

CHAPTER 1

Like wading across a stream: law, reform and the state enterprise

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The implementation of enterprise reform in China has been an integral part of the transition from the traditional command economy to the socialist market economy. Since the early 1980s policy-makers have been analyzing the most useful theories to improve the operation of enterprises and debating the type of legislation that would be most appropriate. The importance attributed to enterprise reform was emphasized with the announcement of the policy of 'change the management mechanisms of the state-owned enterprises and establish the modern enterprise system'. The aim of this essay is to examine the development of enterprise reform in the People's Republic of China (PRC).

There will be three parts to the chapter. The first part of the chapter will set out the historical background to enterprise reform. The second part will discuss the effectiveness of the implementation of the current enterprise reform. The third part will consider future possible changes to the enterprise system.

HISTORICAL BACKGROUND

From the founding of the People's Republic of China in 1949 to the inauguration of the Economic Reform and Open Door policy in 1978, China has built its economy on the basis of public ownership of the whole economy. By 1978, the public sector was responsible for 98% of the Gross National Product (GNP). The public sector accounted for almost 100% of the total industrial output, of which 77.6% was produced by state-owned enterprises and 22.4% by other collectively-owned enterprises in the economy. These collectively-owned enterprises, normally operating in the urban areas, were nearly identical in organization and function as the state enterprises. The state-owned enterprises under the highly centralized command economy, adopted the model of the 'socialist mass-production factory' from the former Soviet Union. The official phrase, 'state ownership and state man-

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agement', characterized the internal structure of the traditional enterprises. Under this system the assets of the enterprises were owned by 'the whole people belonging to all the people, ie to the state'. The management structure involved the state managing and regulating all personnel, finance, physical assets, production, supply and marketing affairs under the guidance of centralized state plans. The responsible departments of the state and local government were both the owner and the manager of the enterprises. The enterprises did not enjoy independent legal status nor did they have any autonomous decision-making power. According to enterprise guidelines set out in the *Seventy Policy Points for State Industries* promulgated in September of 1961, the duty of the enterprise was strictly limited to the fulfilment of the task quotas stipulated by the state plans.

By the end of the 1970s, the state had begun to separate the operation of enterprises from the centralized plans. One planning guideline acknowledged that 'the plan whilst playing a major role in the national economy is to be supplemented by market adjustment'. In effect although centralized planners still maintained comprehensive control over pricing, material control, investment, labour, and wages, the state looked to market forces to improve the economy. The first systematic effort to incorporate market forces into the Chinese economy involved the liberalization of the agricultural economy. Rather than provide foodstuffs that were ordered by the state, farmers were allowed to provide food products that the agricultural markets were demanding. Soon standing markets for the sale of fruits and vegetables were springing up in major cities.

In addition to the incorporation of market forces into the agricultural economy, experiments in reforming the enterprise began in 1978. The first step for enterprise reform involved the state delegating independent management authority to and sharing profits with the enterprise. The readjustment of the management relationship between the state and the enterprise and the initiation of different forms of proportional sharing of the profits by the enterprise brought about a degree of enthusiasm for production from the management and workers of the enterprises under reform. By the mid-1980s, over one million urban enterprises were operating and employing more than 80 million people. The taxes and other administrative earnings from these enterprises constituted over 80% of state revenues. Although state enterprises remained the predominant form of economic organization, enterprises in other economic sectors outside the cities also grew rapidly. Enterprises under reform were no longer merely 'independent production and business management units' but emerged as 'a commodities producer and business manager' in the market.

The reform of the enterprises in the PRC did not occur overnight. By first examining the historical development of the reform, we will be in a better position to understand its present evolution. The historical development of the enterprise reform over the past ten years

may be roughly divided into three stages: legal introduction, legal consolidation and system renovations.

Legal Introduction

The *Decision by the Central Committee of the Communist Party of China on the Reform of the Economic System* ('1984 Decision') passed on 20 October 1984, was a milestone marking the beginning of the enterprise system reform. The 1984 Decision unequivocally illustrated that the socialist economy of the PRC was a planned commodities economy and acknowledged the status and function of the use of commodities in the economy. The 1984 Decision sought to improve commodities production and exchange by strengthening the dynamism of the enterprises, particularly that of the state-owned large and medium-sized enterprises. The 1984 Decision suggested that one of the major deficiencies under the old system was the consolidation of state ownership and direct state management of the enterprise. In recognition of the importance of the 'right to own' and the 'right to manage', it stated that power must be delegated to the management of the enterprises to determine production schedules, purchase supplies, marketing strategies, investment decisions, hiring, firing, rewarding, and pricing on the condition that the enterprises respect the state plans and regulations. The aim of the 1984 Decision was to create an enterprise that was a relatively independent economic entity, a socialist commodities producer and an independent business manager. The intention was that such an enterprise would conduct its own business, be responsible for its own profits and losses, and be capable of reforming and developing itself according to law. It marked the first time that China's government officially recognized the status of the enterprise as a legal person.

On 12 July 1986 the *General Provisions of the Civil Law of the People's Republic of China* (GPCL), were promulgated, and went into effect on 1 January 1987. The GPCL recognized that the state-owned enterprises, like other enterprises, are required to have the status of a legal person. Article 41 states that:

a State owned enterprise or a collectively owned enterprise, after the approval by and registration with the related government authority, acquires the status of a legal person provided that the enterprise meets the State requirements in asset amount, organizational charter and structure, premises and ability to meet civil obligations.

Article 48 further sets forth the fiduciary responsibility of the enterprise stipulating that the legal person of a state enterprise must meet its civil obligations with the assets the state authorizes it to manage. Article 82, in describing the enterprise's legal status, states that 'the State enterprise enjoys the right to manage the assets as authorized by the State, under statutory protection'.

Soon after the 18th Session of the 6th National People's Congress (NPC), on 2 December 1986, the NPC enacted the *Bankruptcy Law of the People's Republic of China* (BL). One of the purposes of the BL was to clarify the claims on assets owned by the state enterprise, if the enterprise went bankrupt. The BL established that at the time of the bankruptcy announcement, all the assets that the bankrupt enterprise is managing are 'bankrupt assets', and must be used to compensate outstanding debts in a legally established order.

On 13 April 1988, the First Session of the 7th National People's Congress enacted the *State Owned Industrial Enterprise Law of the People's Republic of China* (SOIEL), the first enterprise law of the PRC. It sets out a systematic judicial definition of the nature, rights and obligations of the state enterprises. The SOIEL states that:

the State owned industrial enterprise is a socialist commodities production and business management unit that engages in independent management and assumes independent responsibility for its profits and losses, and keeps an independent budget and accounting, in accordance with the law. ... [T]he assets of the enterprise belong to the whole people. The State authorizes the enterprise to manage the State assets based on the principle of division between ownership and management. The enterprise, as authorized by the State, has the right to possess, use and legally dispose the assets as it sees fit.

Finally, it stipulates that the enterprise, pursuant to the law, acquires the status of a legal person, must meet normal civil obligations with its assets, and must have the executive manager of the factory as the legal representative of the enterprise.

From the publication of the 1984 Decision to the enactment of the SOIEL, the juridical concept of the enterprise had incorporated the notion of a planned commodities economy, recognized a viable division between the right to own and the right to manage, and clarified the legal nature and status of the enterprise as an independent commodities producer and business manager. During this period, law-makers carried out reform experiments as if 'wading across the stream by feeling out one stepping stone after another'. A two-step measure of replacing *earnings turned over to the state* with *taxes collected by the state* was implemented in order to reshape the distribution relationship between the state and the enterprise through a uniform tax system. A synchronized reform both in pricing and taxation was planned to rationalize the price structure and speed up the process of implementing market reform. Mandatory planning quotas were gradually decreased while pricing for commodities normally subject to planning guidance was liberalized. At the end of 1986, a new management and responsibility system was adopted throughout China which enabled an enterprise's management to contract out state assets and to keep the earnings above the amount contractually owed the state in order to provide money for expansion, reinvestment, higher wages and more fringe benefits for the employees. As a result of

the interest mechanism in the contracting out system, the enterprise was induced to act to meet the needs of the market in terms of production determined by sales, reinforced marketing, research and development, and information gathering.

During this time, however, law-makers had not decisively come to terms with the notion of the market playing a basic role in allocating resources. Strong administrative intervention remained and the growth of the market was still subject to many constraints. In the general policy debate, the term 'commodities economy' was politically correct, whilst 'market economy' was wrong. These early stages of reform, whilst recognizing the grassroot needs for some form of market economy and beginning the process of decentralization, merely introduced the possibilities of the free market system to the nascent enterprise reform. This early period of reform was, however, only the preparatory stage toward the development of the modern Chinese enterprise.

Legal Consolidation

In the early 1990's the general consensus amongst economists and academics was that the reform of the enterprise system must continue to be market-oriented. The southern inspection tour by Mr Deng Xiaoping and his remark that the 'planned economy is not equivalent to socialism, nor is the market economy equivalent to capitalism' further reaffirmed the commitment of the state to economic reform. In October 1992, the 14th Chinese Communist Party Congress formally declared that the party would strive to establish a socialist market economy within the Chinese economic system. Since the beginning of the reform period, the state, to a considerable extent, has succeeded in the assimilation of a market economy.

For instance, the growth of the commodities market has been substantial. With regard to the total industrial output, the state reduced the rate of mandatory planning production from 80% in the 1980s to less than 20% today. The prices for approximately 90% of the agricultural and other non-staple food stuffs and consumer goods as well as 80% of the means of production are now all subject to the market. Also the 'rural township' enterprises and the 'foreign-invested' enterprises have undergone rapid reform and are contributing significantly to the nation's economic development. Additionally the reform of state enterprises is now high on the law-maker's agenda.

On 23 July 1992, the State Council promulgated *Regulations for the Transformation of Management Mechanisms of the State Industrial Enterprises* ('1992 Regulations'). The law's objective is 'to help usher the State industrial enterprises into the market'. The 1992 Regulations, based on the principles laid out in the SOIEL, redefines the objectives of the management mechanisms in terms of meeting the needs of the market. The rights for greater management autonomy

Company purchases

A company may not purchase its own shares unless shares must be cancelled for the purpose of reducing its capital, or the company merges with another company which holds shares in the former company. The reason for the stringent restrictions on companies purchasing their own shares is the fear that if a company is allowed to purchase its own shares, the balance between the company and its shareholders will be damaged and this may lead to the management of the company taking advantage of its power over the shareholders.

CHAPTER 5

Foreign investment and the new company law

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Since 1979, and the establishment of the open door policy, China has developed an extensive regulatory framework with respect to foreign investment in China. Until recently foreign investment projects have been regulated by laws such as the *Chinese-Foreign Equity Joint Venture Law* (CFEJVL), the *Chinese-Foreign Contractual Joint Venture Law* (CFCJVL) and the *Wholly Foreign-owned Enterprise Law* (WFEL). Within the last year, the government has enacted a new *Company Law* which, it is expected, will change considerably the way China governs investment projects with foreign funds. The aim of this chapter is to discuss how the new law will affect the regulation of foreign investment in China and to contrast it with other relevant regulations. In the first part, I shall set out the general aims of the *Company Law*. In the second part, I will examine the differences in the regulation of corporate structure amongst the *Company Law* and other laws related to foreign investment. In the third part, I shall consider how the government intends to manage potential conflicts of law amongst the regulations.

GENERAL AIMS OF THE COMPANY LAW

China's *Company Law* (CL) is intended to provide an efficient regulatory framework for an advanced enterprise system by taking into account China's past regulatory history and international commercial practice. The application of the CL will provide an effective legal system for foreign investment enterprises which, in turn, should facilitate the profitability and development of economic enterprises. For instance, in the past, regulations restricted the form of foreign investment enterprises to limited companies only; under the current provisions, however, the CL allows a foreign investor to establish a joint stock company together with other investors.

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Other examples of how the CL has liberalized the regulation of foreign investment are provided in articles 83, 135 and 155. These laws state that a joint stock company may issue shares to the public outside the mainland of China upon approval by the Securities Authority of the State Council, that the State Council may adopt regulations governing other kinds of shares involving foreign investment but not provided for in the CL, and that shares of a joint stock company may be traded on a stock exchange outside the mainland of China upon approval by the Securities Authority of the State Council. All these provisions provide a legal basis for the issue and transfer of B shares and H shares. Under current practice, B shares are securities which are subscribed for by, and pay dividends to, foreigners, compatriots in Hong Kong and Macao and overseas Chinese, in foreign currency. H shares are securities where joint stock companies, upon approval, issue shares on the Hong Kong Stock Exchange. At present, a number of Chinese companies are already listed on the Hong Kong Stock Exchange.

CORPORATE STRUCTURE

The implementation of the new CL may be perceived as recognition on the part of the Chinese government of the need to appreciate that the success of the open door policy has brought about the necessity to re-think how China governs her economic enterprises. The considerable economic demands brought to bear on new companies in China have required China to change the way companies are governed.

Registered Capital

The registered capital of a limited liability company is the total amount of the paid-up capital contributed by shareholders at the time of registration. For domestic enterprises, the CL sets a pre-determined minimum registered capital requirement. In contrast, foreign-invested limited liability companies with foreign investment are not subject to either minimum registered capital requirements or requirements that the registered capital be fully paid at the time of registration. For such companies, contribution of the promised capital may be provided after registration.

Organizational Structure

The CL provides that, except for wholly state-owned companies and small companies, limited liability companies shall hold Shareholders' Meetings periodically as well as establish a Board of Directors and a Supervisory Board. Pursuant to the provisions of the CFEJVL and the CFCJVL, however, foreign-invested companies are not obliged

to hold Shareholders' Meetings nor do they have to establish Supervisory Boards. In enterprises with foreign investment, the management role of the Board of Directors is guided by the articles of association and the principle of reciprocity. Whilst the CL stipulates that between 3 and 13 directors in limited liability companies must be appointed, the CFEJVL leaves the discretion to decide the appropriate number of directors to the major partners of the company. The chair of the Board of Directors will be appointed by one partner, whilst the vice-chair will be appointed by the other.

Shareholders

The CL permits only state-authorized investment institutions or departments to establish sole-shareholder companies. Other limited liability companies are obliged to have at least two shareholders. Pursuant to the WFEL, however, foreign-owned enterprises are permitted to be sole-shareholder companies.

Withdrawal of Capital

The CL stipulates that shareholders shall not withdraw capital after the registration of the company. Shareholders, however, may obtain returns from capital investment either through the distribution of dividends or the transfer of capital. In contrast, the CFCJVL allows foreign investors to receive returns from capital through accelerated depreciation.

Capital Distribution

According to the CL, a shareholders' contribution of tangible assets, industrial property rights, non-patented technology and land use rights of a company shall be valued as a capital contribution to the enterprise. The distribution of dividends to shareholders will be calculated in proportion to the shareholders' capital contribution. By contrast, the CFCJVL does not require that the contribution of tangible assets, land use rights, industrial property rights, and non-patented technology by the shareholder shall be valued as part of the capital contribution of the investing parties. Further, the investing partners in contractual joint ventures are not required to distribute dividends according to the proportion of an investor's capital investment.

Also, the CL provides that the amount of capital contribution through industrial property rights and non-patented technology shall not exceed 20% of the registered capital of the limited liability company unless the relevant regulations adopted by the state in respect of the exploitation of new and advanced technology provide otherwise.

The CFEJVL and the CFCJVL, however, do not specifically regulate the proportion between cash and non-cash capital contributions.

Furthermore while all three foreign investment enterprise laws have provisions for tax incentives, the CL does not stipulate the type of companies which may enjoy the tax benefits. The difference is due to the fact that the CL and the three foreign investment enterprise laws regulate different social relations. The CL is limited mostly to the regulation of organizations and conduct of companies. In contrast the three foreign investment enterprise laws regulate not only organizations and the conduct of enterprises but also the control of investments and currency transactions.

Common Welfare Fund

The CL requires that a company should allocate 5% to 10% of its after-tax profits to a common welfare fund to be used for the collective welfare of staff and workers. The laws on enterprises with foreign investment also provide that such enterprises should allocate its after-tax profits to some common welfare fund, but the discretion to determine the proportion of allocation is retained by the Board of Directors.

Companies Existing Prior to the *Company Law*

Companies established and registered in accordance with the law, administrative regulations, local regulations or the *Opinion on Standardization of Limited Liability Companies* and the *Opinion on Standardization of Joint Stock Companies* adopted by the relevant department of the State Council prior to the coming into effect of the CL, shall continue to be recognized under the CL. Those companies which have not met the requirements stipulated in the CL shall be required to make appropriate organizational changes. The CL provides for appropriate time extensions. The State Council shall adopt appropriate detailed implementation regulations.

Duration of Companies

Finally, the CL does not specify the required duration of a company while the CFEJVL and the CFCJVL stipulate that the duration of the ventures must be designated in the joint venture agreement.

CONFLICT OF LAWS

Article 18 of the CL stipulates that:

The present Law shall apply to limited liability companies with foreign investment. Where laws concerning Chinese-foreign equity joint ven-

tures, Chinese-foreign contractual joint ventures and foreign-funded enterprises provide otherwise, such provisions shall prevail.

My understanding is that this provision refers to potential conflicts amongst the CL and the three foreign investment enterprise laws. According to general principles of Chinese jurisprudence, before the CL became effective on 1 July 1994, foreign-invested limited liability companies were only regulated by foreign investment enterprise laws. After 1 July 1994, foreign-invested limited liability companies became subject not only to foreign investment enterprise laws but also to the CL. The CL affects the establishment, dissolution, liquidation, insolvency and legal liabilities of domestic and foreign investment enterprises. The State Council is examining all potential conflicts between the laws concerning foreign-invested limited liability companies and the CL.

One major concern amongst foreign and domestic investors is whether all foreign-invested limited liability companies will have to issue shares to the public after 1 July 1994. These concerns are unfounded because according to China's CL, limited liability companies are not permitted to issue shares to the public. Another concern raised by investors is how the government will manage foreign-invested limited liability companies that convert into joint stock companies. The answer depends upon whether the Securities authority permits such a company to become listed in the first place.

Generally speaking the CL is not meant to replace or repeal the CFEJVL, CFCJVL, WFEL or other important laws that regulate domestic enterprises such as the *Law on Industrial Enterprises Owned by the Whole People*, *Regulations Concerning Urban Collectively-owned Enterprises*, *Regulations Concerning Rural Collectively-owned Enterprises*, or *Provisional Regulations on Private Enterprises*. China needs a number of different regulations to control enterprises because so many different forms of enterprises exist.

CONCLUSION

The new CL is an important contribution to China's development under the open door policy. Whilst the implementation of the open door policy has served to expand the growth of domestic and foreign economic enterprises, it has been made clear to the government that for this growth to be maintained, laws concerning economic enterprises in China needed to be improved and modified. The aim of the new CL, as has been discussed, is to provide a clearer regulatory framework for both domestic and foreign enterprises so as to promote China's further economic development.

stipulated that those committees which have not yet been re-established in accordance with the new law should be terminated by the end of the first year after the law has been put into effect. These arbitration committees should then apply for re-establishment.

The AL is a milestone for the development of the arbitration system in China. The law intends to promote a fair and just arbitration process, to arbitrate economic disputes in a timely fashion, to protect the lawful rights of the interested parties and to promote international trade. The effective enforcement of the law will promote rational economic development in China.

CHAPTER 11

Reflections on the development of economic law in the People's Republic of China

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The government of the People's Republic of China decided early on to adopt the highly centralized approach to economic planning used by the former Soviet Union. After the execution of six five-year plans, China had succeeded in setting up the foundation for an independent and comprehensive industrial and agricultural complex. Policy-makers realized, however, that although the economy had a strong base, there was still an excess of concentration of power and control in the centre. Having realized that the more developed the economy became, the more burdened it would be by highly centralized planning, policy-makers set to reform the economy by reducing the administrative responsibility of the central government. The aim of this chapter is to explain the basic structure of the economic legal system and comment upon present and future concerns.

OBJECTIVES OF THE ECONOMIC REFORM

Economic reform began in the rural areas. In order to improve agricultural productivity, reforms were first brought to the system of people's communes. The reforms were implemented through the establishment of a system of contracts amongst families in order to unite their assets and improve their ability to produce goods for the market. As a result, the rural economy was transformed into a specialty and commodity inclined market. Similar to the countryside, the urban area's industrial productivity suffered from inefficiency and an over-burdensome centralized bureaucracy. The urban area looked to the successful reforms in the rural area as a possible model for their own betterment.

After more than ten years of study and with the avowed goal of developing a commodity economy, policy-makers, during the 14th National Congress of the Communist Party of China, determined that

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the objective of the economic reform was to establish a system of socialist market economy. Under this system the policy-makers determined that law would serve as the foundation of the economic reform and would drive the country toward the achievement of a new commodities-based economy.

LEGISLATION CONCERNING ECONOMIC DEVELOPMENT IN THE 1980s

In the early 1980s, it was established that the commodity economy was to remain guided by socialist principles. Early legal reform emphasized commodity production, price and market reform. A number of new laws were drafted in order to accommodate the economic and social demands of establishing a commodity-oriented economy.

Establishment of Basic Civil Legal Norms

The general rules for the civil law were established in 1986. Since the founding of the new China, the civil relationship between legal persons was regarded as irrelevant to society due to the public ownership of property and the planned economic system. After the establishment of reform and the opening of China, however, the highly centralized planned economy was modified to take into account the development of a commodity economy. In order to cope with the subsequent new property rights created within the reformed system, legislators established a new civil procedure.

This civil law defined the legal relationships between the citizens and juridical persons in the new commodity economy. The law also confirmed that parties involved in civil disputes over property rights in the new economy should have equal status under law. The principles of free will, impartiality, equal value, compensation, honesty and credit should be recognized by the civil law. The general rules of the civil law set out rights and responsibilities for legal persons. The civil law, while not providing the technical requirements traditionally found in the regulations established by common law countries, regulated the norms of the legal relationship between civil subjects.

The law also provided for the protection of those aspects of public ownership still necessary for the reformed economic system. In addition, the civil law provided for a system to solve civil disputes including litigation and mediation.

Establishment of a System of Industrial Property Rights

The *Trademark Law* was enacted in 1982. It provided for a system of trademark registration. The registration system served to promote the development of the commodity economy, protect the owner's

proprietary right in a trademark, maintain the value of trademarks and protect the interests of the consumers. The new trademark law established both voluntary and compulsory registration in China.

A registered trademark possesses certain rights under the law. In case of infringements of the trademark, injured parties could seek justice from the relevant administrative departments of industry and commerce or they could sue in people's courts. In 1993, as a result of the fast changing environment of the market, the trademark law was amended. The main objective of the amendments was to strengthen the protection of service trademarks.

In 1984, in order to encourage invention and creation and to protect the investor's proprietary interest in patents, the *Patent Law* was enacted. Patents may be granted for inventions, products with practical functions as well as the exterior design or appearance of products, among other things. The duration of protection for inventions was 15 years while the duration of protection for products with practical functions as well as exterior designs was five years with the possibility of a three-year extension upon application.

The *Patent Law* was amended in 1992 with the aim of creating more patentable products. Under the new law products including food, beverage and seasoning, medicine and chemicals could now receive patent protection. Under the revised patent law, the duration of a patent for inventions was extended to 20 years while the duration of products with a practical function as well as exterior design was extended to ten years.

Preliminary Establishment of the System of Juridical Persons in Enterprises

Under the planned economic system, no enterprise had the right to operate independently regardless of whether they were part of the industrial, commercial or service market. They did not even possess independent juridical status. In order to accommodate economic development through a market-oriented economy, promote the economic reform and increase the competitiveness of enterprises, enterprises should have the right to operate independently. This meant that the government had to adopt an economic policy whereby business is for all intents and purposes separate from government. In order to achieve this goal, the legal system had to recognize and help establish the enterprise as an independent juridical person.

In 1988, the government enacted legislation concerning entrepreneurial enterprises. The law provided an environment whereby enterprises could operate independently and separately from the central authorities. This law also recognized the principle of separating ownership from management. Granting permission to operate a business meant basically that the state entrusted the enterprise to manage national property. The enterprises had the right to own, use and dispose of

the national property according to law. Not only did the enterprise enjoy rights of use in the property, they also had to bear civil responsibilities and duties. The enterprises managed their own commodity production and accounted for their own surplus and deficit.

Statutory stipulations concerning the rights and interests of the enterprises and the relationship between the enterprises and the government recognized the enterprises' independent management structure and the principle of separating the enterprises from politics. They contained 26 regulations all of which aspired to provide the business a considerable separation from the planned economic system.

Although the structure of enterprises operating in the planned economy was changed, the fundamental structure of the planned economic system remained the same. This raised unique problems for enterprises. Among the different problems raised, the question of how to manage state property and, in particular, how the enterprises were supposed to utilize their property rights were not satisfactorily resolved in the drafting of the legislation. As a result the regulation was very difficult to implement.

Although the law was not perfect it can be said that the law concerning entrepreneurial enterprises established the juridical status of enterprises in a far more explicit way than the rules of the civil law. In order to promote further enterprise reform, the State Council in 1992 issued administrative laws and regulations to provide for further management reform of the state enterprises.

Also in 1992 the State Council enacted a new bankruptcy law. Due to the competitive nature of the market-oriented economy, bankruptcy became a real problem in China. Under the planned economy all industry was part of a big family and no part of that family would ever be over-burdened with debt. In case of deadly difficulties, administrative means were applied for the sake of termination. Because, under a market-oriented economy, individual enterprises were responsible for their own debt, the system of bankruptcy had to be reformed. The new law provided for an application process for bankruptcy, the meetings of creditors, the declaration of bankruptcy and an accounts clearing process. Measures for reconciliation and re-establishment were also provided for in order to give the enterprises the opportunity to start over. The bankruptcy law was originally passed in the form of trial implementation in order to provide maximum flexibility in order to cope with inevitable transitional problems such as the lack of insurance for the unemployed.

A System for Contracts

Between 1981 and 1987, legislation governing economic contracts, foreign-related economic contracts and technical contracts was enacted. Their promulgation illustrated the considerable progress being achieved by the state in its efforts to create a commodity economy.

The economic contract law recognized that trades between juridical persons must be based on notions of equality, mutual benefit, consultation and consensus. According to the law, the relationship between the two parties should be formalized through the conditions of the written contract.

Contracts made according to law are legally binding. This law was very significant for the production management units adapting to changes from a socialist to a market-oriented economy. The economic contract law emphasized that no one party of a contract could force his own will on another party, no unit or person could interfere with a contract's negotiation or implementation, nor could any party to a contract modify or terminate the contract without authorization.

Formerly, economic disputes were settled through intervention or consultation with third party or higher administration authorities. After the enactment of the economic contract law, however, disputes could be settled between the two parties through consultation, reconciliation, arbitration or even legal proceedings in courts. The implementation of the economic contract law therefore illustrated, to a certain extent, the transformation of an economy that once relied on administrative control to one more reliant on a party's rights being protected.

The foreign-related economic contract law was intended to meet the increased economic demands resulting from the policy of opening up to foreign countries and to further develop international trade. The law applied to enterprises and individuals from China and foreign countries. Under the law, Chinese and foreign parties had the discretion to choose their own dispute settlements. Exceptions, however, were made for enterprises with joint capital and management, contracts of jointly managed enterprises within China and contracts for the exploration and exploitation of natural resources. International law would apply where Chinese law was insufficient.

Parties to contractual disputes must first try to resolve their differences through consultation and reconciliation. For those who were not willing or those who failed in consultation and reconciliation, arbitration according to the arbitration clauses of the contract or the arbitration agreements reached afterwards could be sought. Where no arbitration clauses were written, the parties could, as a last resort, bring the case to court. The regulations of the foreign-related economic contract law are in accord with current international legal practice.

The technical contract law was promulgated in order to accommodate the need to convert state-owned technical products into commodities so that the technical products would be available on the market. The law mainly concerned contracts involving technical developments, technical transfers, and technical services. The law stipulates that relevant State Council departments or provincial gov-