OCCASION

This publication has been made available to the public on the occasion of the 50th anniversary of the United Nations Industrial Development Organisation.

DISCLAIMER

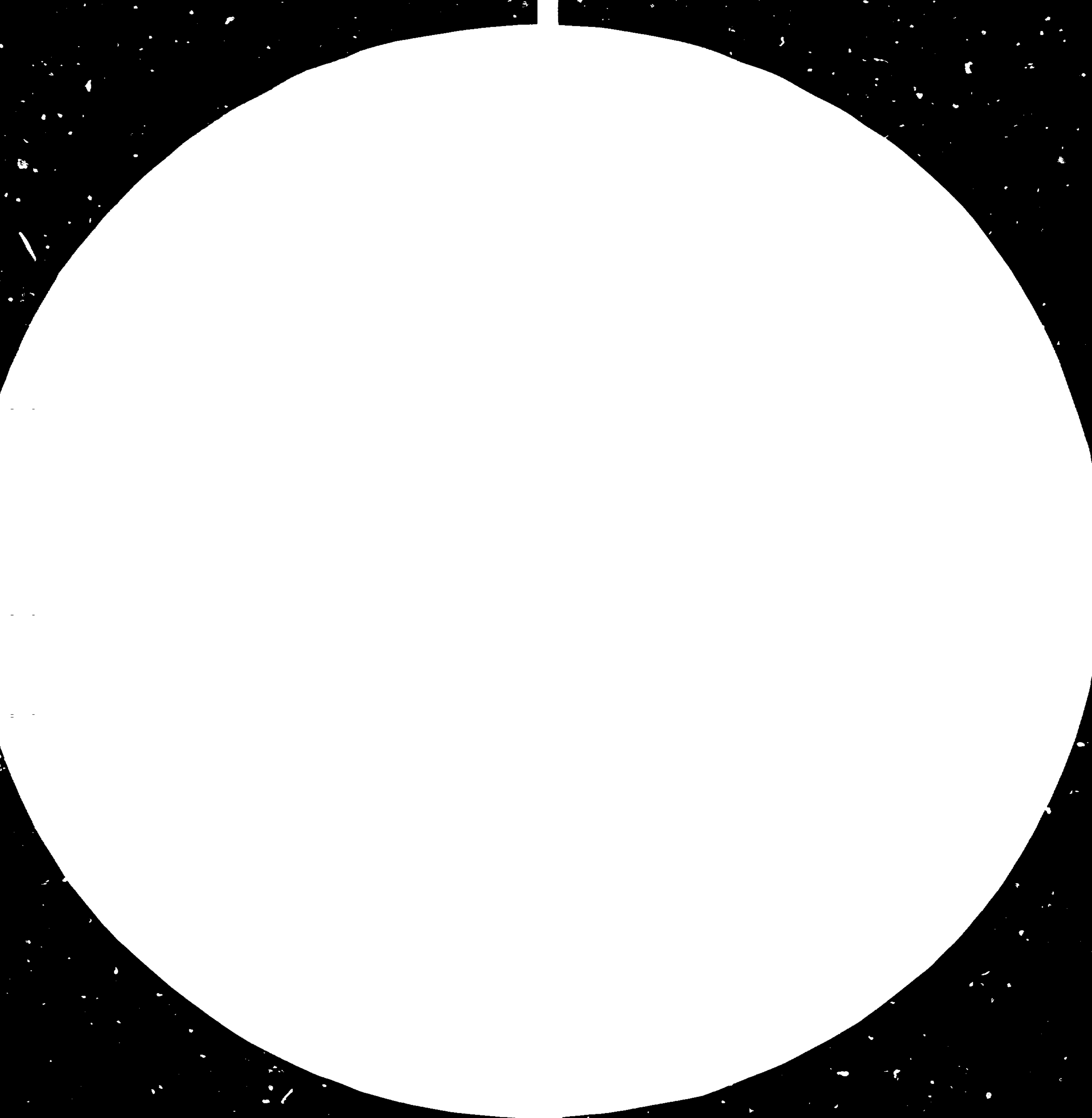
FAIR USE POLICY

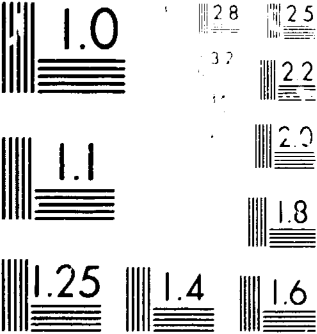
CONTACT

Please contact publications@unido.org for further information concerning UNIDO publications.

For more information about UNIDO, please visit us at www.unido.org

UNITED NATIONS INDUSTRIAL DEVELOPMENT ORGANIZATION
Vienna International Centre, P.O. Box 300, 1400 Vienna, Austria
Tel: (+43-1) 26026-0 · www.unido.org · unido@unido.org




1.0
2.8
2.5
2.2
1.1
2.0
1.8
1.25
1.4
1.6

11299

Distr.
LIMITED

UNIDO/IO.493
10 March 1982

ENGLISH

UNITED NATIONS
INDUSTRIAL DEVELOPMENT ORGANIZATION

CONDITIONS AND OPPORTUNITIES FOR FOREIGN INVESTMENT COOPERATION IN CHINA*

Based on the report of A. Mohr, consultant
Investment Co-operative Programme Branch

* This document has been reproduced without formal editing.

V.82-23351

CONTENTS

CONTENTS (continued)

A. INTRODUCTION

The following brief summary constitutes an introduction to the paper "A Report on Foreign Investments in China" which was prepared early in 1982 by Mr. A. Mohr, a UNIDO Consultant. The paper is an attempt to explain to the potential investor, entrepreneur or interested person, the nature and the meaning of China's present economic policies, and to indicate the opportunities presented to the foreign investor who possesses the far-sightedness to contemplate the gigantic possibilities of this market of over 1,000 million people with its enormous and largely untapped resources and its vast industrial potential.

A.1 The Economic Situation

China's economic development will develop along the lines of the country's readjustment policies which, although principally directed towards national reliance, have accepted the need for a degree of international business activity within China in defined fields, and particularly in the context of modernization of China's industry by admitting foreign investment and industrial participation. As a means of reaching internationally acceptable standards and thus of offering her own products as a serious competitor in the world's export markets, China needs above all to acquire first rate foreign technology, and know how, and to benefit from foreign scientific co-operation.

In pursuit of this policy the first priority has been given to those co-operative projects which are judged to provide a catalyst for the most urgent sectors of national economic development. Thus the rehabilitation and improvement of the national infrastructure - energy related projects including exploration and exploitation of new sources of energy, transport and communications, etc. and the activation of new light and consumer-product industries are particularly important. Quantity production is not the sole aim; such factors as competitive quality, modern design, and product range are considered equally vital.

A foreign investor would err were he to see China solely as an easily accessible business market. What he will gain is early access to a process of national economic development, in which he may find unique opportunities for satisfactory and mutually beneficial long-term participation.

A.2 The Legal Situation

The national effort to modernize the economy and to ensure a sufficient flow of foreign exchange permits six main fields to operate in which foreign investment and co-operation are welcomed:

1. Export processing, in which the foreign partner supplies the raw materials and/or semi-finished articles and the Chinese partner undertakes the manufacturing processes under instruction.
2. Compensation trade, by barter trade or "buy-back".
3. Co-operative production whereby the foreign partner supplies equipment, technology, machinery, and licenses, but no equity, and is compensated by foreign currency or with "buy-back" goods.
4. Joint ventures in which there is a foreign equity partnership of at least 25 per cent in the form of a limited liability company, but no other limitation.
5. Joint operations which are akin to joint ventures, but combine equity and production partnership.
6. Resident offices which may be established with the permission of the relevant Chinese authority.

These forms of co-operation are described in greater detail in Section 3 of the report, q.v..

Although a Company Law is said to be in the course of preparation no legislation covering co-operation with foreign companies yet exists in China apart from the Joint Venture Law (see Section 3.5 of this report), under which the Chinese Government is obligated to protect the foreign investment while placing no limit on the venture's activities. There is, however, no legally assured protection of foreign property and no provision for compensation in case of nationalization or expropriation. When a company is wound up, however, and once the legal and contractual obligations have been met, Foreign Exchange Regulations permit the repatriation of both profits and capital.

In China the management of a Joint Venture should consist of a Board of Directors, the Chairman of which should be Chinese, supported by a president and vice-presidents or a general manager and his assistants.

The average wage of workers, in state owned enterprises, in 1980 was about Yuan 300 monthly, but wages are known to be escalating throughout China. Of tax legislation, the most relevant to this paper are the Income Tax Law covering Foreign Enterprises, dated 1 January 1982 and the Individual Income Tax Law of 10 December 1980.

In China the net income derived from production, business or any other source for any enterprise or economic organization constitutes its taxable income, which is taxed at rates variable between 20 and 40 per cent plus a 10 per cent surcharge for local taxes; although in certain circumstances foreign enterprises can qualify for tax holidays or tax reductions. Arrangements exist for the carrying over of business losses to the next tax-year over a maximum of five years.

In individual taxation, a difference is made between those who have been resident in China for less than one year, and those whose residence exceeds that term, the latter being subjected to Chinese income tax on the whole of their income wherever it may have been earned, although some adjustment is now possible to allow for double taxation (see Sections 5.4). Taxation rates vary between 5 and 45 per cent, while income from royalties, interest, copyright etc. is taxed at a flat rate of 20 per cent.

At present the tax laws offer no incentives for re-investment although some inducements are written into the Joint Venture Law, an anomaly which requires clarification.

A.3 Special Economic Zones (SEZs)

These have so far been established only in the Guangdong and Fujian Provinces where, in common with SEZs planned for the future, special incentives will be offered to foreign companies in the form of a low (15 per cent) rate of income tax, preferential tax treatment, a waiver of some import duties, and a degree of company control over staff recruitment and dismissal.

General

Legislation for the protection of industrial property rights is now in draft, although a degree of such protection can be assured at present by the inclusion of such protection in the terms of agreements and contracts concluded with Chinese partners. Some legislation concerning the registration of trade marks has existed since 1963, granting a degree of trade mark protection over a period of ten years to foreign investors. In general it may be said that the Chinese Government is now taking steps to create in China a modern and broad-ranging body of economic legislation.

1. FOREIGN INVESTMENTS IN CHINA

1.1 Domestic Development

Any review of China's economic development between 1978 and 1981 must take into account the change in public attitude which emerged with the adoption of a new constitution in March 1978 in replacement of the earlier one of January 1975 with its insistence on national self-reliance. The initial reaction to the change was an eagerness to seek assistance from other countries; a trend which was lent force by the economic policies adopted in December 1978 which called a priori for greatly increased expenditure to raise the people's living standards, but failed to restrict other capital expenditures accordingly. The inevitable results were increased costs of administration, an increase in the money supply, and an escalation of prices. Revenues dropped below expenditure, leading to the massive financial deficits of 1979 and 1980 which, without rigorous counter-measures, threatened to get out of control.

At a working conference of China's Central Committee of the Communist Party held in December 1980, the decision was reached to revise the 1981 National Economic Plan by progressive steps thus ensuring (a) a balance between State expenditure and revenue and (b) price stability. To improve and restructure the national economy, which was simultaneously badly affected by stagnation in the oil sector, ten principles were adumbrated calling, inter alia, for accelerated and science-oriented agricultural development, priority for the consumer goods industries, a re-orientation of heavy industry towards the services sector, the preference for labour-intensive over capital-intensive technology, a better utilization of energy, the encouragement of the energy and transport industries, and a logical and graduated introduction of industrial key units without neglecting established enterprises. Essentially, this has meant an end of pandering to public demand; and has redirected the emphasis of investment from heavy industry towards new light industries with high export potential, involving a reliance on

Western management techniques and services. This continuing process of modernization involves considerable retrenchment and expansion, sometimes even requiring an abandonment of projects which are not urgent or which strain the country's capability. The resulting reduction of imports ought not to be taken to indicate a retreat from China's "Open Door" policy, but a decision to preserve foreign exchange reserves by a process of import substitution: a high degree of internal self-reliance has now become the keyword for long-term success.

The following summary indicates progress to date in the main economic sectors:

(a) Agriculture. This industry which has always been the mainstay of China's economy is receiving special attention. Research into agricultural sciences and techniques, e.g. land reclamation is being actively encouraged; and during 1979 and 1980 grain production reached higher levels than ever before. Similarly, there have been dramatic success in the production of cotton and in oil-bearing and sugar-yielding crops; while with assistance from rural people on a self-help basis, there have been notable extensions in the forestry, animal husbandry and forestry sectors.

(b) Light industry. Here stress has been laid on the production of consumer goods; and well designed textiles and household durable articles are now much more widely available in greater quality and variety than previously.

(c) Heavy industry has been given particular attention, with production of overstocked and unessential items being curtailed with a commensurate saving of energy. Heavy industry has been increasingly service-oriented, while the capital input has been reduced with investment being diverted to light industry, transport and communications and the energy sector.

Social conditions are being improved with an increase of housing, public health facilities and cultural activity. Corresponding rises in the wages of workers and executives have been accompanied by improved industrial regulations and discipline, while tax and customs collection have been strengthened and tax-evasion discouraged.

In China, the availability of a large workforce makes the adoption of expensive automation unnecessary except where a clear advantage can be discerned. Outdated and energy-intensive production facilities and technologies are being reexamined in order to conserve power, especially in the eastern and north-eastern areas of China which suffer from energy shortage. The national economic weakness in the transport and energy sectors is well understood, and their development as related subjects is in hand.

For the future, China will be seeking foreign co-operation in the modernization of the economy, but will nonetheless place the main stress on the use of its internal resources. The need to control population growth, too, is seen as a crucial national task, and China will enrol both public information and education, and scientific research into a family planning initiative in its aim to restrict the national population to 1,200 million by the end of this century.

1.2 Foreign Investment and Co-operation in the Period 1978–1981

The stress placed by China on reciprocity in foreign trade relations and on a more flexible business approach involving methods other than direct trade will thus be clear. Compensation, barter and buy-back deals, export processing and co-operative manufacturing are increasingly favoured, although the risks implicit in compensation and barter trade, unless shared with an experienced partner, and confined to familiar trading commodities, are high. In joint ventures too, the interest of the foreign partner must be recognized, even though the venture operates in China and is subject to Chinese law; as much foreign investment in the past has been deterred by lack of legal protection.

China's re-adjustment policies, which have led to the cancellation of many projects and contracts, have provoked criticism from foreign trading partners, especially Japan and the EEC countries, over recent years.

Many companies in the light industrial field, however, have been successful. One Japanese company, for example, has not only gained a foothold in the expanding TV market but stands to benefit from technological spin-offs in the fields of hospital tomography and integrated circuits for computers; while French firms have concluded licensing agreements for the sale of know-how in communication and microcomputer technology, and American firms have taken a more cautious approach with possibilities of buy-back, licensing, counter-trade and even equity arrangements.

1.3 China's Experience with Foreign Investment

There is little doubt that despite some loss of confidence provoked by China's retrenchment, the plethora of foreign investment regulations of the past few years indicates a deepening of the country's commitment to the continuing presence of foreign business there. The need to take into account differences in culture and business approach when concluding business agreements is becoming recognized, the Chinese on their part having to accede to the Western practise of written definition and documentation of the entire agreement in place of their traditional reliance on goodwill and probity of partners. Terms of agreement need very careful definition. Such concepts as failure by "Force Majeure", e.g. by strike action, which the Chinese do not understand, or interruption by "Act of God", inexplicable to a non-believing communist society, are not universally acceptable. The advantage implicit in flexible business arrangements such as local processing and assembly, compensation trade, joint ventures and co-operative production are attractive to a country eager for economic readjustment and modernization, especially when payment is to be by buy-back of products, counter purchase or compensation.

2. THE ECONOMIC SITUATION

2.1 General

The Chinese economy is still in a phase of adaptation and transition, as may be seen from the 1981 statistics. Despite the improved trade performance, the deficit for 1981 of Rmb 2.7 comparing favourably with the figures of 12.7 and 17.06 billion for 1980 and 1979, the hoped-for drop in prices did not occur.

An important contribution to effective business has been the granting to foreign firms in the Special Economic Zones (SEZs) the right to recruit and discharge workers, and to involve them in wage negotiations, since this has an immediate effect on the maintenance of a well-trained and disciplined workforce. Previously, no such right existed. As a result of the decrease in capital construction projects, surplus labour has become a major problem and many unemployed workers are now being enrolled in vocational training schemes or directed to farm or infrastructure jobs. In the Fujian SEZs there is a particular need for the introduction of foreign investment in labour-intensive projects, as skilled manpower is abundant.

Overall the population growth rate in China is probably falling, but in absolute terms the population is expected to continue for some time to increase by some 10-11 million per annum. Urban population is about 14 per cent of the whole.

Two principal factors which influence the feasibility of foreign co-operation in projects are the development of suitable infrastructure and the availability of adequate energy resources. In both these sectors China is making considerable efforts to identify available foreign investment funds, low-interest credit, and appropriate technical know-how.

In particular the development of an adequate infrastructure has called for over-riding priority, huge modernization programmes being foreseen in the transportation field railways, roads, aviation, waterways, ports and shipping which like tourism and communications badly need up-to-date technology and equipment, only available outside China.

The present energy crisis presents a serious problem for China where petroleum production has declined below target level to a degree that even exports to Japan have been curtailed. The spectre of being forced to depend for oil on world markets, however, has been reduced by a timely discovery of new petroleum reserves in the South China Sea and Yellow Sea areas. Tenders from foreign firms for exploration and exploitation have already been invited.

Of the other energy sources, coal and water power are both unevenly distributed. About 70 per cent of all coal mining is concentrated in the north-east of the country at present, although there are plans to develop small mining operations throughout the country in order to reduce transporation costs. There are plans for foreign participation both in coal mining and the manufacture of mining equipment, but it is accepted that in any event the output of coal, like oil, will increase only gradually. Some relief may follow from the exploitation of alternative sources - natural gas, casing-head gas, shale oil, etc.- but no major contribution is anticipated.

In the field of electricity generation, China's thermal powered plants have proved more efficient than its more numerous hydro-electric stations, over 75 per cent of electricity being thermally produced. The country, nevertheless, remains deficient overall in supply of electricity and does not possess a modern integrated supply system at present.

The situation naturally stimulates a demand for nuclear power generation, but as with oil projects this requires prior approval by the Central Government. The question is urgent, however, because coal promises to continue in short supply after 1985 while oil supplies are dependent on the exploitation of new resources.

2.2 Economic and Industrial Sectors

Mining and exploration. China possesses large resources of most basic raw materials needed for iron and steel production, since except in

Guangdong and Fujian coking coal, iron ore and limestone are widely distributed and there are adequate resources of alloying materials - manganese, molydenium, tungsten and vanadium. Much of the coal and iron ore, however, is of low quality requiring careful preparation while there is a shortage of some alloy minerals, e.g. cobalt, chromium, nickel, and of steel scrap. Only about 3 per cent of China's coal is suitable for coking, about 80 per cent having a very high ash content and difficult to concentrate. Of the coking coal, over 50 per cent contains sulphur and is difficult to work, while the large iron ore deposits generally provide low grade ore, although some high grade material is available.

In fact the extent of China's resources of coking coal is unknown and the need for further exploration is likely to remain a priority task for sometime. Prospects appear best in the very broken terrain of the south-west region and in the far west and north-west where rugged natural conditions alternate with desert areas. Large uranium deposits have already been found in the north-west region. Modern equipment is badly needed.

Of other minerals the metallic varieties may be listed first. There are widespread resources of poor quality bauxite, and along the Xiang and Yuan rivers in Hunan the world's largest antimony reserves are to be found. Bismuth, too, exists on a large scale. Important reserves of copper, mainly porphyritic, exist at a considerable depth, but smelting facilities for the metal constitute a major bottleneck and China is anxious to locate the appropriate know-how. There are major lead deposits, with workings, in Hunan, Liaoning and Guangdong; and the world's largest known manganese reserves are virtually confined to the production of steel within China. Mercury like molybdenum is a major product, some being exported, whereas nickel reserves are minor and insufficient for internal demands.

China has large reserves of tin but appears to be in need of tin-plating equipment since it imports tinplate from Japan; and a somewhat similar lack of facilities may be observed with regard to titanium. Of the tungsten produced, about one third is reserved for internal use. The uranium reserves are said to be sufficient, but the necessary technology for ore processing, gaseous diffusion and electromagnetic separation plants has already been acquired.

Of precious metals, it appears that there is enough silver for internal needs although gold and platinum are lacking.

In the non-metallic minerals field, China has deposits of asbestos, barite, borax, diamonds, steatite, talc, prophyllite, pyrites, feldspar, quartz, vermiculite, magnesite, rare earths, granite, gypsum as well as adequate and widespread deposits of clays, lime, building stone, sand and gravel.

From this review it may be seen that a very wide range of mineral deposits exists, some of them of international significance and some quite small or relatively unexplored. The situation indicates a need for foreign assistance, and the Chinese appear to be contemplating some forms of joint venture, etc. to tackle the situation.

Heavy industry. This is now in the process of re-adjustment and in 1981 an output reduction of 5 per cent compared with the previous year was recorded. The planned re-orientation of much heavy and defence industry towards production of durable consumer goods, where practicable, and export items is under way, and simultaneously a larger sector of heavy industry is being committed to the provision of services to light industry and agriculture. This involves a technical transformation and originality in the design and manufacture of new equipment suitable for application in infrastructural projects, e.g. transport and energy, and assistance in the training of proficient personnel.

Light industry. The emphasis on production of goods for everyday consumption has led to a marked rise in national production, the 1981 value of textiles and light industrial output having increased by about 12 per cent over the previous year's total. Priority status is awarded to virtually any light industrial initiative concerned with raw and semi-finished materials, energy or capital construction, technical innovation, transport and communication services or imported technology, or which involves the legitimate use of foreign exchange and bank financing.

The foreign investor will probably see his best prospects in small-scale or medium sized projects, probably labour-intensive, producing consumer goods in demand both within China and on the world's export markets. Existing joint ventures in China will experience a far higher internal and domestic demand for their products than was previously planned or anticipated.

Engineering. With the process of industrial modernization, the Chinese demand for machinery products will continue to expand for at least the next few years, as China seeks to acquire sophisticated equipment from abroad.

In general, China is able to provide its own railway locomotives (except electric), most textile machines, small and medium lathes of moderate precision, small and medium electric motors, a range of electrical equipment, moderate-sized power stations, metallurgical plants, cement and chemical works and coal mines. It experiences problems both of range and volume in producing test equipment, motor vehicles, aircraft, organic chemical and petrochemical equi[illegible] large snips and their engines, mining equipment, and muc[illegible] d it is in these items which represent perhaps 20 per cent of the whole industrial range, which China needs to import along with the related spare parts. Import is also needed of a range of equipment in which Chinese technology is unduly low, and where the readjustment process demands increased technical know-how in the indigenous personnel.

The engineering industry in China as elsewhere is not a compact entity,yet it is possible here to indicate individual branches which may be of particular interest to the foreign investor. In the railway field, for instance, China's factories can maintain and expand their vehicle stock, but nevertheless foreign participation in major expansion projects and production of the most modern locomotive types is welcome. China has recently imported large diesel units and has been in contact with foreign suppliers regarding electrification and modern traffic control systems. The expansion of trade itself has stimulated interest in shipbuilding and aviation, and the acquisition of know-how and of manufacturing licenses is of interest. Chinese agricultural machinery is not yet up to international standards, even though it is adequate for China, but here the need is for labour intensive methods rather than automation. In the fields of power generation, textile machines, mining, metallurgical, petroleum and chemical equipment, instruments and meters China is normally self-sufficient, but modernization programmes will indubitably call for imports.

The motor vehicle industry is defective in the quantity and quality of its products, and heavy lorries have been imported for many years. The world economic situation has recently directed the interest of most major western vehicle makers to China, and the French Peugeot Group has been involved in discussions preparatory to building in China both luxury vehicles for the tourist traffic and uncomplicated rough-terrain vehicles, simply constructed and maintained. The original highly-automated production plans have now been abandoned in favour of a more modest, labour-intensive plant to be operated as a joint venture with a view to export some vehicles. In the radio and electronics field, a flexible approach of this kind appears advisable for foreign entrants. A Hong Kong subsidiary of a British Company, Gestetner International, which produces reprographic equipment has discerned business opportunities in China's stress on education and vocational training, while the U.S. Foxboro Company which makes instruments and systems for process control has not been deterred by China's recent economies, since it seeks a long-term penetration of the vast future market. The demand remains buoyant for material handling equipment, cranes, loaders, lifts, etc., as also for pure consumer appliances such as bicycles, domestic machines, refrigerators etc., all items which are certain to be produced on a large scale to satisfy public needs. It is for the foreign businessman to evolve investment opportunities which do not prove too onerous for China's reserves of foreign exchange.

<u>Consumer products</u>. Economic retrenchment notwithstanding China's main trading partners, Japan, USA and the EEC countries, may rely on the gradual expansion of trade in farm and manufactured products which by 1980 accounted for half the country's total trade.

In China there is a long tradition of textile manufacture, but with synthetic fibres there was a reliance on imports, a trend which has been reversed with the introduction of petrochemical plants bought from abroad as is shown in figures of trade, especially with Japan. Textile exports now exceed imports, and this trend will increase as quality and variety are enhanced by more sophisticated techniques.

By 1981 output of durable consumer items, e.g. watches, bicycles, TV sets, electric appliances, sewing machines, etc. had increased impressively ; production of major lines like cotton yarn and cloth, synthetic fibres, sugar, paper, cigarettes, etc. had reached or exceeded the planned 8 per cent growth targets.

The import of complete production units of the above items is no longer feasible in the period of re-adjustment, but the demand for some technology and equipment for textile and synthetic fibre production, as for many other items remains. The indication is that the foreign businessmen still has the opportunity to enter into the modernization programmes in food processing, canning and preservation industries, as into the cosmetics, paper products and other sectors. For the Chinese, their highly valued handicraft exports, bamboo and straw goods, curtains, cushions, tapestries, ceramics etc., will continue to expand.

<u>Oil refining, petrochemicals, pharmaceuticals, chemicals</u>. China's technical level is from 10 to 15 years behind western standards, so transfer of technology is still essential. Petrochemical production usually covers plastics, synthetic fibres and their intermediates, and nitrogen fertilizers; while production of pharmaceuticals is predominantly in small-scale plants and workshops, industrial development having assumed a different form from the usual western pattern, so that some industrial stimulus could still prove valuable.

China appears to be particularly good in producing antibiotics, and to be strong in fermentation and biochemicals while less so with chemically produced pharmaceuticals like the sulfa drugs. Packaging is poorly developed and modern ampoule, tablet and capsule-producing machinery is lacking, although the prospects for imports are probably poor in the face of tradition.

The chemical fertilizer industry is advanced, but there is probably room for single plants demonstrating new and useful technology, as for compound fertilizers, granulation towers and modern packaging.

In regard to other chemicals the abundant supplies of salt have ensured a developed alkali industry, while the production of heavy chemicals, dyestuffs, detergents, insecticides, etc. are probably adequate. High quality consumer chemicals with modern packaging is a promising field, and in cosmetics, the Japanese and, more recently, the Italians have recorded sucess. From this brief review it may be seen that China's consumer-oriented policy offers great opportunities.

Construction industry. Although there is no immediate scope for high cost initiatives, opportunities do exist for co-operation with Chinese construction organizations working in Third World countries outside China. The Chinese have already expressed their readiness to act as members of a consortium or to sub-contract on a labour only basis in the certainty that their low costs of labour would be attractive. A Japanese contractor is already using a Chinese team for hospital construction in Iraq.

The construction technology and civil engineering sector, particularly in road building, is another potential field for the foreign investor, especially because projects of this sort often lead to sales of plant and equipment as a spin-off, and to opportunities to supply high quality building materials. In general, although the Chinese will normally exploit their own technical knowledge before seeking foreign assistance, the main opportunities for investment in the construction sector are in infrastructure projects.

2.3 Promotion of Joint Ventures and Other Forms of Co-operation

This report has indicated strongly that the Chinese market will be important for many years to come, but it should also be said that the process will be continuous and not one of sudden spurts. The far sighted observer should therefore not be misled by the apparent re-orientation of Chinese policy. China has learned the dangers of building heavy, capital intensive industries on an inadequate infrastructure, and has tried to balance its imports by developing and selling its own resources and technology and thus to avoid serious indebtedness. The economy cannot be expected to grow rapidly during the current Sixth Five Year Plan, which is deliberately aimed at economic readjustment, but accelerated development may be expected from the Seventh Five Year Plan and, thereafter, and a surge of economic strength may be anticipated from the last decade of the present century onwards. At the present time China must be regarded as a potentially rich developing country whose vast resources have so far been barely tapped.

The foreign countries operating in China are well advised to lay the groundwork for their future by maintaining a moderate presence in the country now, and to establish a presence by such means as participation in fairs and exhibitions, by the dissemination of product information and bulletins, and by maintaining close contact with the market, possibly by employing representatives.

Selling to China during the early 1980s when the country will certainly maintain a very tight control over its foreign exchange, will call for a high degree of imagination and flexibility; and earnest consideration will have to be given to the scope for deals involving payment in kind. International companies will need to keep their entire operations under review to determine how raw materials or manufactured products from China accepted in return for machinery or know-how can be marketed outside the country.

China's international contacts have increased very considerably in recent times, and the country has been very active in questions of relevant legislation and jurisdiction, economic courts having been established at most levels. A state of legislating flux persists, however, and still greater efforts are needed.

2.4 The Sixth Economic Plan, 1981-1985

Although this plan was adopted officially in December 1981, its contents have not been made known to date (15 February 1982).

3. PRESENT FORMS OF CO-OPERATION AND FOREIGN INVESTMENT

3.1 Basic Policy

China's economic policies have as a major objective the penetration of world markets by Chinese products, and thus to strengthen foreign exchange reserves by an increasing rate of export. The policy inevitably calls for early access to the best modern technologies and know-how over a vast range of fields including industrial design, marketing, management etc., leading logically to a preference for those foreign enterprises which are in a position to contribute promptly the appropriate technologies and know-how, embracing where possible trade-marked products. The intention appears to favour new forms of industrial co-operation over the traditional trade pattern of goods against monetary payment.

At this point it may be useful to summarize the basic features of China's economic policy:

(i) The modernization of existing plant and equipment; the acquisition of modern equipment for industry and agriculture ; the exploitation of mineral resources.

(ii) The training of the workforce at all levels including specialist and management personnel. Introduction of modern management techniques.

(iii) The acquisition of up-to-date technologies, patents, licenses and trade marks.

(iv) The amassing of a foreign exchange surplus.

(v) The attraction into China of foreign investment.

In the context of these policies the following categories of foreign involvement have developed in China since 1978:

Export processing and trade processing
Compensation trading
Co-operative production
Joint ventures
Joint operations

None of these are exclusive, since an amalgam of two or more forms is possible.

Legal regulations

Apart from the tax laws which are common to all corporate earnings within the PRC, specific regulations have so far been issued to cover joint ventures only, leaving a degree of uncertainly as regards the other forms of co-operation. At present the rights and obligations of contracting parties in an industrial co-operation other than a joint venture must be stipulated in the relevant contracts or agreements, although a Company Law is now in the course of preparation.

3.2 Export (trade) Processing

Briefly this may be called the manufacture of a product or products on behalf of a foreign employer under a fixed salary or fee.

The foreign partner supplies the raw materials or, in some cases, the semi-finished products together with components, packaging materials etc., leaving the Chinese partner to manage the production process in accordance with the instructions and specifications supplied to him by the foreign partner. Payment is made on a fixed scale related to the production level. In principle, it is for the Chinese partner to provide the equipment, machinery and means of production although this may sometimes prove impossible, when machinery must be imported; the cost being adjusted within the fee paid. It is normal for imports of raw materials, semi-finished products, components etc. to be exempted from import taxes and customs dues, but care must be taken to ensure that the final products are then exported and not diverted to the internal market.

The advantages of this system lie mainly in the very low labour costs when compared with production elsewhere, and to the Chinese side the creation of jobs, the introduction of modern designs and ideas, and the accretion of foreign exchange.

Plans exist for about 6,000 small to medium-sized export processing projects, mainly to be established in the SEZs, of which about 70 per cent will produce goods on behalf of partners in Hong Kong or Macao, and 20 per cent for firms in Japan. Income from processing projects over the years 1979/80 is estimated at US$ 100 million per annum.

3.3 Compensation Trade

This term covers both barter and buy-back arrangements. In barter trade, sometimes known as "indirect compensation", the provider of the industrial plant receives his payment in full or in part by means of other products than that produced from his machinery, and this he has to sell usually through compensation dealers. Delivery of goods is usually at the place nominated for payment. In buy-back deals, the payment or part payment is made by deliveries of the produce of the provider's own plant or equipment. Buy-back trade is otherwise known as "direct compensation".

"Compensation Houses" usually comprising interested banks or commercial firms specialize in the selling of barter goods, taking over the task against payment of a fee or an allowance against any venture capital linked with the marketing of the goods.

Compensation trade offers the Chinese partner the opportunity of acquiring the means of production plus incidental supplies of materials either without expenditure of foreign exchange or with less outflow of foreign currency than would otherwise be possible. On the other hand the selling partner is enabled to conclude contracts which shortage of exchange may otherwise have prohibited. In a buy-back deal proper, the implicit payment with finished goods necessarily ties in to the arrangement certain aspects of guaranteed delivery of plant and equipment.

The problems and possible disadvantages of compensation deals should not be overlooked, however. The (Chinese) purchase usually pays a considerably higher price than he would otherwise do to offset the supporting payments to compensation dealers for disposing of the final products and the risks involved for the seller. In both direct and indirect compensation deals (not "countertrade"deals: see 3.3 para. 2 above) the seller must take in payment goods for which little demand and no ready market may exist, thus being forced to conclude a switch deal with an experienced compensation house well before the conclusion of his contract. These possible drawbacks, with the extremely complicated contractual arrangements involved, serve to deter possible investors from barter-type contracts. Barter deals are potentially complicated by problems of availability and quantity of bartered goods, commodity specification, pricing, quality standards, consumer demand, transport costs etc. Buyback deals, especially in the case of long-term financing under such arrangements, are often complicated by the frequent intrusion of quality control. The production of marketable and competitive products will be dependant upon factors beyond the seller's control, while the pricing of buyback goods for delivery years ahead is highly complicated, calling for extremely complex adaptation and escalator clauses to be written into the original contracts.

In the COMECON States barter trade is freely used and established patterns have developed largely because the markets are centrally planned by the national Foreign Trade Organizations (FTOs) which are awarded exclusive responsibility for specific goods within the country, a circumstance unknown in China at the present time. Indeed within China the present trend is towards devolution of responsibility from the centre to the provincial, municipal or local administrative authorities.

Despite the very considerable problems and complications, China is becoming increasingly oriented towards compensation deals because of the advantages already mentioned; and at present such deals valued at US$ 1 million in the provinces and smaller communities, and US$ 3 million in the three major cities, Beijing (Peking), Tiang-Tin and

Shanghai, are under consideration by China's Import-Export Commission. Local government authorities may themselves approve contracts below those limits, although in the coal, oil, crude oil, iron and steel, and mineral resources sectors major compensation projects must be referred to the relevant Ministry.

No less than 330 compensation deals were concluded in a two-year period from mid-1978 involving both large and small projects, 60 per cent being with Hong Kong and Macao and 34 per cent with Japan. Half of these concerned textile, yarn and silk manufacture and one quarter was shared by the rest of light industry. The remaining portion went to the metallurgical, mineral processing, chemical, engineering and food industries. Payment in kind in the smaller and medium sized projects is averagely made within two or three years but in major projects payment over seven to eight years may be permitted.

3.4 Co-operative Production

Co-operative production is basically a combination of compensation agreement and joint venture in which the foreign partner, who holds no share in the original capital of the enterprise, delivers to the Chinese partner the relevant equipment, machinery, components, spare parts and possibly semi-finished products to be used, probably under license, together with the appropriate technology, also supplied by the foreign partner. The crucial advantage for the Chinese partner is the transfer of technology and the gradual assimilation of production techniques and know-how.

The products manufactured are either delivered in the appropriate quantity to the foreign partner as payment for his contribution (buyback system) or are sold on the world market with a distribution of profits in accordance with contractual agreement. As with joint ventures the emphasis is laid on the modernization and development of existing enterprises rather than the creation of new manufacturing plants.

The system can be applied profitably to the tourism industry, since it possesses many features commonly found in franchise agreements.

No firm statistics regarding co-operative agreements are yet available in China, but some major projects are under way for example a US$ 50 million toymaking plant and two petrochemical plants with a combined value of US$ 21 million.

3.5 Joint Ventures

In a joint venture two or more partners form a company and participate in its equity; similar in some degree to a joint stock company or the GmbH partnership in Austrian, German and Swiss law. A joint venture can be stipulated either for a limited or unlimited period, its partners will normally participate in the assets and profits of the company in accordance with their shareholdings; thus this form constitutes the closest degree of co-operation of all between the foreign and Chinese partners. It should be noted that in China a foreigner who is always prohibited from real estate ownership is designated "the user".

Although deeply interested in attracting foreign capital and investment, China appears to have become more cautious and realistic during its present phase of economic readjustment when contemplating co-operation agreements with foreign partners, especially as concerns its basic infrastructural insufficiency and the variable supply of power, water, etc.

China's readjustment policies seem to indicate increasingly certain basic objectives viz

(i) The modernization and adaptation of existing industries using the minimum of capital, while accelerating its efforts to attract foreign currencies.

(ii) The development of new energy sources while simultaneously economising in the use of energy.

(iii) Improving national infrastructure.

(iv) The promotion and development of underdeveloped regions.

Favoured fields for foreign investment appear to be as listed below, although not in order of priority:

Agriculture
Energy
Transportation
Urban development
The machinery and electronics industries
Rehabilitation of the textile and light industries
Tourism industry
Building materials industry

Seventeen joint ventures, mainly in tourism, handicraft and light industry, had been approved by late 1980 including construction of 3 hotels in Peking, rattan furniture making, manufacture of clock faces etc. The majority of joint ventures are concluded with partners in Hong Kong, Macao, and Japan, but single joint ventures have been formed with France, Switzerland and USA and joint contracts for off-shore oil exploration have been concluded with French and Japanese interests. Early in 1981 approx. 70 joint ventures were in the course of negotiation, emphasis being on oil exploration, coal mining and precision instrument manufacture.

3.6 Joint Operations

Joint operations are akin to joint ventures, although they also incorporate features of the co-operative production arrangement. The foreign investor in this case delivers his equipment, technical know-how, management training schemes etc., but his profit share is not necessarily proportionate to his capital contribution. The management of the joint operation remains in the hands of the Chinese partner, and the foreign capital is normally repaid within 5-7 years, but exceptionally up to 10 years. Products are mainly for export.

By early 1981 about 280 joint operations existed, the foreign contribution being an estimated US$ 500 million.

3.7 Establishment of Offices by Foreign Enterprises

In themselves, offices established in China do not constitute foreign investment or co-operative enterprise, but they often are the first effective step towards identifying future business and co-operation with Chinese enterprises. Interim regulations governing the establishment of resident offices in China have already been promulgated. The procedure appears to be uncomplicated and any foreign enterprise contemplating such a resident office should apply to the competent authority for permission, as indicated below:

Type of business	Competent PRC authority
Trading, manufacture, shipping	Ministry of Foreign Trade
Banking, insurance	The People's Bank of China (n.b. In this sector difficulties may arise)
Maritime shipping	Ministry of Communications
AIR transport	The General Administration of Civil Aviation in China
All others	The relevant government commission, ministries or bureaus of the Central PRC Government

Documents required

Application forms should be signed by the Chairman of the Board of Directors or the General Manager of the proposed enterprise, and should include all relevant details such as name and location of the Resident Office, the names of responsible company members, the scope and anticipated duration of activity.

n.b. The legal document approving the formation of the new enterprise must be legalized by the authorities of the country of the initiators. Capital credibility should be documented by a banking institution which has abiding business connections with the initiators. A curriculum vitae of each foreign member of the Resident Office should accompany the application.

4. JOINT VENTURES

4.1.a Substantive Regulations

1. A law on joint ventures was promulgated on 8 July 1979.
2. Two sets of additional regulations concerning (a) registration and (b) labour management of joint ventures were approved on 26 July 1980.
3. The National People's Congress on 10 September 1980 adopted two relative income tax laws, concerning (a) joint ventures, and (b) individual incomes.
4. The income tax law concerning joint ventures (3.(a) above) was amended in December 1981 and a new income tax law concerning the activities of all foreign entrepreneurs in China came into force on 1 January 1982.

4.1.b The Joint Venture Law specifies:

1. Agreement. A joint venture is based upon the Joint Venture Agreement, specific Articles of Association, and possibly upon other contracts. The form shall be a limited liability company.

2. Activities. These are not restricted and there may be joint venture in, e.g. banking, insurance or consultancy. Fields given special favour are:

   Exploration and exploitation of natural resources, e.g. oil, coal.

   Tourism, catering

   Shipping

   Capital goods, e.g. commercial vehicles, electrical equipment

   Construction

   Agriculture and fishing, forestry.

3. Participation. Although the proportion of foreign investment in a project shall generally not be below 25 per cent of the whole, there is no provision forbidding holdings of 50 per cent or above. However, foreign

participation exceeding 49 per cent is unusual. The partners shall share profits, losses and risks in proportion to their contribution to the registered capital of the enterprise. Land and buildings remain Chinese property, the joint venture having the status of "user".

4. Contributions. These may consist of cash, capital goods, industrial property rights, and other forms of investment. The value of all contributions shall be specified either in the Joint Venture Agreement, the Articles of Association or in additional contracts. The contributions of the Chinese participants may be used during the course of the enterprise's activity and a charge shall be paid for use of the assets of the non-Chinese participants during that time. The contributions of the foreign participants, whether in technology, equipment or other forms must be of an advanced type and be relevant to China's needs.

5. Protection of Foreign Investment. The resources of the foreign participant and his legitimate profits, in common with his personal rights and interests in law, are protected by the Government of the PRC in accordance with Chinese Law. It may be commented that this assurance is deficient in that no compensation is yet assured in the event of expropriation or nationalization by the Government.

6. Repatriation or transfer of the profits or of a share in the capital. The net profit shall be distributed between the parties in proportion to their shares in the registered capital after due income tax has been paid and after the various deductions provided for in Articles of Association (e.g. reserve fund contribution, staff social welfare fund contributions, contingency allocations, etc.) have been requited. Once legal and contractual obligations have been met, the foreign partner's profits may be remitted abroad in conformity with the appropriate regulations and any relevant contractual provisions. One party's share

of the registered capital may only be transferred with the consent of the other parties to the joint venture. Provision for such contingency may be written into the contractual agreements. The Provisional Regulations for Exchange Control, promulgated on 18 December 1980, require the foreign partner of a joint venture to apply to the State General Administration of Exchange Control (SGAEC) before transferring foreign capital abroad. When the transfer is effected, the Foreign Exchange Deposit Account of the Enterprise will be duly debited. Re-investment by a foreign partner will attract preferential tax treatment. Provided joint ventures can show that they offer advanced technology according to recognized international standards, applications for income tax reduction or exemption over the initial 2 to 3 years of profitable operation will be acceeded.

7. Funds. Legal provision is made for reserve funds, a fund for expansion of the venture, staff bonus fund, and social welfare funds. Contribution to certain communal funds is obligatory.

8. Duration and termination. No legal limits to a venture's duration exist, this being left to agreement among the parties, although a duration of approximately 10 years is usual for tourism and catering ventures and approximately 20 years for capital goods enterprises. An application to extend an agreement must be made to the competent authority at least six months prior to the agreed termination date. The authorities have the right to terminate any venture prior to the agreed expiry date in circumstances of heavy loss or failure of any party to the venture, including the Chinese partner.

9. Preferences. Raw materials, semi-processed materials, fuels, auxiliary equipment etc. are expected to be purchased within China wherever possible. Such items may be bought outside China in some circumstances using the venture's foreign exchange funds, but the likelihood of obtaining

a loan of foreign exchange from the Bank of China in such circumstances is very remote.
The marketing abroad of the venture's produce through direct channels or associated agencies will be given priority.

10. Wages and salaries. Under the Foreign Exchange Regulations, the wages, salaries and other legitimate income of foreign personnel employed in a joint venture may be remitted abroad after payment of personal income tax in accordance with regulations.

11. Management structure. The Board of Directors will comprise the agreed number of directors under the original agreement and Articles of Association. The Chairman of the Board of Directors must be appointed by the Chinese partner, and all other directors shall be appointed or removed with the agreement of all participants. The foreign partner has the right to appoint one or two Vice-chairmen. The tasks of the Board of Directors are to take the critical decisions of the venture, e.g. production and business programmes, budgetary affairs, distribution of profits, expansion projects, etc. The Board of Directors also appoints the President (or General Manager), the Vice-Presidents (or Assistant General Managers), the Chief Engineer, the Treasurer and the auditors. The President (or in industry the General Manager) is supported by Vice-Presidents (or in industry Assistant General Managers) in the running of the enterprise. Subordinate managers are responsible to the day-to-day operations of the business or industry.

12. Disputes. Disputes arising in the course of a joint venture shall be settled by internal consultation or, if conciliation attempts fail, by either an established Chinese arbitration tribunal or an arbitration body which may be mutually devised by the parties to the venture. In stipulated circumstances the Foreign Trade Arbitration Commission (FTAC) or the

Maritime Arbitration Commission will be the competent arbitration body, while on occasions the Chinese party may accept the decision of a nominated foreign arbitration body, e.g. the Stockholm Chamber of Commerce. It should be noted that since China is not a signatory to any multilateral or bilateral international arbitration convention, there is some doubt as to how a decision by a recognized external arbitration body could be enforced.

4.2 Registration of a Joint Venture

The apposite legal enactment is "Regulations on the Registration of Joint Ventures Using Chinese and Foreign Investment", approved by the State Council on 26 July 1980.

After the Joint Venture Agreement is acceptable to the parties, the Agreement, the Articles of Association and any subsidiary contracts must be referred to the Foreign Investment Commission (FIC) for approval, amendment or rejection. After FIC approval is given the Joint Venture must within one month be registered with the General Administration for Industry and Commerce (GAIC), which will then authorize the Bureau for Industry and Commerce of the appropriate autonomous region, province or municipality to effect local registration. A license to start operations may be issued after examination of the basic documents by the GAIC, but registration with the local authority may be done after the issue of the license and after registration with GAIC. After these steps are completed, registration with the local taxation office and with the Bank of China or other authorized bank must follow.

4.3 Labour Regulations

The existing relevant regulations are "Regulations on Labour Management in Joint Ventures" dated 26 July 1980, and "Regulations for Foreign Investments in Special Economic Zones", but to date there is no overall or unitary law to cover all foreign co-operation enterprises. Probably because China, unlike most industrialized countries, lacks detailed labour legislation, each contract is required to specify a range of substantive facts regarding labour-terms of employment, the dismissal and resignation of staff and workers, their functions and duties, their rights, wages and remunerations, discipline, working hours, leave, industrial insurance, welfare, protection, etc. The position must be stated in full in all labour contracts in respect of joint ventures or enterprises within SEZs, but it should be noted that while employees of joint ventures outside SEZs enjoy a far-reaching protection against dismissal, employees of foreign enterprises within SEZs can be hired or fired without undue complication.

Within the joint ventures, where labour regulation is comparatively firm, the more important requirements are as follows:

1. The labour contract must specify in detail the rights and obligations of employer and emplyee alike.

2. Every joint venture except very small units must form a trade union organization within the company. The labour contract must be signed jointly by the venture and by the trade union organization, and subsequently approved by the Labour-Management Department of the provincial, regional or municipal authority.

3. Personnel must be recruited with the consent of the Labour-Management Department, which will examine each recruit's qualifications.

4. In the case of unsuitability or failure to meet working requirements personnel may be discharged, provided the unsuitability or failure can be shown to affect the production or technical running of the joint venture. Discharged senior personnel will receive compensation from the employer, while discharged office or workface personnel will be directed to other work either by the appropriate local authority or the Labour-Management Department.

5. The trade union may object to the dismissal of any office or workface staff member, and has the right to enter into conciliation procedures with the Board of Directors.

6. The wages of office staff and workers in a joint venture will equal from 120 to 150 per cent of the wages paid to personnel of comparable status in state-owned or other local enterprises.

7. The joint venture is responsible for payment of labour insurance dues for its personnel, to cover medical expenses and other social amenities provided from Government.

Average wages

In China the average monthly wage for workers in state-owned enterprises was Yuan 602 during 1977, Yuan 644 during 1978, Yuan 705 during 1979, and Yuan 803 in 1980. Wage inflation continues to accelerate.

5. TAXATION

5.1 General

Chinese tax classifications cover Income Tax, recurrent Property or Wealth Tax, Registration and Licence Duties, Goods and Service Taxes, and Social Security Contributions. These classifications may be subdivided into national taxation, local taxation, and surcharges.

In the context of foreign investment activities, the most relevant categories of tax are:

i. The Income Tax Law covering Foreign Enterprises (1 Jan. 1982)
ii. Individual Income Tax Law (10 September 1980).
iii. Industrial and Commercial Consolidated Tax Law (1958)

5.2 Tax Law Covering Enterprises

The Tax Law Covering Enterprises of 8 December 1981 has replaced the Income Tax Law Covering Joint Ventures of September 1980 so that law now affects the income of all foreign investments and not joint ventures alone. The following will henceforward be subject to te~ation:

1. All income derived from production, business or any other source.

2. All foreign enterprises operating in China, an "enterprise" being defined as any foreign company, enterprise and other economic organization, including co-operatives and joint business operations with or without Chinese participation.

3. The entire income in a tax year, calculated by the Gregorian calendar, after costs, expenses and losses have been deducted.

4. The entire taxable income will additionally be subject to a local tax levy of 10 per cent.

Foreign enterprises in farming, forestry, animal husbandry or certain other low-profit sectors will be exempted from income tax in their first profit-making year and will receive a reduction of 15 per cent of calculated tax in their second and third years, provided the enterprise is scheduled to last ten or more years. With approval of the Ministry of Finance further reductions may be conceded.

Losses

Losses incurred by a foreign enterprise may be carried over to the following tax year with a compensating adjustment in that year's declared income and the carry over process may be continued for a period not exceeding five years. Foreign companies, enterprises or organizations which maintain no establishment within China will be subject to a 20 per cent income tax levy on interest from dividends, rents, royalties or other sources of income in China, the tax being witheld by the payer. Exemption is conceded to interest on loans made to the Chinese Government or State Banks by international finance organizations. Exemption is also granted in a few other special cases.

Net Income

The promulgation of detailed rules and regulations arising from the Tax Law Covering Enterprises (8 December 1981) is anticipated, but sine die production costs, administration costs, industrial and consolidated tax payments, and depreciation will continue to be accepted as deductible expenses. Depreciation in China must be calculated by the straight-line method.

5.3 Re-investment of Profits

The earlier law (see previous paragraph) offered tax inducements to a foreign partner re-investing his share of profits for a period of at least five years, with a refund of 40 per cent of the tax already paid on the sum re-invested. The incentive was expressly provided under Article 7, para. 3 of the Joint Venture Law, but no such inducement appears in the new Income Tax Law covering Foreign Enterprises dated 1 January 1982. It is felt that this contradiction will be clarified in due course.

5.4 Individual Income Tax

Persons taxable

1. Residents of China for one year or more are subject to Chinese income tax on their entire income, wherever the source may be.

2. Persons not resident in China, or resident there for less than one year are subject to Chinese income tax on their income from Chinese sources only.

Taxable income

1. Income from wages and salaries is taxed at progressive rates ranging from 5 to 45 per cent (see table in Annex I)

2. Income from personal services, royalties, interest, dividends, bonuses, property, and miscellaneous sources is taxed at a flat rate of 20 per cent.

n.b. Certain items of income are exempted from taxation e.g. wage and salary earners may deduct Yuan 800 per month as a tax-free allowance before payment of income tax.

Residents of China for more than one year are subject to full Chinese taxation and must thus pay tax separately on all income earned abroad in addition to their standard Chinese income tax liability. In cases where the individual has been taxed abroad for income earned outside China, Chinese tax regulations permit a tax relief of the equal to the taxation on income abroad calculated according to Chinese tax rules. If a foreigner working in a joint venture in China has paid tax abroad at a rate lower than that of Chinese income tax, he would be required to make up to the Chinese tax authorities the difference between the two assessments.

5.5 Industrial and Consolidated Tax

Rates of taxation vary from 1.5 per cent to 69 per cent, and certain exemptions are granted. The tax is applicable to all enterprises within China and is levied on industrial and agricultural production, retailing, transportation, postal, telecommunications, and services. Domestic and foreign transactions are taxable.

5.6 Double Taxation Agreements

No double taxation agreements between China and other countries are known to exist, but Article 32 of the Income Tax Law covering Joint Ventures states:

"Income tax paid abroad by joint ventures or their branches on their incomes earned outside China may be credited against the amount of income tax to be paid by their head offices upon presentation of the Foreign Tax Payment Certificate. The credit, however, shall not exceed the tax payable on the income abroad, computed in accordance with the rate prescribed by Chinese taxation law."

There is no information about the possible future maintenance of this sort of protection against double taxation. For the present individual taxpayers are similarly protected.

6. SPECIAL ECONOMIC ZONES (SEZs)

6.1 General

These zones, which have so far only been fully activated in Guangdong and Fujian are planned for various provinces as a means of accelerating Chinese economic development and exploiting export opportunities.

Guangdong Province, because of its favourable geographic position, is the more advanced, with three zones, Shen Zhen, Zhuhai and Shantou already in operation. Of these Shen Zhen is the most advanced SEZ, being sub-divided into 4 districts:

1. Luohu District which specializes in commerce, trade and services

2.-3. Shangbu and Shahe Districts which will attract electronics and light industries

4. Shekou Industrial Zone which offers facilities for light and heavy industries as well as for commercial and residential ventures.

The Zuhai SEZ and Shantou SEZ both offer industrial and residential facilities; the former also seeking public utility ventures, while the latter seeks to attract scientific research projects.

Within Fujian Province there is so far one SEZ, Huli in Xiamen, to which initiatives in electrical consumer goods, textiles and garment production and other light industries are to be attracted.

The development of SEZs in the other provinces, autonomous regions or municipalities appears to be at a very early stage. The range of enterprise sought is virtually unlimited but preference will be given to light and service industries and in particular to industries contributing to export and infrastructure development.

6.2 The Guangdong Regulations

It is anticipated that the Guangdong Regulations passed in August 1980 will, in general terms, apply to the other SEZs, since they specify grants of authority, and procedures for initial promotion, application, registration, supervision and termination of ventures. Production, equipment, materials supply, customs matters, and preferential clauses are also dealt with. Within the SEZs foreign investors may set up wholly foreign-owned enterprises using expatriate personnel in senior technical and administrative functions.

6.3 Incentives

Although lant titles invariabley remain Chinese, foreign investors in SEZs are offered preference in matters of rent, land tenure and plot area. A special tax rate of 15 per cent is applied and preferential tax treatment is offered to enterprises which invest US$ 5 million or more, introduce high-level technology, offer long-term capital turnover, or reinvest profits in the SEZs for 5 years or more. A waiver of import duties is granted on machinery, parts, raw materials vehicles etc. and in some cases lower import duties on necessary consumer goods may be offered. Legitimate after-tax profits and other earnings may be repatriated, as may accumulated assets and funds after operations are finished and debts have been cleared.

Foreign enterprises in SEZs also enjoy a greater than normal freedom with respect to staffing, and are permitted to dismiss employees in accordance with their terms of contract should they fail to meet the required standard. Provision exists for the testing of prospective employees before contracts are finalized and in Guangdong the provincial authorities will assist in providing Chinese personnel.

7. PROTECTION OF INDIVIDUAL PROPERTY RIGHTS

7.1 General

No legislation yet exists in China to provide adequate protection for industrial properties, especially those of foreigners, although the preparation of comprehensive legislation based on international practice is now under way. At present a degree of protection of such rights can only be ensured by stipulation within contracts or in some circumstances by concluding an agreement with the Chinese Foreign Trade Authority.

7.2 Patents, Inventions and Technical Innovations

Registration of Patents and protection of Patent Rights does not yet exist in the PRC although in specific instances some protection may be provided within contracts.

Regulations providing awards for inventions and technical innovations were promulgated in October 1963 in order to recognize and reward such initiatives, the benefits accruing to the state.

There are grounds to conclude that a degree of protection of patents etc. can be obtained by entering into special agreement with the authorities.

7.3 Trade Marks

Basic Trade Mark regulations are contained in the "Measures for the Control of Trade Marks" of 10 April 1963 and "Detailed Enforcement Rules for the Control of Trade Marks" dated 25 April 1963. Trade marks may be registered on first application to the competent authority, and must be a single word or combination of words which, when registered, may be applied to a range of products in over 70 defined categories. Once the trade mark has been recognized by the Chinese authorities it can be used within China exclusively by the proprietor Chinese enterprises and joint ventures also have the right of registration of trade marks on application to the Central Administrative Bureau of Industry and Commerce, while overseas enterprise firms operating outside China may apply for registration of trade marks in China provided the country of origin has a reciprocal agreement with the PRC. These now exist with Australia, Belgium, Canada, Czechoslovakia, Denmark, Finland, France, the German Democratic Republic, the German Federal Republic, Greece, Hungary, Italy, Luxembourg, the Netherlands, New Zealand, Norway, Sweden, Switzerland and the United Kingdom, while applications by US enterprises can also be entertained. The trade mark to be registered in China must first be registered in the applicant's home territory. No duration of validity of the registration is specified. It is understood that new trade mark legislation is now under preparation.

7.4 Industrial Designs

At the present time no protective legislation exists in China.

7.5 International Conventions

China is not a signatory to any international convention or agreement in the field of protection of industrial property rights, although there is evidence that the country has accepted the need for such protection. The Agreement on Trade Relations between the USA and the PRC, Article VI, dated 7 July 1979 for instance, includes certain provisions for protection of rights; recognizing the necessity to protect patents, trade marks and copyrights, and agreeing reciprocally on the exclusive ownership and registration of trade marks in each other's country. This agreements has the force of law in both countries and refers significantly to an intention to adhere to international practice, and mutually to grant the same degree of protection of patents and trade marks as is accorded internally by the other party.

The Trade Agreement between China and the EEC dated 3 April 1978 on the other hand, specifies no such protection of industrial property rights.

INDIVIDUAL INCOME TAX IN CHINA

Annual Income range (stated in Chinese Yuan)	Taxation (per cent)
Below 250,000	20
That part of income between 250,000 and 500,000	25
" " " 500,000 and 750,000	30
" " " 750,000 and 1,000,000	35
" " above 1,000,000	40