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# New PRC and Shanghai Regulations for the Encouragement of Foreign Investment

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## I. INTRODUCTION

To stimulate sagging foreign investment, the People's Republic of China (China) promulgated the State Council Regulations Concerning Encouragement of Foreign Investment (State Provisions) on October 11, 1986.<sup>1</sup> An additional sixteen sets of implementing regulations were promised by March 1987.<sup>2</sup> Following the lead of the national government, at least thirty provinces, autonomous regions, special economic zones, and municipalities have issued their own provisions to encourage foreign investment.<sup>3</sup> One example of these local provisions are the Regulations of Shanghai Municipality for the Encouragement of Foreign In-

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1. State Council Regulations Concerning Encouragement of Foreign Investment [State Provisions] (1986), *trans. in* [2 Bus. Reg.] China Laws for Foreign Business (CCH Austl. Ltd.) ¶ 13-509 (June 18, 1987).

2. *See Filling Out the Investment Framework*, CHINA MARKET INTELLIGENCE, Jan. 1987, at 1. Among the implementing regulations already released are Regulations on Employment, Wages, and Welfare in Foreign Enterprises; Customs Regulations for Foreign Enterprises on Imported Materials and Parts for Export Orders; and Provisional Regulations Governing *Renminbi* Loans Mortgaged with Foreign Exchange for Foreign Investment Enterprises. Yet to come are revisions of the current land use regulations, rules for foreign exchange balancing, guidelines on how to qualify as an export-oriented or technologically advanced enterprise, and revisions of registered capital requirements.

3. *Id.* at 2. Local regulations have been promulgated by Anhui Province, Anshan, Beijing, Dalian, Fujian Province, Fuzhou, Gannan Autonomous Region, Guangdong Province, Guangzhou, Guizhou Province, Hebei Province, Hunan Province, Jiangsu Province, Jiangxi Province, Lianyungang, Liaoning Province, Nantong, Ningbo, Qinhuangdao, Qingdao, Shangdong Province, Shanghai, Shenzhen, Tianjin, Xiamen, Xinjiang Province, Yantai, Zhejiang Province, and Zhuhai.

vestment (Shanghai Provisions),<sup>4</sup> which became effective on November 1, 1986.<sup>5</sup>

This Article discusses the State Provisions and, as an example of the local regulations, the Shanghai Provisions. The objective of the Article is to examine the potential benefits of these regulations and to provide examples of where the regulations fail to address certain problems presently faced by foreign investors in China.

The Article will begin with a general overview of the current problems affecting foreign investors. It will then discuss the manner in which the State Provisions attempt to solve these problems and to encourage foreign investment. Finally, the Article will analyze how the Shanghai Provisions supplement the State Provisions in promoting foreign investment.

## II. CURRENT PROBLEMS FACED BY FOREIGN INVESTORS IN CHINA

Although China, under the current modernization-oriented leadership, has gradually accepted foreign investment since 1978, foreign investors still face numerous problems in trading with and investing in China. In the past few years, the most far-reaching problem has undoubtedly been China's severe shortage of foreign exchange. This lack of sufficient foreign exchange, which was the primary motivating factor behind the promulgation of the State Provisions, has made Chinese authorities very reluctant to approve any project which is unlikely to earn a foreign exchange income in excess of expenses.<sup>6</sup> Exceptions are generally made only for advanced technology or defense-related projects.<sup>7</sup>

A second problem often faced by foreign investors is that they are forced to pay unreasonably high costs for land, utilities, and materials. For example, in 1981 a Sino-Japanese joint venture leased a piece of land for a period of three years from a village in the western suburbs of Tianjin for a construction project. The contract called for the payment of RMB7,000 (approximately US\$1,900) in rent for the period, but the joint venture eventually paid RMB72,000 (approximately US\$20,000) for rent and for causing inconvenience to the village during construction. The

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4. Regulations of Shanghai Municipality for the Encouragement of Foreign Investment [Shanghai Provisions] (1986), *trans. in* [Special Zones & Cities] China Laws for Foreign Business (CCH Austl. Ltd.) ¶ 91-030 (Dec. 12, 1986).

5. See *infra* notes 49-57 and accompanying text.

6. Harding, *Investment Climate in China*, BROOKINGS REV., Spring 1987, at 37.

7. See *id.* at 37.

village also sued the company in a local court to claim more damages.<sup>8</sup> Events such as this prompted Zhu Rongji, Vice Minister of the State Economic Commission, to admit that “[s]ome [Chinese entities] are taking a bite of joint ventures and even sucking them dry.”<sup>9</sup>

In addition to high initial costs, foreign investors often face unreasonable, and sometimes unpredictable, taxation. For example, foreign companies which establish representative offices in major Chinese cities may be subject to an income tax even if they are not making any profits in China.<sup>10</sup> The tax calculation is based on the expenses of the operation in China.<sup>11</sup> Rather, a company operating in several different cities will often be required to pay different rates on the same income,<sup>12</sup> since interpretation of national tax legislation often differs from locality to locality.<sup>13</sup>

A foreign investor for various reasons also can encounter unexpected difficulties attempting to comply with Chinese tax laws. Often, assessment of fines and interest are arbitrary and based on the mood of the tax authorities on a given day. For example, the representative of one company went to the local tax office on the appointed day to pay the representative office tax, but upon his arrival found that the entire staff of the office had taken the day off. When he returned a few days later, he was required to pay a large fine for late payment.<sup>14</sup>

Frequently, foreign investors must deal with Chinese government agencies which are inefficient, unreasonable, and plagued with bureaucratic wrangling.<sup>15</sup> Which entity has the authority to approve a particular project, whether central government approval is necessary, and how long the approval process will take are questions which often cannot be answered with certainty. For example, foreign companies technically

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8. For a detailed analysis of this dispute, see *Rights of Joint Venture Upheld*, BEIJING REV., Dec. 8, 1986, at 7-8.

9. *China Business Briefs: Peking Will Unveil Rules to Ease Climate for Foreign Investors*, Asian Wall St. J. Weekly, Oct. 13, 1986, at 18, col. 1.

10. Horsley, *Shedding Light on China's Tax on Representative Offices*, E. ASIAN EXECUTIVE REP., Mar. 1986, at 9-12; Ness & Mitchell, *Taxing US Offices in China*, CHINA BUS. REV., Oct. 1986, at 36.

11. Horsley, *supra* note 10, at 11; Ness & Mitchell, *supra* note 10, at 36 (implying that this is one of three methods of determining the applicable tax).

12. Mitchell, *Local Foreign Investment Regulations: Shopping for the Right Location in China*, E. ASIAN EXECUTIVE REP., Feb. 1987, at 9, 12-18.

13. *Id.*

14. For a description of this story, see Gelatt, *A Fairer Investment Climate in China*, Asian Wall St. J. Weekly, Nov. 3, 1986, at 16, col. 1.

15. See generally *State Council Official Answers Questions*, BEIJING REV., Oct. 27, 1986, at 28 (official of the Investment Working Group of the State Council discussing the inefficiencies of Chinese authorities).

cannot conduct business until they are registered with the Chinese Government.<sup>16</sup> The process of registration can take up to a year to complete. Size and name recognition do not help.

Another problem a foreign investor encounters in China is an underdeveloped infrastructure.<sup>17</sup> The lack of infrastructure has discouraged many investors from investing in China's interior,<sup>18</sup> where such investments are badly needed. Exploration of natural resources is also hindered when transportation is not available. When infrastructure is available to a foreign company, the rates charged are many times what a local company would pay.<sup>19</sup>

China also lacks a pool of skilled and motivated workers. Currently, bonus or overtime payments usually go to the State instead of the worker. This is because contract approval cannot be obtained without a provision requiring direct payment of such bonuses to the government agency responsible for such a worker, or an additional tax is placed on the worker in the amount of the extra payment.<sup>20</sup> As a result, Chinese workers can be extremely difficult to motivate and train. For example, the American Motors plant in Beijing cited inefficient workers as one problem encountered in joint ventures.<sup>21</sup> Without the ability to provide effective incentives to workers, a foreign investor will find it difficult to develop a skilled and efficient work force. The result can be inefficient operations and low quality products, making the operation in China noncompetitive.

In addition, China's labor is not cheap. For example, one foreign investor who wanted to produce a product used in the computer industry was quoted labor rates which, factoring in inefficiencies, were actually higher than the rates in the United States.<sup>22</sup>

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16. Interim Regulations of the People's Republic of China Concerning the Control of Resident Offices of Foreign Enterprises, art. 2 (1980), *trans. in* [1 Bus. Reg.] *China Laws For Foreign Business* (CCH Austl. Ltd.) ¶ 75-000.

17. *E.g.*, China has an inadequate telephone system, congested traffic in cities, limited transportation between cities, and no means of reserving flights to several cities within China in advance. *See* Harding, *supra* note 6, at 38, 41; Cohen & Chang, *New Foreign Investment Provisions*, *CHINA BUS. REV.*, Jan.-Feb. 1987, at 11, 11.

18. Chang, *Northwest China: Shifting Gears*, *CHINA BUS. REV.*, July-Aug. 1986, at 11, 42.

19. *E.g.*, telephone lines for local companies are 300 *renminbi yuan* per line in Shanghai, whereas foreign companies now pay 2500 *renminbi yuan* per line. *See generally* Gargan, *Investing in China: Still Hard*, *N.Y. Times*, June 16, 1987, at D5, col. 1.

20. *See generally* Cohen & Harris, *Equal Pay for Equal Work*, *CHINA BUS. REV.*, Jan.-Feb. 1986, at 11, 11. *See also* Sterba, *Great Wall: Firms Doing Business in China are Stymied by Costs and Hassles*, *Wall St. J.*, July 17, 1986, at 16, col. 2.

21. *Second Thoughts on Investment*, *CHINA MARKET INTELLIGENCE*, July 1986, at 1.

22. For this product, rates in China would have been US\$20 per man-hour while the same

Under the investment conditions described above, China's economic planners have been concerned that China cannot compete with such attractive investment climates as South Korea and Singapore.<sup>23</sup> In an effort to eliminate these obstacles and to encourage foreign investment in China, the State Council<sup>24</sup> promulgated the State Provisions.

### III. STATE PROVISIONS

The State Provisions have the self-proclaimed aims of improving the investment environment, facilitating the absorption of foreign investment, introducing advanced technology, improving product quality, expanding exports to generate foreign exchange, and ultimately developing the national economy.<sup>25</sup>

The provisions grant special preferences to two types of enterprises with foreign investment. The first category consists of production enterprises whose products are mainly for export, and as a result, have balanced foreign exchange earnings. These enterprises are called "export enterprises" in the State Provisions.<sup>26</sup> Because the Chinese often require an enterprise to place artificially high prices on export goods, however, such goods cannot usually compete on the world market.<sup>27</sup> As a result, virtually the only projects which can currently earn foreign exchange surplus are hotels and other tourism-related enterprises.<sup>28</sup> Nonetheless, these enterprises are excluded from the benefits of the State Provisions because they are service enterprises rather than "production enterprises."<sup>29</sup> Thus, the impact of special privileges given to export enterprises is questionable.

The other category of enterprises entitled to special preferences consists of production enterprises which utilize advanced foreign technology

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product could be produced in the United States for US\$15 per man-hour. See Sterba, *supra* note 20, at 16, col. 1.

23. See *China Business Briefs: Peking Will Unveil Rules to Ease Climate for Foreign Investors*, *supra* note 9, at 18, col. 1.

24. As the executive branch of the Chinese Government, the State Council oversees the activities of the various commissions, ministries, and agencies; formulates administrative measures; drafts legislation; and prepares the national economic plan and state budget for approval by the National People's Congress. CHINA MARKET INTELLIGENCE, May 1987, at centerfold (diagram of China's governmental structure).

25. State Provisions art. 1.

26. *Id.* art. 2.

27. Sterba, *supra* note 20, at 16, col. 1.

28. Clare, *Joint Venturing In China: The AMC Experience*, E. ASIAN EXECUTIVE REP., Nov. 1986, at 7, 11.

29. State Provisions art. 2.

to develop new products<sup>30</sup> and to upgrade and replace products in order to increase foreign exchange by exports, or for import substitution.<sup>31</sup> The State Provisions call these enterprises "technologically advanced enterprises."<sup>32</sup> Although all joint ventures in China today arguably could be described as technologically advanced enterprises, the scope of the term depends on the interpretation given it by the various local agencies responsible for certifying these enterprises. Potentially, these agencies can vary their interpretations of the term from case to case to suit their own plans and purposes.<sup>33</sup> The regulations promulgated on January 27, 1987 to implement the State Provisions hopefully will provide uniform guidelines on how to qualify as an export-oriented or technologically advanced enterprise.<sup>34</sup> Shanghai, at least, has rushed to certify a number of joint ventures as technologically advanced enterprises.

The State Provisions enumerate the special preferences available to export and technologically advanced enterprises. Articles 3 and 4 attempt to solve the problem of unreasonably high local costs. Article 3 provides that export and technologically advanced enterprises shall be exempt from payment to the state of all subsidies to their employees except for the payment for labor insurance, welfare costs, and housing subsidies.<sup>35</sup> The seeming generosity of this provision is cast into doubt because the term "subsidies" is not defined. The provision also does not address the additional twenty percent premium over normal Chinese wages which joint ventures have been required to pay their employees.

Article 4 specifies that site use fees for export and technologically advanced enterprises shall be restricted to the five to twenty *renminbi* range per square meter per year where the development fee is included in the site fee. Where the development fee is charged on a one-time basis, the site use fees are limited to no more than three *renminbi* per square meter per year.<sup>36</sup> These fee restrictions, however, are not available for sites located in "busy urban sectors of large cities,"<sup>37</sup> and it is usually

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30. *Id.* art. 2.

31. *Id.*

32. *Id.* art. 10.

33. In fact, this was what happened to the treatment of contracts involving "advanced technology" by local agencies under the 1982 tax rules which grant tax exemptions to these contracts. See Gelatt, *supra* note 14, at 16, col. 2.

34. See Implementing Measures of the Ministry of Foreign Economic Relations and Trade on the Confirmation and Examination of Export-Oriented Enterprises and Technologically Advanced Enterprises with Foreign Investment arts. 2-4 (1987), *trans. in* [1 Bus. Reg.] China Laws for Foreign Business (CCH Austl. Ltd.) ¶ 13-530 (May 17, 1987).

35. State Provisions art. 3

36. *Id.* art. 4.

37. *Id.*

unattractive to locate in rural areas due to a lack of utilities, transportation routes, and skilled labor. Article 4 also states that local government agencies have discretion to grant exemptions for specified periods of time from the site use fees.<sup>38</sup> The effectiveness of these local exemptions is difficult to evaluate because the provisions do not specify a standard by which such discretion is to be exercised.

Articles 5 and 6 provide that export and technologically advanced enterprises shall be given priority in obtaining utilities, transportation services, communication facilities, and short-term revolving funds for their production processes; fees for utilities shall be the same as those paid by local state enterprises.<sup>39</sup>

The State Provisions grant a number of income tax preferences to foreign investors of export and technologically advanced enterprises. Article 7 specifies that when foreign investors remit abroad profits from export and technologically advanced enterprises, the amount remitted shall be exempt from income tax. Article 10 provides for tax refunds to foreign investors who reinvest distributed profits for a period of not less than five years in the establishment or expansion of export or technologically advanced enterprises. The tax refund equals the amount of income tax paid on the reinvested portion.

Article 8 grants a fifty percent reduction in income tax to export enterprises if seventy percent or more of their annual production is exported. This tax reduction becomes effective after the expiration of the period for reduction or exemption of enterprise income tax under existing regulations. Export enterprises that already enjoy a fifteen percent tax rate, including enterprises in the special economic zones, are currently taxed at a ten percent rate. Technologically advanced enterprises shall pay income tax at half the usual rate for an additional three years after the expiration of the tax reduction or exemption period available under existing regulations.

Current tax regulations provide equity joint ventures with a two-year tax exemption followed by a three-year period of half the usual rate of thirty-three percent.<sup>40</sup> Contractual joint ventures and wholly owned enterprises not located within certain special zones generally enjoy no such exemptions and reductions, but instead pay a progressive rate rang-

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38. *Id.*

39. *Id.* art. 6.

40. Income Tax Law of the Peoples's Republic of China Concerning Joint Ventures with Chinese and Foreign Investment [Joint Venture Income Tax Law] art. 3 (1980), *trans. in* [Taxation] China Laws for Foreign Business (CCH Austl. Ltd.) ¶ 33-500 (Apr. 4, 1986). The tax rate is 30% plus a local surtax of 10%, making the effective rate 33%.



ing from twenty to forty percent, plus an additional ten percent local income tax.<sup>41</sup> Because Articles 8 and 9 provide for tax reductions "after the expiration of the period for the reduction or exemption of enterprise income tax in accordance with the provisions of the State," the reductions provided under the new State Provisions are arguably not available to contractual joint ventures and wholly owned enterprises.

The remaining State Provisions offer investment incentives to all enterprises with foreign investment, including Chinese-foreign equity joint ventures, Chinese-foreign contractual ventures, and wholly foreign-owned enterprises. One of the most interesting provisions is article 16, which allows enterprises with foreign investment to refuse to pay for "unreasonable" local charges and to appeal these charges to local economic committees and ultimately to the State Economic Commission. The appeal procedure hopefully will provide a useful alternative to court proceedings already utilized by foreign enterprises in tackling the problem of excessive local charges.<sup>42</sup>

Article 11 exempts export products of enterprises with foreign investment from the consolidated industrial and commercial tax, with the exception of crude oil, finished oil, and other products subject to special state regulations.

Article 13 exempts imports needed by enterprises with foreign investment to carry out their export contract from regular import procedures. Such imports may not be sold in the domestic market or used in manufacturing products for sale in the domestic market. If such imports are used in either manner, the imported materials will be subject to the regular import procedures.

Article 14 gives enterprises with foreign investment the right to mutually adjust their foreign exchange surpluses and deficiencies. That provision goes beyond the January 1986 foreign exchange rules, which allowed currency adjustments only between enterprises with a common

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41. Foreign Enterprise Income Tax Law of the People's Republic of China art. 3 (1980), *trans. in* [Taxation] China Laws for Foreign Business (CCH Austl. Ltd.) ¶ 32-500 (June 18, 1987). Unlike the local surtax levied under the Joint Venture Income Tax Law, the 10% surtax levied on contractual joint ventures and wholly owned enterprises is levied on the taxable income rather than on the tax itself. Thus, the effective rate on that part of income above RMB1,000,000 (approximately US\$270,000) is 50%.

42. After a Sino-Japanese venture had paid a village west of Tianjin more than ten times the original rent required by a lease signed by both parties, the village sued the venture for more compensation. A lower court denied the village's claim, and the Higher People's Court in Tianjin upheld the decision. An official of Tianjin's Foreign Economic Relations and Trade Commission maintained, "Every company is equal before the law, no matter whether it is state-owned, collectively owned, individual or joint venture." See *Rights of Joint Venture Upheld*, *supra* note 8, at 8.

foreign partner.<sup>43</sup> The provision's impact is minimal, however, because of the small number of foreign enterprises with extra foreign exchange. For this provision to work, vehicles of exchange must also be established. Shanghai, for example, has set up a special foreign exchange trade desk at the Bank of China to facilitate exchanges of *renminbi* for foreign exchange certificates.

Article 15 requires government departments and lower level agencies to grant enterprises with foreign investment the right of autonomy in operations with respect to production plans, labor policies, the purchase and sale of products, and the raising of capital. These departments and agencies also shall "support enterprises with foreign investment in managing themselves in accordance with international advanced scientific methods."<sup>44</sup> This provision is a welcomed policy statement, but until it is interpreted by an appropriate government authority, its effect will be uncertain. Although the Ministry of Foreign Economic Relations and Trade is responsible for interpreting the State Provisions,<sup>45</sup> an official from the Investment Working Group of the State Council shed some light on the meaning of the phrase. According to the official, this provision means that

enterprises [operated with foreign capital] will have a free hand in production and management, and we hope will adopt scientific management methods to enhance productivity and boost their economic returns just as they would in other countries. . . . They will not be required to copy the management methods of Chinese state enterprises in handling international affairs.<sup>46</sup>

The effectiveness of this provision depends on the eagerness with which government departments and local agencies are willing to defend this right of autonomy of the enterprises.

Finally, article 17 provides that all examination and approval authorities must respond to documents submitted by enterprises with foreign investment within three months. The provision will undoubtedly increase the efficiency of government authorities, which in the past usually have required much longer than three months to approve or reject proposals of foreign enterprises.<sup>47</sup>

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43. Regulations of the State Council Concerning the Balance of Foreign Exchange Income and Expenditures by Sino-Foreign Equity Joint Ventures art. 9 (1986), *trans. in* [1 Bus. Reg.] *China Laws for Foreign Business* (CCH Austl. Ltd.) ¶ 6-590 (Mar. 4, 1986).

44. State Provisions art. 15.

45. *Id.* art. 21.

46. *See State Council Official Answers Questions, supra* note 15, at 32-33.

47. Lee & Ness, *Investment Approval*, *CHINA BUS. REV.*, May-June 1986, at 14, 14.

As noted above, the State Provisions contain many unclear and undefined terms which are perhaps more appropriate for a policy statement than for a set of laws. The effectiveness of provisions containing such terms will depend on the terms' interpretation by the Ministry of Foreign Economic Relations and Trade and on the forthcoming follow-up regulations.<sup>48</sup> Additionally, the impact of several provisions will depend upon the manner in which local agencies interpret and enforce them.

The State Provisions are, of course, no panacea to many of the problems presently facing an investor in China. The provisions do little to alleviate the foreign currency shortage which denies investors the ability to repatriate sufficient profits to make their projects worthwhile. The provisions also do not address the troublesome labor situation in China, where workers often lack incentive to work, are ill trained for the job, but are nevertheless relatively expensive to hire. Furthermore, the State Provisions do not lower the relatively high income tax rates levied on enterprises with foreign investment that are unable to meet the export or technology requirements of the provisions.<sup>49</sup>

Despite these shortcomings, the promulgation of the State Provisions evince a major change of attitude by China regarding foreign investment. Before the promulgation of the State Provisions, the Chinese attitude toward foreign investment appeared to be that foreigners should be grateful just to have the opportunity to invest in China and that their intention to make money was "downright presumptuous."<sup>50</sup> The promulgation of the State Provisions indicates that China has realized that increased foreign investment will result only from a favorable investment climate and that it is necessary for the Chinese Government to enact statutory incentives to create favorable conditions in order to compete with other popular investment havens in Asia. Thus, the promulgation of the State Provisions may be viewed as a prelude to other more fundamental reforms in favor of foreign investment.

The State Provisions provide substantial monetary and procedural incentives for foreign investment, and for export and technologically advanced enterprises in particular. The most important incentives include various tax preferences, a procedure for appealing unreasonable local costs, the establishment of maximum site use fees, and the time limit placed upon government authorities for acting on project proposals.

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48. See *Filling Out the Investment Framework*, *supra* note 2.

49. The income tax rate is particularly high on contractual joint ventures and wholly owned enterprises. See *supra* notes 40 and 41 and accompanying text.

50. See Gelatt, *supra* note 14, at 16, col. 4 (noting the comments of a foreign businessperson).

The State Provisions continue to be supplemented by both central government implementing regulations and local government provisions. As an example of the local provisions, this Article will next examine the Provisions of the Shanghai Municipality for the Encouragement of Foreign Investment.

#### IV. SHANGHAI PROVISIONS

The Shanghai Provisions, which became effective just three weeks after the promulgation of the State Provisions, are substantively similar to the State Provisions and supplement those provisions in many respects.

The aims set forth in article 1, which are nearly identical to the aims of the State Provisions, include the facilitation of the absorption of foreign investment, the introduction of advanced technology, the expansion of exports to generate foreign exchange, and the hastening of Shanghai's economic development. In keeping with these aims, the Shanghai Provisions offer general investment incentives to enterprises with foreign investment and special privileges to export and technologically advanced enterprises. Although the terms in the Shanghai Provisions are undefined, they are identical to the terms in the State Provisions and probably have the same definitions.

Articles 2 and 3 grant substantial local tax incentives to export and technologically advanced enterprises. These enterprises shall be exempt from local income tax during the period of their exemption from national enterprise income tax and for three years thereafter. Subsequently, the enterprises' local income tax shall be reduced by one-half for another three years. After this last three year period, export enterprises which export seventy percent or more of their products annually shall be exempt from local income tax for that year.

Article 4 gives export and technologically advanced enterprises more concessions in land use fees than the State Provisions. These enterprises shall be exempt from land use fees for three years after their establishment. Beginning in the fourth year, they shall pay fees at one-half of the minimum level specified in "concerned regulations," but no more than RMB2.50 per square meter. The term "concerned regulations" probably refers to article 4 of the State Provisions.<sup>51</sup> As with the State Provisions, land located in "busy urban sectors" is excluded from these concessions.<sup>52</sup>

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51. See *supra* notes 36-38 and accompanying text.

52. See *supra* note 37 and accompanying text.

Under articles 7 and 8, export and technologically advanced enterprises are entitled to priority in obtaining utilities, transportation services, communication facilities, and loans for short-term revolving funds needed for the production process. These enterprises shall pay utility charges according to the scale for local state enterprises.<sup>53</sup>

Remaining provisions provide incentives to all enterprises with foreign investment. Article 5 states that these enterprises are exempt from paying the state housing subsidies for their workers. This may be an empty promise, however, since such enterprises are required to pay for the improvement of the housing conditions of the same workers.<sup>54</sup>

Article 6 allows enterprises with foreign investment to employ workers from other provinces and cities as well as from Shanghai. While this should improve the size of the skilled worker pool, it certainly does not guarantee the availability of such workers. In the past, the Shanghai Government occasionally has denied approval of the use of construction companies which employed workers from Hong Kong or Guangzhou.

Under article 12, enterprises with foreign investment established in development zones will be given more, but unspecified, preferences. The effect of this provision, therefore, cannot be determined until implementing measures are promulgated.

Article 13 goes further than the State Provisions by requiring Shanghai authorities to approve or reject project proposals, feasibility study reports, contracts, and articles of association within thirty days of submission.<sup>55</sup> These authorities must also issue approval certificates within ten days after the submission of necessary documents. Given the slow bureaucracy of Shanghai,<sup>56</sup> this provision should be a welcome change to Shanghai investors.

To implement the State Provisions concerning the adjustment of foreign exchange among enterprises with foreign investment, article 10 provides for the establishment of a foreign exchange adjustment agency. Articles 9 and 11 provide for the establishment of a foreign investment service agency and a commodities service agency to facilitate other aspects of investment by foreign investors and enterprises.

Despite the familiar lack of clarity and precision, the Shanghai Provisions successfully supplement the State Provisions by encouraging foreign investment in China's most developed and technologically advanced

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53. *Id.* art. 7.

54. *Id.* art. 5.

55. *See supra* note 47 and accompanying text.

56. *See generally* Sterba, *supra* note 20, at 16, col. 1.

city. The Shanghai Provisions are especially significant because of their local income tax exemptions. They also go beyond the State Provisions in providing land use fee concessions and in significantly reducing the waiting period for government approval of investment proposals. While the Shanghai Provisions were among the first regulations to supplement the State Provisions, other major cities and special economic and development zones in China have followed Shanghai's lead by promulgating similar regulations,<sup>57</sup> thus creating a more favorable investment climate in many regions of China.

## V. CONCLUSION

Shortly after the initiation of the open-door policy in 1978, the excitement of foreign investors over the tremendous potential of the Chinese market often turned to bitter disappointment when foreign investors began to experience the harsh realities of doing business in China. With this lesson in mind, the author has observed investors taking a cautious approach in evaluating opportunities in China. A similar approach is advised when evaluating these recent changes.

Nevertheless, the State and Shanghai Provisions do provide significant improvements in the Chinese investment situation. The regulations address, at least in part, the problems of unreasonable taxes and fees, excessive bureaucracy, and high input costs. Most importantly, these provisions signal a recognition by the Chinese that these problems exist and should be addressed. However, the effectiveness of these provisions will hinge on the interpretation of certain terms, adherence to the regulations by local authorities, and the language of the implementing regulations. These unknown variables should persuade investors in China to continue their cautious approach.

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57. *See supra* note 3.

