

LEGAL SYSTEM ON  
**FOREIGN TRADE AND  
INVESTMENT IN**

**CHINA**

By Sun Nanshen  
Sun Wen

## Brief Profile of Sun Nanshen

Sun Nanshen is the dean and professor at Law School of Fudan University where he teaches courses of international investment law, international trade law, private international law, etc. which are also his research fields. The main representative publications by Professor Sun include five works on the above fields, i.e. (1) *International Customs of Foreign Investment*, Guizhou People's Publishing House, 1994; (2) *Economic International Law*, Hehai University Publishing House, 1995; (3) *Chinese Legal System on Foreign Trade in Service*, Law Press, 2000; (4) *Legal Systems on Foreign Business Under WTO*, People's Court Publishing House, 2003; (5) *Legal System of Judicial Review Under WTO Mechanism*, Law Press, 2006. In addition, he also published approximately 140 academic articles in various legal journals on legal issues of foreign investment law, foreign trade law, Chinese economic law on foreign business, economic international law and private international law.

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定价: 人民币39.00元

ISBN 978-7-80225-273-8



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新星出版社 NEW STAR PRESS

## 图书在版编目 (CIP) 数据

中国对外贸易与外商投资法律制度 / 孙南申, 孙雯著.

—北京: 新星出版社, 2007.5

ISBN 978-7-80225-273-8

I. 中… II. ①孙… ②孙… III. 涉外经济法—中国—英文 IV. D922.295

中国版本图书馆CIP数据核字 (2007) 第041333号

---

## 中国对外贸易与外商投资法律制度

孙南申 孙雯 著

责任编辑: 张 维

责任印制: 韦 舰

封面设计: 尧 尧

---

出版发行: 新星出版社

出 版 人: 谢 刚

社 址: 北京市东城区金宝街 67 号隆基大厦 100005

网 址: [www.newstarpress.com](http://www.newstarpress.com)

电 话: 010-65270477

传 真: 010-65270449

法律顾问: 北京建元律师事务所

---

国际经销: 中国国际图书贸易总公司 (中国北京车公庄西路35号)

公司地址: 北京邮政信箱第399号 100044

国内经销: 010-65512133

邮购电话: 010-65276452

邮购地址: 北京市东四邮局 7 号信箱 100010

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印 刷: 北京中科印刷有限公司

开 本: 880×1290 1/32

版 次: 2007年5月第一版 2007年5月第一次印刷 (英)

书 号: ISBN 978-7-80225-273-8

定 价: 人民币 39.00 元

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By Sun Nanshen, Sun Wen

Publisher: Xie Gang

Editor: Zhang Wei

Designer: Lydia Lin

First Edition 2007

**Legal System on Foreign Trade  
and Investment in China**

ISBN 978-7-80225-273-8

© NEW STAR PRESS

Published by NEW STAR PRESS

Longji Building, 67 Jinbao Street, Dongcheng District,  
Beijing 100005, China

Home Page: <http://www.newstarpress.com>

E-mail Address: [newstar@newstarpress.com](mailto:newstar@newstarpress.com)

Distributed by China International Book Trading Corporation  
35 Chegongzhuang Xilu, Beijing 100044, China  
P.O.Box 399, Beijing, China

*Printed in the People's Republic of China*

## Foreword

This book is written for the purpose of reflecting the amendment and perfection of Chinese economic laws and regulations on foreign business after China's entry into WTO. With the ends in view, this book provides in depth analysis of Chinese legal system on trade in goods, trade in services, and foreign investment. It highlights legal issues crucial to making trade and investment decision such as conclusion of contracts, capital contribution, dispute settlement, protection of intellectual property rights, foreign exchange control and other array of complex legal requirements.

This book is divided into seven chapters.

Chapter One focuses on introduction to legal system on foreign trade and investment with the objective to illustrate framework, sources, and subject matter of Chinese legal system on foreign business, as well as its relationship with WTO agreements.

Chapter Two is about contract law on foreign business. As it is known to all, all trade and investment activities between parties as companies and enterprises at home and abroad are carried out by making various foreign-related contracts. Contract law directly makes adjustment on trade and investment relationship between these parties to the contract since their rights and obligations have been set in the contracts.

Chapter Three is on foreign trade law which mainly covers legal topics including tariff; various non-tariff measures, and trade in services, espe-

cially financial institution.

Chapter Four focuses on foreign investment law covering a range of essential legal topics and rules, such as legal forms of foreign investment, legal protection, administrative management, investment structure, securities investment, investment liquidation and capital contribution control, etc.

Chapter Five is on intellectual property rights law related to trade, mainly illustrating Chinese legal system on intellectual property protection, especially the scope and standard of protection.

Chapter Six focuses on regulations on foreign exchange control, which makes analysis on foreign exchange management under both current item and capital item.

The last chapter, Chapter Seven, focusing on trial system and judicial review on civil and commercial cases with foreign elements, illustrates in detail judicial jurisdiction and legal application in Chinese courts dealing with foreign-related civil and commercial disputes.

In sum, on one hand, this book outlines China's current policy and legislation development relating to foreign trade, investment, intellectual property protection, taxation, foreign exchange control and so on. On the other hand, it includes case studies of international business or investment transactions between foreign investors and Chinese companies or enterprises. The authors believe that this book would be a helpful reference for the extension of foreign business in China and hope that it would be an essential guide for foreign corporations which plan to establish their business in China.

Sun Nanshen  
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## **CHAPTER 1**

# **Introduction to Legal System on Foreign Trade and Investment**

## **1.1 Framework and Sources of Legal System on Foreign Trade and Investment**

Legal system of China on foreign business can be defined as the overall system of legal rules promulgated by legally competent authorities of China on the foreign business relations between Chinese enterprises or other economic organizations and foreign enterprises, economic organizations and individuals, and on the foreign business administration relations between China's foreign business administration authorities and the parties that engage in foreign businesses. Legal system of China on foreign business is mainly consisted of the legal institutions such as foreign trade, foreign investment, technology introduction, foreign exchange control, and taxation with foreign elements. Laws, regulations and other rules relating to or affecting trade in goods, trade in service, trade-related intellectual property rights, and foreign exchange control are specially the prominent aspects.

Domestic legislations followed by Chinese courts in deciding trade-related administrative lawsuits include the laws enacted by the People's Congress and its Standing Committee, administrative regulations promulgated

by the State Council, regional regulations promulgated by the People's Congresses and their Standing Committees of provincial-level (including autonomous regions and municipalities directly under the State Council), large-scale municipalities and special economic zones, as well as rules promulgated by departments of the State Council and local governments.<sup>1</sup> Application of these laws and regulations shall firstly follow the provisions of the *Law on Legislations*,<sup>2</sup> and the sequence of priority is laws, administrative regulations of the State Council, regional regulations, and rules. Rules are only used as reference of courts and are deemed as supplementary to the laws and regulations.

To clarify and determine the priority sequence of the legal sources in law application, the *Law of People's Republic of China on Legislation* has established the following principles:

(1) The legal force of laws is higher than that of administrative regulations and regional regulations.<sup>3</sup>

(2) The legal force of administrative regulations is higher than that of regional regulations and rules.<sup>4</sup>

(3) The legal force of regional regulations is higher than that of rules made by local governments.<sup>5</sup>

(4) The legal force of rules promulgated by State Council departments is equal to that of rules promulgated by regional governments.

The *Law on Legislation* does not give a clear stipulation on the priority

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1. Local governments refer to the people's governments of provinces, autonomous regions, municipalities directly under the State Council and large-scale cities. See Article 73 of the *Law on Legislation*.

2. See Articles 7, 56, 63 and 71 of the *Law on Legislation*. All the laws mentioned in this book, if not indicate the country, are referred to the laws of the People's Republic of China.

3. Article 79 of the *Law on Legislation*.

4. Article 79 of the *Law on Legislation*.

5. Article 80 of the *Law on Legislation*.

sequence between the legal forces of the rules promulgated by the State Council departments and regional regulations. They are generally deemed to have same legal force and shall be executed within its domain. Problems will arise when courts, in applying the laws and regulations in administrative lawsuits, find that rules promulgated by the State Council departments conflict with regional regulations on a same issue. And this shall have different treatment from case to case since no laws have stipulated on this matter. If rules promulgated by the State Council departments conflict with rules promulgated by regional government's departments, the superior government organs will prevail, except that the superior organs have made special delegation to the subordinates. If the rules promulgated by the State Council departments conflict with regional regulations on the same matter, superior laws and regulations shall be taken into account to see which rules comply with the superior law and regulations.

(1) If a regional regulation complies with laws and superior regulations and rules promulgated by the State Council departments conflict with laws and superior regulations, the regional regulation shall prevail.

(2) If rules promulgated by the State Council departments complies with laws and superior regulations and regional regulations conflict with laws or superior regulations, the rules promulgated by the State Council departments shall prevail.

This is the principle of Compliance with Superior Laws and Regulation in Deciding Conflict of Regulations, which is based on the provisions of the *Law on Legislation*,<sup>6</sup> and the *Law on Administrative Procedures*.<sup>7</sup> According to these provisions, people's courts will, in deciding administrative case, apply the rules that comply with the superior laws and regulations when

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6. Article 86 of the *Law on Legislation*.

7. Article 53 of the *Law on Administrative Procedures*.

provisions promulgated by the State Council departments conflict with each other, or rules promulgated by the State Council departments conflict with rules promulgated by local governments.

## **1.2 Subjects of Legal System on Foreign Trade and Investment**

### **1.2.1 Regulative Relations**

China regulates its foreign business relations and activities mainly through special legislations and regulations. Export to and investment in China from foreign companies and investors are subject to foreign business laws of China. Subject matter of the legal system of China on foreign business may be classified into two kinds of relations: (1) Foreign business relations between Chinese enterprises or other economic organizations and foreign enterprises, economic organizations and individuals. This kind of business relation may be called “horizontal foreign business relation” and is manifested in all kinds of economic and trade cooperation and dealings; (2) Domestic administration of China over foreign businesses. The administration of foreign businesses creates a kind of “vertical foreign business relation” between the administrative authorities of China and the foreign economic organizations and individuals whose business activities are subject to the administration.

Foreign business law of China regulates economic relations with foreign elements. Firstly, at least one of the parties in the economic relations shall be foreign companies, enterprises, economic organizations or individuals; otherwise the relationship would not have foreign elements. In practice, investors from Taiwan, Hong Kong and Macau, as well as other overseas Chinese compatriots who invest in Chinese mainland are generally treated as foreign investors according to foreign business laws of China, thus virtually extends the scope of application of foreign business law.



Foreign business laws of China are mainly substantive legal rules. Private international law rules such as conflict law rules and civil procedures with foreign elements are not included. At the same time, application of foreign business laws may also deal with other legal systems such as civil procedures with foreign elements and international commercial arbitration law in international business law. Substantive rules of China's foreign business law include two major categories: rules on foreign business relations which are mainly embodied in economic contracts and are regarded as indirect regulation, and rules on administration of foreign business which usually stipulate specific rights and obligations of parties and are generally regarded as direct regulation.

### **1.2.2 Administrative Organs**

In China, administration powers on various economic activities with foreign elements, such as import and export, foreign investment, trade in service and foreign exchange control, are generally exerted by the ministries, commissions and administrative agencies under the direct management of the State Council. These ministries and commissions usually include the Ministry of Commerce, the State Development and Reform Commission, the Ministry of Finance, the People's Bank of China, the State Administration of Taxation, the State Administration of Foreign Exchange, China Customs, the State Administration for Industry and Commerce, State Administration of Quality Supervision, Inspection and Quarantine, etc.<sup>8</sup> These central gov-

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8. The Tenth People's Congress in the year 2003 approved the institutional reform plan proposed by the State Council to abolish the State Economic and Trade Commission and the Ministry of Foreign Trade and Economic Cooperation and delegate their administrative powers to the newly established Ministry of Commerce. The State Development Planning Commission was also abolished and changed into the State Development and Reform Commission.

ernment organs all have their subordinates at different levels of governments, such as provincial, municipal and in special economic development zones. The subordinates at lower levels enjoy similar administrative powers of the central government organs and undertake much of the overall administration work on foreign business regulation.

### 1.2.3 Enterprise as Legal Person

Chinese laws have general stipulations on the issue of enterprise as legal person as subjects of foreign business law. For example, Article 18 of *Constitution of P.R.China* provides that “The People’s Republic of China permits foreign enterprises, other foreign economic organizations and individual foreigners to invest in China and to enter into various forms of economic cooperation with Chinese enterprises and other economic organizations in accordance with the law of the People’s Republic of China. All foreign enterprises and other foreign economic organizations in China, as well as joint ventures with Chinese and foreign investment located in China, shall abide by the law of the People’s Republic of China. Their lawful rights and interests are protected by the law of the People’s Republic of China.” Similar provisions also appear in laws and regulations such as *the Foreign Trade Law*. But these laws and regulations do not provide clear definition to the term “enterprise” or “other economic organizations”. On the basis of generally accepted jurisprudential concepts, and relevant rules and general practices in the economic fields, “enterprise” and “other economic organizations” in terms of foreign business law may be defined as legal persons who have met the legal qualification demands for foreign business operation. The definition mainly applies to the so-called “horizontal foreign business relations” between Chinese and foreign subjects.

According to China’s administrative rules and practices in foreign business, the foreign subjects in the legal relations in foreign business,

namely “foreign enterprises and other economic organizations”, refer to enterprises or companies which have registered in foreign countries in the form of legal person, including limited liability companies, stock companies, limited partnership by shares, etc. as well as economic organizations in foreign countries that are not in the form of legal person. The so-called “other economic organizations” refer to the social organizations with independent assets and operate for business purposes to acquire payoff, such as partnership. International financial institutions might also be included in this category.

The legal status of enterprises or companies of Hong Kong, Macau and Taiwan should also be clarified. Since China’s reform and opening up in 1979, large numbers of enterprises or other economic organizations from Hong Kong, Macau and Taiwan have invested in Chinese mainland or have established business cooperation with local enterprises or other economic organizations. The legal status of these enterprises or economic organizations should not be regarded as foreign entities from the standpoint of national sovereignty. But in terms of foreign investment and foreign trade policies, the Chinese government treats these enterprises and economic organizations with same preferential policies and status as those for foreign enterprises. These policies are embodied in a number of laws, which extend the application of foreign business laws to business relations between Hong Kong, Macau, Taiwan enterprises, companies or individuals and mainland enterprises and other economic organizations. Therefore, these organizations and individuals from Hong Kong, Macau and Taiwan are treated as the foreign parties in the relations under regulation because of historic reasons and the differences of political, economic systems between Chinese mainland and Hong Kong, Macau and Taiwan.

According to the *Company Law of P.R.China* revised in 2005, foreign enterprises or companies may establish branches to operate business in China. Foreign companies which plan to establish branches in China shall