

	Article 102	4.2.4.1
	Article 144	11A3
	Article 207	11A7, 12.7.2
	Article 240	7.2
	Article 248	9.2.2
	Article 306	11A1
Supreme People Court's Reply Letter on Whether State Owned Farms Can Be Made Bankrupt And How to Dispose Of Their Land After Their Bankruptcies (最高人民法院關於營農場能否破產及破產後土地如何處置的覆函)		7.2
Supreme People's Court's Reply on Whether Bankruptcy Debts Can Be Set Off Against Unpaid Share Capital ( 最高人民法院關於破產權能否與未到位的註冊資金抵銷問題的覆函)		6.5
Supreme People's Court's Reply on Whether it is Valid for a Debtor to Grant Security on all its Assets to one of its Many Creditors ( 最高人民法院關於債務人有多個債權人而將其全部財產抵押給其中一個債權人是否有效問題的批覆)		6.5
Supreme People's Court's Reply that the Execution Measures against Assets of a Debtor that has not been completed in the Course of Bankruptcy Proceedings shall be stayed ( 最高人民法院關於對破產案件的債務人未被執行的財產均中止執行題的批覆)		5.5.3, 6.5
Standard for Lawyers' Services in Anhui Province (Trial Implementation) ( 安徽省律師服務收標準 ( 試行 ))		4.2.6
Transformation of the Operation Mechanism in respect of All People's Industrial Enterprises Regulation ( 全民所有制工業企業轉換經營機制條例)		6.2.1
Unemployment Insurance Regulations ( 失業保險條例)	Article 33	9.3, 9.3.2
Wholly Foreign Owned Enterprise Law of the People's Republic of China ( 中華人民共和國外資企業法)	Article 6	10.5
		1.7.2.2

## DEFINITIONS OF BASIC TERMS

### In this book:

**1994 Optimisation Scheme Circular** means, in relation to the Optimisation Scheme, the State Council in its 1994 Circular on the Relevant Issues Concerning Trial Insolvency of State Owned Enterprises in Certain Cities ( 國務院關於在若干城市試行國有企業破產有關問題的通知國發 [1994] 59 號 ).

**1996 Optimisation Scheme Circular** means, in relation to the Optimisation Scheme, Circular of The People's Bank of China and State Economic and Trade Commission on Several Issues concerning the Trial Implementation of Mergers and Bankruptcy of State Owned Enterprises [1996] No. 492 ( 國家經貿委、中國人民銀行關於試行國有企業兼併破產中若干問題的通知國經貿企 [1996] 492 號 ).

**1997 Optimisation Scheme Circular** means, in relation to the Optimisation Scheme, the Supplementary Circular of the State Council on Certain Issues concerning the Trial Implementation of Mergers and Bankruptcy of State Owned Enterprises and Reemployment of their Employees in Certain Cities Qao Fa [1997] No. 10 ( 國務院關於在若干城市試行國有企業兼併破產和職工再就業有關問題的補充通知國發 [1997] 10 號 ).

**2002 Draft** means the draft of the new bankruptcy law made in 2002 by the Bankruptcy Law Enactment Committee ( 破產法立法委員會 ) organised by the Financial and Economic Committee ( 財政經濟委員會 ) of the Standing Committee of the NPC.

**2002 Judicial Interpretations** means, in relation to the Existing Bankruptcy Law, the Provisions on Some Issues concerning the Trial of Enterprise Bankruptcy Cases of the Supreme People's Court ( 最高人民法院《關於審理企業破產案件若干問題的規定》 ).

**Allocated Land** means land that is granted by the PRC Government to a grantee for no consideration in return.

**AMC** means an asset management company ( 資產管理公司 ) established under Asset Management Companies Regulations ( 金融資產管理公司條例 ).

**Bankruptcy ( 破產 )** means the process by which a legal person enterprise that is insolvent (as defined below) is wound up by the Court in the PRC; **Bankrupt** shall be construed accordingly.

**Bankrupt Enterprise** means an Enterprise that has been declared Bankrupt by the Court.

**Bankruptcy Expenses (破產費用)** means expenses incurred in the course of the Bankruptcy liquidation that are paid or payable out of the Bankruptcy Assets of an insolvent Enterprise under PRC law.

**Bankruptcy Assets (破產財產)** means assets of a Bankrupt Enterprise that are administered by its Liquidation Committee for distribution to its creditors that have filed their Bankruptcy Debts.

**Bankruptcy Debts (破產債權)** means claims that have been filed with and admitted by the Liquidation Committee of a Bankrupt Enterprise.

**Bankruptcy Law Interpretations** means the Opinions of the Supreme People's Court on the Enterprise Bankruptcy (Trial Implementation) Law of the People's Republic of China (最高人民法院關於貫徹執行中華人民共和國企業破產法(試行)若干問題的意見).

**CEPA** means the Closer Economic Partnership Arrangement between Hong Kong and the PRC (內地與香港關於建立更緊密經貿關係的安排).

**CIETAC** means China International Economic and Trade Arbitration Commission (中國國際經濟貿易仲裁委員會), a leading arbitration commission in the PRC.

**Civil Procedure Law Interpretations** means the Opinions of the Supreme People's Court on certain Issues concerning the Application of the Civil Procedure Law of the People's Republic of China (最高人民法院關於適用《中華人民共和國民事訴訟法》若干問題的意見).

**Civil Procedure Law** means the Civil Procedure Law of the People's Republic of China (中華人民共和國民事訴訟法).

**Civilly Run Non-Enterprise Organisations (民營非企業單位)** means organisations set up under the Provisional Measures on Civilly Run Non-Enterprise Organisations Units Registration (民營非企業單位登記管理暫行辦法).

**CJV** means a Sino-Foreign Cooperative Joint Venture Enterprise (中外合作經營企業) established under the Law of the People's Republic of China on Sino-foreign Co-operative Enterprises (中華人民共和國中外合作經營企業法).

**Collectively-Owned Enterprises (集體所有制企業)** means an Enterprise set up under Collectively-Owned Enterprises in Rural Areas Regulations (鄉村集體所有制企業條例) or the Collectively-Owned Enterprises in Cities and Towns Regulations (城鎮集體所有制企業條例) or otherwise.

**Commercial Bank (商業銀行)** means a commercial bank set up under the Commercial Banking Law of the People's Republic of China (中華人民共和國商業銀行法).

**Company (公司)** means a company established under the Companies Law of the People's Republic of China (中華人民共和國公司法).

**Companies Law** means the Companies Law of the People's Republic of China (中華人民共和國公司法).

**Constitution (憲法)** means the Constitution of the PRC, as amended from time to time.

**Court** means a People's Court of the PRC (人民法院).

**CPC** means the Communist Party of China.

**Domestic Enterprise** means an Enterprise other than an FIE and Foreign-invested Company Limited by shares.

**Draft New Bankruptcy Law** means a new bankruptcy law that is in the process of drafting and according to the Legal Daily of 18 December, 2003 will be examined for approval by the 10th Standing Committee during its session from 2003 to 2007.

**EJV** means a Sino-Foreign Equity Joint Venture Enterprise (中外合資經營企業) set up under the Law of the People's Republic of China on Sino-Foreign Joint Equity Enterprises (中華人民共和國中外合資經營企業法).

**Enterprise (企業) or PRC Enterprise** means a business organisation (whether in the form of Legal Person Enterprise or non-Legal Person Enterprise) formed or otherwise registered in the PRC and under PRC law that carries on business operations in its own name for the purpose of making profits.

**Enterprise Legal Representative (企業法定代表人) or Enterprise Legally Designated Representative** means the person registered as a legal representative of a Legal Person Enterprise under the Enterprise Legal Person Legal Representative Registration Administration Measures (企業法人法定代表人登記管理規定) or otherwise.

**Enterprise Supervision Group (企業清算監管組)** means a group of people comprising the representatives of the Supervising Department of a Legal Person Enterprise, its shareholders, its original management, its major creditors, accountants and/or lawyers that may be appointed by the Court after it has accepted a Bankruptcy application against a Legal Person Enterprise to take control over the assets of such Legal Person Enterprise.

**Existing Bankruptcy Law** means the Enterprise Bankruptcy (Trial Implementation) Law of the People's Republic of China (中華人民共和國企業破產法(試行)).

**Foreign Debts (外債)** means foreign currency loans repayable by domestic organisations such as financial institutions and Enterprises to (i) overseas governments, (ii) supranational organisations; (iii) financial institutions, Enterprises, individuals or economic organisations outside the PRC and (iv) foreign financial institutions within the territory of the PRC (See however, 3.5 about the definition of foreign debts under the New Foreign Debt Administration Tentative Measures (外債管理暫行辦法) that tends to be ignored in practice as of the end of 2003).

Category of Enterprise	Remarks	Sub-category if any
11. wholly foreign-invested Legal Person Enterprises	– WFOEs can only be legal persons.	– N/A
12. wholly foreign-invested Non-Legal Person Enterprises	They do not have the status of a separate legal entity	– branches and representative offices of Foreign Enterprises in the PRC

#### 1.4 LIMITATIONS ASSOCIATED WITH DIFFERENT TYPES OF PRC ENTERPRISES

In general, different entities may incur debts, though not every type of entity may incur Foreign Debts (see 3.5 for more details).

However, if the borrower is an FIE, it will have a rather strict registered capital to total investment ratio as required by the Provisional Regulations of the State Administration of Industry and Commerce on the Ratio between the Registered Capital and Total Investment of Sino-foreign Joint Equity Enterprises (國家工商行政管理局關於中外合資經營企業註冊資本與投資總額比例的暫行規定):

Total Investment Amount	Registered Capital as a Percentage of Total Investment Amount	Minimum Registered Capital Amount
Not exceeding US\$3,000,000	70% or more	N/A
Exceeding US\$3,000,000 and not exceeding US\$10,000,000	50% or more	US\$2,100,000
Exceeding US\$10,000,000 and not exceeding US\$30,000,000	40% or more	US\$5,000,000
Exceeding US\$30,000,000	1/3 or more	US\$12,000,000

In order to increase the borrowing limit, an FIE must first increase its total investment and registered capital amounts.

#### 1.5 NON-ENTERPRISE ENTITIES AND THEIR LIMITATIONS

According to the General Principles of Civil Law, Non-Enterprise entities in the PRC generally include:

- (i) State/Government/Government organs;
- (ii) Social Organisations
- (iii) Public Institutions;
- (iv) Privately Run Non-Enterprise Organisations;
- (v) Individual Industrial and Commercial Households (個體工商戶)<sup>9</sup>;
- (vi) Rural Business Contractors (農村承包經營戶)<sup>10</sup>; and
- (vii) private individuals.

##### 1.5.1 State/Government/Government Organs

Government organs may not incur Foreign Debts save that they may borrow from overseas governments or supranational organisations with the State Council's approval<sup>11</sup>. The MOF is the government organ that incurs debts<sup>12</sup> on behalf of the State. According to the General Principles of Civil Law, the MOF is a legal person<sup>13</sup>.

##### 1.5.2 Social Organisations

Social Organisations are set up by PRC citizens to carry on non-profit making activities to achieve the common aims of its members<sup>14</sup>. Examples of social organisations are:

- 9 Article 29 of the General Principles of Civil Law, debts incurred by Individual Industrial and Commercial Households and rural business contractors shall be undertaken by, where such Enterprises are individually operated, the relevant individuals with their properties or, where such Enterprises are operated by households, the relevant households with their properties.
- 10 Pursuant to Article 27 of the General Principles of Civil Law, rural business contractors are members of collective economic organisations (農村集體經濟組織) that carry on the commodities business in accordance with a contractor contract.
- 11 Article 46, the Detailed Rules for the Implementation of the Administrative Measures on Security Given to Foreign Parties by Domestic Institutions (境內機構對外擔保管理辦法實施細則).
- 12 Article 12, the New Foreign Debts Measures.
- 13 Article 50, the General Principles of Civil Law provides that government organs having independent operation funds will have the status of a legal person.
- 14 Article 2, the Social Organisations Registration Administration Regulations (社會團體登記管理條例).

### 2.3.5 Administrative Regulations made by different Ministries/Commissions of the State Council (部門規章)

Pursuant to the Legislation Law<sup>10</sup>, Ministries/Commissions of the State Council and the PBOC also have power to make administrative Regulations within their scope of authority.

An example of such administrative Regulations is a circular issued by the People's Bank of China and State Economic and Trade Commission on Certain Issues on the Trial Implementation of Mergers and Bankruptcy of State Owned Enterprises Guojing Maoqi [1996] No. 492 (國家經貿委、中國人民銀行關於試行國有企業兼併破產中若干問題的通知國經貿企[1996] 492 號).

## 2.4 THE MAKING OF REGIONAL LAWS AND REGULATIONS

There are five levels of administrative levels in the PRC, four of which are regional (see Appendix 2 for details).

At Regional level there are regional governments that are responsible for the administration of their own administrative units.

Regulations that apply to a particular region can be made by:

- (i) the State Council and its Departments and Commissions<sup>11</sup>;
- (ii) regional People's Congresses and their Standing Committees at the "province, region and city level" (see Appendix 2)<sup>12</sup>; and
- (iii) regional governments at
  - (a) the province, region and city level and
  - (b) in large cities<sup>13</sup>.

An example of administrative Regulations made by the State Council that apply to certain regions is the 1994 Optimisation Scheme Circular. Regulations made by the People's Congresses (人民代表大會) at the province, region and city level are called regional legal rules (地方性法規). For example, in 1993 the Standing Committee of the People's Congress of Guangdong Province passed the Guangdong Province Company Bankruptcy Regulation (廣東省公司破產條例).

Regulations made by regional Governments in the province, region and city level and of large cities are generally referred to as regional regulations

<sup>10</sup> Article 71 of the Legislation Law.

<sup>11</sup> Articles 71 and 72 of the Legislation Law.

<sup>12</sup> Article 63 of the Legislation Law.

<sup>13</sup> Article 73 of the Legislation Law.

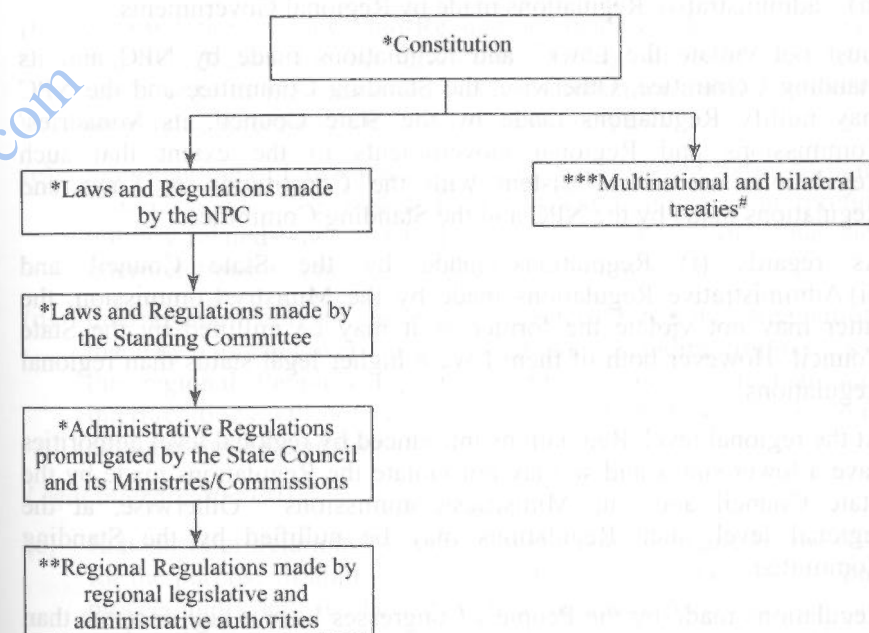
(地方性規章). An example is the Beijing Municipality People's Government in 2000 passing the Beijing Municipality State Owned Enterprise Bankruptcy Work Tentative Provisions (北京市國有企業破產工作暫行規定).

## 2.5 HIERARCHY OF THE LEGAL STATUS OF DIFFERENT SOURCES OF LEGAL RULES

As previously discussed in this chapter, one way to reconcile inconsistencies among legal rules is to gain a clear understanding of their respective legal statuses. The following chart summarises the hierarchy of the respective legal statuses of legal rules within the PRC legal system.

### Hierarchy of Legal Rules in the PRC

There are seven sources of legal rules in the PRC<sup>14</sup>:



\* national Laws and Regulations

\*\* regional Regulations

\*\*\* international treaties

# There are no provisions in the Constitution and the Legislation Law to deal with the relationship between national legal rules and international law.

<sup>14</sup> Judicial Interpretations made by SPC are not covered by the above chart because formally they are not considered a source of legal rules (as Courts may only interpret Laws and Regulations but may not make any legal rules). As they are binding on lower Courts, they are a very important supplement to PRC Laws and Regulations and therefore an indispensable part of the PRC legal system (see 2.6.1 below)

It has been suggested by some PRC academics<sup>15</sup> that national treaties entered into by the PRC government should at least have the status of national Laws but they cannot violate the Constitution. However, if there are any conflicts between such treaties and national Laws, provisions of such treaties will prevail.

There are very detailed provisions on this issue in Chapter 5 of the Legislation Law that explains the hierarchy of different legal rules in the PRC. In summary, the Constitution is the most fundamental law and therefore has the highest legal status in the PRC. No other PRC Laws, Regulations or international treaties may violate any of its provisions.

As the NPC and its Standing Committee are the official law-making bodies in the PRC,

- (i) administrative Regulations introduced by State Council and its Ministries /Commissions; and
- (ii) administrative Regulations made by Regional Governments,

must not violate the Laws<sup>16</sup> and Regulations made by NPC and its Standing Committee. Otherwise, the Standing Committee and the NPC may nullify Regulations made by the State Council, its Ministries/Commissions and Regional Governments to the extent that such Regulations are not consistent with the Constitution or Laws and Regulations made by the NPC and the Standing Committee.

As regards (i) Regulations made by the State Council and (ii) Administrative Regulations made by the Ministry/Commission, the latter may not violate the former or it may be nullified by the State Council. However both of them have a higher legal status than regional Regulations.

At the regional level, Regulations introduced by regional level authorities have a lower status and so may not violate the Regulations made by the State Council and its Ministries/Commissions<sup>17</sup>. Otherwise, at the regional level, such Regulations may be nullified by the Standing Committee.

Regulations made by the People's Congresses have a higher status than Regulations made by the regional governments at the same and lower levels<sup>18</sup>. Regulations made by the regional governments at a higher level rank in priority to Regulations made by the regional governments at lower levels<sup>19</sup>.

15 See Ma Chengyuan and Li Juqian, *International Law*, the People's University of China Press (馬呈元, 李居遷, 國際法, 中國人民大學出版社) June 2003.

16 Article 79 of the Legislation Law.

17 Article 79 of the Legislation Law.

18 Article 80 of the Legislation Law.

19 Article 80 of the Legislation Law.

## 2.6 INTERPRETATIONS OF LAWS AND REGULATIONS

### 2.6.1 Different types of interpretations of PRC Laws and Regulations

There can be many different types of 'interpretations' of PRC Laws and Regulations that (i) are made by different PRC government authorities for the purposes of applying the relevant PRC Laws and Regulations, and (ii) are binding within their own domains such as:

#### *Legislative interpretations*

- (a) interpretations of the Constitution and Laws by the Standing Committee;

#### *Administrative interpretations*

- (b) interpretation of Laws and Regulations made by the State Council and its delegates for the purpose of carrying out its administrative work (only to the extent that such interpretations will not violate underlying intention of the Constitution and Laws);
- (c) interpretation of Laws and Regulations made by the Central Military Commission (中央軍事委員會) for the purposes of interpreting military-related Laws and Regulations (only to the extent that such interpretations will not violate the Constitution and Laws);
- (d) interpretation only to the extent of relevant regional Regulations made by regional government authorities and standing committees of the regional People's Congress (only to the extent that such interpretations will not violate the Constitution, Laws and national administrative Regulations);

#### *Legal interpretations*

- (e) Judicial Interpretations of Laws and Regulations made by the SPC for the purpose of applying the same to cases in the course of court proceedings (only to the extent that such interpretations will not violate the Constitution and Laws); and
- (f) interpretations of Laws and Regulations made by the Supreme People's Procuratorate for the purpose of applying the same to discharge their duties (only to the extent that such interpretations will not violate the Constitution and Laws).

### 2.6.2 Judicial Interpretations by the SPC

Judicial decisions are, generally speaking, not legally binding in the PRC. Therefore Judicial Interpretations in this sense do not cover interpretations

### 3.3 OVERVIEW OF PRC SECURITY SYSTEM

There are five types of security that are recognised under PRC law namely guarantees ( 保証 ), mortgages ( 抵押 ), pledges ( 質押 ), liens ( 留置 ) and deposits ( 定金 )<sup>2</sup>. PRC security has certain unique features, for example.

- (a) Security does not cover future assets. So new or supplemental security documentation is necessary to cover such assets.
- (b) Security also does not cover floating assets. So there are no floating charges in the PRC.
- (c) Although there are mortgages but, they unlike common law mortgages, do not involve transfer of proprietary rights. So there is no security by way of assignment in the mortgages PRC.
- (d) Rights in general can be pledged which is essentially similar to a fixed charge under common law.

2 A guarantee is a contractual undertaking by a guarantor in order to perform the obligations of a debtor when that debtor fails to perform his obligations (Article 5, the Security Law).

A mortgage is an act of a debtor, or a third party, who, without transferring possession, designates property as security against the claims of a creditor. When the debtor fails to honour his obligations, the debts owing to the creditor will be paid from the proceeds from the transfer, auction or sale of the property (Article 33, the Security Law).

A pledge is the act of a debtor or a third party in transferring possession of movable property to the creditor as security for the creditor's claim. If the debtor fails to perform his/her obligations, the creditor may obtain ownership of the movable property or be compensated with the proceeds of its auction or sale (Article 63, the Security Law). Under PRC law, rights may also be pledged (Article 75, the Security Law).

A lien is the act of the creditor in obtaining possession of the debtor's movable property. When the debtor fails to honour his/her obligations, the creditor may be compensated from the proceeds obtained from the auction or sale of the property (Article 82, the Security Law).

As regards deposits, the parties may agree by contract that one party shall provide a deposit as security for his obligations to the other party creditor. When the debtor has honoured his obligations, the deposit shall be applied to set off against the purchase price or be refunded. Where the deposit provider fails to honour his obligations, the deposit will be forfeited. If the other party fails to perform his obligations as stipulated the deposit shall be refunded, together with compensation provided for in the contract (Article 89, the Security Law).

There is a complicated approval and/or registration system even if the security is not Foreign Security<sup>3</sup>.

### 3.4 OVERVIEW OF FOREIGN EXCHANGE CONTROL IN THE PRC

RMB is the official currency in the PRC but it is not fully convertible. The PRC now does not have exchange control over its current account transactions, though it still has exchange control over its capital account transactions.

#### Current Account Transactions

Foreign exchange controls over current account transactions have been cancelled. The payment for imports and exports of goods are still subject to the so called verification and cancellation system ( 核銷制度 ) of the SAFE, where the authenticity of the transactions underlying the payment will be verified to avoid fake foreign trade transactions. While domestic entities may purchase foreign currencies from DFXBs with RMB to settle foreign currency payment, they need to produce the relevant supporting documents for verification by the SAFE/"designated foreign exchange banks". Also domestic entities are still required to (i) repatriate foreign currency income into the PRC and (ii) subject to certain exceptions, sell them to designated foreign exchange banks.

3 For example,

- where the security is a mortgage on land use rights (without buildings erected thereon) in the PRC, then, the security shall be registered with the relevant land bureau within 15 days (Article 3, Circular on Certain Issues in relation to the Mortgage of Land Use Rights (關於土地使用抵押登記有關問題的 通知));
- where the security is a mortgage on building, the security shall be registered with the relevant building bureau within 30 days in accordance with the Article 30, Administration of Mortgage of Urban Real Estate Procedures (城市房地產抵押管理辦法) (in the author's experience, this time limit may not be strictly followed in some regions of the PRC);
- where the security is a pledge over equity interests in an FIE, approval of the original approving authority (Article 12, Certain Regulations on Changes to Shareholdings in Foreign Investment Enterprises (外商投資企業投資者股權變更的若干規定));
- where the security is on shares in a PRC listed company, registration at [the China Securities Depository & Clearing Corporation Limited] (Article 103, Explanations of Certain Issues Concerning the Security Law of the People's Republic of China);
- where the security is a mortgage on equipment or machinery, Mortgages on machinery shall also be registered with the SAIC (Article 42, the Security Law. Also see the Administration Measures in accordance with the provisions the Registration of Mortgages over Movable Properties of an Enterprise (企業動產抵押登記管理辦法)).