ECONOMIC DEVELOPMENT AGREEMENTS - FOREIGN INVESTMENT IN CHINA

The question of the governing law of Economic Development Agreements between states and foreign investors remains controversial. In SPP v. Arab Republic of Egypt [1984] Australian I.L. News, (1983) 22 ILM 752, the latest reported arbitration, the tribunal reached a somewhat novel conclusion as to the governing law of the agreement in issue. In China, such agreement normally contain an arbitration clause but many leave open the choice of the governing law : Australian Financial Review, 1 June 1984 at 37. While the Chinese authorities would not accept foreign law, foreign investors argued that Chinese law was incomplete and elusive. The report quoted a Peking lawyer, Mr. Zhang Si-Zhi, as saying:-

> "The laws at present in our country are not very perfect and the mutual trust between us (and foreign companies) is still not solid, so many people remain doubtful about our systems relating to laws, Mr. Zhang said.
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> In 1979, we wrote down laws relating to our open-door foreign policy but many things have cropped up that were not considered then.
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> We should acknowledge that our laws are not perfect or complete but on the other hand our laws are enough to guide our work.
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> We want to accelerate the pace of law-making, but the key lies in practice and there is no need for our foreign friends to worry about this."

Readers may note that the Chinese Economic Contract Law, 198 reproduced in (1983) 22 ILM 330, provides in Article 55 that the "regulations governing foreign economic and trade contracts will be formulated separately with reference to the principles laid down by this law and the international practice." (Our emphasis)

The Chinese Law on Joint Ventures, 1979, appears at (1979) 18 ILM 1163, the Regulations thereunder appear at (1983) 22 ILM 1033. Further relevant regulations appear at (1983) 22 ILM 1451 The Income Tax Law concerning Joint Ventures appears at (1980) 19 ILM 1452 and the Regulations thereunder at (1981) 20 ILM 384 The Income Tax Law concerning Joint Ventures with Foreign Investment appears at (1981) 20 ILM 1452, and the Regulations on Special Economic Zones in Guandong Province, 1980 appear at (1980) 19 ILM 1454.

US based investors will find the US Chinese Investment Incentive Agreement, 1980 of interest: 1980 19 ILM 1483. Article 6 provides for negotiation and arbitration of disputes regarding interpretation or where "in the opinion of one of the Governments" ... a question of public international law arising out of any investment or project or activity related to such investment arises. The arbitral tribunal shall base its decision on the applicable principles and rules of public international law. Each state shall appoint an arbitrator and the two arbitrators shall appoint a President. If such appointments are not made either Government may request the Secretary General of the UN to make the necessary appointment or appointments. The Tribunal

shall decide by majority vote.

The report in the Australian Financial Review also alleged that foreign investors, who had recently set up joint ventures with China to service the offshore oil industry in the "special economic zones", had been attracted by the provision in the law governing taxation in those zones that "all" foreign ventures would be eligible for the incentive tax rate of 15 per cent. However, the translation of the Regulations on Special Economic Zones in the Guandong Province, 1980 published in 1980 19 ILM 1454 provides in Chapter 3, under the heading "Preferential Treatment":

> Article 14. The rate of income tax to be paid by enterprises in the special zones is to be 15 per cent. Preferential treatment will be given to enterprises established within 2 years of the promulgation of the regulations, enterprises with an investment of at least five million US dollars and enterprises involving higher technologies or having a longer cycle of capital turnover.

If these are the regulations or law referred to in the article in the Australian Financial Review, there appears to be a discrepancy in that the word "all" is missing. However this may be expected in translations, and presumably the Chinese text is authoritative. In any event, a reading of Article 14 seems to indicate that the intent was to offer any enterprise which satisfies the requirements of the Article a tax rate of 15 per cent The complaint noted in the Review was that in 1983 foreign investors setting

> "... up joint ventures with China to service the offshore oil industry in the "special economic zones" declared by the Government were suddenly informed that their enterprises would not be eligible for the 15 per cent incentive tax rate offered to other foreign enterprises in the zones.
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> Although the law governing taxation in the special economic zone stated that "all" foreign ventures would be eligible, the companies were informed that an internal directive overruling this law had been issued. This move in reality doubled the tax from 15 per cent to the 33 per cent levied on joint ventures outside the zones."

The report concludes that investors -

> "... who had calculated costs and signed contracts on the basis of a 15 per cent tax rate found themselves committed to a much higher tax rate by virtue of an unpublished "restricted" document and with no course of appeal."

Of course this is a phenonomen not unknown to investors in Western countries. States may even enter into "stabilisation clauses" promising to maintain a given tax regime; it is rare that such promises would be enforceable under the law of the state concerned : Commonwealth Aluminium Corporation Limited v. Attorney General (Queensland) [1976] Qd R. 231; Revere

Copper v. OPIC (1978) 56 ILR 258

US based investors will no doubt find the provisions of the US Chinese Double Tax Convention signed in May by President Reagan of interest. Full details are not yet to hand. In addition a new cultural agreement was signed to replace the one terminated when the US granted political asylum to the tennis player, Hu Na. An Agreement on Co-operation in the Peaceful Use of Nuclear Energy was also signed. American "visits", i.e. inspections to verify compliance with safeguards against re-processing of spent fuel and re-export of technology are included Hitherto, China has seen such safeguards as an intrusion into her sovereignty. However, in October 1983, she joined the International Atomic Energy Agency, which was interpreted by commentators as a willingness to make concessions on this question : The Economist 5 May 1984 at 18, 78.

A recent issue of Columbia Journal of Transnational Law, Volume 22 No.1 (1983) contains articles on China's legal development, as well as a selected bibliography.

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