Incoming Telegram/Japan at 1.

⁶ The Implementing Regulations were designed to "flesh out" the Joint Venture Law of 1979 and to address many of the more complex problems facing joint ventures under the 1979 Joint Venture Law. Incoming Telegram/Implementing Regulations, *supra* note 4, at 1.

⁷ The Implementing Regulations provided needed clarity in an area where confusion had reigned and should, therefore, represent a significant step in encouraging foreign investment in China. *Id.*; BEIJING REV., Nov. 9, 1981 at 6.

The PRC provides many measures to encourage investment. For a list of current economic legislation dealing with promotion of investment, see Pattison, *China's Developing Legal Framework for Foreign Investment: Experience and Expectations*, 13 LAW & POL'Y. INT'L. BUS. 89, 93-95 (1981). Yet, even with new Implementing Regulations or trade laws, the ability of the Chinese to promote investment will depend on the degree to which the government acknowledges the law and fulfills the purpose of the joint venture. The Chinese government must enforce these new details of joint ventures in a manner that will truly encourage investment. A careful observer of China's current political sphere will notice that even though written laws are in force, mass executions, arrests without charges, and a lack of due process all continue to occur. From these actions, though not of a commercial nature, one may infer that the Chinese government will ignore written laws when the laws are not in its best interest. Address by Dr. Thomas W. Ganschow, "Introduction to the Law and the Politics of the People's Republic of China," Meeting of the International Law Society of the University of Georgia, Athens, Georgia (April 16, 1982) [hereinafter cited as Ganschow Address]. Also, even if the Chinese do make a sincere attempt to adhere to and administer their written law, they lack the skilled people to do so. With a country of over one billion people, and only 2,000 lawyers, the vast majority of the nation will continue to practice law as it always has, through interpersonal communication. *Id.* Although the Chinese are researching western law, it will still be some time before the legal community, or at least the commercial legal force, will be ready for a strong international practice. See also *supra* notes 2, 5 and accompanying text. In the optimism following the fall of the Gang-of-Four in 1976, China set ambitious economic growth targets, initiated reforms to restructure the country's economic system, and decentralized decision making. Trade Report, *supra* note 1, at 1. This

this Recent Development discusses several important aspects of the new Implementing Regulations, including the clarifying function and the Implementing Regulations' new administrative procedures, tax regulations, labor relations, and access to the Chinese home market as examples of incentive measures.

Generally, any union of business will have debatable issues. In fact, the vagueness of the 1979 Joint Venture Law, combined with the traditional Chinese approach to law and the Chinese lack of experience in the international business arena, may make a joint venture with China particularly susceptible to discord.⁸ Historically, experience has taught the Chinese to be wary of codified laws.⁹ As early as 220 B.C. China had extremist, legalistic leaders

optimism inspired an active pursuit for Chinese-Western trade relations. For a history of the evolution from Chairman Mao policies to the 1976 optimism which culminated in 1979 with the Joint Venture Law, see Bosco, *supra* note 1, at 217-22; *see also* Pattison, *supra* note 7, at 91-92.

⁸ *See* Trade Report, *supra* note 1, at 7-10 for a discussion of the motivating factors and expectations of capitalist and socialist parties to a joint venture. Any potential investor in China must recognize some of the challenges of direct investment in China, usually in the area of capital structure, management, contributions, pricing, profit distribution, or repatriation. Klingenberg & Pattison, *supra* note 1, at 839. For a general overview of expectations in the areas of taxation, exchange rates, dispute resolution, and copy and patent rights, see Note, *supra* note 3, at 128.

In addition to business complications arising out of any capitalist/socialist business union, China is prone to difficulties because of its expectations of non-contracted obligations, limitations on government authority, lack of accountability, and the differing professional standards and social and economic values. *See generally* Dept. of Commerce, Incoming Telegram, Subject: After the Contract is Signed: The Experience of U.S. Companies in Shanghai, International Trade Administration: China Office (Aug. 1984) [hereinafter cited as Incoming Telegram/After the Contract].

This eagerly awaited code was a disappointment to those seeking a "how to do business with China" handbook. Bosco, *supra* note 1, at 221. Such fundamental concerns as taxation, maximum percentage of foreign ownership, profit margins, and types of investment being sought were left undefined with the result that the ad hoc negotiation process continued. *Id.* The only credit given the 1979 Joint Venture Law was that it was a "sweeping statement" that at least provided a very broad framework. Note, *supra* note 1, at 145.

Although the 1979 Joint Venture Law was published quickly, it may have purposefully been limited to general terms. Through this technique, the Chinese could capitalize on any investment already in existence and at a later date determine the operational details that they would require of future joint ventures. Note, *supra* note 1, at 144, 148; *see also* Sabin, *Negotiation is the Key to Success*, Boston Sunday Globe, Oct. 28, 1979, § A, at 1, col. 1 (discussion of process of creating legal details through negotiation).

⁹ Carl, *Contemporary Law in the People's Republic of China*, 32 S.W.L.J. 1255, 1256 (1979). China has never had a tradition of comprehensive national codes. The Conformist, Buddhist, and Taoist religious beliefs which are strong factors of Chinese life, and the Chinese experience with legalism, both within China and externally, have caused China to steer away from codified law. *See* Lee & Lai, *The Chinese Conceptions of Law: Confucian Legalist and Buddhist*, 29 HASTINGS L.J. 1307 (1978).

who fostered a strong dislike for written laws.¹⁰ Additionally, the religious doctrines that permeate China, although not directly fostering a dislike of written laws, end support to the concepts of mutuality of benefits and equality as means of social control. Confucianism teaches that if written law is used to govern society, as soon as that written law ceases to be operative, society will fail to obey all rules.¹¹ Buddhism, the principal religious creed in China, teaches the concept of compromise. This concept is based on the belief that in a typical dispute, both parties, from their individual perspective, are correct in their assertions.¹² To maximize these individual goals, therefore, pursuing a compromise solution is better than invoking a judicial or individual action that would result in one party being a loser and the other a winner.¹³ Had the 1979 Joint Venture Law been intended strictly for domestic use, its lack of detail would have been fortified by this Chinese practice of mutuality of benefits and equality;¹⁴ however, since the Joint Venture Law was proposed for international use, its lack of detail has been viewed as legally ambiguous by potential investors.¹⁵

¹⁰ During the short-lived Chin dynasty (221-206 B.C.) legalistic thought prevailed. The legalist emphasized state power and control rather than morality. The legalists' attempts to control thought consisted of the burying of the 400 scholars and the burning of books. Ganschow, *supra* note 7. The Legalists became symbols of oppression in Chinese history. Mitchell, *Dispute Settlement in China*, 4 A.S.I.L.S. INT'L L.J. 71 (1981).

¹¹ Confucianism recognizes five relationships upon which behavior is based: affection between father and son, righteousness between sovereign and subject, respective duties between husband and wife, order between elder and younger, and sincerity between friend and friend. Lee & Lai, *supra* note 9, at 1308-09.

For a discussion of Confucianist beliefs and the role they play in Chinese contracts and codified laws, see Carl, *supra* note 9, at 1256; Lee & Lai, *supra* note 9, at 1308-12; Note, *supra* note 2, at 1230-32. For these reasons it is of little surprise that in 1949 the PRC abolished all laws of the Nationalist government. During the first few years of the Communist regime, various statutes were enacted, but these statutes did not include commercial, civil, or criminal codes. P. CHEN, LAW AND JUSTICE: THE LEGAL SYSTEM IN CHINA 2400 B.C. TO 1960 A.D. (1973). Later, in the cultural revolution of 1966, the few written laws and remnants of the Chinese legal profession were abolished. Bosco, *supra* note 1, at 219; see also S. TANG & J. MAHONEY, COMMUNIST CHINA: THE SEMESTIC SCENE (1967).

¹² The major contribution of the Buddhist philosophy was the concept of compromise. See Carl, *supra* note 9, at 1256-57.

¹³ *Id.* A solution through compromise, as opposed to a judicial winner-loser situation, allowed each party to maintain dignity and preserved harmony in the community. An elder was selected to mediate and reach an objective solution. This use of compromise resulted in the Chinese view of litigation as a disgraceful means of dispute settlement. *Id.*

¹⁴ The concept of mutual benefits and profits not only is known to the Chinese through their religious and political history but also is supported by the Chinese Communist Party. One of the essential premises of true Marxism is that all participants benefit equally.

¹⁵ Incoming Telegram/Implementing Regulations, *supra* note 4, at 1. The informality of the 1979 Joint Venture Law created uncertainty in the minds of Western investors and was

Since 1979, the Chinese government has attempted to appease recalcitrant investors by enacting a number of laws and agreements to clarify Chinese law on joint ventures.¹⁶ Despite these supplements, hesitant investors still felt that significant problems complicated the operation of joint ventures under the 1979 Joint Venture Law.¹⁷ The lack of investment, however, did not dampen

viewed as merely a policy statement on future developments in China. See *Bosco*, *supra* note 1, at 221.

Had the response to the law been more in the nature of recognizing a commitment to a new business structure, the chances of investment may have been greater. Those who focused upon the lack of detail failed to take into account that in only a few short years the Chinese have altered, if not discarded, 300 year-old business ways and have adopted a system foreign to them. For additional perspective regarding the 1979 Joint Venture Law, see *Note*, *supra* note 3, at 145.

¹⁶ Since the enactment of the Joint Venture Law of 1979, the Chinese have attempted to explain and supplement the skeletal joint venture law with the following legislation: the Income Tax Law of the PRC Concerning Joint Ventures with Chinese & Foreign Investment, Sept. 10, 1980; Detailed Rules and Regulations for the Implementation of the Income Tax Law, Dec. 14, 1980; Individual Income Tax Law of P.R.C., Sept. 10, 1980; Detailed Rules for the Implementation of the Individual Income Tax Law of the People's Republic of China, Dec. 14, 1980; Regulations on Labor Management in Joint Ventures using Chinese and Foreign Investment, Aug. 26, 1980; Regulations for the Registration of the Joint Ventures Using Chinese and Foreign Investment, Aug. 26, 1980; Interim Regulations Concerning the Resident Offices of Foreign Enterprises, Oct. 30, 1980; Provisional Regulations for Exchange Control of the P.R.C., Dec. 18, 1980; Detailed Regulations for the Implementation of Exchange Control with Respect to Foreign Representative Offices and Their Employees, Aug. 10, 1981; Rules Governing the Carrying of Foreign Exchange, Precious Metals and Payment Instruments in Convertible Currency into or out of China, Aug. 10, 1981; Detailed Rules and Regulations on Exchange Control Relating to Individuals, Dec. 1981; Economic Contract Law, Dec. 13, 1981; Regulations on Special Economic Zones in Guangdong Province, Aug. 26, 1980; Provisional Regulations for Business Registration (Guandong Special Economic Zone), Jan. 1, 1982; Provisional Labor and Wage Regulations (Guandong Special Economic Zone), Jan. 1, 1982; Feasibility Study Elements (no date supplied). *Trade Report*, *supra* note 1, at 37-99. In relation to the United States, the Chinese have made further attempts to end the ambiguities of the Joint Venture Law by assenting to legal frameworks between the PRC and the United States that purport to explain further the Chinese expectation of joint ventures. Trade Agreement, Feb. 1, 1980; Maritime Agreement, Sept. 17, 1980; Aviation Agreement, Sept. 17, 1980; Textile Agreements, Sept. 17, 1980; Consulate Agreements, Sept. 17, 1980; Extension of Eximbank, Apr. 1980; Overseas Private Investment Corp. (OPIC), Oct. 7, 1980; Approval of Certain Military and Technology Sales, July 1981; Revised Licensing Guidelines, July 1980; U.S. Granted China Preferential Administrative Treatment, July 1980; U.S. Issued Regulations on Sales to China, Dec. 1981, See *Trade Report*, *supra* note 1, at 4-6.

¹⁷ Although the Chinese believed that these laws and agreements would clear up ambiguities surrounding the joint venture law, foreign investors still steered away, complaining that some areas continued to be vague. For example, in the area of arbitration, despite the Chinese reputation for strict adherence to their contractual obligations, investors felt that the PRC failed to provide adequate enforcement guarantees, since the Chinese would not set out a guarantee or procedure for arbitration awards. *Note*, *supra* note 3, at 142-44. Another example is in the area of patent and property rights. Foreign investors believed that the lack of a "discernible enforcement mechanism" for property rights was still an obstacle to tech-

China's desire for international trade,¹⁸ so China again attempted to reform its business and legal policies. The issuance of the 1983 Implementing Regulations was an attempt to clarify the 1979 Joint Venture Law and invite investment from abroad, clearly evidencing this ideological shift.

The first function of the Implementing Regulations, clarifying the Joint Venture Law, is met through many facets of the regulations, but discussion will be limited to two clarifying measures. First, the manner in which the Implementing Regulations are organized and printed, as compared with the law they modify, indicates a change in the Chinese approach to business-oriented laws. The text of the 1979 Joint Venture Law consisted of fifteen cryptic articles; the new Implementing Regulations contain 118 articles.¹⁹ Second, while the format of the 1979 Joint Venture Law was merely a sporadic listing of unrelated rules,²⁰ the Implementing Regulations are not only set out in sixteen subject-based chapters, but also are subcategorized.²¹ The length of the new Implementing

nology transfers. Note, *supra* note 1, at 146.

A final complaint by investors was that even though the new laws and regulations provided details, investors were still unsure as to exactly how, and when these new laws and regulations would work in conjunction with the 1979 Joint Venture Law. See Trade Report, *supra* note 1, at 14-16.

¹⁸ See Wall St. J., Oct. 26, 1983, at 5, col. 1. Since 1979, a variety of laws have been published to promote trade, and they apparently have been successful. During the last decade China has had an eight-fold growth in foreign trade; trade levels went from \$4.3 billion in 1970 to \$34 billion in 1980, and it is estimated that trade levels will reach \$63 billion by 1985. Klingenberg & Pattison, *supra* note 1, at 810-11.

The 1983 Implementing Regulations also evidence China's growing appetite for trade. Article 4(2) seeks enterprises that need minimal investment yet produce quick returns and fast profits — a somewhat capitalist notion of business. See Implementing Regulations, *supra* note 5, art. 4(2); see also *id.* art. 12.

The re-establishment of diplomatic relations in 1976 between the United States and China caused a new Chinese approach toward relations with the West. In January 1979, Premier Deng Xiaoping toured the United States. Following that tour, in March 1979, \$197 million in American claims which had existed since the 1949 Communist freeze on all western assets in China were liquidated. The Chinese showed their eagerness to trade with the West when they published the 1979 Joint Venture Law. The United States response was demonstrated by Senate approval of H.R. Con. Res. 204, which extended Most Favored Nation status to the PRC, on January 24, 1980. 126 CONG. REC. 5348-51 (daily ed. Jan. 24, 1980). For an in-depth analysis of the PRC's transition from Mao, see Bosco, *supra* note 1, at 218-23. For a discussion on the handling of the liquidation of claims, see Wash. Post, Mar. 2, 1979, at A1, col. 1. For an overview of this modern transitory phase of PRC history which has been marked by increased Chinese willingness to adopt more written rules of law, see Note, *supra* note 1, at 133-34.

¹⁹ Trade Report, *supra* note 1, at app. A.

²⁰ *Id.*

²¹ Incoming Telegram/Implementing Regulations, *supra* note 4.

Regulations and their division into subject matter-based chapters may be incidental, but it suggests an attempt by the Chinese government to move toward a legal system that is clearer and more closely aligned with international practices.²²

In the realm of substantive law, the 1979 Joint Venture Law failed to illuminate fully many elements of a joint venture. The Implementing Regulations attempt to supplement the law in all these areas,²³ but a review of only the joint venture formation pro-

²² Actually, much of the procedural details of joint ventures have already been provided through legislation and agreements which came into force after the publication of the 1979 Joint Venture Law. Since many of these laws did not specifically state that joint ventures were subject to these laws, however, the relationship between the joint ventures and the new rule was unknown. The Implementing Regulations provide some guidelines as to how the laws interrelate. For example, taxing of joint venture personnel is under the jurisdiction of the Individual Income Tax Law of the People's Republic of China, Sept. 10, 1980. See Implementing Regulations, *supra* note 5, art. 70.

Other methods besides the Implementing Regulations have been used to clarify the 1979 Joint Venture Law and to prompt investment. In light of the generally strong business ties between China and Japan, concern arose over the failure of Japanese businesses to exploit the China joint venture opportunity. This arousal of government concern in Japan led to a MITI-sponsored investment survey in April 1984. The MITI-sponsored investment survey, staffed mostly by specialists from the Japan-China Association of Economy and Trade, was dispatched to China to discuss Japan's perceived obstacles to further joint venture activity. The result of this investment survey was the identification of seven impediments to joint ventures as seen by the Japanese. The Japanese feel that through this survey, the publication of the Implementing Regulations, and other accords made by China, some of these obstacles have been weakened. Incoming Telegram/Japan, *supra* note 5, at 1.

The MITI-sponsored survey designated these seven factors as investment impediments to all foreign joint venture partners: (1) terms of the joint venture, (2) lack of legal framework, (3) inaccessibility to the Chinese market, (4) high cost of land use, (5) forced use of Chinese components, (6) control of business decisions, and (7) excessive regulation and paperwork. *Id.* at 1-3.

By creating a legal system similar to the system currently practiced in the West, the Chinese perhaps believe that Western investors would feel more familiar with China and will be more inclined to invest. This attempt to imitate Western laws has been urged upon the Chinese by investors and lawyers who are seeking uniformity and standard forms of business in the PRC. Note, *supra* note 3, at 144. Some commentators feel that until the Chinese adopt a Western-oriented system, investors will suffer great losses. See Bosco, *supra* note 1, at 240-41.

Prior to the Implementing Regulations, there was debate over both the lack of detail and the interpretation of the details provided. In their effort to understand the ramifications of a joint venture in China, many authorities have even debated the validity of translations of the 1979 Joint Venture Law. For example, the Chinese word "ying" has been translated into English by some as "might" and by others as "must." This particular debate has led to what is termed a "lawyer's nightmare." Bosco, *supra* note 1, at 225 n.34. See also ROWLEY, FAR EAST ECON. REV. 50 (1979) (discussion of other interpretations and implications of the word "ying"). The Chinese hope to avoid debates such as these by supplying a glossary. Commentators have previously stated that not until the language of Chinese law is standardized and mutually understood will investment increase. Bosco, *supra* note 1, at 224-25.

²³ The MITI group found several impediments exclusive to Japan: (1) Chinese prejudice,

cess is sufficient for determining whether the Implementing Regulations are fully capable of satisfying this clarifying purpose.²⁴

The 1979 Joint Venture Law barely defined the joint venture formation process. Only one article touched upon the formation process,²⁵ and this article provided merely a short outline. Under the 1979 Joint Venture Law the joint venture parties had to submit agreement documents to the Foreign Investment Commission (FIC).²⁶ Within three months, the FIC would approve or deny the joint venture.²⁷ Upon FIC approval, the joint venture could register for an operating license with the General Administration for the Industry and Commerce of the People's Republic of China (GAIC). Once the license was received, production could begin.²⁸ The law failed to enunciate the particular department responsible for the registration of joint ventures, the time span for registration, and a number of other factors relevant to joint venture formation. By comparison, the new Implementing Regulations devote an entire chapter to the formation of a joint venture.²⁹ In addition, requisites for joint venture approval, controlling government authority, required documentation, applicable law, and estimates of timing are all illuminated in the new Implementing Regulations.

Under the new regulations, before a joint venture can begin operation it must first secure approval from the proper PRC agency. Whereas the 1979 Joint Venture Law failed to disclose clearly the proper PRC agency, the new regulations designate MOFERT as

(2) Japanese business practices, and (3) alternative yet satisfactory business arrangements already in operation between China and Japan. Incoming Telegram/Japan, *supra* note 5, at 3-5.

²⁴ The formation process of a joint venture in China is not necessarily more important than other areas of operation, but the remainder of the relationship is planned during this phase. See generally Incoming Telegram/After the Contract, *supra* note 8.

²⁵ Trade Report, *supra* note 1, at app. A., art. 3.

²⁶ *Id.* Article 3 fails to supply the criteria upon which the Foreign Investment Commission (FIC) and General Administration for Industry and Commerce of the People's Republic of China (GAIC) based their decision to authorize or deny a proposed joint venture. Bosco, *supra* note 1, at 224; Klingensberg & Pattison, *supra* note 1, at 820; see also *infra* notes 35, 36 and accompanying text.

²⁷ The purpose of the approval and registration requirements of the FIC and GAIC is to ensure that both China and foreign investor thoroughly consider the joint venture, for "review will effectuate the extra degree of clarification needed in such cross-cultural endeavors." Klingensberg & Pattison, *supra* note 1, at 821. However, since the 1979 Joint Venture Law did not disclose any of the requirements for a positive decision by the FIC and GAIC (*supra* note 26), the decision on the sufficiency of the "cross-cultural endeavor" was left entirely in the hands of the Chinese. *Id.*

²⁸ Trade Report, *supra* note 1, at app. A, art. 3.

²⁹ Implementing Regulations, *supra* note 5, arts. 8-18.

the national-level ministry empowered to supervise joint ventures.³⁰ The regulations note that in certain statutorily specified situations, a local government department office can act as the direct supervising authority.³¹

The Implementing Regulations also provide potential investors with a second significant formation feature—approval criteria.³²

³⁰ Ministry of Foreign Economic Relations on Trade (MOFERT) replaces FIC and GAIC, as the sole national administrative office over joint venture approval and operations. *Id.* art. 8.

Although the Implementing Regulations have put foreign investors on notice as to the "national" authority over joint ventures, they fail to address or alleviate problems which exist due to the extensive "departmentalization" of authority in the Chinese bureaucracy. The different levels of bureaucracy, accountability, and responsibility have made contract negotiations difficult and eventual enforcement of contract terms equally complicated.

A 1984 United States Department of Commerce survey of three American businesses operating in Shanghai confirmed that serious problems exist due to the faceting within the Chinese bureaucracy. Though the Americans working in Shanghai feel that the Chinese honor their contracts (and are punctilious in holding the United States party to its obligations), all have found their Chinese counterparts are limited in their ability to meet their own responsibilities. As one said:

In the negotiations, they kept insisting that equipment and materials were available in China and should be subtracted from what we were to supply. Then, when we are all set to do something, we suddenly find it isn't available. The troops that we do business with at the lower levels, who are not part of the negotiations, cannot get the stuff. You finally wind up having to get it for them.

Authority and responsibility in China are so compartmentalized that, in the situation just described, the Chinese client was unable to procure materials outside its own bureaucratic "system," where it has no priority claim on scarce supplies. The Chinese organization which negotiated the contract was an import-export corporation under the ministry of foreign trade; the negotiators made contractual commitments on behalf of a Chinese corporation in a totally separate "system" under an industrial ministry, without knowing whether the corporation could actually fulfill these responsibilities.

In China's compartmentalized system, commitments made without authority will not necessarily be honored by the entity which has control. Moreover, discovering who does have authority is an ad hoc process for the Chinese as well as for the expatriate. In fact, the situation is so complex that probably no one has full knowledge. One American engineer recounted, '[o]ne of our biggest difficulties has been to find the person on the Chinese side who can make a commitment. Unless you have a particular individual's commitment, we'll ignore what someone else on the Chinese side might have said. Furthermore, they won't necessarily admit that they can't make the commitment.' In addition, authority over some matters may lie with more than one organization.

Incoming Telegram/After the Contract, *supra* note 8, at 1-3.

³¹ Implementing Regulations, *supra* note 5, arts. 8-18. Although this provision attempts to localize the operation and authority over a joint venture, problems will still exist because not all facets of the joint venture are contained within the local area or authority. Access to raw materials, labor requirements, and distribution processes are just a few of many facets of a joint venture operation which are under national, not local, control. *See id.*

³² *Id.* arts. 3, 4, 5. In Art. 3 of the Implementing Regulations, the Chinese government lists the six business areas which it feels will produce the best "socialist modernization."

The previous law failed to specify any particular types of ventures the Chinese found especially desirable. In contrast, the Implementing Regulations specify the purposes, the economic potential, and the industrial areas³³ and capabilities for which China is currently seeking joint ventures. These factors will influence the FIC/MOFERT decision to approve or disapprove a joint venture application. Also, the Implementing Regulations list certain types of joint ventures that will be denied the right to operate.³⁴

A third formation feature clarified by the new Implementing Regulations is the requirements for documenting a joint venture.³⁵ Three agreement documents are involved in a joint venture formation: the joint venture contract, the joint venture agreement, and the articles of association. The Implementing Regulations distinguish these three documents³⁶ by designating the most essential documents,³⁷ specifying particular facts that must be included in the documents,³⁸ establishing language requirements,³⁹ and assigning responsibilities to the parties during the application process.⁴⁰ Considering that contract negotiations are generally the ini-

Article 4 lists the economic results that a joint venture must stress to receive approval. Article 5 lists the elements of a joint venture which preclude approval by MOFERT.

³³ Along with those industrial areas listed in the Implementing Regulations, the Chinese gave the MITI Group (*supra* note 22) a list of nine industries for which it desired joint venture proposals, including transportation, energy, metallurgy, machinery, electronics, new-type construction materials, non-ferrous metals, rare metals, and agriculture. Most existing joint ventures are in the light industry, spinning, machinery, and electronics areas, which may be a guide for future investment.

³⁴ *Id.* art. 5.

³⁵ See Implementing Regulations, *supra* note 5, arts. 9, 13, 14, and 17 (complete outline of the documentation requirements).

³⁶ *Id.* art. 13.

³⁷ See *supra* note 20.

³⁸ Implementing Regulations, *supra* note 5, art. 14.

³⁹ *Id.* art. 9.

⁴⁰ *Id.* art. 12. Respective responsibility during the application process is certainly important, but there are other aspects of responsibility which joint venture parties should be aware of. For instance, in an effort to protect themselves later, contractors should be wary of "bureaucratic obstruction" in China.

If the experience of the United States engineering firms in Shanghai suggests any lesson for future business negotiations, it is that a contract should be written to minimize penalties for delays caused by bureaucratic obstruction. Bureaucracy is pervasive and authority so fragmented that there is no effective project schedule, which frustrates most Americans working in Shanghai. One employee whose company is supplying technical assistance to a Shanghai client said:

[O]ne of the major problems is that we can't find the schedule. Officially they did not change the schedule, but we know they're behind schedule. We will probably all go home as scheduled, because our contract is based on total man-months in China, not on their progress. If we knew what the new schedule is, we could

tial source of contact between China and joint venture investors, and that the contract later acts as a guideline to future expectations,⁴¹ the Implementing Regulations' assistance of foreign inves-

probably have [made more efficient use of our people's time in China].

Incoming Telegram/After the Contract, *supra* note 8, at 3. A well negotiated contract may be able to protect the investors from incurring liability due to "bureaucratic obstruction."

⁴¹ "An observer of Chinese commercial negotiating style has commented that for the Chinese, conclusion of a contract means that the two parties now understand each other well enough that each can expect further favors from the other. . . ." One of the United States engineers working in Shanghai noted his client's tendency to ask for services not specified in the contract "in the spirit of cooperation," i.e., for no additional fee. The Chinese client may hold quite a different view from the American party about what constitutes a "favor" or concession, and what is owed by one party to the other. For example, one of the Americans working in Shanghai remarked that the Chinese do not recognize or reward delivery of a product which exceeds the specification agreed to in the contract. Another commented:

Like many American companies, we were anxious to get a foot in the door, so (the Chinese client) got a good deal. But we're actively negotiating for a couple more jobs, and the problem we have is, they think the second will be cheaper than the first, and we're thinking the opposite: with our foot in the door, we'll charge a normal profit.

The experience of American engineering companies in Shanghai indicates that the more complete and detailed the contract, the easier for the man in the field to resist the client's request for such "favors." One U.S. company now working in Shanghai offered the Chinese a contract package similar to one the company was using in Third World and East Bloc countries. With that background, the company was able to define the scope of work precisely.

Incoming Telegram/After the Contract, *supra* note 8, at 2.

In light of the Chinese understanding of a "contract," and the expectations that arise from a contract, any data that the Implementing Regulations provide on the contract negotiation and operation should be of assistance to potential investors.

Another facet of a contract that cannot be underestimated is how the contract covers the living situation of employees sent by the foreign investor to China.

The Chinese system tends to put the expatriate in a position of dependency, his sponsoring unit taking responsibility for his personal situation vis-a-vis the multitude of bureaucracies which impinge on his life in China. Many Americans find the dependency itself frustrating, doubly so when the 'sponsor' seems inadequate to discharge these responsibilities. Most of those now here have found, however, that they gradually outgrow this dependence and learn to fend for themselves. At a minimum, a contract should clarify the employee's visa and customs status.

This subject falls into contractual limbo because housing, visa status, and customs privileges are beyond control of the Chinese organization which is the party to the contract and must be negotiated with organizations which are outside its "system." The Chinese client or partner of the United States company, as its sponsor, represents it in these negotiations (usually leaving the company in the dark about what is going on). However, many of the American engineers resident in Shanghai believe their sponsors were naive themselves about the regulations and failed to investigate before the expatriates arrived. As a result, they unintentionally misled the United States companies about conditions for their employees in China.

Id. at 4. For a general discussion of other problems that foreign business representatives

tors' understanding of Chinese expectations is certainly a step toward improved business relations.

Other aspects of joint venture formation are further clarified by the Implementing Regulations. As for related and applicable law, clauses in the Implementing Regulations put potential investors on notice of the relationship between previously enacted Chinese laws and the total body of law regulating joint ventures.⁴² These clauses attempt to provide investors with a breakdown of how China's laws will affect joint venture operation.

Finally, the Implementing Regulations substantially clarify the approximate time span of the registration process.⁴³ During the three-month period during which MOFERT reviews the joint venture application, the parties are free to amend the documentation originally submitted.⁴⁴ The regulations provide one month for an approved joint venture to apply for a license with the FIC.⁴⁵ For contract and agreement purposes, the date that the operations license is issued serves as the official date of the establishment of the joint venture.⁴⁶

Additional substantive Implementing Regulations address the formation registration process of joint ventures, as well as other, previously vague areas. These regulations provide detailed information on the selection of the board of directors,⁴⁷ access to raw materials,⁴⁸ the role of officers and managers,⁴⁹ the jurisdiction for

face in Shanghai, see *id.* at 4-6.

⁴² Implementing Regulations, *supra* note 5, arts. 1, 26, 29, 69, 70, 73, 91, 96, 100.

⁴³ *Id.* arts. 10, 11.

⁴⁴ *Id.* arts. 8, 10.

⁴⁵ *Id.* art. 11.

⁴⁶ *Id.* art. 11. Again, the mere inclusion of the time schedule for amending the joint venture documents during the application and registration process evidences the increased emphasis on detail in the Implementing Regulations.

⁴⁷ Implementing Regulations, *supra* note 5, arts. 33-41.

⁴⁸ Article 57 of the Implementing Regulations states that joint ventures must preferentially use Chinese components and raw materials if available. Reaction to this clause is varied, but Japanese investors find this clause an impediment to investment. The reasoning is that:

[g]iven the fledgling state of China's industrialization, these parts are often of inferior quality; despite this fact, the joint venture will be charged the internationally prevailing price. This means the foreign investor can be squeezed on one side by Chinese determination of production costs (both fixed and variable) and on the other by Chinese setting of the selling price.

Incoming Telegram/Japan, *supra* note 5, at 3; see also Implementing Regulations, *supra* note 5, arts. 58, 59.

The Japanese investors have noted that this raw material requirement can have repercussions both in China and on the sale of products destined for export into a competitive mar-

arbitration,⁵⁰ the methods of accounting and finance,⁵¹ and other areas that needed clarification.

With the ambiguities in the 1979 law clarified, the major concern of the Chinese government is whether this clarification will encourage foreign investment in China.⁵² There are a variety of aspects of business in China about which potential investors considering investments in China need further information when deciding whether to invest in China. In some of the traditionally primary⁵³ areas of business concerns, such as taxation, labor, and market access, the Implementing Regulations expand Chinese law, making it more precise and, therefore, more attractive to investors. For the sake of analysis of the investment incentive function of the Implementing Regulations, discussion will be limited to these specific business areas.

Generally, one of the most important methods of attracting for-

ket. The Japanese are dismayed by the effect of certain Chinese materials on their quality control standards. "As part of the bilateral exchange of personnel, the Japanese have trained some Chinese in quality control principles, but these trainees cannot always convince Chinese bureaucrats that buying components abroad may be preferable to supporting domestic industry. As a result, this is another factor discouraging Japanese investment." Incoming Telegram/Japan, *supra* note 5, at 3.

⁴⁹ Implementing Regulations, *supra* note 5, arts. 33-41.

⁵⁰ *Id.* arts. 109-12.

⁵¹ *Id.* arts. 80-90.

⁵² The Chinese issued the 1983 Implementing Regulations to promote foreign investment by clearing up the previous legal ambiguities. Incoming Telegram/Implementing Regulations, *supra* note 4, at 1. For a discussion of loan areas under the 1979 Joint Venture Law that were strictly limited to negotiation, and hence ambiguous to some investors, see Bosco, *supra* note 1, at 224. For a discussion of specific areas of business that may not be fully defined in the Implementing Regulations, see also *id.*; Klingenburg & Pattison, *supra* note 1, at 808-09; Note, *supra* note 3, at 147-48.

⁵³ Another "primary" attraction of a joint venture in China is a low cost of production due to the key element of inexpensive land. Such has not been the case, however.

The Chinese government . . . has set land prices quite high, both when fixing rent and when assessing land as a capital contribution to a joint venture. Since all land is state-owned, no other price mechanism to restrain government determination exists. A range of rental fees is provided in local statutes, leaving the exact charge to negotiations between the parties. The April MITI mission complained about high rents and the Chinese promised further discussions, apparently recognizing the danger of discouraging joint venture business.

Land assessment as a contribution to the Joint Venture is handled somewhat differently. Japanese businesses have complained of a Chinese tendency to assess the land so as to match the capital contribution made by the foreign investor, thereby neatly achieving at least 50% ownership and control. The 1983 Supplementary Regulations to the joint venture law took a step forward, however, by giving responsibility for assessments to the central government, facilitating a standardization of the process.

Incoming Telegram/Japan, *supra* note 5, at 2.

ign investment is by creating a favorable tax environment.⁵⁴ The 1979 Joint Venture Law provided a general scheme of tax rules,⁵⁵ but it was not clear whether this cursory scheme would benefit foreign business investments. The 1980 Chinese Income Tax Law supplemented the general tax section of the Joint Venture Law, but investment still fell short of expectations.⁵⁶ To remedy this lack of investment, the Implementing Regulations now not only assist potential investors in measuring the effect that the previously-enacted tax laws could have on joint ventures,⁵⁷ but also they state certain joint venture conditions that will give rise to tax reductions and exemptions.⁵⁸ Yet, even with this addition of tax details, two

⁵⁴ Taxation considerations play a major role in determining the structure that a joint venture will take. Flicker, *Western Joint Ventures to Carry Out Industrial Cooperation Agreements in the Soviet Union: Selected Problems for United States Parties*, 13 INT'L L. 485, 490 (1979). For an overview of the United States tax treatment of various types of joint ventures and the effect of the United States-U.S.S.R. income tax on the joint venture structure, see *id.* at 490-93.

A dichotomy exists in reference to the Joint Venture Law ambiguities. The ambiguity concerning taxation can be viewed as a facet "flexible enough to accommodate almost any scheme," or a provision guaranteeing firm Chinese control. See Note, *supra* note 3, at 149-50.

⁵⁵ See Trade Report, *supra* note 1, at app. A, art. 7. The 1979 Joint Venture Law provided that the joint venture will pay an income tax on gross profits pursuant to the PRC's tax laws and that upon reinvestment, restitution of a portion of the paid income tax would be allowed. The 1979 Joint Venture Law failed to provide the tax rates or the percentage of restitution. Note, *supra* note 3, at 136-37. At the time the 1979 Joint Venture Law had been issued there was in China an extensive amount of tax law already in existence, but the 1979 Joint Venture Law failed to enumerate how these previously enacted laws would affect joint venture operations.

⁵⁶ Problems still existed in many vital areas of taxation; for example, what might qualify as a legitimate contribution to capital might not qualify for tax relief. Surrency & Sable, *Chinese Removing Joint Venture Barriers*, Legal Times of Wash., Oct. 2, 1979 at 2. For a review of the tax incentives of joint ventures, see Note, *supra* note 3, at 137. For the manner of tax deductions in reference to the expansion reserve fund, bonus and welfare funds, see Klingenburg & Pattison, *supra* note 1, at 829. For a discussion of the tax scheme when the joint venture is no longer operating at a loss and no longer exempt from taxation, see *id.* For a discussion of whether the joint venture will be subject to China's Industrial and Commercial Consolidation Tax, see Note, *supra* note 1, at 137. Tax laws that issued subsequent to the 1979 Joint Venture Law filled in some gaps in the law by, among other things, providing more precise definitions and terms and spelling out how taxable income is to be calculated. Trade Report, *supra* note 1, at 13; see *supra* note 14. The laws also informed investors of accounting procedures and the relationship between municipality tax laws. Trade Report, *supra* note 1, at 13-14.

⁵⁷ See Implementing Regulations, *supra* note 5. The 1979 Joint Venture Law failed to resolve whether a joint venture would be liable for other Chinese taxes; this Implementing Regulation chapter helps resolve the liability questions. Trade Report, *supra* note 1, at 12-13.

⁵⁸ Article 7 of the 1979 Joint Venture Law (Trade Report, *supra* note 1, at app. x) permitted a partial refund of taxes when a foreign partner reinvested any or all of its net profit

tax questions remain: first, how much of a reduction or exemption is permissive, and second, are these specified situations the only situations in which reductions and exemptions will be allowed.⁵⁹

The answers to these and other tax questions will not be found in the Implementing Regulations, but may only be developed through direct negotiations.⁶⁰ A foreign investor perhaps should view the current tax regulations as merely a negotiating base, rather than an enforcement mechanism upon which to base claims.⁶¹ Codified laws, which are still new to China, must be used in conjunction with the traditional methods of problem solving.⁶² Thus, potential investors who prefer to see black-letter law explicitly define the allowable rate of tax reductions may view the Implementation Regulations as providing inadequate incentives to invest.⁶³ On the other hand, investors who use the Implementing Regulations as a negotiating base and trust their own negotiating skills and position may view the Implementing Regulations as an opportunity to reach a most advantageous taxation agreement.⁶⁴

"within Chinese territory," but its language failed to articulate whether the phrase required reinvestment to take place through the joint venture. Due to this failure to articulate terms, any tax refund in this area must be determined and organized through negotiations. See Klingenberg & Pattison, *supra* note 1, at 828-29; *see also* note 21 (discussion of some of the hazards of negotiating). The Implementing Regulations attempt to define more clearly when these refunds are permissible. Incoming Telegram/Implementing Regulations, *supra* note 4, arts. 71, 72.

⁵⁹ *See supra* note 47.

⁶⁰ When negotiating a contract it must be remembered that this loose amalgamation of contract principles has survived for years because it centers around concepts of informal negotiations and, most importantly, good faith on the part of the negotiators. See Hoffheimer, *Law and Modernization in China: The Juridical Behavior of the Chinese Communists*, 7 GA. J. INT'L & COMP. L. 515, 530-50; Lee, *Chinese Communist Law: Its Background and Development*, 60 MICH. L. REV. 439, 472 (1962). For example, the lack of provisions relating to breach of contract or employee wages is probably based upon assumed good faith in contractual obligations, rather than any attempt to gain unfair advantage over the foreign trading partner. *Supra* note 3, at 652.

⁶¹ Ganschow Address, *supra* note 7. *See also generally* Incoming Telegram/After the Contract, *supra* note 8.

⁶² *See Lee, supra* note 60 for discussion.

⁶³ Overall, many other factors come into play here, therefore, some investors would rather rely on a tax scheme that is less ambiguous and provides more definite tax incentives. Letter from Leo Carter of Solo Cup Co. to Eileen M. Golden (Oct. 31, 1983) [hereinafter cited as Carter Letter]. *See generally supra* note 7.

⁶⁴ Given that the applicable tax scheme is a major factor in a joint venture, all potential investors will be concerned with its provisions. See Flicker, *supra* note 54, at 490-93. Some investors will see a loosely defined tax system as one in which an advantage can be negotiated. Interview with Thomas Schoenbaum, Director of the Dean Rusk Center, University of Georgia School of Law, Athens, Ga. (November 1983). These investors recognize that it may be possible to negotiate some tax breaks, but the tax aspects are certainly not touted as

In addition to the creation of a favorable tax environment, another important aspect of a joint venture operation capable of producing investment incentives is labor.⁶⁵ The 1979 Joint Venture Law left procedures covering the employment and discharge of workers and staff members completely subject to joint venture negotiations.⁶⁶ The 1979 Joint Venture Law was, further, silent in the essential areas of labor quantity, labor quality, and wage rate structures. In 1980, the PRC published regulations addressing many of these sensitive labor issues.⁶⁷ In an effort to make Chinese joint ventures attractive to Western investors, the Implementing Regulations address other significant labor concerns, such as the relationship between labor and management,⁶⁸ trade union participation in joint venture operations,⁶⁹ and even a salary bonus system based on a somewhat capitalist, "more work-more pay" concept.⁷⁰ These regulations, in conjunction with the previous labor laws and regulations, should, at least in theory, assist potential investors in understanding the impact that the Chinese labor system would have on joint venture operations.⁷¹

Conceptually, few labor problems would inhibit foreign investment in China, but some problems may frustrate the actual execu-

something to attract one to a joint venture with China. See Carter Letter *supra* note 63.

⁶⁵ Another way investors hope to exploit joint venture opportunities is by employing lower paid Chinese workers. Incoming Telegram/Japan, *supra* note 5, at 2. In addition to the use of the site (see *supra* note 52), the only significant operational contribution that the Chinese can make to the joint venture is labor. Trade Report, *supra* note 1, at 15. In reference to the original contributions to the joint venture, the Chinese are seeking technology, capital, equipment, and business skill; thus, use of the site and labor appear to be the only initial investments outstanding after the foreign contribution. *Id.*

⁶⁶ See *id.* app. A, art. 10.

⁶⁷ Regulations on Labor Management in Joint Ventures Using Foreign Investment, 26 Aug. 1980, official translation printed in *id.* at 56. These regulations technically give employers a "good deal of latitude in the hiring, training, disciplining, and dismissal of workers." *Id.* at 14. This latitude is based on the contract between the joint venture and the appropriate trade union or employee. *Id.* at 14-15.

⁶⁸ Implementing Regulations, *supra* note 5, arts. 91-94.

⁶⁹ *Id.* arts. 95-99.

⁷⁰ *Id.* art. 93. In reference to Chinese workers, Article 93 codifies the responsibility system: "Each according to his work, and more for those who work more." Incoming Telegram/Implementing Regulations, *supra* note 4, at 2. "This change or clarification of the labor work incentive, increased pay, is viewed as a significant step in encouraging foreign investment in China." *Id.* at 1.

⁷¹ As for the pay scale of the Chinese worker in a joint venture, Chinese regulations "require joint ventures to pay wages 20-50% above the domestic rate, depending on the worker's skill level." Incoming Telegram/Japan, *supra* note 5, at 2-3. The actual wages paid to Chinese employees will most often be officially determined during contract negotiations.

tion of the labor laws.⁷² First, some joint venture participants have felt that they did not have the power to dismiss a poor worker, and the Implementing Regulations do not remedy such a problem.⁷³ Second, the Implementing Regulations fail to provide an adequate guide for measuring the impact that trade unions might have upon the management of a joint venture.⁷⁴ A foreign investor will be particularly conscious of this concern because a trade union may in reality be an arm of the PRC government.⁷⁵ Third, the Chinese government has not made its labor supply significantly more attractive to foreign investors than the labor forces of other developing countries competing for the same industrial investments. China is only one of many nations offering inexpensive labor as an incentive for investment.⁷⁶ When compared with some South American, African, and other Asian nations, the Chinese labor pool

⁷² Some labor problems that foreign investors face in China are not capable of being solved through laws or regulations. For example, Chinese work practices are another source of criticism by the American engineers on site in Shanghai: "It's an unsafe work environment. There's junk all over, and so many people, most of them sitting down watching. All of the basic construction is pretty low level. The people are doing a pretty good job, but they had to be taught everything to our standards. And it's difficult to get them to maintain it." Incoming Telegram/After the Contract, *supra* note 8, at 4.

Another basic difference Americans find in the Chinese work style is the lack of confidentiality. None of those now working in Shanghai entrusts confidential matters to Chinese secretaries or assistants, and all assume that their letter, telephone and telex communications are public knowledge. One American explained that because privacy is not respected, the Chinese themselves act to defend their own confidential affairs against intrusion in ways the American finds inimical to the functioning of the organization. "We refurbished all of the offices. The next day, there was paper over all the windows on the doors into the offices. I asked why, and they said, 'so nobody can peek in.'"

Id. Solutions to difficulties of this kind can only be resolved through knowledge of the Chinese labor force and legitimate American expectations.

⁷³ "Although joint ventures normally have the right to hire and fire, many say that in practice the ventures have no such authority: 'You can't hire and fire on your own no matter what they say.'" Wall St. J., Sept. 27, 1983, col. 2-3. See Incoming Telegram/Implementing Regulations, *supra* note 4, at 2; see also Trade Report, *supra* note 1, app. A, arts. 6 & 11, (regulations dealing with staff workers and other personnel contracts).

As for management personnel, Article 41 of the Implementing Regulations "permits the dismissal of officers for graft, or serious dereliction of duty." Due to this high threshold for dismissal, incompetence, by inference, may have to be tolerated. *Id.* at 2.

⁷⁴ Carter Letter, *supra* note 63.

⁷⁵ "Faced with operations in a nation so heavily structured around labor while often basing much of a venture's program upon relatively low labor costs, the venture participants are likely to raise questions concerning the use and treatment of personnel." Klingenberg & Pattison, *supra* note 1, at 826.

⁷⁶ China possesses an abundance of both natural and human resources. Note, *supra* note 3, at 116.

suffers from a serious language barrier, cultural unfamiliarity,⁷⁷ differing professional standards,⁷⁸ and a vast lack of contact with the Western world. To encourage investors to select the Chinese labor force over the labor forces of nations with which investors are familiar, the Chinese government may have to grant investors major concessions to balance the risks the foreign investor would assume.

A final major concern of most potential investors and perhaps the most promising investment incentive is market accessibility.⁷⁹ Usually a foreign investor will provide the developing country with technology,⁸⁰ management skills,⁸¹ and the use of foreign currency,

⁷⁷ A 1984 United States Department of Commerce publication reviewed the cultural ties of China and how these ties affected the joint venture operations with many nations. It stated that in comparison, several factors make the Japanese experience different from the American one.

The close cultural ties between the two Asian nations give Japanese businessmen [sic] a potential headstart when investing in China, but also have their drawbacks. Japanese negotiators complain of a prejudice on the part of the Chinese which causes them to favor Westerners over Japanese. The Chinese, it is claimed, concede terms to Americans which they will not concede to Japanese. The Chinese may openly discriminate. For example, China pays an absence fee to foreign companies as compensation for the lost services of technicians sent to China. This fee is less for Japanese and Koreans than for Americans. In sum, despite the breadth of their crucial 'hands on' experience in China, the Japanese perceive themselves as at a disadvantage when dealing with the Chinese.

Incoming Telegram/Japan, *supra* note 5, at 3.

⁷⁸ See generally Incoming Telegram/After the Contract, *supra* note 8, at 2-3.

⁷⁹ "Access to the Chinese domestic market is the goal of most foreign investors, who hope that joint venture arrangements will win them preferential entree [sic] to this huge customer pool. The Chinese, however, often permit this investment because of its export potential and try to convert production into foreign exchange." Incoming Telegram/Japan, *supra* note 5, at 3.

⁸⁰ See *supra* note 32. The Japanese have already determined what forms of technology they plan to export.

⁸¹ Teaching management skills is not an easy operation. Some Americans have already been involved in teaching management methods to Shanghai clients. The American manager of one project described the problems of changing Chinese management practices in these terms:

They accept new ways of management in principle, but they have difficulty putting them into practice. The biggest problem is that they don't know how to define what a problem is. The reasons for a failure have never been accepted or explored. It's the old 'face' thing. Management doesn't want to hear about uncertainties or failures, only accomplished facts . . . They don't work together as a good team. Part of the problem we've had is getting them to work together; we've had to force them to hold meetings where everybody who should be present is present . . . They don't like to get into a meeting where they have to talk about problems. No one will commit to anything until the problem's been solved. That's been the toughest thing to try to change.

Incoming Telegram/After the Contract, *supra* note 8, at 4.

while the developing nation in turn supplies cheap labor.⁸² Sometimes the developing country's supply of labor may be inadequate to compensate the contributions of the foreign investor fully. If, however, the developing nation is able to supply both a cheap labor force and an extensive new market of consumers, then its attractiveness to foreign investors may increase dramatically.⁸³ China, therefore, with its vast population and recent surge of consumerism, has one of the greatest opportunities among the developing nations to attract foreign investment by granting joint ventures access to its home market. The 1979 Joint Venture Law failed to mention, much less make accessible, the Chinese consumer market. The Chinese market, however, has been opened to some extent by joint venture contract negotiations that took place under this cryptic 1979 law.⁸⁴ For example, in a pre-Implementing Regulations joint venture between a West German elevator manufacturer, Schindler Holding AG/Jardine (Far East) Holding, S.A. (Schindler) and China Construction Machinery Corporation (CCMC), the joint venture company was granted the right to sell joint venture products within the PRC.⁸⁵ The contract also granted the joint venture company the exclusive right to sell "services" for elevators manufactured by the joint venture company, as well as for any elevators that were "imported under the direct control of or under a contract with CCMC."⁸⁶ Most importantly, the contract allowed the joint venture company to act as a sales agent in the

⁸² The most essential element that the Chinese can contribute is labor. Klingenberg & Pattison, *supra* note 1, at 826.

⁸³ Entry into this virgin market is not without complications.

What percentage of production may be sold inside China is negotiated by the parties; explicit settlement of this issue can prevent the Chinese government from unexpectedly routing shipments for export. Defining a domestic allotment percentage, however, is perhaps the easiest step when selling within China. The next stage involves circumnavigating China's poor transportation system, inefficient distribution process, and unfamiliar pricing mechanism. This last factor is particularly frustrating to investors since the Chinese set selling prices to offer a profit margin which depends on the quality of the item. If the Chinese determine that a good is 'inferior,' they may set a price below cost. China is trying to smooth the various complications . . . but the problem is the basic primitiveness of China's infrastructure and the incompatibility of its economic system with modern business practice.

Id. Incoming Telegram/Japan, *supra* note 5, at 3. In essence, "the frustrations of trying to reach the Chinese market are such that . . . unless they are willing to wait for potential longer term rewards, [investors] are discouraged from joint ventures."

⁸⁴ Trade Report, *supra* note 1, at 112, § 6.1.

⁸⁵ *Id.* at 112, § 6.3.

⁸⁶ *Id.*

PRC for those Schindler products produced irrespective of the joint venture company stating that, "[t]he Joint Venture company shall with the help of CCMC assist clients and organizations to acquire Schindler products to be installed in their buildings."⁸⁷ Through these negotiations Schindler gained access to the Chinese market for both its joint venture products and its products produced outside of China. This agreement manifests China's willingness in certain situations to open its market to foreign products produced both domestically and abroad. Unfortunately for China, many foreign investors are unwilling to negotiate such an agreement; they want the joint venture law to establish market accessibility and assurances even before negotiations begin.⁸⁸

The 1983 Implementing Regulations clearly attempt to establish these market rights as a matter of law.⁸⁹ Articles 56 and 61 open the Chinese market to those joint venture products that China is seeking actively. Article 61 "opens the door to the prized Chinese market by permitting domestic sales for products urgently needed in China."⁹⁰ Article 56 assists in opening the Chinese consumer market by integrating the sales programs of the joint venture into the requisite state and local economic plans. These two articles allow "urgently needed" joint venture products to be sold in China and if the joint venture product does not fall into the "urgently needed" category, it may, at the discretion of the Chinese, still be sold in China by being included in the national market scheme.⁹¹

A third article of the Implementing Regulations, though it does not specifically open the Chinese market, recognizes the sale of joint venture products in China and proposes to subsidize the sale of urgently needed products from joint ventures that are experiencing a foreign exchange imbalance.⁹² Article 75 states that when a joint venture that sells its products in the domestic market experiences an imbalance of foreign exchange, that imbalance will be solved in either of two ways. The imbalance either will be corrected with funds taken from the local government foreign exchange reserve, or if this first approach is not possible, then the

⁸⁷ *Id.* at 29. Foreign investors will have to make independent assessment of the marketing possibilities in China. *Id.*

⁸⁸ Incoming Telegram/Implementing Regulations, *supra* note 4, at 2.

⁸⁹ See Implementing Regulations, *supra* note 5, at 56; Incoming Telegram/Implementing Regulations, *supra* note 4, at 1; Implementing Regulations, *supra* note 5, art. 61.

⁹⁰ See *id.* at 1.

⁹¹ Implementing Regulations, *supra* note 5, art. 75.

⁹² *Id.* art. 75; Incoming Telegram/Japan, *supra* note 5, at 2.

State Planning Commission and MOFERT will remedy the imbalance by including the particular joint venture foreign exchange deficit in the state plan.⁹³ These methods of financial support will presumably protect the success of the venture.⁹⁴ The text of Article 75 may be ambiguous,⁹⁵ but since Article 75 clearly permits domestic sales of joint venture products, and the PRC will finance such sales, the Chinese market is clearly opening to the foreign investor who chooses to enter a joint venture.

This release of the "prized Chinese market" is not without complications.⁹⁶ Arrangements like that of Schindler, where apparently products made outside of China and those produced by the joint venture may be sold in China, can still come into existence through negotiation, but they are not guaranteed by law. Important elements of market accessibility, such as protection from competition, are still nebulous and, therefore, subject to clarification through either negotiation or supplemental legislation. Also, questions remain as to the definition and classification of "urgently needed" products and the degree of market accessibility upon expiration of that need.

The Implementing Regulations have created an avenue of access to the Chinese market, but details of how that avenue will operate remain unclear. Potential investors who fear a PRC change in policy regarding market access will require some evidence of Chinese adherence to the law before depending on market access as a justification for investment.⁹⁷

⁹³ Implementing Regulations, *supra* note 5, art. 75.

⁹⁴ Incoming Telegram/Implementing Regulations, *supra* note 4, at 2. The Chinese have at least made provisions for joint venture products to be sold in and out of China by including a provision for the ration of production to be allocated to domestic sales among the elements to be included in a joint venture agreement. See Implementing Regulations, *supra* note 5, art. 14.

⁹⁵ Incoming Telegram/Implementing Regulations, *supra* note 4, at 2. The complications revolve around ambiguity and enforcement of rights granted by law (such as the right to hire and fire workers). See *supra* note 78 for further discussion.

⁹⁶ Incoming Telegram/Implementing Regulations, *supra* note 4, at 2.

⁹⁷ See *supra* note 7. In reality, China's failure to adhere to the commercial laws that it has established will be no greater wrong than the lack of adherence of many Western nations. Being bound by a contract has not prevented nations from implementing an embargo, ceasing production of needed materials, nationalizing facilities, or refusing to accept goods. The policy of independence and keeping control in Chinese hands is practiced in China. See Note, *supra* note 2, at 1238. China, like the United States, Europe and Japan, tries to take advantage of the world market while protecting its own interests. *Id.* As to the ability of the Chinese to adhere to the terms of contracts:

[P]roject managers for the three United States engineering companies in Shanghai were unanimous that their Chinese clients have adhered to the terms of their

In addition, the Implementing Regulations address many other fundamental areas of joint ventures.⁹⁸ Arbitration,⁹⁹ management control,¹⁰⁰ production schedules,¹⁰¹ banking and accounting proce-

contracts. As one said, though, 'The difficulties are not in the contract. With hindsight, I don't think there's anything in our contract I'd change. The difficulty is in the implementation.' The problems these companies have experienced in implementing their contracts in Shanghai generally can be traced to three causes: differences in the way the Chinese and U.S. sides view their non-contractual obligations to one another; the limitations of authority in the Chinese bureaucratic system; and, at the personal level, basic differences in professional standards and relative social and economic values.

The problems and frustrations [foreign investors] feel are most exasperating generally are not directly related to the terms of their companies' contracts with the Chinese. In other words, the difficulties they have encountered would not have been avoided if the contracts had been written differently Few of the problems had seriously jeopardized continuation of a project, and when any had threatened to do so, the Chinese acted to alleviate the situation.

Incoming Telegram/After the Contract, *supra* note 8, at 1.

Generally, as in any business relationship which is trying to develop in a new environment, most Americans surveyed by the Department of Commerce in Shanghai recounted the business tie with China as "a process of learning to work and live in an economic and social environment totally unlike what they are used to. Sharing the lessons of this experience can accelerate the learning process for others, but there is no way to bypass it entirely." *Id.*

⁹⁸ Some areas of operation of a joint venture cannot be addressed with laws or regulations. See *supra* note 71. Also, professional and personal frustration due to the maze of bureaucracy cannot be addressed in regulations, but can certainly have a severe effect on the joint venture operation.

The Americans working in Shanghai and dealing with Chinese bureaucracy on a daily basis believe that the implications of this system only emerge with experience and were not understood by those who negotiated their company's contracts. Said one, "implementation of our contract has been significantly different from what the negotiators anticipated. There was very little recognition by our side of the impact and control of the authorities. We were totally naive about what it takes to get things done . . . I don't think our people had any inkling of the bureaucracy that exists.

Incoming Telegram/After the Contract, *supra* note 8, at 4. The Chinese bureaucracy can cause extended delays, and "even though the contract can protect the U.S. company against financial loss caused by these delays, the resulting inefficiency conflicts with the engineers' professional standards and, often, their personal values. The result for some has been a high level of frustration." *Id.* at 4. These experiences of past investors are conveyed to future investors, and should they be viewed negatively, are not able to be overcome through the mere publication of Implementing Regulations.

⁹⁹ For a history of the growth of arbitration, see Klingenberg & Pattison, *supra* note 1, at 831. Various articles discuss the problems that existed after the 1979 Joint Venture Law in the area of arbitration. See *id.*, *supra* note 1, at 830-32; Note, *supra* note 3, at 128, 142-45; Note, *Foreign Investment in the People's Republic of China: Compensation Trade, Joint Ventures, Industrial Property Protection, and Dispute Settlement*, 10 GA. J. INT'L & COMP. L. 233, 244-45 (1980).

¹⁰⁰ For a clear understanding of the management problems that existed before the publication of the Implementing Regulations, see Jaslow, *Practical Consideration in Drafting a Joint Venture Agreement with China*, AM. J. COMP. L. 217-30 (1983); Klingenberg & Patti-

dures,¹⁰² property rights,¹⁰³ determination of profit,¹⁰⁴ and repatriation¹⁰⁵ must all be clearly perceived by both joint venture parties before the joint venture agreement. In all of these fundamental areas, the Chinese have used the Implementing Regulations to clarify the previously vague Joint Venture Law, and this clarification process has led to a legally defined joint venture structure that is similar to joint venture laws used throughout the world.

Overall, the first function of the 1983 Implementing Regulation—the clarification of ambiguities surrounding the 1979 Joint Venture Law—has been accomplished. The manner in which the Regulations are organized and the detail they provide certainly expands the proposals which were first presented to the commercial world in the 1979 Joint Venture Law.¹⁰⁶ As for the second function, the stimulation of foreign investment, the Implementing Regulations appear to have gone as far as the Chinese are currently capable of going. Whether the Implementing Regulations will actually stimulate foreign investment in China may no longer depend upon the Chinese government, but rather on Western investors. Potential investors have before them many developing nations, all lobbying for investment. Investment in many of them would involve little risk.¹⁰⁷ Few, if any, however, can offer investors the vast market that China can.¹⁰⁸ The Chinese government and people lack experience in international commercial transactions and are, therefore, often awkward in their early commercial dealings with the West. Nevertheless, they have proven over the centuries to be both diligent workers and eager learners.¹⁰⁹ The Implementing Regulations

son, *supra* note 1, at 817-19; Note, *supra* note 3, at 137-42; Note, *supra* note 2, at 147-50.

¹⁰¹ For a discussion of production schedules, which includes access to raw materials, pricing and plant output, see Klingenberg & Pattison, *supra* note 1, at 809-10, 824, 832; Note, *supra* note 3, at 146. For a discussion of schedule problems due to bureaucracy, see Incoming Telegram/After the Contract, *supra* note 8, at 1-3.

¹⁰² See Trade Report, *supra* note 1, at 30-32; Klingenberg & Pattison, *supra* note 1, at 832-33.

¹⁰³ See Klingenberg & Pattison, *supra* note 1, at 816-23.

¹⁰⁴ Jaslow, *supra* note 100, at 230-46.

¹⁰⁵ Klingenberg & Pattison, *supra* note 1, at 811-12, 821-22.

¹⁰⁶ See *supra* notes 27-53 and accompanying text.

¹⁰⁷ See *supra* notes 74, 75 and accompanying text.

¹⁰⁸ See Wall St. J., *supra* note 18, at 1, col. 1. For a review of the growing consumer market in China, see *supra* note 98.

¹⁰⁹ Ganschow Address, *supra* note 7. Their centuries of successful existence should make their diligent work habits and ability to overcome difficulty obvious to Western investors. The adherence to old ways (see *supra* note 7) is being discarded by the issuance of new, codified laws. See *supra* notes 13, 14 and accompanying text. Reliance by the Chinese on good faith in all relationships, including contractual, should make reliance on their present

have provided a vast array of legal details, yet many important issues remain open for private negotiations.¹¹⁰ Such negotiations, if pursued in good faith, are capable of providing a wealth of opportunity.¹¹¹ A decision to seek fruitful negotiations now rests with investors. Potential investors have before them a true "joint venture" opportunity.¹¹² Both investors and China are apprehensive about potential pitfalls, but the current joint venture law offers both parties a short-term trial opportunity for a business relationship that could be the inception of a great commercial and political alliance. As the old Chinese proverb says, "How can you catch tiger cubs without entering the tiger's cave; so brave we must be!"¹¹³

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promises plausible. See note 59 and accompanying text.

¹¹⁰ See Carter Letter, *supra* note 62.

¹¹¹ For a discussion of the good faith element of negotiations, see *supra* note 59 and accompanying text. Negotiations made in bad faith can lead to a loss of face for the parties involved. See generally *supra* notes 49, 52 and accompanying text.

¹¹² For a general business description of a "joint venture," see M. GODON, MATERIALS ON COOPERATIVE JOINT BUSINESS VENTURES (1977).

¹¹³ Translation and comment by Zhao Wei Hou, Research Scholar, Department of Law and Institute of International Law, Wuhan University, Peoples Republic of China, while doing extended research at the University of Georgia School of Law, Athens, Georgia, May 1984.

