

12-1-1989

# Foreign-Direct Investment from a Western Perspective

Kevin Hobgood-Brown

---

## Recommended Citation

Kevin Hobgood-Brown, *Foreign-Direct Investment from a Western Perspective*, 12 Loy. L.A. Int'l & Comp. L. Rev. 31 (1989).  
Available at: <http://digitalcommons.lmu.edu/ilr/vol12/iss1/7>

This Symposium is brought to you for free and open access by the Law Reviews at Digital Commons @ Loyola Marymount University and Loyola Law School. It has been accepted for inclusion in Loyola of Los Angeles International and Comparative Law Review by an authorized administrator of Digital Commons@Loyola Marymount University and Loyola Law School. For more information, please contact [digitalcommons@lmu.edu](mailto:digitalcommons@lmu.edu).

My plea, then, is for future symposia to provide us with more focus on the law in operation and context, set in the cultural matrix that alone gives it meaning.

## Foreign-Direct Investment From A Western Perspective

KEVIN HOBGOOD-BROWN\*

Over the last ten years, there has been a tremendous explosion of laws and regulations promulgated in China relating to foreign trade and investment. This article discusses some of these legal developments, commenting on some of the business implications from a Western business perspective.

One of the recent developments that the western business community in China views very favorably is last year's passage of the Contractual Joint Venture Law. Finally, after approximately seven thousand of these contractual joint ventures had been approved over the last seven or eight years, China had a law which lent some credibility and predictability to this very popular form of doing business. This was a very positive and eagerly awaited development.

In addition, new rules have recently been promulgated for the arbitration of international trade disputes under the China International Economic and Trade Arbitration Commission. This commission is an arbitral body under the China Council for the Promotion for International Trade. Some of the most significant developments embodied in these new rules are: (1) for the first time, foreign arbitrators are able to sit on the arbitral panel; and (2) the fee schedule is now staggered (this will make a difference where larger disputes are the subject of arbitration). The new arbitration rules are an important development which I think will encourage the resolution of international trade disputes in China.

The Equity Joint Venture Law was passed in 1979. Presently, the Chinese government is considering whether it should expand the law to include something called a "joint stock company." The characteristics of a joint stock company are unknown at this time, but are eagerly awaited by the foreign business community. There is also talk

---

\* Attorney at Law, Graham & James, San Francisco, California.

of revising the Equity Joint Venture Law to permit a foreigner to be appointed the chairman of the board of directors of an equity joint venture. Under the current law, the chairman must be a citizen of the People's Republic of China.

Finally, there is a proposal to consolidate the income tax laws for the equity joint venture and the foreign enterprise income tax laws. This will be a positive development. It will lend a much needed degree of consistency to the application of the tax laws and will also result in a tax reduction for foreign enterprises and wholly foreign-owned enterprises doing business in China.

We anticipate that a copyright law will be proposed and passed within the next twelve months. This could be very important to American high-tech investors doing business in China. Also, we expect there will be regulations concerning software protection. Although the most recent drafts of these proposed regulations have not been made public, I understand they will prohibit the illegal copying, plagiarism or sale of software. This is another development that is eagerly awaited by the western business community.

On a bilateral government level, Americans have been waiting for a bilateral investment treaty. A draft bilateral investment treaty has been discussed for a number of years, and only a few disputed issues remain. The American side has insisted on enumerating a set of discriminatory practices which would be prohibited by the treaty. Additionally, it has insisted that the treaty make some reference to a minimum standard of international practice with regard to investment protection. I think the parties are now fairly close together on these issues, and we should see some positive movement next year.

We also hope to see further improvement in the development of China's overall legal system. For example, improvement is needed in the dissemination of new laws and regulations. When China promulgates new laws and regulations, there is no immediate notice available to either the foreign community or to the Chinese bureaucrats responsible for implementing the laws and regulations. Some measures have been taken to improve this situation, but I think a greater effort is required. Second, there must be a greater effort to actually implement the laws and regulations already passed. Foreign businesspeople frequently find that as they go into negotiations or approach a Chinese agency to address problems, the people they deal with are unaware of these new laws and regulations. Improved internal education with the

various agencies and departments charged with implementing the laws and regulations is necessary to correct this problem.

Finally, one of the hallmarks of the Chinese system is that a certain degree of flexibility is built into it. Foreign investors always welcome flexibility, so long as there is predictability in the system as well. But, I think that at the lower levels of bureaucracy, there is a reluctance to be flexible in implementing laws in some areas, i.e., tax laws. This is another area where we hope to see some improvement in the near future.

From a Western perspective, there are other areas of concern to watch in the future. The first is foreign exchange. Without oversimplifying the problem, there is a greater demand for foreign exchange in China than there is a supply. Over the past several years, a number of laws and regulations were created to try to bring some logic and consistency to the allocation of foreign exchange in China, and to make sure foreign exchange is used wisely. Some regulations were designed to allow a greater degree of flexibility in allowing designated foreign investment enterprises greater access to foreign exchange. Specifically, technologically advanced enterprises and enterprises engaged in import substitution projects will continue to receive preferred access to foreign exchange. We welcome this in the Western business community.

Another positive development is the proliferation of currency swap centers. These centers, established in all of the major Chinese cities, permit both foreign investment enterprises and domestic Chinese operations to swap Renminbi for foreign exchange. The exchange rates can be very high. Rates have gone as high as eight Renminbi to one U.S. dollar; this is quite a bit off the official exchange rate. The positive element here is that this system provides some relief for a foreign investment enterprise when foreign exchange is not available from more official channels.

Labor continues to be an important factor for foreign-direct investment in China. Labor is one of the most complicated areas in which foreign-direct investment has had difficulties integrating into the existing Chinese economy. The labor system and labor management techniques that most foreign investment enterprises choose to use in China are quite different from those practiced in China over the last forty years. A number of laws and regulations have been promulgated on the national and local level to set guidelines for labor management. Many of these laws and regulations reiterate the principle

that foreign investment enterprises should have autonomy in their hiring and firing of employees and in the maintenance of the disciplinary systems within their organizations. Many enterprises have had difficulty applying this principle. As a result, a number of labor dispute cases involving the firing of employees and the attempted hiring of employees from state-owned enterprises have been arbitrated in Shanghai, Guangzhou, and Beijing. Recently, the Shanghai Intermediate Court upheld for the first time the right of a foreign investment enterprise to fire an employee for cause.

Finally, two areas are often overlooked in legal discussions of trade and investment in China, but which, from a businessperson's perspective, are probably the most important. The first is the development of the infrastructure of the country: communications, transportation, and sources of supplies, raw materials and energy sources. Frequently, foreign investors have negotiated good contracts for themselves, yet have ended up facing huge operational problems due to a lack of infrastructural support. For example, an inability to get raw materials to the factory or to get a consistent power supply is such an operational problem. Although the Chinese government has made concerted efforts to address these problems, all foreign investors must be aware that it takes a long time to solve these kinds of fundamental problems.

The second area is the foreign businessperson's awareness of the cost/benefit analysis of investing in China. Notwithstanding the improved laws and regulations and the support structures created to encourage foreign investment and economic development in China, if foreign businesspeople cannot make a profit and repatriate that profit, they will not invest in China. This fact of business life was insufficiently acknowledged by the Chinese government in the early 1980s. Recent events have indicated that the government is becoming sensitive to this fact, and will take steps to create an environment where foreign businesses can realistically achieve their business goals.