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CHINA'S NEW LAW ON JOINT VENTURES USING CHINESE AND FOREIGN INVESTMENT

by
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Ms. Shen is presently associated with the Law Institute of the Chinese Academy of Social Sciences, which is instrumental in drafting legislation for the People's Republic of China. Before coming to study at Southern Methodist University, Ms. Shen was closely involved with the practical implementation of China's joint venture law and participated in various joint venture negotiations. She also serves as Legal Advisor of the Chinese National Travel Service (Beijing Branch).

The full texts of the joint venture law and the income tax law concerning joint ventures follow Ms. Shen's essay.

THE Law of the People's Republic of China on Joint Ventures Using Chinese and Foreign Investment was promulgated for implementation in July 1979. Since then it has aroused interest from industrial and financial circles throughout the world. A number of foreign commentators have expressed the opinion that the law is a reasonable one, characterized by its adaptability. Since early 1980, many foreign businessmen have traveled to China to negotiate specific joint ventures with various Chinese business entities. Discussions on several joint ventures have been completed and many others are in progress. Among the joint ventures that have been authorized and made public by the Foreign Investment Commission of the People's Republic of China are:

- (1) the Beijing Air Catering Company, Ltd., at the Beijing International Airport, established by the Beijing Regional Administration of the Civil Administration of China and China Air Catering, Ltd., of Hongkong;
- (2) the Jianguo Hotel in Beijing, to be jointly built and managed by the Beijing Branch of the China International Travel Service and the Zhong Mei Hotel Development Venture, Ltd., of Hongkong;
- (3) the Great Wall Hotel in Beijing, to be jointly built and managed by the Beijing Branch of the China International Travel Service and the E-S

Pacific Development and Construction Company, Ltd., of the United States;

(4) the Xinjiang Tianshan Woolen Textiles Corporation in Urumqi, jointly established by the Urumqi Woolen Mill and the Hongkong Tianshan Wooltex Company, Ltd.;

(5) the Palace Hotel, to be built and managed jointly by the Chinese International Travel Service and Yick Ho, Ltd., Hongkong; and

(6) the China-Schindler Elevator Company, Ltd., established by the China Construction Machinery Corporation, Schindler Holding, A.G. of Switzerland, and Jardine Schindler (Far East) Holdings, S.A. in Hongkong.¹

As indicated by these authorized joint ventures, the adoption of the Law on Joint Ventures Using Chinese and Foreign Investment heralds a new era in economic cooperation, trade relations, and technological exchanges between the People's Republic of China and foreign countries. In the realm of international economic cooperation, nations seeking industrial expansion and renovation customarily attempt to attract foreign capital for the establishment of international joint ventures. The participants may be either natural or juristic persons. Although the juristic persons generally are corporations, they may also include national departments or international organizations. The nation whose government authorizes an international joint venture may establish it either within its own borders or in a foreign country. Ventures authorized under China's joint venture law, however, will operate within the Chinese territories so as to facilitate the law's purpose of introducing advanced technology and equipment to China.

In view of the disparities in economic and governmental systems that exist around the world, it is natural that each country has its own policy, principles, and specific measures for implementation of international joint ventures. In the 1950s, the People's Republic of China, Poland, and Tanzania jointly established the Ocean Transportation Companies, but this venture has not developed sufficiently to serve as a model for joint ventures under the new law. The promulgation of the Law on Joint Ventures Using Chinese and Foreign Investment, however, is certain to change the situation. The law should prove conducive to the absorption of foreign capital and to the importation of advanced technology and equipment. The law is also expected to raise the level of management, thus accelerating the development of China's national economy.

Article 1 of the joint venture law makes the goals and purposes of the law clear in stipulating:

With a view to expanding international economic co-operation and technological exchange, the People's Republic of China permits foreign companies, enterprises, other economic entities or individuals . . . to incorporate themselves, within the territory of the People's Re-

1. As of Dec. 1, 1980, the number of joint ventures authorized under the new law totalled 17. CHINA ECONOMIC NEWS, No. 42, Dec. 1, 1980, at 3.

public of China, into joint ventures with Chinese companies, enterprises or other economic entities . . . on the principle of equality and mutual benefit and subject to authorization by the Chinese Government.

The law has confirmed unequivocally the legal status of joint ventures in China and the principles to which these joint ventures should adhere. The law has, on the one hand, taken into consideration special conditions in the new period of socialist construction in China, and, on the other hand, has followed the reasonable and traditional practices that are observed in international joint ventures at the present. As a result of this balance, the joint venture law should lead to the creation of ventures that function harmoniously with the governmental policies and business practices of all participants.

Among the provisions of greatest significance to potential foreign investors under the Chinese joint venture law is article 2. In anticipation of foreign businessmen's understandable concern for the security of their capital and profits in China, drafters of the law explicitly declared in article 2 that "[t]he Chinese Government protects . . . the resources invested by a foreign participant in a joint venture and the profits due him pursuant to the agreements, contracts and articles of association authorized by the Chinese Government as well as his other lawful rights and interests." This policy declaration should assuage any concern on the part of foreign investors that their joint venture would be nationalized, or their profits otherwise withheld by the government. Although according to international custom, each state reserves the power to nationalize the property of its own people and of foreigners to meet urgent needs such as national defense, participants in joint ventures will clearly receive just compensation in the event that such a taking should become necessary. Moreover, the governmental protection for joint ventures pledged in article 2 will prevent unlawful interference with joint ventures by any organization, association, or individual.

American investors have another basis for confidence in the Chinese investment climate. In October 1980 the Overseas Private Investment Corporation (OPIC), a United States Government corporation, signed an agreement with China to insure American investments in China against political risks. The commencement of the OPIC program, which will also make loans available for investment in China, should lead to a significant increase in the use of the joint venture law.²

Whereas several countries have laid down complicated procedures for the application and authorization of joint ventures, sometimes requiring a year or more for the government to study an application and authorize it, the procedure delineated in China's joint venture law is relatively simple and convenient. Article 3 of the law stipulates that "[a] joint venture shall apply to the Foreign Investment Commission of the People's Republic of

2. See *U.S., China Clear Way for OPIC to Insure American Investments*, Wall St. J., Oct. 8, 1980, at 31, col. 1.

China for authorization of the agreements and contracts concluded between the parties to the venture and the articles of association of the venture formulated by them" When the Foreign Investment Commission receives these documents, it must either authorize or reject the application within three months. According to article 3, upon receipt of authorization by the Commission, "the joint venture shall register with the General Administration for Industry and Commerce of the People's Republic of China and start operations under license." This single application and authorization procedure, allowing for automatic licensing from the General Administration upon registration therewith, is designed to eliminate redundancies in the authorization process and to expedite the actual operations of authorized ventures.

As to the permissible scope for investment of foreign capital, some other countries, taking into account conditions peculiar to their own countries, have set some restrictions in order to promote their economic independence. Foreign businessmen are not permitted, for example, to invest in such basic and far-reaching enterprises as electrical power, public transportation, coastal navigation, public services, and mass media.³ These nations also preclude foreign investment in industrial departments of strategic importance and other key industrial departments.

The Chinese joint venture law contains no provision restricting the scope of foreign investment, and consequently it may fairly be said that the law is flexible and favorable to all parties. Under China's joint venture law, authorization of any proposed joint venture will be a function of the following factors: whether the venture will prove beneficial to the development of the Chinese national economy and the realization of modernization;⁴ whether it will provide a much needed impetus to China's export rate and thereby improve its international balance of payments; whether it will be conducive to the development of China's scientific research; and whether the operation of the venture would have an adverse impact upon the environment. Proposals to be given first priority are those joint ventures involving companies (1) whose products are competitive on world markets, (2) that will be able to apply advanced technology to China's existing enterprises by reconstruction, (3) that will use advanced technology and updated equipment of which China is in dire need, and (4) that will be able to augment their income in foreign exchange.⁵

Many aspects of the law encourage foreign investment. Consider, for example, the relative proportions of domestic and foreign investment. In

3. See, e.g., BRAZIL CONST. arts. 173-74 (1946, amended 1967); Kalsi, *Encouragement of Private Foreign Investment in the Developing Country: Provisions in the Laws of Kenya*, 6 INT'L LAW. 576, 584 (1972); *Law on the Promotion of Mexican Investment and the Regulation of Foreign Investment* (Art. 4), *Diario Oficial* (Mar. 9, 1973), translated in 12 INT'L LEG. MATERIALS 643 (1973).

4. China's primary objective in promulgating the joint venture law is to encourage industrial, agricultural, scientific and technological, and national defense modernization throughout China.

5. This information was gained during the course of this author's legal experience with the departments involved.

order to increase international economic cooperation and technological exchange and to absorb foreign investment, China's joint venture law does not rigidly adhere to the fifty-one percent domestic minimum, forty-nine percent foreign maximum formula common to traditional international practices. China does not set general restrictions on the maximum proportion of the investment contributed by foreign participants. Quite to the contrary, under article 4 of the law, the proportion of the investment contributed by foreign participants is stated in terms of minimum, not maximum, investment and in general shall not be less than twenty-five percent of a joint venture's registered capital.

In those ventures authorized to operate under China's joint venture law, investments, risks, and profits will be shared by the parties to the ventures on the principle of equality and mutual benefit. The purpose of a joint venture is, of course, to benefit both participants. The host country will receive advanced technology and equipment and the foreign participants will receive their lawful share of the profits. During the running of joint ventures, the principles of equality and mutual consultation will be fully respected, a practice that will be conducive to China's absorption of foreign investments. The provisions in the joint venture law concerning the transfer of one party's share in the registered capital and the prescribed method for valuation of each investment demonstrate these principles.

To illustrate, article 4 of the law provides that foreign investment shall take the form of a limited liability company without the issuance of negotiable stock representing equity interests. The profits, risks, and losses of a joint venture shall be 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. Under article 5, investments in joint ventures may consist of either tangible or intangible property. The latter includes the reserved right of discovery, contribution of licenses, the knowledge of special technology, and the right to use a trademark. As the valuation of such intangible contributions can be an extremely complex matter, article 5's provision that the value of each contribution be ascertained by joint assessment of the parties takes on a special significance. Examples of permissible tangible contributions include cash, capital goods, and industrial equipment. The law contains a special provision for contributions in the form of a physical site for the venture's operation. Under article 5, the investment contributed by a Chinese participant may include the right to the use of a site provided for the joint venture during the period of its operation. If such a contribution does not constitute a part of the investment from the Chinese participant, however, the joint venture is obliged to pay the Chinese Government for its use. The fees for using a site shall be determined by the local people's government, taking into consideration the specific conditions, the infrastructure, and the purpose of using the land. Based upon the range of land fees collected in the past, the fees charged to a joint venture for using a site shall not exceed the current land

rents in neighboring countries and regions. This provision is also designed to facilitate profitable operations for the venture.

As is common in international practice, the Chinese law on joint ventures adopts the system of a board of directors, the organ of a joint venture vested with supreme powers. Article 6 of the law, which provides for the establishment of the board, epitomizes the principles of mutuality, cooperation, and equal participation underlying the law. The size and composition of the board of directors shall be stipulated in the contracts and the articles of association after consultation between the parties to the venture, who take into consideration the proportions of their shares in investment. Each director shall be appointed or removed by his own side.

The board of directors is empowered to discuss and take action on, pursuant to the provisions of the articles of association of the joint venture, all fundamental issues concerning the venture, namely, expansion projects, production and business programmes, the budget, distribution of profits, plans concerning manpower and pay scales, the termination of business, the appointment or hiring of the president, the vice-president(s), the chief engineer, the treasurer and the auditors as well as their functions and powers and their remuneration, etc.

The board of directors shall have a chairman and one or two vice-chairmen. The chairman shall be appointed by the Chinese participants and a maximum of two vice-chairmen shall be appointed by the foreign participants. The chairman shall be in charge of calling and presiding over the meeting of the board of directors. As the law contemplates that the joint ventures will be operated in China, a Chinese chairman should prove most beneficial to the venture as a whole; he will likely have superior access to and familiarity with other Chinese departments impacting upon a particular venture. It must be recalled, moreover, that the chairmen cannot make significant decisions independently. As points of contention between participants arise, they will be negotiated and resolved by all joint venture participants, guided by principles of equality and mutual benefit. If these negotiations are unsuccessful, differences may be resolved by a majority or two-thirds vote, depending upon the margin established in the venture's articles of association. Finally, should this voting mechanism prove unsuccessful, resolution will be accomplished through arbitration.⁶

The joint venture's president and vice-presidents are the leading personnel of the executive board, responsible for the daily routine work. The president and vice-presidents shall be chosen from the various parties to the joint venture. The joint venture law further stipulates that employment and discharge of workers and staff members are to be provided for by the agreement and contract of a joint venture according to law. That is, a joint venture is empowered to employ and discharge workers and staff members, and the existence of this power should be reflected in the agreement and contract. As China has a socialist economic system, there is no free labor market in the country. Prospective workers and staff members

6. The arbitration procedure is considered more fully later in this essay.

initially are recommended for employment by the departments in charge of joint ventures or local labor authorities and are accepted by the joint ventures after passing qualifying examinations, with priority given to those with high marks. As of 1980 all domestic enterprises in China, whether of state or collective independent ownership, will have initiated the examination method of hiring. Workers and staff members who fail to perform their jobs competently shall be discharged according to the terms of the joint venture contract.

The duration of a joint venture generally refers to the contract term of a joint venture. No provision in China's joint venture law expressly regulates the duration of ventures. Rather, the duration of each venture is left to the discretion of the parties, guided by the principles and purposes of the law. The issue of duration has aroused much concern among foreign investors, who naturally do not wish to risk capital unless the venture's operations will be permitted to continue long enough to produce returns on their investments. Were the joint venture law to specify an unrealistically brief duration, foreign investors would undoubtedly seek more hospitable investment climes. A joint venture of indefinite duration is unrealistic also. The duration of each venture must take into account the characteristics of the specific line of business. For example, the duration for heavy industry generally is much longer than that for light industry. Based on these considerations, article 12 of China's joint venture law stipulates that the duration may be determined by the joint venture participants with reference to the particular line of business and specific circumstances. In consonance with average durations of international joint ventures throughout the world, the contract term of a joint venture probably will be approximately ten years for tourism related ventures, approximately fifteen years for light industry, and considerably longer for heavy industry, generally about twenty-five years. The contract terms of the Jianguo Hotel, the Great Wall Hotel, and the Palace Hotel joint ventures are ten years.

Article 14 of the joint venture law is the major provision for dispute resolution. The article enumerates three procedures for resolving disputes among joint venturers: consultation among the board of directors, conciliation, and arbitration. The drafters contemplated that, upon the occurrence of a dispute among participants, the board of directors must initially attempt to settle the differences privately by focusing on the principle of justice and by respecting the interests of all parties concerned, as well as the interests of the joint venture as a viable business entity. If no agreement is reached on the issue after consultation by the board, then either a formal arbitral body of China or another arbitral body of the parties' choice will propose a settlement that it deems equitable to all concerned. The participants may then voluntarily adopt the proposal of the arbitral body. Resolution by this process is known as conciliation. Should conciliation fail, the dispute will be settled through binding arbitration by one of the arbitral bodies referred to above. In view of the fact that the joint

ventures will be operated within Chinese territory and thus subject to Chinese laws and regulations in general, it will ordinarily prove most advantageous for the parties to provide in their contracts for referral of their disputes to the Foreign Economic and Trade Arbitration Commission, a formal Chinese arbitral body that enjoys much international prestige.

The long-range success of China's joint venture law will depend upon China's prompt enactment of collateral laws and regulations that facilitate foreign investment. Laws governing the conservation of natural resources, and foreign exchange regulations to apply to proceeds of joint ventures, are among the current priorities of the National People's Congress. The regulation most likely to influence China's ability to attract foreign capital will be that establishing the rate of income tax to be applied to a joint venture's gross profits. In September 1980 the National People's Congress enacted a Tax Law Concerning Joint Ventures. According to this legislation, the income tax rate for joint ventures is to be thirty percent of gross profits, plus a local surtax of three percent, bringing the overall tax rate to thirty-three percent.* A foreign participant that exercises its right under article 10 of the joint venture law to remit its share of net profit to a bank outside China will pay an additional ten percent tax on the remitted amount. Special tax reductions are available for joint ventures of long duration (typically, heavy industrial ventures) and for agricultural ventures. The tax law also contains a strong incentive for reinvestment of profit within China, in the form of a forty percent tax refund for any foreign participant that so reinvests its share of net profit for a minimum of five

* *Editor's note:* Although an income tax rate of 33% would be within the norm for developing nations seeking to modernize with the assistance of foreign capital, whether the tax law will be retained in its present form is not yet certain. Because China currently does not have sufficient energy supplies, transportation facilities, and managerial skills to industrialize at a very rapid pace (indeed, the improvement of these and other economic conditions is a basic purpose underlying the joint venture law), profits derived from joint ventures in their incipient stages probably will not be as great as they otherwise would be. Thus a 33% rate of tax on gross profits may present a disincentive to Americans and other potential investors in China, and accordingly the Chinese Government is considering a decrease in the tax rate and modifications of other provisions of the law. *See generally Can China Joint Ventures Be Independent?*, Asian Wall St. J. Weekly, Dec. 17, 1979, at 10, col. 2.

Another tax matter of concern to potential American participants in Chinese joint ventures arises from the fact that the joint ventures will technically be neither corporations nor partnerships, but rather "limited liability companies" of a purely contractual nature. Thus, for United States tax purposes, it is not clear how an American participant's interest in a joint venture will be characterized. If the joint ventures are deemed "partnerships" for United States tax purposes, the American participant's profits would be subject to immediate taxation; conversely, if the joint venture is deemed a "corporation," the American participant would enjoy the advantages of tax deferral. This issue has arisen previously when other developing nations have utilized the limited liability company as the vehicle for absorbing foreign capital, and some American participants have succeeded in obtaining Private Letter Rulings from the Internal Revenue Service to the effect that the joint ventures in which they hold an interest will be deemed "corporations" for United States tax purposes. Until a general revenue ruling is issued to resolve this uncertainty, American participants in Chinese joint ventures should also seek Private Letter Rulings to secure for themselves the benefits of tax deferral. *See generally* W. STRENG, INTERNATIONAL BUSINESS TRANSACTIONS: TAX AND LEGAL HANDBOOK 224, 252-61 (1978); *see also* King, *Host Country Aspects of Joint Ventures and Other Ways of Doing Business with the Soviet Bloc Countries and Yugoslavia*, 10 INT'L LAW. 101, 102 (1976).

years. Moreover, article 7 of the joint venture law itself provides that those ventures equipped with "up-to-date technology by world standards" will be eligible for a reduction of, or exemption from, income tax for the first two or three profitable years. This provision will expedite the technological modernization of China, which in turn should enhance the profit-making potential of joint ventures operating within the developing business climate.

APPENDIX I

THE LAW OF THE PEOPLE'S REPUBLIC OF CHINA ON JOINT VENTURES USING CHINESE AND FOREIGN INVESTMENT*

(Adopted by the Second Session of the Fifth National People's Congress on July 1, 1979)

The Law of the People's Republic of China on Joint Ventures Using Chinese and Foreign Investment was promulgated and became effective on July 8. Following is an unofficial translation of the full text of the law.—Ed.

Article 1. With a view to expanding international economic co-operation and technological exchange, the People's Republic of China permits foreign companies, enterprises, other economic entities or individuals (hereinafter referred to as foreign participants) to incorporate themselves, within the territory of the People's Republic of China, into joint ventures with Chinese companies, enterprises or other economic entities (hereinafter referred to as Chinese participants) on the principle of equality and mutual benefit and subject to authorization by the Chinese Government.

Article 2. The Chinese Government protects, by the legislation in force, the resources invested by a foreign participant in a joint venture and the profits due him pursuant to the agreements, contracts and articles of association authorized by the Chinese Government as well as his other lawful rights and interests.

All the activities of a joint venture shall be governed by the laws, decrees and pertinent rules and regulations of the People's Republic of China.

Article 3. A joint venture shall apply to the Foreign Investment Commission of the People's Republic of China for authorization of the agreements and contracts concluded between the parties to the venture and the articles of association of the venture formulated by them, and the commission shall authorize or reject these documents within three months. When authorized, the joint venture shall register with the General Administration for Industry and Commerce of the People's Republic of China and start operations under license.

Article 4. A joint venture shall take the form of a limited liability company.

* Reprinted from BEIJING REVIEW, No. 29, July 20, 1979, at 24-26. The text from the *Beijing Review* was also distributed in press release No. 79/001 by the Embassy of the People's Republic of China at Washington, D.C.

In the registered capital of a joint venture, the proportion of the investment contributed by the foreign participant(s) shall in general not be less than 25 per cent.

The profits, risks and losses of a joint venture shall be 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.

Article 5. Each party to a joint venture may contribute cash, capital goods, industrial property rights, etc., as its investment in the venture.

The technology or equipment contributed by any foreign participant as investment shall be truly advanced and appropriate to China's needs. In cases of losses caused by deception through the intentional provision of outdated equipment or technology, compensation shall be paid for the losses.

The investment contributed by a Chinese participant may include the right to the use of a site provided for the joint venture during the period of its operation. In case such a contribution does not constitute a part of the investment from the Chinese participant, the joint venture shall pay the Chinese Government for its use.

The various contributions referred to in the present article shall be specified in the contracts concerning the joint venture or in its articles of association, and the value of each contribution (excluding that of the site) shall be ascertained by the parties to the venture through joint assessment.

Article 6. A joint venture shall have a board of directors with a composition stipulated in the contracts and the articles of association after consultation between the parties to the venture, and each director shall be appointed or removed by his own side. The board of directors shall have a chairman appointed by the Chinese participant and one or two vice-chairmen appointed by the foreign participant(s). In handling an important problem, the board of directors shall reach decision through consultation by the participants on the principle of equality and mutual benefit.

The board of directors is empowered to discuss and take action on, pursuant to the provisions of the articles of association of the joint venture, all fundamental issues concerning the venture, namely, expansion projects, production and business programmes, the budget, distribution of profits, plans concerning manpower and pay scales, the termination of business, the appointment or hiring of the president, the vice-president(s), the chief engineer, the treasurer and the auditors as well as their functions and powers and their remuneration, etc.

The president and vice-president(s) (or the general manager and assistant general manager(s) in a factory) shall be chosen from the various parties to the joint venture.

Procedures covering the employment and discharge of the workers and staff members of a joint venture shall be stipulated according to law in the agreement or contract concluded between the parties to the venture.

Article 7. The net profit of a joint venture shall be distributed between the parties to the venture in proportion to their respective shares in the registered capital after the payment of a joint venture income tax on its gross profit pursuant to the tax laws of the People's Republic of China and after the deductions therefrom as stipulated in the articles of association of the venture for the reserve funds, the bonus and welfare funds for the workers and staff members and the expansion funds of the venture.

A joint venture equipped with up-to-date technology by world standards may apply for a reduction of or exemption from income tax for the first two or three profit making years.

A foreign participant who re-invests any part of his share of the net profit within Chinese territory may apply for the restitution of a part of the income taxes paid.

Article 8. A joint venture shall open an account with the Bank of China or a bank approved by the Bank of China.

A joint venture shall conduct its foreign exchange transactions in accordance with the Foreign Exchange Regulations of the People's Republic of China.

A joint venture may, in its business operations, obtain funds from foreign banks directly.

The insurances appropriate to a joint venture shall be furnished by Chinese insurance companies.

Article 9. The production and business programmes of a joint venture shall be filed with the authorities concerned and shall be implemented through business contracts.

In its purchase of required raw and semi-processed materials, fuels, auxiliary equipment, etc., a joint venture should give first priority to Chinese sources, but may also acquire them directly from the world market with its own foreign exchange funds.

A joint venture is encouraged to market its products outside China. It may distribute its export products on foreign markets through direct channels or its associated agencies or China's foreign trade establishments. Its products may also be distributed on the Chinese market.

Wherever necessary, a joint venture may set up affiliated agencies outside China.

Article 10. The net profit which a foreign participant receives as his share after executing his obligations under the pertinent laws and agreements and contracts, the funds he receives at the time when the joint venture terminates or winds up its operations, and his other funds may be remitted abroad through the Bank of China in accordance with the foreign exchange regulations and in the currency or currencies specified in the contracts concerning the joint venture.

A foreign participant shall receive encouragements for depositing in the Bank of China any part of the foreign exchange which he is entitled to remit abroad.

Article 11. The wages, salaries or other legitimate income earned by a

foreign worker or staff member of a joint venture, after payment of the personal income tax under the tax laws of the People's Republic of China, may be remitted abroad through the Bank of China in accordance with the foreign exchange regulations.

Article 12. The contract period of a joint venture may be agreed upon between the parties to the venture according to its particular line of business and circumstances. The period may be extended upon expiration through agreement between the parties, subject to authorization by the Foreign Investment Commission of the People's Republic of China. Any application for such extension shall be made six months before the expiration of the contract.

Article 13. In cases of heavy losses, the failure of any party to a joint venture to execute its obligations under the contracts or the articles of association of the venture, force majeure, etc., prior to the expiration of the contract period of a joint venture, the contract may be terminated before the date of expiration by consultation and agreement between the parties and through authorization by the Foreign Investment Commission of the People's Republic of China and registration with the General Administration for Industry and Commerce. In cases of losses caused by breach of the contract(s) by a party to the venture, the financial responsibility shall be borne by the said party.

Article 14. Disputes arising between the parties to a joint venture which the board of directors fails to settle through consultation may be settled through conciliation or arbitration by an arbitral body of China or through arbitration by an arbitral body agreed upon by the parties.

Article 15. The present law comes into force on the date of its promulgation. The power of amendment is vested in the National People's Congress.

APPENDIX II

THE INCOME TAX LAW OF THE PEOPLE'S REPUBLIC OF CHINA CONCERNING JOINT VENTURES WITH CHINESE AND FOREIGN INVESTMENT*

Article 1

Income tax shall be levied in accordance with this Law on the income derived from production, business and other sources by any joint venture with Chinese and foreign investment (hereinafter called joint venture for short) in the People's Republic of China.

Income tax on the income derived from production, business and other sources by branches within or outside the territory of China of such joint ventures shall be paid by their head office.

* Unofficial Translation supplied by the Information Department of the Foreign Ministry, People's Republic of China.

Article 2

The taxable income of a joint venture shall be the net income in a tax year after deduction of costs, expenses and losses in that year.

Article 3

The income tax rate on joint ventures shall be 30%. In addition, a local surtax of 3% of the assessed income tax shall be levied.

The income tax rates on joint ventures exploiting petroleum, natural gas and other resources shall be stipulated separately.

Article 4

In the case of a foreign participant in a joint venture remitting its share of profit from China, an income tax of 10% shall be levied on the remitted amount.

Article 5

A newly established joint venture scheduled to operate for a period of 10 years or more may, upon approval by the tax authorities of an application filed by the enterprise, be exempted from income tax in the first profit-making year and allowed a 50% reduction in the second and third years.

With the approval of the Ministry of Finance of the People's Republic of China, joint ventures engaged in such low-profit operations as farming and forestry or located in remote, economically underdeveloped outlying areas may be allowed a 15-30% reduction in income tax for a period of 10 years following the expiration of the term for exemptions and reductions mentioned in the preceding paragraph.

Article 6

A participant in a joint venture which reinvests its share of profit in China for a period of not less than five years may, upon approval by the tax authorities of an application filed by the said participant, obtain a refund of 40% of the income tax paid on the reinvested amount. A participant which withdraws its reinvested funds within five years shall pay back the tax amount refunded.

Article 7

Losses incurred by a joint venture in a tax year may be carried over to the next tax year and made up with a matching amount drawn from that year's income. Should the income in the subsequent tax year be insufficient to make up for the said losses, the balance may be made up with further deductions against income year by year over a period not exceeding five years.

Article 8

Income tax on joint ventures shall be levied on an annual basis and paid in quarterly instalments. Such provisional payment shall be made within 15 days after the end of each quarter. The final settlement shall be made within 3 months of the end of a tax year. Excess payments shall be refunded by the tax authorities or deficiencies made good by the taxpayer.

Article 9

Joint ventures shall file their provisional income tax returns with the local tax authority within the period prescribed for provisional payments. The taxpayer shall file its final annual income tax return together with its final accounts within 3 months of the end of the tax year.

Article 10

Income tax levied on joint ventures shall be computed in terms of Renminbi (RMB). Income in foreign currency shall be assessed according to the exchange rate quoted by the State General Administration of Exchange Control of the People's Republic of China and shall be taxed in Renminbi.

Article 11

When joint ventures go into operation or when they change the nature of their business, change their address, close down, and make changes in or transfer registered capital, such joint ventures shall register with the General Administrative Bureau for Industry and Commerce of the People's Republic of China; and within 30 days of such registration, present the relevant certificates to the local tax authority for tax registration.

Article 12

The tax authorities have the right to investigate the financial affairs, account books and tax situation of any joint venture. Such joint venture must make reports according to the facts and provide all relevant information and shall not refuse to co-operate or conceal the facts.

Article 13

A joint venture must pay its tax within the prescribed time limit. In cases of failure to pay within the prescribed time limit, the appropriate tax authority, in addition to setting a new time limit for tax payment, shall surcharge overdue payments at one half of one per cent of the overdue tax for every day in arrears, starting from the first day of default.

Article 14

The tax authorities may, acting at their discretion, impose a penalty on

any joint venture which has violated the provisions of articles 9, 11 and 12 of this Law.

In dealing with any joint venture which has evaded or refused to pay tax, the tax authorities may, in addition to pursuing the tax, impose a penalty of not more than five times the amount of tax underpaid or not paid, according to the seriousness of the offence. Cases of gross violation shall be handled by the local people's courts according to law.

Article 15

In cases of disputes with tax authorities about tax payment, joint ventures must pay tax according to the relevant regulations first before applying to higher tax authorities for reconsideration. If they do not accept the decisions made after such reconsideration, they can bring the matter before the local people's courts.

Article 16

Income tax paid by a joint venture or its branch in other countries may be credited against the assessed income tax of the head office as foreign tax credit.

Where agreements on avoidance of double taxation have been concluded between the Government of the People's Republic of China and the government of another country, income tax credits shall be handled in accordance with the provisions of the related agreements.

Article 17

Detailed rules and regulations for the implementation of this Law shall be formulated by the Ministry of Finance of the People's Republic of China.

Article 18

This Law shall come into force from the date of promulgation.

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