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Keith Jennings
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GOVERNMENT CONTROL AND FOREIGN INVESTMENT
- A Study of Foreign Investment Laws in Australia and China

John Shijian Mo
(LL.B Jilin, 1982, LL.M, Dal. 1986)

A thesis submitted in March 1991 in fulfilment of the requirements of degree of Doctor of Philosophy at the University of Sydney, Faculty of Law
Synopsis

Both Australia and China are capital importing countries, although Australia is also a capital exporting country and China has begun to invest abroad in recent years. Foreign investment has been and will be playing a crucial role in the development of the national economy in both Australia and China. This makes a comparison between Australia and China, countries with different legal traditions, cultural backgrounds and economic conditions, a useful exercise. In addition, the promising economic relations between Australia and China demand a systematic and detailed investigation into the system of foreign investment law and policy in each country. In particular, this thesis attempts to investigate the role of government in the regulation and administration of foreign investment in the two countries.

The Australian and Chinese Governments approach the regulation and administration of foreign investment in very different ways. Australian foreign investment law and policy are affected by the common law legal tradition and by a federal system which divides power between federal and State governments. Chinese foreign investment law and policy are based on the Chinese legal tradition, with a political system which retains a centrally controlled economy. The differences in dealing with issues of foreign investment are seen in many areas of foreign investment law, such as company law, exchange control, taxation, and provisions for the settlement of disputes. In this thesis, the roles of government in these various areas of foreign investment law and policy in Australia and China are examined and compared.

In Australia the regulation and administration of foreign investment are within the authority of the federal Government. The investment law and policies consist of Acts, in particular, the Foreign Acquisitions and Takeovers Act 1975 (Cth), and policies made by the Executive under various discretionary powers, not all statutory in origin. The federal Treasurer, assisted by the Foreign Investment Review Board, an independent body, is responsible for the administration of foreign investment law and policy and for making decisions in relation to foreign investment proposals. He also consults other Departments of the Government and State Governments in reaching a decision. The exercise of executive power is a matter falling within foreign investment Guidelines, and cooperation between the federal and State governments is a matter to be dealt with in the administration of the Guidelines.

Foreign investment in China is administered by government authorities at various levels. Subordinate regulations made by executives at various levels are an important part of foreign investment law and policy in China. But the rule of law is still an issue in the administration of foreign investment in China, where policy often prevails over law and regulations.
Exchange control does not exist in practice in Australia. Although the Banking (Foreign Exchange) Regulations 1946 (Cth) have not been repealed, they ceased to be operative by order of the federal Treasurer and Reserve Bank. In contrast, foreign exchange control is still an important issue in Chinese foreign investment law. Foreign investors are required to comply with regulations regarding to the use and transfer of foreign exchange within or to and from China.

Taxation is an important aspect of foreign investment law in Australia and China. In general, Australia applies the same rules to both foreign and local companies carrying on business in Australia, while China applies special rules to foreign-related companies. Tax concessions are widely used in China as a means of attracting and encouraging foreign investment. Inconsistencies have been found resulting from concessions given by both central and local governments separately and independently.

Dispute resolution in the two countries suggests both similarities and differences. Judicial and non-judicial means of dispute resolution are accepted in both countries, but Chinese courts have not played any significant role in resolving disputes involving foreign investment. Australia and China differ in their positions on the issue of sovereign immunity. Although China in theory still adheres to the doctrine of absolute sovereign immunity, it has accepted restricted sovereign immunity in some circumstances, e.g. in the Australia-China Investment Promotion and Protection Treaty, on the basis of reciprocity.

The Australia-China Investment Promotion and Protection Treaty is the first bilateral investment protection treaty entered into by Australia. The Treaty forms a basis for further economic cooperation between the two countries and contains provisions for the settlement of foreign investment disputes involving States and individuals. The provisions of this Treaty are examined in the context of foreign investment law and policy of Australia and China, and various potential issues and their possible solutions discussed.
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Last but not least, I give my deep gratitude to my parents. Without their love and encouragement, life would have been intolerable.
### Synopsis

#### Acknowledgement

#### Selected Table of Abbreviations

#### Introduction

<table>
<thead>
<tr>
<th>Chapter 1</th>
<th>Concepts and Terminology</th>
<th>5</th>
</tr>
</thead>
<tbody>
<tr>
<td>1.1.</td>
<td>Meaning, Forms and Features of Foreign Investment</td>
<td>5</td>
</tr>
<tr>
<td>1.2.</td>
<td>Meaning of Foreign Investment Law</td>
<td>8</td>
</tr>
<tr>
<td>1.3.</td>
<td>Foreign Investment Law in Australia</td>
<td>8</td>
</tr>
<tr>
<td>1.4.</td>
<td>Foreign Investment Law in China</td>
<td>10</td>
</tr>
<tr>
<td>1.5.</td>
<td>Problems of Government Control</td>
<td>12</td>
</tr>
<tr>
<td>1.5.1.</td>
<td>Contradictions Implied in the Notion of Control</td>
<td>12</td>
</tr>
<tr>
<td>1.5.2.</td>
<td>Purposes of Controlling Foreign Investment</td>
<td>13</td>
</tr>
<tr>
<td>1.5.3.</td>
<td>The Forms of Control Over Foreign Investment</td>
<td>15</td>
</tr>
<tr>
<td>1.6.</td>
<td>Some Concepts and Terms in the Contexts of Australian and Chinese Foreign Investment Laws</td>
<td>16</td>
</tr>
<tr>
<td>1.6.1.</td>
<td>Australian Legal System versus Chinese Legal System</td>
<td>16</td>
</tr>
<tr>
<td>1.6.2.</td>
<td>Federal Government versus Central Government</td>
<td>18</td>
</tr>
<tr>
<td>1.6.3.</td>
<td>States versus Provinces</td>
<td>19</td>
</tr>
<tr>
<td>1.6.4.</td>
<td>Statute versus Fa</td>
<td>20</td>
</tr>
<tr>
<td>1.6.5.</td>
<td>Regulations versus Tiaoli</td>
<td>20</td>
</tr>
<tr>
<td>1.6.6.</td>
<td>Policy versus Zhence</td>
<td>21</td>
</tr>
<tr>
<td>1.6.7.</td>
<td>Defining &quot;Control&quot;</td>
<td>22</td>
</tr>
<tr>
<td>1.7.</td>
<td>New Economic Policies of the PRC</td>
<td>22</td>
</tr>
<tr>
<td>1.7.1.</td>
<td>A Historical Perspective on the New Economic Policies</td>
<td>22</td>
</tr>
<tr>
<td>1.7.2.</td>
<td>Contents of the New Economic Policies</td>
<td>28</td>
</tr>
</tbody>
</table>

<table>
<thead>
<tr>
<th>Chapter 2</th>
<th>Administration of Foreign Investment in Australia</th>
<th>32</th>
</tr>
</thead>
<tbody>
<tr>
<td>2.1.</td>
<td>An Overview</td>
<td>32</td>
</tr>
<tr>
<td>2.2.</td>
<td>Administrative Mechanisms for Foreign Investment Control in Australia</td>
<td>38</td>
</tr>
<tr>
<td>2.2.1.</td>
<td>An Overview of the Federal Mechanisms</td>
<td>38</td>
</tr>
<tr>
<td>2.2.2.</td>
<td>Statutory Power of the Treasurer</td>
<td>39</td>
</tr>
<tr>
<td>2.2.3.</td>
<td>Statutory Powers of Other Departments</td>
<td>44</td>
</tr>
<tr>
<td>2.2.4.</td>
<td>Functions of the Foreign Investment Review Board</td>
<td>44</td>
</tr>
<tr>
<td>2.2.5.</td>
<td>Power of Other Statutory Bodies to Control Foreign Investment</td>
<td>46</td>
</tr>
<tr>
<td>2.2.5.1.</td>
<td>Power of the Australian Broadcasting Tribunal</td>
<td>46</td>
</tr>
<tr>
<td>2.2.5.2.</td>
<td>Power of the Trade Practices Commission (TPC)</td>
<td>47</td>
</tr>
<tr>
<td>2.3.</td>
<td>Foreign Investment Policy in the Guidelines</td>
<td>51</td>
</tr>
<tr>
<td>2.3.1.</td>
<td>Control of Foreign Investment Under FATA</td>
<td>51</td>
</tr>
<tr>
<td>2.3.1.1.</td>
<td>The Functions of FATA</td>
<td>51</td>
</tr>
<tr>
<td>2.3.1.2.</td>
<td>Takeovers Prohibited Under FATA</td>
<td>53</td>
</tr>
<tr>
<td>2.3.2.</td>
<td>Control Under Other Statutes or Regulations</td>
<td>56</td>
</tr>
<tr>
<td>2.3.2.1.</td>
<td>Control in Manufacturing and Service Industries</td>
<td>56</td>
</tr>
<tr>
<td>2.3.2.2.</td>
<td>Control in Banking</td>
<td>58</td>
</tr>
<tr>
<td>2.3.2.3.</td>
<td>Control in Civil Aviation</td>
<td>59</td>
</tr>
<tr>
<td>2.3.2.4.</td>
<td>Control Over the Media</td>
<td>61</td>
</tr>
<tr>
<td>2.3.2.5.</td>
<td>Control over Mining</td>
<td>64</td>
</tr>
<tr>
<td>2.4.</td>
<td>Examination Procedures for Investment Proposals</td>
<td>67</td>
</tr>
<tr>
<td>2.5.</td>
<td>Control of Foreign Investment by State Governments</td>
<td>67</td>
</tr>
<tr>
<td>2.5.1.</td>
<td>Introduction</td>
<td>67</td>
</tr>
<tr>
<td>2.5.2.</td>
<td>Local Control in New South Wales</td>
<td>68</td>
</tr>
<tr>
<td>2.5.3.</td>
<td>Local Control in South Australia</td>
<td>69</td>
</tr>
<tr>
<td>2.5.4.</td>
<td>Local Control in Tasmania</td>
<td>71</td>
</tr>
</tbody>
</table>
TABLE OF CONTENTS

2.5.5. Local Control in Queensland 71
2.5.6. Local Control in Western Australia 72
2.6. Executive Power in the Administration of Foreign Investment 73
  2.6.1. Executive Power in General 73
  2.6.2. Executive Power to Regulate Foreign Investment 76
  2.6.3. State Power to Regulate Foreign Investment 79
2.7. Conclusion 81

Chapter 3 The Administration of Foreign Investment in China 85
  3.1. An Overview 85
  3.2. Mechanisms for Controlling Foreign Investment in China 93
    3.2.1. Power of the State Council 93
    3.2.2. Power of the Ministry for Foreign Economic Relations and Trade (MOFERT) 94
      3.2.2.1. Introductory 94
      3.2.2.2. Criteria for Decentralizing the Power of Approval 97
      3.2.3. Power of Other Departments and Statutory Bodies to Control Foreign Investment 99
    3.2.4. Power of Other Departments and Statutory Bodies to Control Foreign Investment 101
      3.2.4.1. Introduction 101
      3.2.4.2. Local Legislation in SEZs 102
      3.2.4.3. Concurrent Power of Central and Local Governments 103
  3.3. Sectors Open to Foreign Investors 106
  3.4. Application Procedures 108
  3.5. Delegated Power and the Administration of Foreign Investment 109
    3.5.1. Introduction 109
    3.5.2. Hierarchical Power Structure in the Constitution 109
    3.5.3. Conditional Legislative Power of the State Council 111
    3.5.4. Delegated Power of Other Departments 112
    3.5.5. Local Legislative Power in Relation to Foreign Investment 113

Chapter 4 Executive Power and Foreign Exchange Control 117
  4.1. An Overview 117
  4.2. Constitutional Issues Relating to Exchange Control 123
    4.2.1. Status of the Competent Authorities 123
    4.2.2. Constitutional Restraints and the Exercise of Delegated Power 127
    4.2.3. Separation of Powers and the Regulatory Power of the Competent Authorities 129
  4.3. Independence of the Central Banks and Exchange Control 134
    4.3.1. Constitutional Restraints and the Australian Reserve Bank 134
    4.3.2. Constitutional Restraints and the People's Bank of China 139
    4.3.3. The Central Bank and Government Policy 142

Chapter 5 Some Issues of International Taxation in Australia and China 147
  5.1. An Overview 147
  5.2. Features of Taxation Power in Australia and China 154
    5.2.1. Concurrent Taxation Power in Australia 154
    5.2.2. Exclusive Taxation Power in China 156
  5.3. Features of Taxation Authorities in Australia and China 158
    5.3.1. Defining the Tax Authorities 158
    5.3.2. The Commissioner's Discretions in International Taxation 159
    5.3.3. Power of the Ministry of Finance in the Taxation of Foreign Investment 162
    5.3.4. Power of General Taxation Bureau in the Taxation of Foreign Investment 163
  5.4. Discretionary Power of the Tax Authorities 164
    5.4.1. Features of Discretion 164
<table>
<thead>
<tr>
<th>Section</th>
<th>Title</th>
<th>Page</th>
</tr>
</thead>
<tbody>
<tr>
<td>5.4.2.</td>
<td>Defining the Tax Authorities' Discretion</td>
<td>166</td>
</tr>
<tr>
<td>5.4.3.</td>
<td>The Necessity for Tax Authority Discretions</td>
<td>167</td>
</tr>
<tr>
<td>5.4.4.</td>
<td>Functions of Tax Authorities' Discretions</td>
<td>168</td>
</tr>
<tr>
<td>5.4.5.</td>
<td>Categories of Tax Discretions</td>
<td>169</td>
</tr>
<tr>
<td>5.5.</td>
<td>Assessing the Tax Authorities' Discretions</td>
<td>171</td>
</tr>
<tr>
<td>5.5.1.</td>
<td>Discretions, Legal Rules and Fairness</td>
<td>171</td>
</tr>
<tr>
<td>5.5.2.</td>
<td>The Exercise of Tax Authorities' Delegated Power</td>
<td>176</td>
</tr>
<tr>
<td>5.5.3.</td>
<td>Judicial Control of Discretion</td>
<td>177</td>
</tr>
<tr>
<td>5.6.</td>
<td>Residential Tests and International Taxation</td>
<td>180</td>
</tr>
<tr>
<td>5.6.1.</td>
<td>Significance of the Residence Test</td>
<td>180</td>
</tr>
<tr>
<td>5.6.2.</td>
<td>Tests for Determining Residence of Company</td>
<td>182</td>
</tr>
<tr>
<td>5.6.3.</td>
<td>Tests for Determining Residence of Individuals</td>
<td>185</td>
</tr>
<tr>
<td>5.7.</td>
<td>Source Tests and International Taxation</td>
<td>187</td>
</tr>
<tr>
<td>5.7.1.</td>
<td>Classification of Sources</td>
<td>187</td>
</tr>
<tr>
<td>5.7.2.</td>
<td>Australian Sources and Foreign-Related Resident Companies</td>
<td>189</td>
</tr>
<tr>
<td>5.7.3.</td>
<td>Australian Sources and Non-resident Companies</td>
<td>192</td>
</tr>
<tr>
<td>5.7.4.</td>
<td>Chinese Sources and Foreign-Related Companies</td>
<td>194</td>
</tr>
<tr>
<td>5.7.5.</td>
<td>Australian Sources and Foreign Individuals</td>
<td>195</td>
</tr>
<tr>
<td>5.7.6.</td>
<td>Chinese Sources and Foreign Individuals</td>
<td>196</td>
</tr>
<tr>
<td>5.7.7.</td>
<td>Issues of Foreign Tax Credits</td>
<td>198</td>
</tr>
<tr>
<td>5.8.</td>
<td>Issues Arising Under the Australian-Chinese Double Tax Treaty</td>
<td>201</td>
</tr>
<tr>
<td>5.8.1.</td>
<td>The Australian-Chinese Treaty and the OECD and UN Models</td>
<td>201</td>
</tr>
<tr>
<td>5.8.2.</td>
<td>Issues of Residence</td>
<td>202</td>
</tr>
<tr>
<td>5.8.2.1.</td>
<td>Tests For Determining Residence Adopted in the Treaty</td>
<td>202</td>
</tr>
<tr>
<td>5.8.2.2.</td>
<td>Issues of Individual Residence</td>
<td>204</td>
</tr>
<tr>
<td>5.8.2.3.</td>
<td>Issues in Relation to Residence of Companies</td>
<td>207</td>
</tr>
<tr>
<td>5.8.3.</td>
<td>Tax Sparing Provisions</td>
<td>209</td>
</tr>
<tr>
<td>5.9.</td>
<td>Some Miscellaneous Issues</td>
<td>210</td>
</tr>
<tr>
<td>5.9.1.</td>
<td>Issues of Controlled Foreign Companies (CFC)</td>
<td>210</td>
</tr>
<tr>
<td>5.9.2.</td>
<td>Thin Capitalization Rules and Foreign Investment</td>
<td>212</td>
</tr>
<tr>
<td>5.9.3.</td>
<td>Issues of Tax Concessions - Inconsistency Between the Central and Local Governments in China</td>
<td>214</td>
</tr>
<tr>
<td>5.9.3.1.</td>
<td>Disputable Local Concessions</td>
<td>214</td>
</tr>
<tr>
<td>5.9.3.2.</td>
<td>Illegality of the CICT Concessions</td>
<td>215</td>
</tr>
<tr>
<td>5.9.3.3.</td>
<td>Illegality of IIT Concessions</td>
<td>217</td>
</tr>
<tr>
<td>5.9.4.</td>
<td>Illegality of Concessions On Enterprise Taxes</td>
<td>218</td>
</tr>
<tr>
<td>5.9.4.1.</td>
<td>Exemption of Withholding Tax in Shenzhen</td>
<td>218</td>
</tr>
<tr>
<td>5.9.4.2.</td>
<td>Questionable Criteria for Tax Concessions in Zhuhai</td>
<td>220</td>
</tr>
<tr>
<td>5.9.4.3.</td>
<td>Questionable Refund on Reinvested Amount in Guangzhou</td>
<td>221</td>
</tr>
<tr>
<td>5.9.5.</td>
<td>Illegality of the Concession on Accelerated Depreciation in Shenyang</td>
<td>222</td>
</tr>
<tr>
<td>5.10.</td>
<td>Conclusion</td>
<td>222</td>
</tr>
</tbody>
</table>

Chapter 6 Settlement of Foreign Investment Disputes | 224 |

6.1. Settlement of Commercial Disputes in Australia | 224 |
| 6.1.1. | An Overview | 224 |
| 6.1.2. | Courts and Commercial Disputes | 227 |
| 6.1.2.1. | Jurisdiction of the High Court Over Commercial Disputes | 227 |
| 6.1.2.2. | Jurisdiction of the Federal Court Over Commercial Disputes | 228 |
| 6.1.2.3. | Jurisdiction of State Supreme Courts | 229 |
| 6.1.2.4. | Jurisdiction of Lower Courts Over Commercial Disputes | 230 |
| 6.1.2.5. | Informal Proceedings Within the Judicial System | 231 |
| 6.1.3. | Alternative Dispute Resolution in Australia | 233 |
| 6.1.3.1. | Methods of ADR in Australia | 233 |
# TABLE OF CONTENTS

| (1) Negotiation                        | 233 |
| (2) Mediation                          | 235 |
| (3) Independent Expert Appraisal       | 236 |
| (4) Case Presentation                  | 236 |
| (5) Conciliation                       | 237 |
| (6) Hybrid Arbitration                 | 238 |
| (7) Arbitration                        | 239 |
| (8) Private Judge                      | 241 |
| 6.1.3.2. Institutionalized ADR Services in Australia | 242 |
| (1) The Institute of Arbitrators Australia | 242 |
| (2) Australian Centre for International Commercial Arbitration | 242 |
| (3) Australian Commercial Dispute Centre | 243 |
| (4) Roles of the Institutions in Comparison | 243 |
| 6.2. Settlement of Foreign Investment Disputes in China | 244 |
| 6.2.1. An Overview                     | 244 |
| 6.2.2. Judicial Dispute Resolution in China | 246 |
| 6.2.2.1. Jurisdiction of the Courts Over Commercial Disputes | 246 |
| 6.2.2.2. Courts and Foreign Commercial Disputes | 247 |
| 6.2.2.3. Court-conducted Mediation     | 251 |
| 6.2.3. Non-judicial Dispute Resolution in China | 252 |
| 6.2.3.1. Methods of Non-judicial Dispute Resolution | 253 |
| (1) Negotiation                        | 253 |
| (2) Mediation                          | 254 |
| (i) Chinese Term for Mediation         | 254 |
| (ii) History of Mediation in China     | 254 |
| (iii) Forms of Mediation in the PRC    | 256 |
| (iv) Mediation by the People's Mediation Committees | 258 |
| (v) Administrative Mediation           | 258 |
| (vi) Institutional Mediation           | 260 |
| (3) Arbitration                        | 260 |
| 6.2.3.2. Settling Investment Disputes Through Non-judicial Means | 264 |
| 6.3. Settlement of Investment Disputes Through Litigation | 267 |
| 6.3.1. Some International Law Issues Concerning Judicial Settlement | 267 |
| 6.3.2. State Immunity and Litigation   | 268 |
| 6.3.2.1. Australian Position on State Immunity | 268 |
| 6.3.2.2. Present Position of China on State Immunity | 270 |
| 6.3.2.3. Positions of Australia and China in Relation to Sovereign Immunity and Potential Disputes | 277 |
| 6.3.3. Issues of Judicial Assistance   | 281 |
| 6.4. Settlement of Disputes Involving Investment from Taiwan | 283 |
| 6.5. Conclusion                        | 285 |

## Chapter 7 The Australia-China Investment Protection Treaty

| 7.1. An Overview                       | 287 |
| 7.2. Treaty Definition of Nationals   | 294 |
| 7.3. Treatment of Investment Under the Treaty | 296 |
| 7.3.1. The Principles of Treatment Adopted in the Treaty | 296 |
| 7.3.2. Meaning of "Fair and Equitable Treatment" | 296 |
| 7.3.3. Meaning of Non-Discrimination  | 297 |
| 7.3.4. Meaning of Most-Favoured-Nation Treatment | 299 |
| 7.3.5. Issues Relating to the Application of the Principles | 300 |
| 7.4. The Governments' Responsibilities Under the Treaty | 301 |
| 7.4.1. Encouragement of Investment    | 301 |
# TABLE OF CONTENTS

<table>
<thead>
<tr>
<th>Section</th>
<th>Page</th>
</tr>
</thead>
<tbody>
<tr>
<td>7.4.2. Responsibility to Facilitate Entry and Sojourn of Personnel</td>
<td>302</td>
</tr>
<tr>
<td>7.4.3. Transparency of Law and Policies</td>
<td>304</td>
</tr>
<tr>
<td>7.4.4. State Responsibility and Nationalization</td>
<td>305</td>
</tr>
<tr>
<td>7.4.4.1. Provisions on Expropriation and Nationalization</td>
<td>305</td>
</tr>
<tr>
<td>(1) Public Interest As Basis of Nationalization</td>
<td>306</td>
</tr>
<tr>
<td>(2) Non-Discrimination In the Process Of Nationalization</td>
<td>307</td>
</tr>
<tr>
<td>(3) Consistency With Law As A Restraint Upon Nationalization</td>
<td>307</td>
</tr>
<tr>
<td>(4) Reasonable Compensation In Nationalization</td>
<td>308</td>
</tr>
<tr>
<td>7.4.4.2. Treaty Obligations and the Historical Perspective of the PRC in Relation to Nationalization</td>
<td>311</td>
</tr>
<tr>
<td>7.4.5. Responsibility in Relation to Foreign Exchange Control</td>
<td>316</td>
</tr>
<tr>
<td>7.4.6. Government Responsibility and Government Contracts</td>
<td>318</td>
</tr>
<tr>
<td>7.4.6.1. The Treaty Obligation in Relation to Government Contracts</td>
<td>318</td>
</tr>
<tr>
<td>7.4.6.2. Government Contracts and Australian Law</td>
<td>318</td>
</tr>
<tr>
<td>7.4.6.3. Government Contracts and Chinese Law</td>
<td>320</td>
</tr>
<tr>
<td>7.5. Limited Sovereign Immunity Under the Treaty</td>
<td>326</td>
</tr>
<tr>
<td>7.6. Settlement of Disputes Under the Treaty</td>
<td>327</td>
</tr>
<tr>
<td>7.6.1. Types of Disputes Under the Treaty</td>
<td>327</td>
</tr>
<tr>
<td>7.6.2. Settlement of Disputes Involving Private Parties</td>
<td>328</td>
</tr>
<tr>
<td>7.6.3. Arbitration Proceedings for Resolving Private-State or State-State Disputes</td>
<td>329</td>
</tr>
<tr>
<td>7.7. Application of the Treaty and National Law</td>
<td>332</td>
</tr>
<tr>
<td>Conclusion</td>
<td>335</td>
</tr>
</tbody>
</table>

**Appendix:**

Selected Addresses of Authorities for Foreign Investment Control in China | 339 |

Selected Bibliography - Books                                            | 342 |

Selected Bibliography - Articles                                          | 350 |

Selected Bibliography - Reports, Documents and Newspapers...             | 360 |

Table of Cases                                                            | 363 |
<table>
<thead>
<tr>
<th>Abbreviation</th>
<th>Description</th>
</tr>
</thead>
<tbody>
<tr>
<td>AAA</td>
<td>American Arbitration Association</td>
</tr>
<tr>
<td>AALCC</td>
<td>Asian-African Legal Consultative Committee</td>
</tr>
<tr>
<td>AAT</td>
<td>Administrative Appeals Tribunal</td>
</tr>
<tr>
<td>ABL</td>
<td>Australian Business Law</td>
</tr>
<tr>
<td>A.B.L.R.</td>
<td>Australian Business Law Review</td>
</tr>
<tr>
<td>ABT</td>
<td>Australian Broadcasting Tribunal</td>
</tr>
<tr>
<td>AC</td>
<td>Law Reports: Appeal Cases</td>
</tr>
<tr>
<td>ACDC</td>
<td>Australian Commercial Dispute Centre</td>
</tr>
<tr>
<td>ACICA</td>
<td>Australian Centre for International Commercial Arbitration</td>
</tr>
<tr>
<td>ACLC</td>
<td>Australian Company Law Cases</td>
</tr>
<tr>
<td>ACLR</td>
<td>Australian Company Law Reports</td>
</tr>
<tr>
<td>A.C.T.</td>
<td>Australian Capital Territory</td>
</tr>
<tr>
<td>ADR</td>
<td>Alternative Dispute Resolution</td>
</tr>
<tr>
<td>AGPS</td>
<td>Australian Government Printing Services</td>
</tr>
<tr>
<td>AIC</td>
<td>Administration of Industry and Commerce</td>
</tr>
<tr>
<td>AIPA</td>
<td>Australian Industrial Preservation Act 1906 (Cth)</td>
</tr>
<tr>
<td>ALJ</td>
<td>Australian Law Journal</td>
</tr>
<tr>
<td>ALJR</td>
<td>Australian Law Journal Reports</td>
</tr>
<tr>
<td>ALR</td>
<td>Australian Law Reports</td>
</tr>
<tr>
<td>ALRC</td>
<td>Australian Law Reform Commission</td>
</tr>
<tr>
<td>Ame.Bar.Ass.J.</td>
<td>American Bar Association Journal</td>
</tr>
<tr>
<td>Ame.J.Comp.L.</td>
<td>The American Journal of Comparative Law</td>
</tr>
<tr>
<td>Ame.J.Int'l L.</td>
<td>The American Journal of International Law</td>
</tr>
<tr>
<td>ASILS Int'l L.J.</td>
<td>ASILS International Law Journal</td>
</tr>
<tr>
<td>ATC</td>
<td>Australian Tax Cases</td>
</tr>
<tr>
<td>ATD</td>
<td>Australian Tax Decisions</td>
</tr>
<tr>
<td>ATPR</td>
<td>Australian Trade Practices Reporter</td>
</tr>
<tr>
<td>ATR</td>
<td>Australian Tax Reports</td>
</tr>
<tr>
<td>Abbreviation</td>
<td>Description</td>
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</tr>
<tr>
<td>Aus.T.S.</td>
<td>Australian Treaty Series</td>
</tr>
<tr>
<td>B.Y.B.Int'l L.</td>
<td>British Year-Book of International Law</td>
</tr>
<tr>
<td>Beijing Rev.</td>
<td>Beijing Review</td>
</tr>
<tr>
<td>Boston College Int'l &amp; Comp.L.Rev.</td>
<td>Boston college International and Comparative Law Review</td>
</tr>
<tr>
<td>Brooklyn J.Int'l L.</td>
<td>Brooklyn Journal of International Law</td>
</tr>
<tr>
<td>Cali.L.R.</td>
<td>California Law Review</td>
</tr>
<tr>
<td>Cali.W.Int'l L.J.</td>
<td>California West International Law Journal</td>
</tr>
<tr>
<td>CCH</td>
<td>Commerce Clearing House, Inc.</td>
</tr>
<tr>
<td>CCP</td>
<td>Chinese Communist Party</td>
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<tr>
<td>CCPIT</td>
<td>China Council for Promotion of International Trade</td>
</tr>
<tr>
<td>CFC</td>
<td>Controlled Foreign Companies</td>
</tr>
<tr>
<td>China L.R.</td>
<td>China Law Reports</td>
</tr>
<tr>
<td>CICT</td>
<td>Commercial and Industrial Consolidated Tax</td>
</tr>
<tr>
<td>CLP</td>
<td>China Law and Practice</td>
</tr>
<tr>
<td>CLR</td>
<td>Commonwealth Law Reports</td>
</tr>
<tr>
<td>Col.L.Rev.</td>
<td>Columbia Law Review</td>
</tr>
<tr>
<td>Den.J.I.L.P.</td>
<td>Denver Journal of International Law and Politics</td>
</tr>
<tr>
<td>Det.Coll.L.Rev.</td>
<td>Detroit College Law Review</td>
</tr>
<tr>
<td>East Asian Exec.Rep.</td>
<td>East Asian Executive Reports</td>
</tr>
<tr>
<td>EEC</td>
<td>European Economic Community</td>
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<tr>
<td>F.2d</td>
<td>Federal Report, 2nd Series</td>
</tr>
<tr>
<td>F.Supp</td>
<td>Federal Supplement</td>
</tr>
<tr>
<td>FATA</td>
<td>Foreign Acquisition and Takeovers Act 1975 (Cth)</td>
</tr>
<tr>
<td>FCN</td>
<td>Friendship, Commerce and Navigation</td>
</tr>
<tr>
<td>Fed.B.J.</td>
<td>Federal Bar Journal</td>
</tr>
<tr>
<td>FEIT</td>
<td>Foreign Enterprise Income Tax</td>
</tr>
</tbody>
</table>
SELECTED TABLE OF ABBREVIATIONS

FETAC: Foreign Economic and Trade Arbitration Commission
FIRB: Foreign Investment Review Board
FLR: Federal Law Reports
FSIA: Foreign Sovereign Immunity Act (US)
FSIA: Foreign State Immunity Act (Australia)
FTA: Foreign Takeovers Act 1975 (Cth)
FTAC: Foreign Trade Arbitration Commission
GATT: General Agreement for Tariffs and Trade
GTB: General Tax Bureau
H.K.L.J.: Hong Kong Law Journal
Harv.L.R.: Harvard Law Review
IAA: Institute of Arbitrators Australia
IBRD: International Bank for Reconstruction and Development
ICJ: International Court of Justice
ICSID: International Centre for Settlement of Investment Disputes
IFC: International Financial Corporation
IIT: Individual Income Tax
ILM: International Legal Materials
IMF: International Monetary Funds
Int.Bus.Lawy.: International Business Lawyer
Int.Lawy.: International Lawyer
ITAA: Income Tax Assessment Act 1936 (Cth.)
JVIT: Joint Venture Income Tax
J.W.T.L.: Journal of World Trade Law
KB: Law Reports: King's Bench Decision
L.& Pol.Int'l Bus.: Law and Policy in International Business
MAC: Maritime Arbitration Commission
Med-arb: Mediation and Arbitration
MIGA: Multilateral Investment Guarantee Agency
NIEO: New International Economic Order
NPC: National People's Congress
NCUSCT: National Council for U.S.-China Trade
OECD: Organization for Economic Cooperation and Development
PCIJ: Permanent Court of International Justice
PMC: People's Mediation Committee
Poly.L.Rev.: Poly Law Review
PRC: People's Republic of China
QB: Law Reports: Queen's Bench Division
RET: Real Estate Tax
SAEC: State administration of Exchange Control
SASR: South Australian State Reports
SIA: Sovereign Immunity Act
SMH: Sydney Morning Herald
SR(NSW): State Reports (New South Wales)
<table>
<thead>
<tr>
<th>Abbreviation</th>
<th>Description</th>
</tr>
</thead>
<tbody>
<tr>
<td>Syd.L.Rev.</td>
<td>Sydney Law Review</td>
</tr>
<tr>
<td>TAA</td>
<td>Taxation Administration Act (Cth.)</td>
</tr>
<tr>
<td>TC</td>
<td>Tax Cases</td>
</tr>
<tr>
<td>Tex.Int'l L.J.</td>
<td>Texas International Law Journal</td>
</tr>
<tr>
<td>TPA</td>
<td>Trade Practice Act</td>
</tr>
<tr>
<td>TPC</td>
<td>Trade Practices Commission</td>
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<tr>
<td>UN</td>
<td>United Nations</td>
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<tr>
<td>UNCTC</td>
<td>United Nation Centre for Transnational Corporation</td>
</tr>
<tr>
<td>U.N.S.W.L.J.</td>
<td>University of New South Wales Law Journal</td>
</tr>
<tr>
<td>URET</td>
<td>Urban Real Estate Tax</td>
</tr>
<tr>
<td>Vand.J.Transnat'l L.</td>
<td>Vanderbilt Journal of Transnational Law</td>
</tr>
<tr>
<td>VDR</td>
<td>Variable Deposit Requirement</td>
</tr>
<tr>
<td>VLR</td>
<td>Victorian Law Reports</td>
</tr>
<tr>
<td>VR</td>
<td>Victorian Reports</td>
</tr>
<tr>
<td>VVLPT</td>
<td>Vessel and Vehicle Licence Plate Tax</td>
</tr>
<tr>
<td>Wash.L.J.</td>
<td>Washington Law Journal</td>
</tr>
</tbody>
</table>
Introduction

Comparing two legal systems with fundamental differences in almost every aspect, such as those of Australia and China, is a formidable task. The difficulties arise from differences in political structures, economic systems, legal traditions, and cultural backgrounds. Both the comparability of such legal systems and the value of any such comparison may be questioned by some comparatists, who insist on a narrowly defined closeness of relationship between legal systems as the basis for any meaningful comparison. However, the mere fact that Australia and China are rapidly developing business relations, and that both governments play an important role in the control of foreign investment, creates a need to compare the respective systems of foreign investment law.

In order to develop economic relations, both practitioners and policy-makers in the two countries need appropriate knowledge of the other's legal system, and of its interaction with their own. It may even be that some common legal principles, such as those needed in a bilateral treaty, can be examined and established through such a comparison, so that economic contacts between the two countries may be facilitated. That possibility should not be ignored, even if the relationship between the two countries is, as it has been, at a rather low ebb.

Although Australia and the People's Republic of China had no formal diplomatic relations until 1972, economic contacts between them have developed rather rapidly since then. In 1972 the two-way trade between the two countries was $A 84 million, but in the year 1986-87 the figure reached $A 2.2 billion. Chinese sources confirmed these figures and reported that in 1987 trade between Australia and China was US $1.61 billion, of which China's imports represented US $1.3

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1 For example, see A. Watson, Legal Transplants (Edinburgh, Scottish Academic Press, 1974) 5.

2 This thesis was commenced when Australia and China were rapidly developing their economic relationship, which, however, has been affected by the Beijing Massacre on 4 June 1989 and the subsequent suppression of the democratic movement in China. In the long term, however, the economic relationship between the two countries can still be expected to resume; indeed, some business activities have already been resumed. It was reported that a meeting to promote Australian and Chinese business ties was held in Shanghai in May 1990 (Aus. Fin. Rev. 31 May 1990); and that an Australian company, Solar International Holdings, recently established a joint venture with the North China Industries Commission to produce hard resin lenses in China (The Australian 1 June, 1990). Whether and to what extent Australian companies will go back to China will depend mainly on how the Chinese Government is able to improve the investment climate, so that investing in China could be profitable.

3 58:10 Australian Foreign Affairs Record (1987) 594.
billion.\(^4\) As at February 1988 more than fifty Sino-Australian joint venture agreements had been signed, with two of them involving Chinese investment in Australia.\(^5\) In the light of these developments, some Australian officials predicted that by the year 2000 China could become Australia's largest trade partner, although in 1988 China ranked only in third place in Australia's foreign trade.\(^6\) Such developments stimulate this comparative study.

This thesis seeks to set out and compare the systems of foreign investment law and the role of governments in the administration of foreign investment in Australia and China. It is also a study of the functions of government control over foreign investment in the context of increasing international business contacts. While the basis of the comparison is the recognition that both Australia and China are capital-importing countries, the facts that, by accepted economic criteria Australia is a developed country and China is a developing country, that Australia has a common law system and China has its own distinct legal tradition, that Australia is a federation and China is a country with a unitary system of government, add both generality and variety to the comparison.

This is fundamentally a comparative study and the first three Chapters set out the general background for the study. Chapter 1 discusses some basic conceptual issues relating to foreign investment law in Australia and China, Chapter 2 examines the administration of foreign investment in Australia, and Chapter 3 the administration of foreign investment in China. The remainder of the thesis deals with and compares issues of foreign investment in various areas of law. Chapter 4 investigates issues of government control relating to foreign exchange in Australia and China. Chapter 5 examines issues of government control relating to the taxation of foreign investment in Australia and China. Chapter 6 deals with issues of dispute resolution in relation to foreign investment disputes. Chapter 7 concentrates on the issues arising from the Australian-Chinese Investment Protection and Promotion Treaty. Finally, some conclusions will be drawn on the form and effect of government control over foreign investment in Australia and China, as well as some of the questions arising from the comparison.

The comparative study of Australian and Chinese foreign investment laws is a hitherto unexamined topic. Many sections of the thesis are unavoidably descriptive,


\(^5\) These investments are the purchase of 10% interest in the Portland smelter in Victoria in 1983 and the purchase of 40% interests in a project of the iron ore mine in Western Australia's Pilbara region.

not only because of the unfamiliarity and inaccessibility of the materials to most readers, but also because of the differences in many respects of the laws and policies of the two countries. Analysis of many issues has been hindered by the limited amount of information available, and by the difficulties in making a "meaningful comparison". Nevertheless, this thesis is intended, from a comparative perspective, to tackle a number of legal issues arising from Australian and Chinese foreign investment laws and from the context of Australian and Chinese reciprocal investment activities, which by the mere fact of their existence call for attention and study.

Comparability includes "comparability of law" and "comparability of problems". Watson argues that "(v)ariations in the political, moral, social and economic values which exist between any two societies make it hard to believe that many legal problems are the same for both except on a technical level". He further argues that when a comparison is made between the laws in two countries, "except where the systems are closely related, the differences in legal values may be so extreme as to render virtually meaningless the discovery that systems have the same or a different rule". However, the "value" and "meaning" in Watson's arguments must be further qualified. It seems that Watson refers to "value" in law reform and in the possibilities of direct application of a successful rule of one country to a similar situation in another. This is certainly not the only meaningful use of comparative studies. In fact, as long as a comparative study can provide any positive and practical use to society, e.g. for political, economic or legal purposes, a "meaningful comparison" has been achieved. A comparison may have different meanings in different circumstances and for different purposes. For the purposes of legal reform, a comparison between the Australian and British practices may provide a direct answer to unresolved issues in either of them. This comparison is undoubtedly meaningful. But for the purposes of developing economic relations, a comparison between Australian and Chinese law is as meaningful as a comparison between Australian and British law. This is because economic relations between Australia and China can only be developed by increasing understanding between them, including understanding of each other's legal system. Direct application of one's rule to another is not the purpose of such comparison and is not envisaged by either countries at this stage. Rather, to understand each other and explore the differences as well as similarities in their laws with regard to the same issues are the aims of this comparison. The knowledge of each other's legal system holds a key to the success

7 Watson, supra note 1, at 4-5.

8 e.g. the making of the Foreign State Immunities Act 1985 (Cth).
in developing their economic relations. Thus comparability between Australian and Chinese foreign investment law and policy is based on both technical descriptions and practical needs, which simply are that Australia and China are situated in the same geographical region and that their economic futures are related. For this reason, a comparison between Australia and any Asian country, or between China and any Asian country, is equally meaningful as a comparison between Australia and China. In the sense of practicality, a comparison between two systems which do not share the same legal tradition is as meaningful as a comparison between two countries which share the same legal tradition.
Chapter 1 Concepts and Terminology

1.1. Meaning, Forms and Features of Foreign Investment

Foreign investment, as the term implies, involves investment between more than one country. The term is often used by a recipient country to refer to capital and technology from foreign sources. Thus, foreign investment, in its ordinary sense, refers to projects, which are invested or participated in, or supported or financed by foreign companies or individuals, or in some cases by foreign governments. Forms of foreign investment include capital, technology, managerial skills, and other tangible and intangible property or rights agreed upon by the parties involved in a foreign investment project.

Generally speaking, foreign investment is divided into two categories: "direct investment" and "portfolio investment". Here "direct investment" refers to the establishment of a local subsidiary by a foreign enterprise, or the takeover of an existing company by a foreign company for the purposes of controlling the company or exercising influence over its management. "Portfolio investment" refers to a situation in which foreign investors receive financial returns from their investment but do not seek control over, or do not have the power to control, the enterprise concerned. A third category, "investing through licensing agreements", may also be considered.1 A licensing agreement is an agreement between a foreign licensor and a local licensee regarding the transfer of a particular technology or item of intellectual property, or of a legal right attached to a certain franchise. In this arrangement, the foreign investor usually acquires a capital gain or other income through the utilization and protection of his or her rights, but does not necessarily control the licensee's enterprise or participate in its management. Counter-trade or production by franchise are examples.

Foreign investment has had a long history in human society. Although direct foreign investment developed in the 20th century, the history of foreign lending (a traditional form of portfolio investment) can be traced back at least to the fifteenth century.2 Foreign lending has been provided either by governments or private investors to governments or private borrowers, and can be divided into public and private lending, depending on the parties involved.3

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3 For a history of international lending, see id., at 7-21.
International financial institutions\(^4\) have played an important role in portfolio investment since the Second World War. Examples of these institutions are the World Bank, also known as the International Bank for Reconstruction and Development (IBRD), and the International Monetary Fund (IMF). Both were created in 1944 as specialized agencies of the United Nations for the purpose of promoting international economic development. Since then many other international financial institutions attached to the World Bank and IMF, such as the International Financial Corporation (IFC), and many regional development banks have been established. Most institutions normally make loans to the governments of member countries at fixed interest. But IFC, unlike other institutions, invests only in private enterprises and does so in any form except for capital stock.\(^5\) The loans provided by these international institutions are a special type of foreign investment. From the point of view of the institutions, loans are not normally provided for the purpose of pursuing profits; but to the borrowers, the loans are treated in the same way as ordinary foreign investment. The difference between the loans provided by these special financial institutions and those provided by private financial institutions is that the former is not granted merely for commercial interest, but the latter is.

Multinational enterprises are a typical vehicle for direct foreign investment. Here the term "multinational enterprises" ("transnational enterprises" or "transnational corporations") is used in a broad sense, referring to any enterprise which operates in more than one country. This form of direct foreign investment was created before 1914, but has been significantly developed since then.\(^6\) As a means of investment, multinational enterprises have several advantages. By this means, a parent company may directly control foreign sources of raw materials, effectively distribute products in foreign markets, easily transfer funding or technology or managerial skills which are necessary for the development of the business between the parent company and its subsidiaries, and seek to minimize its tax liabilities, which vary in different countries. However, two issues in relation to the use of multinational enterprises

\(^4\) This term here refers to international financial institutions established at governmental level, rather than those private financial institutions carrying on international business.


must be noted. First, multinational enterprises are not the sole form of foreign investment. Secondly, not all multinational enterprises are relevant to direct foreign investment. In fact a foreign company may carry on international trade in another country through local branches, representative offices or selling agents which do not engage in any investment activity. In this case, the multinational enterprise has not directly invested in that country.

The advantages of multinational enterprises to foreign investors imply potential conflicts between the investors and recipient countries. Control of local natural resources and market by foreigners not only risks provoking nationalistic feelings amongst local population in general, but also can endanger the autonomy of the national economy in some cases. Sometimes the dominance of foreign investors may harm competition and restrain the development of the local economy, whose success, after all, is the main purpose of attracting foreign investment by recipient countries. For these reasons, local participation in foreign investment projects has been a common requirement adopted by many host countries in determining the benefits of a foreign investment project to the recipient country. But the arguments against the potential dangers of foreign investment to a host country should never be accepted as an excuse to reject all foreign investment. International economic contacts, in particular foreign investment, could be a very effective source of the capital and technology needed to develop the economy of a recipient country. This is particularly true in Australia, which has traditionally relied on foreign capital to develop its national economy, and China, which is a developing country urgently needing foreign capital and technology to modernize its economy. The issue is how to encourage and control foreign investment properly so that the recipient country may benefit from the inflow of foreign investment.

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7 For example, a foreign investor may establish in another country a new business which does not have relationships with any existing enterprise, and purchase shares in local companies through this business. In this case, no multinational enterprise is involved.

8 A classical example of this case is control of natural resources by foreign companies which may ignore the future needs of the host country for the natural resources, or policy orientation for the use of a specified resource, such as uranium, for pursuing profits by the companies.

9 For example, see R. Seidman, "Foreign Private Investors and the Host Country" (1985) 19 J.W.T.L. 637, 650; J. Spence & W. Rosenfeld, Foreign Investment Review Law in Canada (Toronto, Butterworths, 1985) 104; and Commonwealth of Australia, Overseas Investment in Australia (Canberra, AGPS, 1968) 1. In China, this can be seen in the Joint Venture Law, which allows foreigners to invest in China in the form of joint ventures. The restriction has been relaxed, but not abolished, since 1986, and foreigners are also allowed to operate in the form of wholly foreign owned enterprises.
1.2. Meaning of Foreign Investment Law

The foreign investment law of a country can be broadly understood as a body of laws, regulations and policies of that country aimed at encouraging or restricting foreign investment. These laws, regulations and policies deal with issues such as the establishment of foreign enterprises, the operation of joint ventures between foreign and local investors, takeovers of local interests by foreign interests, the sectors of economy open to foreign investment, the restrictions on and incentives to foreign investment, taxation, and foreign exchange control.

Many so-called "branches" of law are more or less relevant to foreign investment. For example, there is Foreign Acquisition and Takeovers Act 1975 (Cth) (FATA) in Australia; but the registration of foreign companies is currently governed by the Companies Acts of each State, takeovers involving the media are subject to the Broadcasting Act 1942 (Cth), the taxation of foreign investment is subject to tax laws, and exchange control is regulated in the Banking (Foreign Exchange) Regulations 1946 (Cth). Similarly, although Chinese foreign investment law consists mainly of Acts and regulations which are made especially for foreign investment, it also involves many areas of law, such as contracts and arbitration or litigation procedures, which are applicable to both foreign investment and Chinese enterprises.

1.3. Foreign Investment Law in Australia

Australia has a federal system of government and a common law tradition. Under the federal Constitution of 1900, power to legislate on foreign investment is vested in the federal Parliament. Like most powers under the Constitution, the

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10 Traditionally the company law has been enacted by each State, although a uniform version of company law was adopted throughout Australia in 1962. In 1989, the federal Corporations Act was passed, but was challenged by the NSW, SA and WA Governments in the Federal Court, which supports the States' position in relation to several key provisions of the Act. *NSW v Commonwealth* (1990) 8 ACLC 120. However, the federal Parliament passed the Corporations Legislation Amendment Act 1990 (no.110). This Act amends numerous provisions of the Corporations Act 1989. Whether this Act has resolved the constitutional dispute arising from the 1989 Act is yet to be seen.

11 For example, Foreign Economic Contract Law, CCH, China Laws for Foreign Business para.5-550; Provisional Rules of Procedure of the Foreign Trade Arbitration Commission of the CCPIT, CCH, China Laws for Foreign Business para.10-500, in addition, arbitration rules also include the Provisional Rules of Procedure of the Maritime Arbitration Commission of CCPIT, CCH, China Laws for Foreign Business para.10-540; and Law of Civil Procedures (Tentative), CCH, China Laws for Foreign Business para.19-200.

12 The Commonwealth Constitution, s.51(i),(xiii),(xx) & (xxxix).
power to regulate foreign investment is concurrent rather than exclusive. The State parliaments may make laws and regulations in relation to foreign investment, such as the registration of foreign companies, provided that there is no inconsistency as defined in s.109 of the Constitution between the federal and State laws. In this sense, State power in the area of foreign investment is primarily restricted by s.109 of the Constitution, which invalidates State laws in case of inconsistency. The application of s.109 extends to a federal policy which has been given by the federal Parliament such an effect as to prevail over a State law. But when a policy is not directly supported by law, it has no effect on the State law. As will be seen, in some sectors of the economy the federal Government asserts jurisdiction on the basis of policy rather than legislation.13 The use of policy not directly supported by any federal law results in the inapplicability of s.109, which governs the inconsistency between federal and State laws only. Federal investment policies in their present form call for voluntary cooperation from States and foreign investors. This is one of the features of foreign investment law and policy in Australia.

Federal Parliament has passed several Acts which are directly or indirectly relevant to foreign investment. The FATA is so far the only federal Act especially dealing with foreign investment in Australia. By contrast, the Banking Act 1959 (Cth) has a special Chapter on foreign exchange control, which represents an important aspect of foreign investment control. Under this Act, the Banking (Foreign Exchange) Regulations 1946 (Cth) were maintained.14 But most of the rules relating to foreign investment are to be found in general laws applicable to both foreign and domestic investors. For example, foreign investors are subject to particular Acts or regulations in various sectors of the economy, such as the Broadcasting Act 1942 (Cth) in the media, the Civil Aviation Act 1920 (Cth) in international and domestic aviation,15 and the Environmental Protection (Impact of Proposals) Act 1976 (Cth) and Environment Protection (Nuclear Codes) Act 1978 (Cth) in relation to environmental issues.16 It is evident that the rules which may be classified as "foreign investment law" in Australia take many forms.

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13 e.g. establishing new businesses (rather than takeovers) by foreign investment in mining sector and news papers.

14 Most provisions of the Regulations have been suspended by notices of the Treasurer and the Reserve Bank in accordance with the Regulations.

15 Aviation industry has been deregulated since October 1990. Foreign operators are allowed to hold less than 15% of interests in Australian domestic airlines.

16 The Commonwealth has, as observed by Professor Crawford, "one way or another, legislative power over most large-scale mining and environmental matters". This power certainly extends to control of foreign investment in the area of
Two reasons may be suggested for such a variety of legislation on foreign investment. First, the common law tradition, which tends to deal with problems on a case by case basis, has its impact on the system of Australian foreign investment law. As a result, the provisions on foreign investment are incorporated in separate laws and regulations gradually, wherever control over foreign investment is considered to be necessary.17 Secondly, the initial open-door policy adopted by Australia toward foreign investment has greatly affected the development of Australian foreign investment law.18 The system has been built up gradually, separately and passively in response to various needs for control, which in turn have been affected by the balance of interests between foreign and local investors, the economic situation of the country and the perceived priorities (political and economic) of the Government of the day. The need to codify foreign investment law in Australia has not been felt.19 Thus Australian foreign investment law is an accumulation of a body of legal principle and regulation, developed gradually on case-by-case basis, to be found in many separate pieces of legislation, as well as through a variety of government policies which may or may not be directly supported by legislation.

1.4. Foreign Investment Law in China


17 Alternatively, provisions in existing laws may be given additional effect so that they apply to foreign investment.

18 Australia followed a general open-door policy toward foreign investment until 1939, and control over foreign investment was gradually introduced in particular contexts whenever the restrictions were considered desirable.

19 It appears that as long as the government policies on foreign investment receive cooperation from the States and foreign investors at their present forms, the need to codify foreign investment law in Australia will not arise.

20 Under the central Government of China, there are Provinces, Autonomous Regions and Municipalities directly under the central Government.

21 For discussion on the functions and status of the NPC, see A.Tay, "Introducing China's Business Law and Practice" CCH, China Laws for Foreign Business para.2-200.

22 See Tay, id, para.2-205.

23 The Constitution of the PRC, Arts.58, 62 & 67, CCH, China Laws for Foreign Business para.4-500. The supremacy of the NPC can been seen at least superficially in the Chinese Constitution. However, the "supremacy of the NPC" in fact is
Council, which is the highest executive body of the country, may exercise limited legislative power as accorded by the Constitution, and local governments may also exercise legislative powers provided that none of the laws and regulations passed by them is inconsistent with the laws of the NPC and regulations of the State Council. Because of this, foreign investment law in China consists of laws and regulations of both the central and local governments.

Unlike Australia, foreign investment law in China is treated as an independent branch, which is sometimes called "foreign economic law". The concept of "foreign economic law" is, however, broader than the concept of "foreign investment law", and includes also legislation dealing with issues of international trade, which is not the main concern of this study. For this reason, in this thesis reference to foreign investment law in China means only laws and regulations which are relevant to the establishment of foreign or joint ventures; the taxation of foreign-related enterprises; labour management within, and registration of, foreign-related businesses; foreign exchange control; and other issues directly concerning foreign investment.

The existence of Chinese foreign investment law as an independent branch distinguishes the Chinese system from the Australian system. The Chinese economic system and the history of foreign investment in China are among the reasons for the difference. Because State ownership, collective ownership and the State plan have been the main bases for the Chinese economic system from 1949, in particular before 1979, there was no foreign investment in China before 1978. Laws then passed cannot be appropriately applied to foreign investment, which is mainly based on private ownership and the principles of laissez-faire economy. With the inauguration of the "open-door" policy and encouragement of foreign investment, subdued by the "super-supremacy of the Communist Party" whose ideology is the basis of the Constitution.

24 Id., Art.89. Its legislative power is limited to the extent that none of its regulations is inconsistent with the Constitution and the law of the NPC.

25 The local governments of China may promulgate local legislation according to the Constitution, the laws passed by the NPC and regulations made by the State Council. See the Constitution, Arts.99 & 116; and Organic Law of Local People's Congress and People's Governments of the PRC at Different Levels, Arts.7, 38, & 51, in Dept. of Legislation Supervision, Bureau of Legislation, the State Council, ed. Collected Legislation of China on Encouragement of Foreign Investment (Zhong Guo Gu Li Wei Shang Tou Zi Fa Gui Xuan Bian) (Beijing, Chinese University of Politics and Law Press, 1987, in Chinese) 4-5. For discussion on the authority of law in the hierarchy of Chinese political system, see Tay, supra note 21, para.2-230.

26 This excludes projects under foreign aids, which are not foreign investment in a commercial sense.
China has passed many special laws and regulations dealing with foreign investment. In addition, the absence of foreign investment in China before 1978 imposed no restriction on China’s ability to consider foreign investment as a whole and to establish investment law as a new and independent branch of law. In terms of form and quantity, China has passed more Acts and regulations directly relevant to control of foreign investment than Australia.

1.5. Problems of Government Control

1.5.1. Contradictions Implied in the Notion of Control

Today, countries accepting foreign investment have adopted at least some measures of control over foreign investment, whether they are countries with a state-planned economy or a laissez-faire economy. Like trade protection policy, control over foreign investment can also be regarded as a protective measure against external economic forces. Indeed, more often than not, governments use various controlling measures to keep a balance between national interests as a whole (which require the import of foreign capital and techniques) and particular local interests (which may be victims of foreign competitors). The attempt to maintain a balance between conflicting interests can particularly be seen in the foreign investment law and policies of Australia. Foreign investment has been commonly accepted as a useful means of developing a national economy, as well as international economic relations. For a host state, foreign capital and advanced technology which are not available from the domestic sources are utilized to meet the needs of domestic market and, eventually, to speed up the development of the national economy.


28 e.g. attempted control over foreign purchase of real estate.

29 Dick Bryan argues that there is "no doubt the foreign investment, both as equity and debt, can add to the productive base of the economy, and secure a level of investment and growth beyond that which could be financed by domestic savings". D.Bryan, Foreign Investment Policy Issues for Australia (Discussion paper No.5 1989-90, Legislative Research Service, Commonwealth of Australia, 1989) 23.

30 A number of studies of the impact of foreign investment on Australian economy has been conducted by economists. Foreign investment has been broadly regarded as helpful to Australian economy. For example, D.Carr commented that although the benefits of direct foreign investment to general economic progress in Australia is superficial, the impact of foreign investment on various aspects of the economy, such as mining, improvement of skills, higher productivity and competition, is positive. D.Carr, Foreign Investment and Development in the Southwest Pacific: With Special Reference to Australia and Indonesia (New York, Praeger Publishers, 1978) 12-36. In addition, positive effects of American investment on Australian economy are also
capital exporting State, the export of idle capital and the transfer of advanced
technology whose development or use are limited by the capacity of the domestic
market can maximize economic returns for the owners of capital and technology, and
also benefit the country by generating foreign exchange. This is why foreign
investment has been accepted as an important form of international economic contact.
In addition, because perhaps of the endless struggle for trade protection among
nations, foreign investment, which may provide an alternative means of breaking
through the protective barriers or penetrating foreign markets, has become popular.

Governments which encourage foreign investment are often in a dilemma. On one hand, they need foreign capital and advanced technology to boost their economies. On the other, they have to support the growth of the local economy, some aspects of which are inevitably disadvantaged by stronger foreign competitors. Excluding foreign investment from the local markets (though this would literally eliminate the conflicts between foreign and local interests) provides no solution for a country which depends largely on foreign investment for its development. Thus a realistic option is to maintain a balance between levels of foreign ownership and local ownership in the national economy through legal and economic calculation. The balance can perhaps be determined by taking into account economic priorities of the nation, the effect of particular foreign investment on the local economy, the competitiveness of foreign capital and technology on international markets and, last but not least, the political influence of nationalists in the recipient country.

1.5.2. Purposes of Controlling Foreign Investment

To maximize the benefits of foreign investment to a country's economy and to minimize the harm which foreign investment can do to the local economy is the principal aim of government control.

The precise direction of control is often affected by the priority pursued by governments. For example, China at its present stage has set so-called "socialist

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31 This task requires governments to allow foreign investors to share profits and managerial responsibility with local investors. This fact alone has caused fear and dissatisfaction among some local businessmen and politicians.

32 In this context, national economy refers to capital, tangible and intangible assets, or such property owned by nationals of a recipient country.
modernization" as a priority.\textsuperscript{33} In order to realize "socialist modernization", China has to direct foreign investment so that it does not contravene the "socialist principles" upheld by it.\textsuperscript{34} Thus China expects foreign investment to boost its economy and to assist the plan of socialist modernization, but refuses to grant foreign investment permanent status in the Chinese economy in the long term.\textsuperscript{35} The Chinese Government therefore decides that, presently, China, on one hand, has to accept foreign investment, but on the other, has to limit the development of foreign investment in China.

\textsuperscript{33} See the Constitution, Preamble. The meaning of the socialist modernization is not very clear. The confusion raises from the changing concepts of socialist economy. The private ownership of businesses, except to a limited extent such as small family retailing business or self-employed service professions, was prohibited in China a decade ago, but now private-owned enterprises which can have as much as thirty partners and virtually unlimited employees are allowed. See the Provisional Regulations of the PRC on Private Enterprises, in CCH, China Laws for Foreign Business para.13-546. It is not clear whether foreign-related enterprises will be accepted as part of the "socialist economic system" of China when China reaches the goal of modernization.

\textsuperscript{34} "Socialist modernization", in general, reflects a totalitarian idea of modernization, which seeks to combine Western economic prosperity and Chinese political system without "modernizing" (endangering) the political belief held by the Communist Party and Chinese economic structure based on public ownership of property and a central-planned economy.

\textsuperscript{35} Chinese law, in particular the Constitution, has not expressly indicated a positive attitude toward foreign investment in the future. It does not clearly indicate that private ownership of business and property by foreign investors will be recognized as one of the bases of the Chinese economic system. Rather, Article 6 of the Constitution states that only the State and collective ownerships are the bases of Chinese economic system. The lack of future guarantee from the Chinese Government may be the crucial reason for lack of large and long term foreign investment projects in China. A similar view was expressed by Pattison, who observed that provisions of the Joint Venture Law in relation to protection of foreign investors' rights "have none of the strengths of a constitutional guarantee for foreign investment, such as that found in Yugoslavia". J.E.Pattison, "China's Developing Legal Framework for Foreign Investment: Experience and Expectations" (1981) Law. & Pol.Int'l Bus. 89, 112. By contrast, a Chinese scholar argued that the present Constitution of the PRC is a "landmark document" for foreign investors, and that under the Constitution foreign investment is not only allowed but also protected by the law of the PRC. An Chen, "To Open Wider, or To Close Again: China's Foreign Investment Policies and Laws" (1984) 6:1 N.Y.L.S.J.Int'l & Comp. L. 1. He implied that the Constitution has provided enough protection to foreign investment in China. However, Armstrong expresses his doubt on the guarantee to protect foreign investment in China in a different way. He comments that the Chinese Constitution is not generally supreme in China and Chinese courts cannot enforce the guarantee in the Constitution even there is any. In addition, the Constitution can be amended by the NPC which in turn is controlled by the Communist Party. See W.Armstrong, "The Development of Commercial Law for Foreign Investment in China" (1989) 12:1 Houston J.Int'l L. 55, 57.
Government control of foreign investment could be a highly controversial issue, given the discrepancy of power to control between central (federal) governments and local (State) governments and potential disagreements over methods of control by executive action. This thesis examines this issue in the context of Australian and Chinese foreign investment laws. The effect and rationale of government control in Australia and China will be evaluated.

1.5.3. The Forms of Control Over Foreign Investment

The specific form through which governments administer foreign investment matters varies. In determining which particular form is to be adopted, two factors are often considered. First, a government must adopt a form which is consistent with its legal system, in particular its constitutional structure. For example, delegated legislative power in Australia is required to be specific and certain, but in China can be general and wide. This results in the existence of voluminous regulations on foreign investment made by the executive body in China. Secondly, a government must adopt a form which is understandable, and (as far as possible) acceptable, to foreign investors. Thus, foreign investment may be properly encouraged and controlled according to the policy of the recipient country. For this purpose, the Chinese Government has accepted many international practices and reduced the volume of "internal documents", which have been generally criticised by foreign investors.36

In the context of policy and regulation, two categories - legal rules and administrative measures - can be distinguished. Legal rules refer to Acts or regulations governing foreign investment, which are made or changed by the legislature or the executive under the authorization of the legislature. In addition, in Australia case law made by judges is also considered a form of law. Acts, regulations and case law are directly enforceable in the courts of law. By contrast, administrative measures include those policies and government statements concerning foreign investment. They are not directly enforceable as such but may often be indirectly enforced and supported by the sanction of laws which grant the government discretionary power (e.g. power to suspend the application of a provision of law, or to grant an export permit). These measures can be made by an executive body within its other existing powers. In practice the significant difference between those two forms often lies rather in their forms than their effect.

In order to exercise control over foreign investment, a government must establish appropriate mechanisms for control. The status (statutory or non-statutory)

36 Tay, supra note 21, para.2-265.
and structure of the mechanisms vary. For example, in Australia, the Department of the Treasury is the authority to approve a foreign investment proposal, and the Foreign Investment Review Board (FIRB), an independent body accountable to the Department of the Treasury, is the authority which examines foreign investment proposals on behalf of the Department of the Treasury. The two authorities have a different status. One is an executive body; the other is a non-statutory body established under the executive power of the Australian federal Government.

The form of control, which is suitable to the legal, political, economic, and administrative structure of the country, is important if a government is to administer foreign investment effectively. For example, the Chinese legal system and its history in the past forty years contribute to the fact that the Chinese Government has to emphasize formal legal rules as a main means of control. The reason is twofold: historically, it had to do so in order to create an atmosphere of legality, which did not generally exist in China between 1949-1979;³⁷ moreover, it can legitimately do so through the legislative power of the central and local governments under the new (1982) Constitution. If the Chinese Government were to use the form of investment guidelines, such as those adopted by the Australian Government, as its basic guidance to foreign investment in China, foreign investors would feel insecure in dealing with this socialist country, and may consequently be discouraged. Similarly, because of the differences in their economic systems, the Chinese Government controls foreign investment through its administrative departments while the Australian Government establishes the FIRB as an independent body to examine investment proposals on the Treasurer's behalf. Avoiding direct involvement in market economy is perhaps the reason for the existence of FIRB.

1.6. Some Concepts and Terms in the Contexts of Australian and Chinese Foreign Investment Laws

1.6.1. Australian Legal System versus Chinese Legal System

The Australian legal system, based on the common law tradition, is a transformation of the English legal system into a federal system. Bearing the marks of the Westminster model, which is characterized by the direct and close relationship between the parliament and executive (with ministers being the members of the parliament and the executive directly accountable to the parliament), legislative, executive and judicial functions of the Government are divided, or shared, among the Parliaments, the executive arms of the respective governments and the courts of

³⁷ In the 1950s, roughly between 1950 and 1954 there was a little interlude of "socialist legality". But the effort was defeated by the "Anti-rightist movement" initiated by Mao in 1955.
law in Australia. Accordingly, the federal Parliament exercises legislative power, but may delegate power to ministers; the executive exercises administrative functions of the government; and the courts enforce the law. Close connections are found among the three branches of the governments, in particular between the parliament and executive. The fact that members of the executive government are also parliamentarians allows the executive, apart from being accountable to the parliaments, to influence the exercise of legislative functions to a great degree. On the other hand, the power of the courts to make case law contributes either independently to the sources of law or interactively to the exercise of the legislative power by the parliaments.

The Australian legal system is also characterized by the division of power between federal and State governments. The federal Government exercises powers in accordance with the Commonwealth Constitution, which sets forth limitations on federal powers. In practice, constitutional issues hardly arise from the exercise of control over foreign investment in Australia, but such issues can arise and the system needs to be understood.

The legal system of the PRC is influenced by both civil law and Soviet law systems. But it follows neither strictly. In fact, the present legal system in the PRC is a mixture of several legal traditions and political ideologies. In particular, it has incorporated the Chinese legal tradition whose marks can be seen in the extensiveness of the executive power and various aspects of legal philosophy; the civil law tradition whose influence can be seen in the efforts of the Chinese Government to codify criminal and civil laws; Soviet law, whose legal concepts have been accepted in many areas of Chinese law, in particular in its Civil Code; and Communist theories as modified by the CCP, whose dominant position and principles have been entrenched by the Constitution and the law. In a broader sense, Chinese law today may also have been affected by the common law, although that "influence" might well be deemed a matter of coincidence occurring, perhaps inevitably, in the process of law-making in modern society. However, the affinity to the common law is seen in the Chinese approach to legislation taken after 1978, which deals with particular issues first rather than sets out basic legal principles for particular rules, as the civil law tradition normally does. In another words the PRC has developed many separate laws on foreign investment before sorting out the legal basis for the existence of foreign-related enterprises in the Chinese Civil Code, which is supposed to be the basis for all laws and regulations on civil matters in China.

The functions of government are divided, but not strictly, among three branches of the Government in China. The National People's Congress (NPC), although exercising mainly legislative power, is formally the highest authority in
China. But the executive has general administrative and regulation-making power whose validity is not dependent upon the authorization by the NPC. The judiciary, consisting of the courts and procuratorates, exercises the judicial functions of government. Unlike the Australian system, the Chinese courts do not have power to make case law, although the Chinese National Supreme Court occasionally issues circulars or decisions for the purposes of interpreting a law or applying a provision by means of analogy. These directions of the National Supreme Court have much the same effect as case law. Unlike Australia, Chinese law is uniform throughout the country. No discrepancy between the law of the NPC and regulations of the State Council or between the law of the central Government and regulations of local governments is allowed, at least in theory.

1.6.2. Federal Government versus Central Government

The federation was formally established in 1901 by the Commonwealth Constitution 1900. At present, there are 6 States and 3 Territories in the Commonwealth of Australia. The relationship between the federal Government and State governments is defined by the Commonwealth Constitution, which also divides powers between them. The power to regulate foreign investment falls within federal legislative power. Thus the federal Government of Australia has power to regulate foreign investment by virtue of the Commonwealth Constitution. Although the "Australian Government" is not a precise legal concept under the Commonwealth Constitution, in this thesis, it is used to refer to the Commonwealth Government.

The Chinese Government has also prevailing power to control foreign investment. Under the Chinese unitary state system, the central Government is the highest authority in the country. Founded in 1949, China is currently controlled by the last major communist party in the world, which in order to cling to its political power has refused to adopt Western ideas of democracy. At present, China consists of 30 Provinces, Autonomous Regions and Municipalities directly under the central Government, excluding Taiwan, Hong Kong and Macao. The Chinese

38 It should be noted that in the context of the Constitution, the Commonwealth Government or federal Government, rather than the "Australian Government", are more common terms. H. Renfree, The Executive Power of the Commonwealth of Australia (Sydney, Legal Book Pty Ltd, 1984) 46-7.

39 The rejection of Western ideas of democracy denies Chinese people's involvement in resolving various problems arising from the undergoing "economic reform". As Professor Tay observes "(d)emocracy does not solve problems; it provides rather the necessary climate for discussing them seriously and tackling them with genuine involvement from below". See A. Tay, "Communist Visions, Communist Realities and the Role of Law" 13 Bulletin of the Australian Society of Legal Philosophy (1989) 237-52.
Constitution allows the central Government to form uniform laws, rules and policies, which must be followed by local governments. But local governments may issue measures or regulations pursuant to the laws, regulations, or policies of the central Government.

The differences in the State system of Australia and China massively affect the formation and operation of investment law and policies in the two countries. Restricted by its constitutional power and the structure of the federation, the Australian Government has to deal with constitutional issues in relation to the power to regulate foreign investment. The failure of the federal Government to pass a federal Corporations Act in early 1990 has forced it to seek alternatives, such as amending the Corporations Act 1989 (Cth) in the light of High Court's decision in NEW v Commonwealth, advocating another uniform version of Companies Act, to pass separate statutes on corporate affairs (to avoid constitutional obstacles), or to obtain reference of power from the State governments with regard to the regulation of corporate matters. The federal Parliament chose to amend the Corporation Act 1989 (Cth) and passed the Corporations Legislation Amendment Act 1990. By contrast, the Chinese Government does not have any constitutional difficulty in assuming total control of foreign investment and corporate affairs throughout the country. Thus, Chinese foreign investment laws, which include considerable volumes of local legislation, are formulated under the direction of the central Government.

1.6.3. States versus Provinces

"State" in the context of the Australian Constitution refers to basic political units having a certain autonomy and which constitute the Australian federation. Most of them came into existence first as British colonies before the federation was created. The State governments are to a degree independent from the federal Government. Their sovereignty and power are subject to the Commonwealth Constitution, which specifies the scope of power of the Commonwealth Government. In most areas of foreign investment, the State governments and federal Government exercise concurrent power, but federal law prevails over State law by virtue of s.109 of the Commonwealth Constitution in case of discrepancy arising within the limits of federal power.

The counterparts of Australian States and Territories in China are Provinces, Autonomous Regions and Municipalities directly under the central Government, which, where appropriate and convenient, will together be referred to as "Provinces".

40 (1990) 8 ACLC 120.

41 No.110 of 1990.
in this thesis. The Provinces in China are subordinate to the central Government of China. They must follow the laws and policies of the central Government, but may enact specific rules and policies provided that these rules and policies are not inconsistent with the Constitution, the law of the NPC, regulations of the State Council and policies of the central Government.

1.6.4. Statute versus Fa

"Statute" is a term adopted in Australian law referring to legislation (Acts) passed by federal or State parliaments. Being a source of law recognized in common law tradition, it is often the basis, or the source of power, for regulations made by the executive. Its counterpart in Chinese law is "fa", which can be translated in English as "law". But "Fa" has a dual meaning in Chinese law. Broadly, it refers to all sources of law, such as legislation passed by the NPC, regulations made by executive, local legislation and international treaties signed by China. But in a narrow sense, it specifically refers to the legislation passed by the NPC and the its Standing Committee. In the latter case, "fa" is often comparable with "Act" in Australian law.

1.6.5. Regulations versus Tiaoli

"Regulations" (or statutory rules) in the context of Australian law refer to delegated legislation made by the executive pursuant to statutes passed by parliament. They are specified rules for the implementation of Acts passed by parliaments. Their equivalents in Chinese law are "tiaoli" (which can also be translated as "provisions"), "banfa" and "guiding", which are made by the executive or local governments pursuant to the Constitution, the law of the NPC, or regulations of the State Council (in the case where the Departments of the central Government or local governments make specified rules pursuant to the regulations of the State Council). But rules and regulations made by the executive or local governments also bear other names in Chinese law, such as "guize" (rules), "xize" (detailed rules), "jueyi" (resolution or decisions), "mingling" (order or decree). These terms, as well as "tiaoli", "banfa" and "guiding", do not have clear and precise meanings in Chinese law. In general they refer to a source of law made by the executive or local

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42 Tay, supra note 21, para.2-225.

43 "Delegated legislation" in Australian law means a "legislative instrument made by a body to which the power to legislate has been delegated". D.Pearce, Delegated Legislation in Australia and New Zealand (Sydney, Butterworths, 1977) 1.

44 These and other terms, their hierarchy of authority and their overlap and frequent ambiguity are discussed in Tay, supra note 21, para.2-225.
governments, but do not suggest any subtle distinction among themselves. Their legal significance can only be understood in a particular context of Chinese law. In this thesis, regulations and statutory rules in Australian law are regarded as comparable with regulations, rules, detailed rules, resolution, decisions, orders, decrees and provisions made by the competent authorities in Chinese law.45

1.6.6. Policy versus Zhence

Policy in the context of Australian foreign investment law refers usually to a government statement or guidelines which are publicly accessible, and may extend to departmental directives issued by responsible Ministers to officers in charge. Such directives may not be readily accessible, depending on the law governing the exercise of that executive power.46 In China, policy ("zhence") refers to government statements and internal rules (neibu wenjian) which have restricted circulation and are not publicly accessible.47 The difference between departmental directives in Australia and internal rules in China is that an "internal rule" is confidential and available only internally within a specified governmental department.

Policy in both Australia and China, in a broad sense, provides assistance to the implementation of law, or may suggest the direction for legislation. The importance of government policy in the enforcement of law is recognized in both Australia and China, although more explicitly in the latter. For example, in China, Art.4 of the Economic Contract Law expressly states that the validity of a contract is also subject to government policy; and in Australia, the High Court has confirmed the need for an executive body to consider government policy in exercising its power.48 This suggests that while a policy which is supported by legislation or

45 This excludes some rules made by a government agency, such as Regulations on Foreign Currency Deposits and Special Renminbi Deposits by the Bank of China, (CCH, China Laws for Foreign Business para.8-570), which in theory cannot be directly enforced in the Chinese courts.

46 For instance, sometimes officers in charge are not required to give reasons for their decisions. Thus, if a departmental directive is involved in this case, it is not publicly accessible.

47 For discussion, see Tay, supra note 21, para.2-265.

48 See Ansett Transport Industries (Operations) Pty Ltd v Commonwealth (1977) 139 CLR 54, where Barwick CJ. comments that "observance of government policy by the Comptroller-General of Customs" does not breach his duty under law (at 61); Murphy J. observes that an executive power should be exercised "in accordance with the discretions and policy of the Minister" (at 87).
which presages the changes in legislation may be indirectly enforceable or taken into account by an Australian court, it may be directly enforceable in a Chinese court.  

1.6.7. Defining "Control"

The term "control" will be repeatedly used in this thesis. Generally, the term is used in one of three meanings: the power to control, the process of exercising control and the effect of control over various matters. The power to control foreign investment in Australia and China is the power to regulate or administer foreign investment under the relevant Constitution by the legislatures and executives in the two countries. The power to control is a constitutional power which exists regardless of whether it has been fully exercised. The process of exercising control refers to actions of a government or its agents to regulate, manage, encourage, or discourage foreign investment through either legal means or administrative measures. In the process, the power to control foreign investment is implemented. The effect of control is the result of exercising the power to control. It emphasizes the fact that some laws and policies have been implemented or that a system of control has been established or that a target of control has been reached. The three meanings of control represent different aspects of control and together constitute the concept of control.

1.7. New Economic Policies of the PRC

1.7.1. A Historical Perspective on the New Economic Policies

The New Economic Policies are the bases of China's open-door policy, under which millions of dollars of foreign investment are attracted to China. The history of the New Economic Policies has been closely associated with and directly affected by the political changes in China since the 1970s. A brief review of political history of the New Economic Policies is essential to understand the current open-door policy, its legal implications, its economic ramifications and its potential limitations in the future. In a communist country like China, politics has never been

49 For example, a HK company signed a contract with a Chinese cultural organization of a local government on 10 March 1982. The contract was approved on 22 March 1982. But on 7 June 1982, the central Government issued a new policy prohibiting governmental organizations from engaging in commercial activities. The local Government thus terminated the contract signed by the HK company and the organization. The HK company challenged the decision of the local Government at the local court, which, however, gave retroactive effect to the policy and decided that the contract was invalid. X Teahouse, Hong Kong v Workers' Cultural Palace, Y County 2:9 CLP (1988) 31.

50 A different approach to the review of the history of China's open-door policy can be found in Pattison, supra note 35, at 89.
separated from law. This is evident even in names of many law school and legal journals.\textsuperscript{51} Thus it is necessary to examine the views of some Chinese politicians regarding the New Economic Policies.

The so-called New Economic Policies of the PRC came into existence in 1978 at the Third Plenary Session of the Party's Eleventh Central Committee. In this meeting the Party decided that the focus of the Party's work should be turned to economic construction and the development of China's "socialist economy", rather than the political and ideological movements which had haunted China since the mid-1950s.\textsuperscript{52} This meeting represented the end of Mao's era in Chinese history,\textsuperscript{53} although Mao's Thought, which was redefined as a crystallization of the ideas of many revolutionaries of the "old generation", is still upheld as one of the fundamental principles in the Chinese Constitution.

The present New Economic Policies are commonly but vaguely accepted as the masterpiece of the present paramount leader of China, Deng Xiaoping, who obtained effective control of the Party soon after the Third Plenary Session of the Party's Eleventh Central Committee. Since then Deng's myth has replaced Mao's in Chinese politics. Compared with most politicians of the old generation in China, Deng has a relatively open mind and a pragmatic view of economic development. His pragmatic view ("No matter it is a black cat or a white cat, it is a good cat as long as it catches rats") was taken as evidence of his "bourgeois" attitude toward the theory of class struggle, for which he paid a price during the "Cultural Revolution" (1966-76). But Deng is neither the first Chinese politician in the PRC history who

\textsuperscript{51} For example, Chinese University of Politics and Law.

\textsuperscript{52} The need to change the Party's policy has been emphasized by Deng. He states that:

...the reason for China's backwardness in history was its isolation from the rest of the world. After the founding of the PRC, some countries put a blockade on us and created some difficulties for us; thus we were still isolated to some degrees. In addition, some "leftist" policies, in particular the "Great Cultural Revolution" brought us disaster. To conclude, our experience in the past 30 years was that it is impossible to develop economy by closing the door of China and the economy can never be developed in this way.


\textsuperscript{53} Mao Zedong, the late Chairman of the CCP died in 1976, but his myth continued at least for another two years mainly because the then Party's boss, Hua Guofeng, derived his position and authority directly from Mao's "will" made before his death. Mao appointed Hua his successor, and thus Hua continued to deify Mao for the purpose of maintaining his position in the Party.
held a liberal view of economic policy, nor the real producer of or motivating force behind the policy which was intended to liberalize the Chinese economy from the impractical Marxist economic model and to lead to a peaceful and successful transformation of the Chinese economy (and even the political system) from a backward economy to a productive economy. As will be seen, the late President Liu Shaoqi had proposed a selective use of Western approaches to economic development before the establishment of the PRC. As will be seen also, in the past 6 years Deng has constantly imposed constraints on the reform program allegedly initiated by himself, repeatedly rejecting so-called "bourgeois liberalism", which loosely covers everything from ideological preference to economic reform that may endanger the economic foundation of the socialist-controlled totalitarian society. From the dismissal of Hu Yuebang from his position as a result of the student unrest in 1987 to the June Massacre in 1989, Deng showed a negative attitude toward democratic ideas despite their close association with the so-called New Economic Policies.

The similarities in the views of Liu and Deng can be seen in both their liberal views of economic reform and their conservative attitude toward political reform. Limited by the historical circumstances around him, Liu did not really discuss the issue of opening China to foreign investment. But he predicted, as early as 1949 - before the CCP gained control of China - the co-existence of private ownership and state-private cooperative ownership of property in the then approaching PRC. His view certainly affected the Party's economic policies to some extent in the 1950s, when the Party changed the economic structure of China from a so-called five-elements composition (State ownership, collective ownership, state-capitalist cooperative ownership, private capitalist ownership, and private

54 Deng admits this himself. He once said that "I proposed China's economic policy of opening to the outside world, but as to the details of the specific of how to implement it, I know very little indeed". The Magnificent Goal of Our Four Modernizations and Our Basic Policies, Fundamental Issues in Present-day China (collected speeches of Deng Xiaoping) (Beijing, Foreign Language Press, 1987) 67.

55 Deng indicated his rejection of "bourgeois liberalism" on numerous occasions. For example, see "Abstract" of his conversation with some unofficial visitors from Taiwan, in Selected Important Documents Since the Third Plenary Session of the Party's Eleventh Central Committee (Shi Yi Jie San Zhong Quan Hui Yi Lei Dang De Zhong Yao Wen Yi Xuan Bian) (Beijing, People's Publishing House, 1987, in Chinese) 877. His views are particularly directed against the demands of some Chinese people for "democracy" and "freedom" as recognized in Western society.

ownership of small family business or peasant\(^{57}\) to a three-elements composition (state ownership, collective ownership and small business)\(^{58}\), through a transitional program based on the "voluntary" cooperation of private owners of property and compensatory purchase of private property. But it was not clear whether the actual transition took place faster than the "long fierce and arduous" period predicated by Liu.\(^{59}\) In fact, the so-called Socialist Reform and Great Leap Forward in the 1950s were conducted by Mao Zedong, who began to deify his image in the Party during 1955-58 after eliminating some of his political opponents within the Party through the infamous Anti-rightist Movement. This suggests that the transition was probably carried out basically at a pace set by Mao. Nevertheless, had the transition been carried out in a slower pace as predicated by Liu, the Chinese economy could probably have been in a better shape than it was before 1978. Liu's liberal view of economic reform was also seen in his view of labour management,\(^{60}\) and the experiment with the "trust" as a form of industrial operation or management.\(^{61}\) The implications of his views could be followed beyond the literal meaning of his statements, made under the reign of Mao, who had already begun eliminating

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\(^{57}\) Broadly, in the context of ownership of property, state ownership means that property belongs to the State (or people); collective ownership means the property belongs to a specified group of people; state-capitalist cooperation refers to a co-ownership between the Government which obtained control of the property through either requisition or under-valued purchase and Chinese individuals who were classed as capitalists by their wealth; private capitalist ownership refers to enterprises which were left intact by the Government either because they are insignificant in economic value or they did not operate in the crucial sectors of the economy; small business and peasant are in the same category which refers to self-employed private ownership.

\(^{58}\) Private ownerships were either incorporated into State ownership or collective ownership, and peasants were organized into collective ownership.

\(^{59}\) Liu, supra note 56, at 426.

\(^{60}\) In 1964, Liu argued that China should have a flexible labour system, allowing the existence of contractual workers. He argued that the then labour system which allowed the state-owned and collective-owned enterprises to employ only permanent workers was irrational, and that the State should allow enterprises to employ contractual or seasonal workers. Thus, labour flow could be adjusted by the demands of the society. "Establishing a Labour System in Which Permanent and Contractual Workers Coexist" Selected Works of Liu Shaoqi (Liu Shaoqi Wen Quan) vol.2 (Beijing, People's Publishing House, 1985, in Chinese) 470.

\(^{61}\) The term "Trust" here is not a legal concept. Rather it was understood by Chinese as an advanced form of monopoly consisting of many enterprises which either provide similar products or have a close association. The concept was probably borrowed from the then Soviet law and was intended to be used as an operational form of the socialist enterprises. Liu supported the idea of Trust despite the fact that the concept was allegedly developed in Western capitalist countries. "Experiment of Trust" in Liu, id, at 473.
dissidents by accusing his opponents of being revisionists who intended to turn China into a capitalist country.

Deng and Liu shared the same limitation on their economic policies. As early as 1949, Liu had argued that in China economic development should be directed to prevent two tendencies: towards capitalism and towards adventurism. The tendency toward capitalism "means regarding our economic development policy as one aimed at promoting an ordinary capitalist economy, pinning all hopes on the growth of the private capitalist sector, making unprincipled concessions to capitalists, yielding to the weakness of the petty bourgeoisie republic". The tendency toward adventurism "means going beyond realistic limits in drawing up economic plan and measures by trying to bring in too many socialist measures too early and without preparation". Liu described the efforts to prevent these two tendencies as a "struggle on two fronts". Like Liu, Deng is also struggling on two fronts, which are to carry on the economic reform and to resist Western ideology. To carry on economic reform, Deng must confront on one hand the faction of Mao-styled old guards who turn a blind eye to the backwardness of China's economy; and on the other front, the real reformers whose demands are affected by "Western ideologies", such as democracy, free speech and human rights. For this reason, he suppressed the real reformers, who recognize the need to carry on a political reform for the purposes of ensuring economic reform. Whilst intending to create an "economic miracle" to save the Party from being drowned in the poverty it has created, Deng attempts to maintain the old political structure and traditional moral or political values of the Party, which have been the bases of his political power. Ossified ideology and personal ambition motivated by this ideology are perhaps the common limitation on both Liu and Deng, although Liu's views were also restricted by the historical circumstances, whereas Mao would mercilessly crush any of his political rivals by accusing them of political impurity.

62 Liu, id, at 428.
63 Ibid.
64 Ibid.
65 Ibid.
66 Deng has repeated numerous times the importance of improving economic situation in China since 1978. For example, see Deng, "Reform is the Only Way for China to Develop Its Productive Forces" in supra note 54, at 120.
67 For example, Deng "The Party's Urgent Tasks on the Organizational and Ideological Fronts" id, at 24.
The New Economic Policies inaugurated in 1978 must now be seen and understood in the light of events in June 1989. The suppression of student demonstration in June 1989 marked a major setback in the New Economic Policies. The dismissal of the former premier Zhao Ziyang indicated the change in the balance of power between the reformers, whose priority is to develop China's economy, and the conservatives whose priority is to maintain the Party's rule (and their privileges). At present, it appears that China still formally adheres to its open-door policy, but has expressly closed the door to Western ideologies and philosophy, which have resulted in (or perhaps resulted from) the economic success of Western countries. This approach to economic development, if it is to be carried out literally, will render unlikely the predicted goals of modernization in China. The inevitable failure of the approach originates from two self-contradictory propositions. The first is the attempted effort to marry two incompatible partners: state and collective ownership of property, which dominate the Chinese economy, and the enthusiasm or the sense of responsibility of workers motivated by personal interests in the ownership of property rather than by political education. The second is the assumed compatibility between the inefficient Chinese economic structure which is characterized by impractical planning and corruption, and productive Western economic models which are built on the bases of free market economy and democratic government. Without the basis of a democratically managed free market economy, it is impossible for China to absorb fully advanced technology and managerial skills of the industrialized countries, nor could China be able to compete successfully with industrialized countries in the international market which cannot be regulated by China. A totally central-controlled economy has few advantages in pursuing economic success in today's international market which is based on the notion of laissez-faire economy. But to change the present Chinese economic structure means also political reform, because necessary measures, such as the "autonomy" of State-owned enterprises, independence of management from the Party's interference, market pricing, and the existence of private enterprises, which are crucial to create an environment where high productivity can be obtained, inevitably result in the loss of the Party's dictatorship and the demolition of the moral and political values which support the existence of the present Chinese totalitarian society. Deng does not want this to happen, nor do most of the leading figures in power. Deng does not ignore the

68 This was in fact noted by Professor Tay in 1986. She observed that "Deng has made it clear that the reforms do not mean that China is abandoning the socialist road. The primacy of the Party and the dictatorship of the proletariat, the correctness of Marxism-Leninism-Mao Zedong Thought and the centrality and overwhelming importance of the State and collective economy based on public ownership of the means of production remain". A.Tay, Law in China: Imperial,
colour of cats any more. Rather he wants any cat that catches rats to be turned into
the same colour no matter whether the rule of nature allows it or not, and regardless
of whether the cat can still catch rats afterwards. The refusal of political change by
the old guard in China will certainly hinder the development of economic reform.
But the impact of the anti-democracy mentality reflected in the now deferred
economic reform is rather complicated. Many factors such as economic necessity for
survival may force the conservatives in China to make concessions in their attempt to
preserve the purity of their distorted Marxism-Chinese communism, a mixture of
totalitarian mentality and personal ambition to power under the justification of mass
interests or revolutionary violence. Given these factors, although it is unrealistic to
predict an end to China's economic reform which was initiated in 1978, the reform is
doomed to fail in its present form of anti-democracy sentiment, adopted after June
1989.

The events in June 1989 have damaged the foreign investment climate in
China, but have not destroyed it. Investing in China today may still be worthwhile.
Apart from political factors, many other elements such as administrative efficiency
and economic structure affect the climate for foreign investment as well. Thus the
political changes in the New Economic Policies alone do not necessarily bear
detrimental consequences for the profitability of a foreign investment project in
China, at least for the time being. The ramifications of the political changes in the
open-door policy largely remain to be seen. Although in the long-term the interests
of foreign investors depend on the success of the New Economic Policies, the current
profitability of an investment project depends very much on the temporary policy of
the Chinese Government, which has been courting foreign investment since June
1989. In addition, the rejection of Western political ideas by the Chinese
Government does not directly affect the operation of foreign-related enterprises
which are regulated, and even protected, by many written laws.

1.7.2. Contents of the New Economic Policies

The New Economic Policies do not have a fixed or simple content. In fact,
the term refers to a series of economic policies of an experimental nature adopted
since 1978, and purporting to aim at increased economic efficiency and improved
productivity. The original idea of economic reform was proposed by the State
Economic Committee in 1979.69 Broadly, the proposed reform included seven goals:

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69 "Preliminary Opinions on the General Plan of the Reform on the Economic
Management System" in the State Economic Reform Committee, ed. Collected
Documents on the Plan of Chinese Economic Reform (1979-87) (Zhong Guo Jin Ji

Republican, Communist (Sydney, Centre for Asian Studies of Sydney University,
1986) 29.
expanding the managerial and operational autonomy of enterprises; establishing specialised companies or syndicates;\(^{70}\) reinforcing the functions of banks as financial providers or facilitators; redefining the powers and functions of central and local governments in the administration of the economy; redefining the relationships between planned economic and market economy; implementing democratic management in enterprises;\(^71\) and reinforcing the roles of policy, legislation and administrative supervision on economic matters.\(^{72}\) These goals were modified in the development of the New Economic Policies.\(^{73}\) In practice, some of these proposals were implemented, and some were not. The measures of reform which have been actually carried out in China can be divided into 8 categories. These concern the following areas of economic reform: development of collective, private and other forms of ownership of property; adoption of various forms of management based on

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\(^{70}\) Under the conventional model of economic management in the PRC, factories or working units are restricted by geographical and administrative (departmental) systems. The aim of this policy is to break the irrational structure of management.

\(^{71}\) One of the implications of this policy which has special interest to foreign investors is the "restructuring of management practices to accommodate the objective laws of economics". This means to accept managerial methods and skills of Western enterprises. P.R.Brown, "China's New Joint Venture Law: Analysis and Economic Overview" (1981) 4:1 Boston College Int'l & Comp.L.Rev. 115, 118-9.

\(^{72}\) State Economic Reform Committee, supra note 69, at 9-17.

\(^{73}\) For example, in 1982, the Committee suggested the following objectives: increasing the roles of various economic elements (ownership of property); establishing managerial systems based on economic responsibilities (in contrast with a distributing system of disincentive nature); rationalizing relationships between enterprises; relaxing central control; increasing the function of market economy; introducing flexible wage system (as against the "iron-bowl" system); reinforcing the roles of legislation, judicial and administrative supervision on economic matters; rationalizing the cooperation between the central and local governments; changing the managerial system in State-owned enterprises; and establishing effective system of economic administration. "General Plan on Economic Reform" id, at 62-8. In 1987, the Committee raised five topics as the goals of the reform. These include: to reinforce the reform in relation to the management of State-owned enterprises, such as separation of ownership of property (enterprises) and the rights to use or manage property (enterprises), managerial responsibilities in state-owned enterprises, the distributing system affecting the relation between the State and some enterprises, and the distributing system within state-owned enterprises; to develop market economy in agricultural and industrial markets, in raw material market and in foreign trade system; to develop financial market; to control economy through macroeconomic techniques, such as the central bank, taxation, and control over investment on fixed assets; and to carry on new experiments in the areas of financial system, administrative system, operational form of state-owned enterprises and house distribution system. "Summary of the Measures on Economic Reform in 1987" id, at 186-196.
contractual relations; increase of enterprise autonomy; rationalization of enterprises and companies; recognition of the market economy and acceptance of market prices; separation of responsibilities between the Party and management; development of legislation relating to economic matters; and administrative supervision on economic matters.\textsuperscript{74}

An open door to foreign investment is part of the New Economic Policies. In fact it is the essential part. Inflow of foreign capital provides funding needed urgently for China's economic development; reforms in foreign trade provide opportunities to expand China's export capacity; the adoption of foreign managerial skills provides assistance to economic reform in China's domestic enterprises; the acceptance of foreign techniques helps China to improve its productivity, which is the ultimate goal of the New Economic Policies; and last but not least, foreign legal knowledge has been considered extensively in China's push for "law and order", which has resulted in voluminous Acts and regulations. As will be seen, many measures of reform, such as defining responsibility by contracts, market-oriented pricing, encouraging private ownership of property and providing necessary legal and administrative guarantees (in contrast to the abuse of inaccessible Party or Government internal rules) to the enforcement of economic reform are based on experience and knowledge developed in foreign countries, in particular Western countries.

Open door policies in the context of foreign investment consist of several basic measures: allowing foreign investment to operate in the form of joint or solely foreign-owned enterprises and foreign representative offices; applying relatively flexible rules of exchange control to foreign investors; giving extensive tax concessions to foreign investors in the SEZs; developing law and regulations on the protection of foreign investment such as patent law, trademark law and contract law; and concluding double tax treaties and bilateral investment protection treaties which ensure both the effect of tax incentives given to foreign investors and the interests of foreigners in China. These measures had achieved considerable success, at least before 4 June 1989.\textsuperscript{75} Literally, the open door policies are still the same after 4


\textsuperscript{75} The impact of the events in June 1989 on Chinese foreign trade can be seen in the statistics provided by Chinese sources. During 1987-88, China's exports increased by 15.5%, imports by 17.7% and total by 16.6% compared with the previous year. 32:2 Beijing Rev. 6-12 March 1989, at 16. By contrast, during 1988-89, the exports increased only by 10.5%, imports by 7% and total by 8.6% compared with the previous year. In addition, tourism suffered 22.7% decrease compared with 1988. 33:9 Beijing Rev. 26 Feb.-4 March 1990, at VI.
June 1989. But the political instability and the prospect of remaining the only major communist country in this rapidly changing world have weakened substantially the suitability of China as a place for investment. It is unclear how China can adhere to an open-door policy while rejecting the ideas, philosophy and legal principles which are seen by many Chinese, especially the young and educated, as not only the basis for an investment climate attractive to foreign investment, but also a vital element for the success of modernization. In passing laws which were not passed thirty years ago, and addressing rights of foreign investors in its Civil Code and courts, China is precisely doing what the Soviet Union was doing in the Lenin era, when the Soviet Union eagerly promised guarantees and safeguards for the legal rights of foreign investors and provided a legal infrastructure necessary for foreign investment. Past experience suggests that without reliable guarantees of legal rights and a necessary infrastructure, foreign investment could not be effectively enticed to China. Today still, without a good investment climate, there is no reason why foreign investors have to invest in China, given that the newly opened Eastern European market is a rather attractive place for profitable ventures. Therefore, if China really pursues its economic development as a priority, it simply cannot afford to impose a strict ideological ban on foreign-related enterprises and investment activities.
Chapter 2 Administration of Foreign Investment in Australia

2.1. An Overview

Australia has traditionally been a capital-importing country. Precise statistics of the inflow of foreign capital before 1948 are not available, but foreign capital inflow, in particular from the United Kingdom, was then a main source of capital supply for the development of the Australian economy. The volume of foreign investment in Australia has rapidly increased since the Second World War. The post-War boom has been characterized by the increase of investment from the United States, Japan, New Zealand and other countries. This has gradually undermined the domination of British capital in Australia's overseas borrowing. Although Japan has recently been the largest investor (e.g. during 1988-89, Japanese investment reached $9.1 billion, followed by the United States ($3.7 billion) and the United Kingdom ($3.6 billion)), the United Kingdom is still the largest investor in terms of aggregated investment.

In general, overseas capital has flowed into Australia in three forms: direct investment, portfolio investment and loan money. All these forms directly or indirectly fall within the constitutional power of the federal Government. But the federal Government adopted largely an open-door policy, and did not introduce restriction on any form of investment until end of the 1930s when the Second World War broke out. The first measure of control which affected foreign investment to a considerable extent was the restriction on transactions involving portfolio investment and loan money introduced in the Defence ( Monetary Control) Regulations 1939 (Cth). But the federal Government did not impose any substantial limitation on

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1 R. Withers, "The Role of Foreign Investment in the Development of the Australian Economy - Some Factors to be Considered" 1 A.B.L.Rev. (1973) 5, 7.

2 Withers, id., at 5-7; and N.G. Butlin, Investment in Australian Economic Development 1861-1900 (Cambridge, Cambridge University Press, 1964) 25-31. In the latter book, Table 7 at page 29 lists data on overseas borrowing between 1861 and 1890. During most of that period, overseas borrowing reached a considerable amount compared with the gross domestic capital formation of the same year.

3 For example, between 1947-48, the foreign investment in Australia totalled $77 million. But in the year between 1970-71, the total amount of foreign investment in Australia reached $1,493 million. See the federal Treasury, Treasury Economic Paper no.1, Overseas Investment in Australia (Canberra, AGPS, 1972) 5.


5 During 1988-89, UK investment in aggregation reached $44 billion, US investment was $39.2 billion and Japanese investment was valued at $26.5 billion. Id, at 27.

6 Withers, supra note 1, at 9.
direct foreign investment until 1975 when the Foreign Takeover Act was passed, although it passed the Australian Industries Preservation Act in 1906 which dealt with some aspects of restrictive trade practices that inevitably involve foreign corporations in Australia.7

When rules relating to foreign companies in Australia were absent in federal legislation, they could be found in the company laws of each State and Territory. State company laws could be relevant to direct foreign investment in the sense that they could have dealt with various aspects of foreign investment, such as the establishment of foreign-owned companies, the transfer of company shares from local shareholders to foreign shareholders, or the operation of foreign companies in a State. But, based, as they were, on earlier British laws, the laws regulating companies and partnerships adopted by each State at that time neither noted the issues of establishment of foreign-owned companies and foreign takeovers in local companies, nor laid down any substantial limitation on the operation of foreign companies.8

Thus, in the company laws of the Australian States (or colonies before the federation), foreign investors were given the same treatment as local investors as far as the capacity to form a company or to subscribe to shares in local companies was concerned.9 The issue whether there should be some restrictions on the capacity of foreign investors to pursue business in the States was largely ignored. Two reasons may be suggested for this. First, the Australian colonies occupied a new continent and most people, in particular the law-makers, were immigrants from the United Kingdom. The respective identities of local investors and foreign investors were hard to distinguish. Secondly, the laws in the Australian colonies were strongly

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7 Section 5 of the Act was intended to prohibit foreign corporations and trading or financial corporations formed within the Commonwealth from engaging in unfair competition, and section 8 was intended to prohibit these corporations from monopolizing any part of the trade or commerce within Australia to the detriment of the public. But several key sections of the Act were held to be invalid by the High Court in Huddart, Parker & C. Pty Ltd v Moorehead, (1908) 8 CLR 330. This decision was later overruled in Concrete Pipes Ltd Case, (1971) 124 CLR 468, but the AlP A never operated as such.

8 For various statutes of States and Territories relating to companies, partnerships, and voluntary associations before the 1930s, see R.Baxt, Second Australian Supplement to the Third Edition of Gower’s Modern Company Law (Sydney, Law Book Company, 1974) 15-56.

9 P.Spender & G.Wallace, Company Law and Practice (Australia, the Law Book Co of Australian Ltd, 1937) 15-6; and C.M.Collins, Australian Company Law (Australia, the Law Book Co of Australia Ltd, 1940) 51.
influenced by British law, which allowed foreign investors to form companies or to subscribe to shares of local companies without any restriction.10

The State company laws also set forth rules regarding the recognition of foreign companies,11 and they usually defined a foreign company as a company incorporated outside the State.12 Although the rules on the registration of foreign companies varied between the States,13 they were more or less confined to matters of form. Again, British practice adopted since the beginning of the eighteenth century,14 which based the recognition of foreign companies and their capacities to carry on business in England on the ground of international comity,15 was followed by the courts in the Australian States.16 Some States even waived the requirement for the registration of a foreign company which only invested funds or other property in the State.17 In these States the mere investment of funds or other property were not regarded as carrying on business in the States, and therefore registration was not required. Thus portfolio investment as such made by foreign individuals or foreign companies was not regulated by the laws of these States.

Though foreign companies were normally treated in the same way as local companies, certain foreign companies were not granted the same right to hold land in some States. This might be regarded as a restriction on foreign investment. For example, before 1911 no foreign companies were allowed to hold land in


11 Although the High Court supported the federal power to set out conditions on the recognition of foreign corporations, federal Government had not passed any law in relation to the recognition of foreign corporations until 1989, when it passed a federal Corporations Act. Some crucial provisions of the Act, however, are held to be invalid by the High Court in 1990. NSW v Commonwealth (1990) 8 ACLC 120.

12 J.Barton, The Australian Company Secretary (Sydney, Sydney and Melbourne Publishing Company Ltd, 1911) 396; and Collins, supra note 9, at 171.

13 Barton, id, at 398-409; and Collins, id, at 171-5.


15 Id, at 64-5 & 69.

16 For example, see United Service Insurance Co. Ltd. (in Liq.) v. Lang (1935) 35 SR(NSW) 487 & 491; and Spender, supra note 9, at 86-7.

17 For example, see s.264(14) of the Companies Act 1920 of Tasmania, and s.357 (1) of the Companies Act 1934-35 of South Australia.
Queensland. Even after 1911, certain types of foreign companies were still restricted from doing so in Victoria, South Australia, and Tasmania where foreign companies were classified as either British and British-related companies, or as non-British companies, and only British or British-related companies were allowed to hold land. This restriction was abolished gradually after the 1930s, and by the time the Uniform Companies Act 1961-62 was proposed, foreign companies were allowed to own land throughout Australia.

The earliest attempt of federal Government to control foreign takeovers was reflected in the Australian Industries Preservation Act 1906 (Cth). Chronologically, another attempt on exercising federal legislative power in relation to corporate affairs, which might affect foreign takeovers, was the National Security (Capital Issue) Regulations 1939 (Cth). These Regulations gave the federal Treasurer power to control the formation of new companies, increases in the capital of existing companies, and the issue or transfer of securities, mortgages, or assets of companies. As a matter of fact, under these Regulations the federal Government exceeded the limitation of s.51(xx) as construed by the High Court in 1908, whose narrow interpretation of s.51(XX) was still effective in 1939. Probably due to the special circumstances of war in which the defence power under s.51(vi) and incidental power under s.51(xxxxix) of the Constitution were resorted to, these Regulations were never challenged. Though these Regulations were applicable to both local and foreign companies, given the circumstances and the function of the Regulations as wartime measures, they were likely to impose greater restrictions on foreign companies than on local companies. These Regulations were repealed soon after the end of the War.

One of the purposes of controlling foreign investment today is to promote local participation in Australian companies. But the differences between foreign ownership and local ownership in Australia did not attract much public attention in this country until the 1950s, when concern began to be expressed over the profits earned by foreign corporations. Since then greater control over foreign

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18 Barton, supra note 12, at 401.
19 Collins, supra note 9, at 174.
20 Baxt, supra note 8, at 402.
21 For example, regs.3, 4, 5 & 6.
22 See G.McColl, ed. Overseas Trade and Investment (Penguin Book, 1972) 151. This issue was also debated in the federal Parliament. For example, in 1958 the Government was criticized for inviting the U.S. investment to Australia, where the U.S. firms earned higher interest than in the United States, and thereby the US firms
investment, in particular on foreign takeovers, was gradually introduced by a series of policy statements of the Government, known as the "Guidelines". These Guidelines were initially issued to encourage foreign investment, such as the Government Policy Statement announced in 1958. The basic spirit of this Statement was to encourage the inflow of foreign investment into Australia. Emphasis was given to investment projects which were likely to help in the balanced development of Australian resources and bring skills and "know-how" into Australia. General control over foreign takeovers in the Guidelines was not introduced until 1968, when a new paragraph concerning local participation in foreign investment projects was inserted in the Government Policy Statement.23 The 1968 Guidelines suggested a new position in favour of general control over foreign investment in Australia.

Attempting again to regulate foreign corporations, and trading or financial corporations formed within the Commonwealth, the federal Government passed the Trade Practices Act (TPA) in 1965. In 1971, the Act was challenged in the High Court. This time the High Court allowed a broader construction of s.51 (xx). Although the majority of the Court in the Roela Concrete Pipes Ltd. Case held that the sections in question were invalid mainly because s.7 of the Act did not clearly define the operation of these sections,24 the Court unanimously agreed that s.51(xx) should be construed in a manner much broader than the interpretation in Huddart Parker Case, and that the Commonwealth Parliament has power to regulate the activities of foreign corporations and trading or financial corporations formed within the Commonwealth.25 The power to regulate foreign investment, such as takeovers involving foreign corporations and trading or financial corporations formed within the Commonwealth, was thus "returned" to the federal Parliament. But the High Court did not give a full and clear interpretation of s.51(xx). In a sense, the disagreement and "resultant confusion" are inevitable, because under common law tradition judges are expected to construe law only when a need for doing so has arisen. Thus potential depth of any law will probably remain unexplored until an issue has been raised. This standard practice was also adopted in Tasmanian Dam

had been accused of taking "from Australia the enormous profits that should remain in this country". Hansard, Representatives 5th Aug to 28 Aug 1958, at 396-7.

23 Commonwealth of Australia, Overseas Investment in Australia (Canberra, AGPS, 1968) 1, hereinafter referred to as the 1968 Guidelines.

24 Roela Concrete Pipes Ltd. Case (1971) 124 CLR 468, per Barwick CJ. at 495-9, Menzies J. at 501, Windeyer J. at 513, and Owen J. at 513.

25 Id. at 489, 491, 499, 510, 511-3, 515 and 513.
where the High Court, although it dealt with s 51(xx), did not attempt to provide a clear and full interpretation of s 51(xx). While some judges attempted expressly or impliedly to give a wide interpretation of s 51(xx), the others only discussed some sections of the World Heritage Properties Conservation Act 1983 (Cth) as relevant to s 51(xx). The Court's practice has suggested that it indeed preferred to construe the corporation power on a case by case basis.

The decision of the High Court in the *Rocla Concrete Pipes Ltd Case* encouraged the development of Australian foreign investment law. In 1972 the Companies (Foreign Take-Overs) Act (Cth) was passed, a special authority for controlling foreign investment was proposed, and a Variable Deposit Requirement (VDR) scheme for controlling foreign borrowing was introduced by the government policy statement. A special authority - the Committee on Foreign Takeovers - was set up in 1972, which was followed by the establishment of another relevant authority - the Foreign Investment Committee - in 1974. Both these Committees were incorporated into the Foreign Investment Advisory Committee in 1975, which was subsequently replaced by the Foreign Investment Review Board (FIRB) in 1976. Since then, the FIRB has been the special authority in charge of reviewing foreign investment proposals involving either foreign takeovers or establishment of new businesses controlled by foreign investors.

Today the federal Parliament has extensive power to regulate various aspects of foreign investment within the Commonwealth. Its power under s.51(xx) to regulate foreign corporations, and financial and trading corporations formed within the Commonwealth is reinforced by several other heads of federal legislative power, in particular s.51(i), (v), (xxix) and (xxxix). These sections together directly or indirectly vest the federal Government with more or less complete authority over foreign investment matters. But the exercise of this power has been subject to

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26 (1983) 158 CLR 1

27 For example, Mason J commented that "my earlier conclusion that the legislative power is not confined to the trading activities of trading corporations is in a sense an answer to this submission. The other answer is that s.51(xx) designates as the subject of the power the corporate persona itself, e.g. the artificial person created by incorporation". (1983) 158 CLR 1, 157. Murphy J commented that the "corporations power is plenary. It must be read with all the generality which the words of s.51(xx) admit". (1983) 158 CLR 1, 179. The clearest interpretation of s 51(xx) was given by Deane J who observed that "the legislative power conferred by s.51(xx) is not restricted to laws with respect to trading corporations in relation to their trading activities. It is a general power to make laws with respect to trading corporations". (1983) 158 CLR 1, 270.

28 For example, Menzies J. stated that "I am not prepared to attempt to define the limits of the power conferred by s.51(xx)." See *Rocla Concrete Pipes Ltd. Case* (1971) 124 CLR 468, 511.
constant contest between the federal and State governments. The federal Acts
The federal powers to regulate foreign takeovers and restrictive trade practices
involving either foreign or local investors are supported by the High Court, but
the federal power to regulate the formation of trading or financial corporations
which may attract foreign investment is denied by the High Court, in particular
in the 1991 Corporations Case.

suggest that the overlapping of power in the regulation of foreign investment in
Australia will not be immediately resolved by the passing of a federal Corporations
Act.

In fact, the administration of foreign investment involves many areas which
have been traditionally regulated by State governments. The division of power in
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is one of the issues to be discussed in this chapter. The other is the separation of
power between the legislature and executive, in particular the exercise of federal
executive power in the administration of foreign investment. Since the federal
Foreign Investment Guidelines, the basic document dealing with foreign investment
in Australia, exist in the form of government policies, the ambit and effect of
executive power need clarification. These issues will be discussed in detail below:
first in the setting of the federal division of power, and secondly in the context of
the separation of powers within the Australian model of responsible government.

2.2. Administrative Mechanisms for Foreign Investment Control in Australia
2.2.1. An Overview of the Federal Mechanisms

The administrative mechanisms of the federal Government consist of the
federal Treasury and Foreign Investment Review Board, and, to a limited extent,
other government Departments and statutory bodies. Departments of the federal
Government, such as the Department of Transport and Communication and the
Ministry for Mining, have statutory power which may apply to foreign investment
within specified areas. Statutory bodies, such as the Australian Broadcasting
Tribunal (ABT) and the Trade Practices Commission (TPC) which administer a

29 NSW v Commonwealth, (1990) 8 ACLC 120.

30 Dept. of the Treasury, Australia's Foreign Investment Policy: A Guide for
Investors (Canberra, AGPS, 1989); hereinafter referred to as Guidelines.

31 The Ministry for Transport and Communication has power under Air Navigation
Act 1920 (Cth) to prevent entry into airline operations by foreign corporations. The
restriction will possibly be relaxed, given that the Government deregulated airline
industry in October 1990. The Ministry for Mining has power to issue export licence
under the Customs (Prohibited Exports) Regulations 1958 (Cth), and can thereby
control exports of the specified minerals in Australia.
constant contest between the federal and State governments. The federal Acts governing foreign takeovers and restrictive trade practices have been supported by the High Court, but several crucial sections of federal Corporations Act in relation to federal power to regulate the formation of trading or financial corporations which may be invested by foreigners have been denied by the High Court. This seems to suggest that the overlapping of power in the regulation of foreign investment in Australia will not be immediately resolved by the passing of a federal Corporations Act.

In fact, the administration of foreign investment involves many areas which have been traditionally regulated by State governments. The division of power in relation to control of foreign investment between the federal and State governments is one of the issues to be discussed in this chapter. The other is the separation of power between the legislature and executive, in particular the exercise of federal executive power in the administration of foreign investment. Since the federal Foreign Investment Guidelines, the basic document dealing with foreign investment in Australia, exist in the form of government policies, the ambit and effect of executive power need clarification. These issues will be discussed in detail below: first in the setting of the federal division of power, and secondly in the context of the separation of powers within the Australian model of responsible government.

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particular business sector or a specified operation, may interfere with takeovers or transactions involving foreign investment in these sectors.

For the purposes of controlling foreign investment, the mechanisms have two basic functions—the examination of foreign investment proposals and supervision of the operation of foreign-related businesses. The power to examine investment proposals arising from Foreign Acquisition and Takeover Act 1975 (Cth) (FATA)\textsuperscript{32} is exercised by the Treasurer with the assistance of the Foreign Investment Review Bureau (FIRB). Occasionally, the Treasurer may consult other responsible Departments as required.\textsuperscript{33} The supervisory power is exercised by the Treasurer (also with the assistance of FIRB) and by special statutory bodies and Departments, such as the ABT and the Ministry for Transport and Communication which may also examine investment proposals falling within their statutory powers.\textsuperscript{34}

The federal Treasury republishes Australia's Foreign Investment Policy - A Guide for Foreign Investors (the Guidelines) from time to time, whenever substantial changes have been made to the Guidelines. Its power to administer foreign investment, like ordinary executive power, derives from federal statutes, delegated legislation, and when there is no directly relevant legislation, from the executive power under s.61 of the Constitution, embodying, among other things, the prerogative or common law powers of the Crown conferred on the Governor-General.\textsuperscript{35}

2.2.2. Statutory Power of the Treasurer

The "statutory power" here is used to refer to executive power conferred by an Act of Parliament or by regulation made pursuant to Parliamentary authorization. The principal legislation concerning foreign investment in Australia is the FATA and the Banking (Foreign Exchange) Regulations 1946 (Cth). A number of other Acts, such as the Broadcasting and Television Act 1942 (Cth) (introducing control in the broadcasting and television sector, and over ownership of newspapers associated with

\textsuperscript{32} Foreign Takeovers Act 1975 (Cth) was amended by Foreign Takeovers Amendment Act 1989 (Cth) (No.14, 1989), and Foreign Takeovers Act 1975 was then renamed Foreign Acquisition and Takeovers Act 1975.

\textsuperscript{33} For example, it was reported that the FIRB on behalf of the Treasurer referred a redevelopment plan in Paddy's Market, Sydney, proposed by the Howin Group and Foa Group of Singapore to the Australian Heritage Commission, which suggested the FIRB call for more information. Aus.Fin.Rev. 4 May 1990.

\textsuperscript{34} e.g. under the Broadcasting Act 1942 (Cth) and Air Navigation Act 1920 (Cth).

television and radio licensees),\textsuperscript{36} the Customs (Prohibited Exports) Regulations 1958 (Cth) (affecting control in the mining sector), and the Air Navigation Act 1920 (Cth) (affecting control in civil navigation) also vest power to control foreign investment in the Government. These powers are often not directly vested in the Treasurer, but the Treasurer may issue policy statements based on these powers over foreign investment on behalf of other Departments (or on behalf of the Government as a whole). In addition, statutes on environmental protection,\textsuperscript{37} continental shelf management, taxation, dispute resolution, and treatment of aliens may also reinforce and supplement the government's power in particular cases.

Of the relevant legislation, FATA is the principal Act. It gives the Treasurer power to approve, with or without conditions, or to reject, foreign investment proposals for takeovers. Under the Act, not only the change of control from local to foreign owners,\textsuperscript{38} but also between foreign interests, as a result of acquisition in a corporation,\textsuperscript{39} are subject to the Treasurer's approval. In addition, any arrangement concerning a corporation's constitution, directors or any change which may result or has resulted in controlling power being transferred from local interests to foreign interests or between different foreign interests, is also subject to the Treasurer's discretion.\textsuperscript{40} Where foreigners have acquired shares or assets, or power of control over an Australian corporation, the Treasurer may direct the persons concerned to dispose of the shares and assets, or to modify the agreement or

\textsuperscript{36} Broadcasting (Ownership and Control) Act 1987 (Cth), No.68 of 1987, amended Broadcasting and Television Act 1942 (Cth). The Tribunal was authorized to establish an Associated Newspaper Register in charge of the registration of any newspaper which has 50% or more circulation within a service area of a television or radio licence. (Section 91AAE of the amended Broadcasting Act 1942.) Cross media interests such as a prescribed interest in a newspaper by a television and radio licensee are restricted. (See Broadcasting (Ownership and Control) Act, No.56, 1988, ss.92IB & 92ZL) The Act only gives the federal Government authority to control the ownership of the newspapers which are associated with a holder of a television or radio licence.

\textsuperscript{37} The Commonwealth does not have specific environmental power. But as pointed out by Prof. Crawford, this situation, 'in no way prevents the Commonwealth from legislating with respect to those matters, provided the law is also, in a formal sense, a law "with respect to" one of the granted heads of power'. Thus, the federal Government may regulate environmental matters under various heads of powers, such as s.122 (legislation with respect to Territories), ss.51(ii) and 96 (financial power), s.51(xxix) (external power) and s.51(xx) (corporations power). J.Crawford, "The Constitution and the Environment" paper unpublished as at December 1990.

\textsuperscript{38} FATA, ss.18(2)(b)(i) & 19(2)(b)(i).

\textsuperscript{39} Id, ss.18(2)(b)(ii) & 19(2)(b)(ii).

\textsuperscript{40} Id, ss.20 & 21.
arrangement, for the purpose of restoring control to a state similar to that before the relevant takeover was carried out.

FATA provides three tests which must be considered by the Treasurer in exercising his powers. Two of them have been mentioned in the previous paragraph. The third is the "national interest" test, under which the Treasurer may exercise the power of control if he is satisfied that the result of an acquisition or arrangement is contrary to the "national interest". However, the test is too broad to assure any specific standard.

"National interest" is adopted as a supplementary criterion for the Treasurer in judging the effect of foreign takeovers which do not fall within other descriptions in FATA. No definition of "national interest" is given in the Act. Nor has any judicial interpretation of the term been given. Nevertheless, as suggested by the Government in its explanatory notes on the FTA Bill 1986, and, in its practice of examining foreign investment proposals, "national interest" is indeed a very flexible and broad concept.

"National interest" is flexible, because there is no certain or specified test for determining whether a particular project is consistent with or against the "national interest". An investment project which increases productivity and creates employment may endanger the environment to some extent, thus resulting in conflict between interest groups, e.g. the timber industry and conservationists. Often arguments for both sides may be relevant to the "national interest". In the context of foreign investment, "national interest" is often affected by political considerations and

41 These are the change of control and change of ownership tests.

42 Sections 18, 19, 20 & 21.

43 Although no express explanation about the "national interest" has been provided by the Parliament and Treasurer, the Foreign Takeover Bill 1975: Explanatory Memorandum implied that the test was adopted for the sake of flexibility and practicability. (The Bill is reprinted in Hamilton, ed, Foreign Investment Law and Regulations in Australia (Sydney, Longman, loose leaf service) 47.) Because of the complexity and variety of foreign investment, a flexible test is needed to implement government policies. Probably, the ambiguity of the test has been worded deliberately in order to give the Treasurer a wide discretion in interpreting and applying this test.

44 Hamilton, ibid.

45 For example, in March 1989, the federal Government disapproved a proposal made by Japanese Nara Construction Co Ltd to participate in a redevelopment project in Woolloomooloo Bay, Sydney. The refusal was based on the arguments of "national interest" and environmental protection. But the Treasurer did not explain why the project was against "national interest". See "Japanese sniff the reek of egoism in Keating's ban on Nara Group" Aus.Fin.Rev. 16 March 1989.
ideologies. The debate on the "Multi Function Polis" in the federal election in March 1990 may be an example.46

The concept of the "national interest" is broad, because it can bring practically any factor relevant to foreign investment into consideration. Matters such as "competition, productive capacity, technological change, development of new markets, production, quality and range of products and services, level of prices and efficiency which would be sufficient to justify the change in foreign control of the business concerned" may be regarded as criteria for the "national interest".47 Foreign takeovers resulting in monopoly, high prices and loss of productivity are thus against the "national interest". By contrast, foreign takeovers resulting in foreign control but increasing productivity, developing new markets or enhancing technological levels may be seen as consistent with the "national interest". The broadness of the concept of "national interest" also extends to matters such as the impact of a takeover on exports, imports, industrial relations, defense policy, environmental policy, and regional development policy.48 In addition, Australian participation, or the interests of Australian employees, shareholders and creditors of the target business are also taken into account in determining whether a takeover is consistent with the "national interest".49 The broadness of the concept of "national interest" is suggested not only by the variety of the criteria which can fall within this concept, but also by the uncertainty of some criteria which vary in different circumstances.50

The flexibility and broadness of "national interest" is seen in FATA, where it is used to judge any takeover carried out either within or outside Australia, or involving both Australian and foreign assets. For example, a proposal of overseas

46 Supporters of the MFP concept may argue that the project will bring highly advanced technology into Australia, increase Australia's export capacity, provide trainings for Australian scientists and advance the economic development of Australia; and thus, the idea is consistent with "national interest". On the other hand, the opponents may argue that the project will create an "enclave" in Australia, which despite the economic benefits is against its "national interest".

47 Hamilton, supra note 43, at 47. The importance of competition and diversity in banking sector to "national interest" has been illustrated by the federal Treasurer's statement on the proposed merger of ANZ and National Mutual. The text of the statement is reprinted in Aus.Fin.Rev. 24 May 1990, at 4.

48 Id., at 48.

49 Ibid.

50 For example, government policies on defence, environment and urban development may change from time to time. So are the tests of competitiveness and productivity, which vary in different sectors of economy and in different periods of time.
takeover involving Australian assets of a specified amount ($3 million before 1989 and $20 million from the enactment of the Foreign Takeovers Amendment Act 1989 (Cth)),\textsuperscript{51} is required to notify FIRB, because "on rare occasions, such transactions could result in a change in the control of a major Australian business that would be against the national interest."\textsuperscript{52} Here a $3 million threshold was seen as crucial to the "national interest" before 1989 but a $20 million threshold is seen as appropriate after 1989. The Explanatory Memorandum for the Foreign Takeovers Amendment Bill 1988 does not bring out the reason for the change. Presumably, the $20 million threshold is regarded as appropriate because foreign companies falling under the Act include those which have subsidiaries or other assets in Australia. However, the difference between the artificial thresholds can only be explained by the changes in the understanding of, or in the criteria for determining, the "national interest".

The flexible features of the "national interest" concept can be further illustrated by the application of the "national interest" test in the Treasurer's practice, which has occasionally treated the dominance of foreign interests in Australian companies as a threat to "national interest". For instance, in December 1987, the Treasurer rejected a proposal by News Ltd to acquire John Fairfax's holding of 43.4% of AAP Information Services Pty Ltd (AAPIS), which was regarded as "a major provider of news and information to the media and the financial business community in Australia".\textsuperscript{53} The possibility that the proposed acquisition "would result in News Ltd holding 86.8% of AAPIS and having a dominant position on the AAPIS board and share register"\textsuperscript{54} was considered to be dangerous to AAPIS' independence "as an impartial news gathering and distribution service".\textsuperscript{55} The "national interest", which was deemed to be endangered by News Ltd's proposed takeover of AAPIS, was the ground for the refusal. However, the mere dominance of a foreign company in an Australian business, even if it is apparently an important or unique one, is not always viewed as contrary to the "national interest". On the same occasion, News Ltd's proposal to purchase Fairfax shares in Australian Newsprint Mills Holding Ltd (ANMH), which would result in News Ltd controlling 88.4% of the equity in ANMH, was approved, although ANMH "is the sole domestic

\textsuperscript{51} Section.13 of FATA as amended, the new threshold for notification of takeovers is $20 million or a prescribed amount.

\textsuperscript{52} Hamilton, supra note 43.

\textsuperscript{53} Treasurer's Press Release, no.120, 1987.

\textsuperscript{54} Ibid.

\textsuperscript{55} Ibid.
supplier of newsprint to the Australian market". The availability of imported newsprint in the domestic market, and expected increases in Australia's export capacity, were given as reasons justifying the proposed takeover. In the latter case, another element - increase in export capacity - was used to justify the loss of Australian control in assessing the "national interest". In addition, the protection of the environment could also be an element in considering the national interest.

2.2.3. Statutory Powers of Other Departments

Another department which may directly approve or reject foreign investment proposals is the Department of Transport and Communication. Under the Air Navigation Act 1920 (Cth), the Department has power to issue airline licences. No criteria for approval or disapproval of proposals are set forth in the Act, nor by the Air Navigation Regulations 1920 (Cth). A broad discretionary power is vested in the Australian Government.

2.2.4. Functions of the Foreign Investment Review Board

The FIRB was established in 1976 to advise the federal Treasurer on foreign investment matters. A close connection exists between the Treasury and the FIRB, which is directly accountable to the Treasurer. The closeness between the two bodies is illustrated by the arrangement that the Executive Member of the FIRB's Board is the head of the Foreign Investment Division of the Treasury Department. As an advisory body to the Treasurer, the FIRB performs various functions ranging from the examining of a particular proposal to the monitoring of foreign investment matters in general.

The functions of the FIRB were enumerated by the Treasury, in its statement on Australia's Foreign Investment Policy 1987, as follows:

56 Ibid.
57 Ibid.
58 It was reported that from July 1986 to April 1987, only one proposal, involving the development of a mineral sands deposit at Shelburne Bay, Queensland, was rejected on "national interest" grounds. The impact of the proposed project to the environment, not the percentage of Australian participation in the project, was regarded as contrary to the national interest. FIRB, Annual Report 1986-7, at 25.
59 Section 199.
61 Guidelines, supra note 30, at 1.
62 Id, at 2.
- to advise the Government on foreign investment matters generally;
- to examine foreign investment proposals and to make recommendations to
  the Government on those proposals;
- to foster an awareness and understanding of the Government policy in the
  community at large and in the business sectors, both in Australia and abroad;
- to provide guidelines, where necessary, to foreign investors on those aspects
  of their proposals that may not be in conformity with Government policy and
  suggest ways by which the proposals might be amended; and
- to maintain an awareness of the activities of foreign-controlled businesses
  operating in Australia.

The existence of FIRB is based on the delegation of executive power by the
Treasurer. The functions of the FIRB are an extension of the discretionary powers
of the Treasurer (on behalf of the executive government) to control foreign
investment, derived from the Commonwealth Constitution, and Acts of the federal
Parliament.63 The FIRB, while reviewing foreign investment proposals on behalf of
the Treasurer, has no decision-making power and may only make a recommendation
to the Treasurer in favour of or against a given investment proposal. In practice,
however, its recommendation is likely to be accepted by the Treasurer,64 and the
FIRB thus in fact plays a crucial role in the process of examination.

The FIRB itself has so far attracted more criticism from economists than
lawyers. Criticism has been mostly directed against the Government's policy to
exercise control, and thus the existence of the FIRB rather than its operation in a
particular case. It has been argued that whether the Board itself or the existence of
control assists the development of national economy is doubtful, because some
potential investors have decided to invest in other countries, or have had to modify
their investment proposals. The proposals modified have, in many cases, become
counter-productive or economically inefficient and, so it is said, have resulted in the
loss of job opportunities and in the reduction of foreign capital inflow.65 In
addition, it has been argued that the criteria for the approval of the investment

63 e.g. the FATA, the Banking (Foreign Exchange) Regulations 1946 (Cth), the
Broadcasting and Television Act 1942 (Cth), the Trade Practices Act 1974 (Cth), the
Air Navigation Act 1920 (Cth), the Customs (Prohibited Export) Regulations 1958
(Cth), the Environment Protection (Impact of Proposals) Act 1974 (Cth), and the
Income Tax Assessment Act 1936 (Cth).

64 As noted by M.Sexton & A.Adamovich, The Regulation of Foreign Investment in
Australia (Sydney, CCH, 1981) 80-1.

65 A.Gunther, Foreign Investment in Australia: 1960-1981 University of Reading
Discussion Papers in International Investment and Business Studies No.71, April 1983
at 9; and W.Kasper, Capital Xenophobia: Australia's Control of Foreign Inv-
proposals applied by the FIRB are not clear-cut or well known. Thus it is possible that foreign investment has been discouraged in some cases.

2.2.5. Power of Other Statutory Bodies to Control Foreign Investment

2.2.5.1. Power of the Australian Broadcasting Tribunal

The Tribunal was established in 1977 as an independent statutory body. Its power to grant, renew, suspend, and revoke licences, to make decisions in relation to the ownership and control of licences, to direct licensees with regard to matters such as standards of programs and types of programs to be broadcasted in peak hours, and to hold public inquiries into matters within its responsibilities are granted by the Broadcasting and Television Act 1942 (Cth). Though the Tribunal has extensive power to control the ownership of media licences, the exercise of the power sometimes was disputed. The much publicized Bond Inquiry is an example. Several decisions of the Tribunal on the licences held by Bond and his associates were challenged in the Federal Court, which delivered its judgments in favour of the Bond Corporations, though the Federal Court's decision was in turn set aside by the High Court.67

The Tribunal's power to direct the ownership of the licences includes a power to control foreign ownership. If a foreign person is in a position to exercise control, either directly or indirectly, of a company holding a radio or television licence, or

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66 Gunther, id. at 10-1; Kasper, id. at 58; and "Investors need to know the rules" The Australian 10 April 1990.

67 In June 1988, Bond Media challenged the legal basis of an inquiry conducted by the Tribunal in relation to a $40,000 defamation settlement between Bond Media and the former Premier of Queensland, Sir Joh Bjelke-Peterson in the Federal Court. Morling J. decided that the inquiry was not authorized by the Act. Bond v ABT (1988) 81 ALR 195. In December 1988, Bond Corporation Holdings Ltd brought an action against ABT in relation to the Tribunal's decision not to grant an extension of time to the Corporation which was obliged to dispose of its prescribed cross-media interests prohibited by the Act. Gumow J. decided that the Tribunal had misconstrued s.92FAB(9) of the Act. Bond Corporation Holdings Ltd v ABT (1988) 84 ALR 669. The Tribunal appealed against Judge Gumow's decision to the Full Bench of the Federal Court in February 1989, but the appeal was dismissed. ABT v Bond Corporation Holdings Ltd (1989) 86 ALR 424. The Bond Corporations took another legal action against the ABT's decisions and conducts in the Full Court of the Federal Court. The Court set aside some "decisions" made by the ABT. Bond v ABT (1989) 89 ALR 185. The ABT appealed to the High Court of Australia which set aside the orders of the Full Court of the Federal Court in 1990. (1990) 94 ALR 11.
two or more foreign persons hold more than 20% of the total of the amount paid on all shares in the company carrying such voting rights, or of the total of the amount paid on all shares in the company, the Tribunal may refuse to renew the license. These limitations were considered by the Tribunal in 1987 in Licence Renewal - 6IX Perth Case, where the citizenship of Mr. Holmes a Court, the Chairman of the Bell Group which had a prescribed interest in the licences concerned, was investigated. Had Mr. Holmes a Court not been an Australian citizen, his interests in the Bell group would have been subject to the restrictions in the Broadcasting Act 1942 (Cth). However, at the end of the inquiry, the Tribunal was satisfied with the explanation in relation to the once confused status of Mr. Holmes a Court, and decided that ss 90G and 92D were inapplicable.

The ambit of government control under FATA and BTA are different. Foreign investors are allowed to operate to a much more limited extent in the broadcasting and television sector, where one foreign person must not be in a position of control, directly or indirectly, and two or more foreign persons must not hold more than 20% of voting power in a company. But foreign investors are allowed to hold a higher percentage of company shares under FATA. The difference can be explained by the Guidelines, which encourage foreign investment in the general manufacturing sectors but restrict foreign control of Australian business in sectors that are regarded as essential or key sectors of the national economy. Broadcasting and television businesses, due to their influence and the sensitivity of the ownership issue to the public, are thus treated by the Government as restricted sectors for foreign investment.

2.2.5.2. Power of the Trade Practices Commission (TPC)

68 The 20% rule has not been able to prohibit foreign companies from indirectly holding more than 20% shares (up to 49.9%) in a licensee company through their subsidiaries. The rule is expected to be tightened up by the proposed new legislation, but foreign companies may be allowed to hold more than 20% non-voting shares in a company holding a broadcasting licence. SMH, 28 May 1990, at 3.

69 Broadcasting Act, ss.90G & 92D.

70 Id, s.81(1) & (2).


72 The sensitivity of foreign ownership in television industry can be seen in the arguments for and against the proposed increase of foreign ownership limits as reported on newspapers. See "TV foreign ownership fears 'a load of garbage'" Aus.Fin.Rev. Feb.14, 1990.
The present TPC was established by the Trade Practices Act 1977 (TPA) which amended the TPA 1974. It is a statutory body, which, in the exercise of its general powers under the TPA 1977 (Cth), may exercise control over foreign investment from time to time. It can bring proceedings for contravention of the Act in restrictive trade practice cases. This includes, subject to Ministerial consent, the institution of prosecutions for offences against the consumer protection provisions of the Act. The Commission also has discretion under the Act to grant authorization on public benefit grounds to some types of "restrictive trade practices" which are otherwise prohibited. It can make decisions on various applications (including those submitted by foreign-related companies) for authorization,73 and bring actions against companies for violation of Part IV.74 Similarly, in the case of exclusive dealings, the Commission has discretion to revoke the protection given by the notification procedure. In addition, the Commission may ask for information, documents and evidence relating to activities which are deemed to involve the practices prohibited by the TPA.75 Under the Act, the Commission is not obliged to treat the existence of foreign interests as a special consideration.76 Rather, its main concerns are to encourage fair competition and trading, to protect consumer interests, and to promote economic efficiency and effective resource utilisation, all of which, however, may benefit from foreign investment and foreign investment-related activities in Australia.

Restrictive trade practices as regulated by the TPA arise from various activities, such as contracts, arrangements or understandings restricting dealings or

73 For example, International Commodities Clearing House Ltd, a corporation owned by six UK banks, applied for a further self-regulatory measure to be adopted in relation to the Sydney Futures Market. Authorization was granted. International Commodities Clearing House Ltd (1987) ATPR (Com.) para.50-066. Fletcher Challenge Ltd (FCL), a company incorporated in New Zealand, applied for authorization regarding the proposed acquisition by Velfro Pty Ltd (a wholly owned subsidiary of FCL) of 25% of the issued capital in Australian Newsprint Mills Holding Ltd and NNM Investment Ltd. Authorization was granted. Fletcher Challenge Ltd (1988) ATPR (Com.) para.50-077. In these two cases, FATA was not applicable, but TPA was.

74 For example, TPC v British Building Society & Ors (1988) ATPR para.40-880.


76 Sections 50 & 50A give TPC and Trade Practices Tribunal power to interfere with acquisitions within and outside Australia, under the condition that the acquisitions have resulted, or likely to result, in a dominant position of an acquirer in Australian market. The power to control is not based on the transfer of ownership from local interests to foreign interests.
affecting competition, contracts, arrangements or understanding in relation to prices, contracts affecting competition, covenants in relation to prices, secondary boycotts, prohibition of contracts, arrangements or understandings affecting supply or acquisition of goods or services, monopolization, exclusive dealing, resale price maintenance, price discrimination, mergers, and acquisitions outside Australia. These activities concern daily business operations of both local and foreign interests. Thus activities of foreign investors in Australia may involve restrictive trade practices, although these activities will not always fall within the ambit of FATA.

Section 50 of the TPA may affect acquisitions by foreign investors of Australian businesses within Australia. The basic function of s.50 is to prevent or to remove any element or activity which is deemed to be detrimental to fair competition, increase in productivity and protection of consumer interests. Accordingly, if an acquisition is regarded as resulting, or likely to result, in a dominant position of the acquirer under s.50, the acquisition is prohibited. The prohibited mergers and acquisitions specified by s.50 can be further divided into

77 TPA, s.45.
78 Id. s.45A.
79 Id. s.45B.
80 Id. s.45C.
81 Id. s.45D.
82 Id. s.45E.
83 Id. s.46.
84 Id. s.47.
85 Id. s.48.
86 Id. s.49.
87 Id. s.50.
88 Id. s.50A.
89 For example, Australian Meat Holdings Pty Ltd (an Australian Company) proposed to acquire Thomas Borthwick & Sons (Australasia) Ltd (a subsidiary of Borthwick, a UK company). This acquisition of a foreign-owned company's shares in Australia by a local-owned company does not fall within the ambit of FATA, but is subject to the TPA. The Commission therefore initiated a legal proceeding against the proposed takeover at the Federal Court on 25 January 1988. Subsequently, the proposed takeover was found to be contrary to s.50 of the TPA. See TPC v Australia Meat Holdings Pty Ltd (1988) ATPR 49,465.
three categories: transferred dominance, aggregated dominance, and strengthened
dominance. Briefly, transferred dominance refers to a situation where the target
of the takeover is already in a position to control the market before the takeover; aggregated dominance refers to a situation where a dominant position is created, or likely to be created, as the result of a merger between two businesses which had obtained some control of the market but had not achieved a dominant position in the market before the merger; and strengthened dominance refers to a situation where the acquirer eliminates its competitors to reinforce its position to dominate the market. The Commission has applied s.50 to various cases. For instance, during 1987-88, the Commission reviewed the acquisition of shares and assets of Goodman Field Watties Ltd in Australia and New Zealand by Naarden, a Unilever subsidiary. Section 50 was considered but was decided to be inapplicable because effective competition was deemed to remain in the market after the acquisition. During the same period, an overseas takeover between Nestles of Switzerland and Rowntree Macintosh of the UK was also examined, because both companies have subsidiaries in Australia. No infringement of s.50 was found. It is clear that some acquisitions involving foreign investors in Australia, especially in the case of a merger between local and foreign companies which results in a so-called "aggregated dominance", are subject to the TPA. Although a proposed merger may not exceed the 20% or 40% threshold for foreign ownership set forth in FATA, the merger may still trigger off s.50.

Section 50A affects a takeover of an overseas company which has subsidiaries in an Australian market. It is thus directly relevant to foreign investment in Australia. Section 50A was added in 1986 for the purpose of dealing with acquisitions outside Australia, which, while not directly falling under s.50, result in an acquirer's dominant position in the Australian market. This situation occurs when parent

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91 Paragraph (a) of ss.50(1) & 50(1A) includes takeovers of such nature. TPC v Ansett Transport Industries (Operations) Pty Ltd & Ors (1978) ATPR para.40-071. But s.50(2c), inserted in 1989, seems to exclude the takeovers "where the acquirer's transferred dominance is no greater than the dominance of the target". CCH, ATPR para.8-190.

92 Paragraph (a) of ss.50(1) & 50(1A) applies also to such takeovers.

93 Paragraph (b) of ss.50(1) & 50(1A) refers to such takeovers. The application of ss.50(1) & 50A(1A) is subject to ss.50(4) & 50(5) of TPA.


95 Id, at 78.
companies of two Australian companies are merged. As a result, a dominant position of the two foreign subsidiaries in the Australian market may be created. Section 50 does not directly apply to this situation. Under the Act, the Trade Practices Tribunal is given power to make a declaration prohibiting such acquisitions. As at December 1990, s.50A had not been applied to acquisitions relating foreign investment in Australia, nor had it been discussed in detail by the Court.96

The Trade Practices Commission does not have any direct connection with the Trade Practices Tribunal. The Commission is an administrative body, whereas the Tribunal is a quasi-judicial body whose president must be a judge of a Federal Court.97 The Tribunal is an appeal body which deals with matters relating to decisions of the Commission with respect to authorization and notification of exclusive dealings. The Tribunal has power to confirm, set aside or vary decisions of the Commission. Under its power to review, it may perform all the functions and exercise all the powers of the Commission. The Tribunal’s power has direct implications for foreign investment when s.50A is involved.

2.3. Foreign Investment Policy in the Guidelines98
2.3.1. Control of Foreign Investment Under FATA
2.3.1.1. The Functions of FATA

FATA specifies five situations in which control over foreign takeovers may be introduced. These are acquisitions or issues of shares,99 acquisitions of assets,100 arrangements relating to the directorship of corporations,101 arrangements relating to control of an Australian business,102 and acquisitions of urban land in Australia.103 The crucial criterion for deciding if control is applicable is whether the consequence

96 In TPC v Australian Iron and Steel Pty Ltd & Ors CCH, ATPR para.41-001, the TPC took legal action in the Federal Court against BHP’s acquisition of NZ Steel. Section 50A is briefly mentioned but not considered by Lockhart J. in this case. This was the only reported case relating to 50A as at December 1990.
97 TPA, s.31A.
98 The Guidelines can be divided into two main categories: control over foreign investment under FATA, and control sanctioned by specific legislation or supported by the executive power. These categories will be reviewed separately.
99 FATA, s.18.
100 Id, s.19.
101 Id, s.20.
102 Id, s.21.
103 Id, s.21A.
of an acquisition or arrangement has resulted in a substantial increase of foreign control in an Australian corporation or a prescribed foreign corporation which either carries on business in Australia or is a holding company of an Australian corporation; and if so, whether the increase of foreign control has or will endanger the national interest of Australia. This criterion suggests functional differences between FATA and the TPA. The former concerns the percentage of foreign ownership in a company. The latter deals with the impact of a monopoly in Australia resulted from a takeover. In the case of foreign takeovers, a proposed acquisition will be subject to FATA if foreign control in the target company has been increased. But a takeover which does not increase foreign ownership in a target company may be subject to the TPA if dominance arises as a result of the takeover.

FATA has extraterritorial effect. Section 16 of the Act expressly states that the "Act applies both within and outside Australia". In fact, ss.19 & 21 of the Act apply to any acquisition of assets of an Australian business, or an arrangement in relation to an Australia business carried on solely by prescribed corporations. An acquisition of a prescribed corporation that carries on Australian business may fall within the ambit of s.19, even if the takeover actually takes place outside Australia. Similarly, an arrangement made outside Australia involving prescribed corporations may be subject to s.21 as long as the arrangement concerns an Australian business. The extraterritorial effect of FATA is reinforced in s.34, which deals with the criminal jurisdiction of Australian courts in relation to the matters defined in the Act. Under this section, the Treasurer may bring a legal action against a prohibited takeover carried out outside Australia. As at December 1990 the

104 "Australian business" according to s.7 of FATA refers to a business carried on wholly or partially in Australia in anticipation of profits or gain, including the holding of a mining right but excluding a business involving governments (the Commonwealth, State or local governments) or statutory corporations constituted for a public purpose in Australia.

105 "Prescribed corporation" as defined in s.13 of FATA, means a trading or financial corporation; a foreign corporation that holds assets valued at $20,000,000 in land, in mineral rights or in an Australian corporation; a foreign holding company of an Australian corporation whose assets exceed $20,000,000; a holding company of a foreign company that holds prescribed amount of assets ($20,000,000) in Australia, or that controls an Australian corporation; a foreign corporation that holds more than one-half of the assets in a holding corporation which in turn holds a prescribed corporation; or a foreign corporation with one-half of its assets consists of assets in its Australian subsidiaries.

106 This section states that a provision of the Judiciary Act 1903-1973 (Cth) vesting a State court jurisdiction over offences against the law of Australia has effect, in relation to offences against FATA "not committed within any State, as if that jurisdiction were so invested without limitation as to locality".
Treasurer has not exercised his power under FATA to block acquisitions taking place outside Australia.

The extraterritorial effect of FATA can be compared with s.50A of the TPA, which purports to catch any overseas merger or takeover that have detrimental impact on Australian market. The two Acts emphasize different aspects of a takeover. FATA will be applicable if an overseas acquisition of a prescribed corporation results in control of an Australian business by a different foreign corporation or if it exceeds the limits on foreign ownership allowed by the Act. By contrast, s.50A of the TPA focuses on the resultant dominance of a foreign acquirer in Australian market, which can be created when foreign corporations of Australian subsidiaries have been merged. The applicability of each provision depends on the result of a proposed overseas acquisition. Sometimes, both Acts may be triggered, although the application of one Act alone would be effective to prevent a proposed takeover.

2.3.1.2. Takeovers Prohibited Under FATA

According to whether a proposed takeover results in prescribed foreign control in the target company, the following takeovers proposals are subject to examination by the FIRB and approval by the Treasurer:

1. a proposal relating to an acquisition or issue of shares (including an option to acquire shares), which would result in the control of the corporation being transferred from local interests to foreign interests, or if control over the corporation is to be transferred between different foreign persons;

2. a proposal relating to an acquisition of, (including an option to acquire), an Australian business by foreign corporations through the purchase of assets (including acquisitions of rural properties);

3. a proposal relating to an agreement or an alteration of the memorandum or other constituent document of an Australian corporation which would result in an increase of foreign control in the corporation or a change of the existing foreign control in the corporation;

4. a proposal by a foreign corporation relating to an arrangement or a termination of an arrangement which concerns the leasing or letting on hire.

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107 Foreign control is deemed to exist if more than 15% of voting power or interests of issued shares in the corporation is held by a foreign person or together with his associates, or more than 40% of voting power or interests of issued shares in the corporation is held by two or more foreign persons. FATA, s.18(7).

108 FATA, s.19.

109 An acquisition of rural property of less than $3 million in value is exempt from FIRB examination. FATA, s.13A.

110 FATA, s.20.
of, or the granting of other rights to use, assets of such a business or relating to the participation by a person in the profits or management of an Australian business;

(5) a proposal by a "foreign person" as defined by FATA relating to the acquisition of Australian urban land, which does not fall within the exempted categories specified by the Treasurer.

In the 1987 Guidelines the federal Government exempted the issue of pro-rata shares and acquisition of a non-trading company (such as a shell or shelf company) from examination, if the total assets involved were less than $1,000. However, the 1989 Guidelines omit these exemptions. As a result, pro-rata share issues and small shell companies will fall under the thresholds set forth in FATA and thus be exempted.

In the case of acquisitions, the Government has exempted proposals involving assets of relatively small value from examination. FATA defines the concepts "exempt corporation" and "exempt business", and accordingly proposals involving total assets of less than $3 million in rural land and $5 million in other cases are exempt from examination. Although the thresholds for exemption were formally incorporated into FATA only in 1989, they were set forth in the Guidelines as early as 1987.

The Foreign Takeovers Amendment Act 1989 extends the application of FATA to foreign investment involving rural or urban land. This is one of the most important changes made to FATA since its enactment in 1975. The present controlling measures on foreign investment in urban and rural real estate are a mixture of law and policy. The newly inserted s.21A of FATA grants the Treasurer power to interfere with acquisitions of urban land by foreign investors. The power extends to the exemption of certain acquisitions from examination. This may retrospectively give effect to some exemptions announced by the Treasurer in

111 FATA, s.21.
112 Id, s.21A.
114 Section 14 of the Amendment Act.
116 Foreign Takeovers Amendment Act 1989 inserts 1A under s.25 of FATA, which states that "where the Treasurer is empowered to make an order under subsection 18(2), 19(2), 20(2), 21(2) or 21A(2) in relation to the acquisition, agreement, arrangement, issue or alternation specified in the notice, the Treasurer may, instead of making such an order, decide that the Commonwealth Government has no objection to the proposal specified in the notice..." This subsection suggests that the Treasurer may give approval to an application which is otherwise prohibited.
1987.117 Under s.21A of FATA, the Treasurer may announce government policies regarding foreign investment in real estate.118 In fact, the Guidelines require acquisitions of commercial and residential real estate by foreign investors to be approved. However, the Government has indicated that acquisitions of real estate for development, acquisition of non-residential commercial real estate where Australian investors have 50% equity participation, acquisitions of residential property by foreign companies as their residence, acquisitions of home units or similar accommodation prior to completion or "off-the-plan" where 50% of ownership of the property is held by Australians and acquisitions by foreign nationals as temporary residence are normally approved "unless they are judged contrary to the national interest".119

Because the policy with regard to the exemptions and proposals likely to be approved is intended to direct acquisitions in the future, there arises the issue of the enforceability of the Treasurer’s policy statement. It has been accepted in Australia that the Government may not make a promise or understanding which fetters its future executive actions. This principle was recognized in the Amphitrite case120 and was confirmed in a number of other cases.121 The Guidelines, in their present form, although they are reliable for practical reasons, cannot in theory impose

117 These exempted acquisitions are as follows: acquisitions by certain foreign-controlled charities or charitable trusts; acquisitions by certain life assurance companies; acquisitions by certain general insurance companies; acquisitions by Australian pension funds of foreign employers for the benefits of Australian superannuants; acquisitions of offices and residences by foreign governments for use as official mission or staff residences; acquisitions from real estate developers of residential apartments, units and dwellings under construction or "off the plan"; acquisitions of industrial or commercial real estate that are wholly and directly incidental to the conduct of the normal business activities of the foreign interest concerned; acquisitions of interests in time share scheme where the entitlement of the foreign interests and its associates is less than four weeks per year. 1987 Guidelines, supra note 113, the Corrigendum. In 1989, several other acquisitions, such as acquisitions of units involving certain public trusts or companies, acquisitions by certain companies involving overseas Australians, acquisitions by immigrants to Australia and acquisitions of property valued at less than $5 million in non-residential commercial real estate, are added to the listed exemptions. See Foreign Acquisitions and Takeovers Regulations 1989 (Cth).

118 Section 21 states that the Treasurer may make an order in relation to either a specified person, or a specified class of persons or of interests in land.

119 Guidelines, supra note 30, at 9.

120 Amphitrite case [1921] 3 KB 500.

contractual obligations on the Treasurer. Flexibility is perhaps a reason for the Government to have incorporated the exemptions in its Guidelines, rather than in FATA.

2.3.2. Control Under Other Statutes or Regulations

2.3.2.1. Control in Manufacturing and Service Industries

The Government encourages foreign investment in the manufacturing, service, resource processing, non-banking financial intermediaries, insurance, stockbroking, tourism (hotel and resorts) and primary industries (other than mining). Under the Guidelines, the establishment of a new business involving total investment of $10 million or more is not required to demonstrate economic benefits or to provide for Australian equity participation. Acquisitions in these sectors are subject to the thresholds set forth in the Foreign Takeovers Amendment Act 1989 (Cth), which are $3 million in rural land and $5 million in other sectors of the economy. Takeovers under these thresholds are not required to be approved.

The federal policy in relation to foreign investment in these sectors has been occasionally supported or accepted by some State governments. For example, the federal Government restricted foreign investment in life insurance companies during the 1960s and 1970s. This policy was reflected in the A.C.T. Companies (Life Insurance Holding Companies) Ordinance 1968, rejecting the attempted takeover by British investors of MLC Ltd, a life insurance company, and its holding company. This Ordinance, which was later repealed, was the first Australian legislation restricting foreign investment in life insurance companies. In 1985, the federal Government decided that non-bank financial institutions and insurance companies should be fully opened to foreign investment. As a result, a proposal for foreign takeover involving such businesses is now, like foreign takeovers in most sectors of the economy, governed by FATA.

With respect to these sectors, several questions should be mentioned. First, the administration of foreign investment by the federal Government in these sectors

122 The Guidelines can be compared with the "News Release", issued in the name of the Minister for Immigration and Ethnic Affairs, discussed in Salemi case. In that case, Barwick CJ. observed that the "Minister's statement was no more than a statement of policy. Statements of policy as a rule do not create legal obligations, though they may understandably excite human expectation as distinct from legal expectation". (1977) 14 ALR 1, 9.

123 Guidelines, supra note 30, at 6.

124 In 1968, the High Court's narrower interpretation of s.51(xx) of the Constitution was still effective. This was probably why the A.C.T. Ordinance was used to block the takeover.
can be substantially simplified if the federal Corporations Act can be accepted voluntarily by each State. As at February 1991, whether the amended Corporation Act 1989 (Cth)\textsuperscript{125} can be accepted by the States still remained to be seen. The alternatives to a federal Corporations Act might be to require all Australian financial and trading corporations or foreign corporations to register under federal law, or to convince the States to adopt separately another uniform version of Companies Acts in each State.\textsuperscript{126} Secondly, before the amended Corporations Act 1989 (Cth) enters into force, various general federal statutes and regulations governing these sectors may be regarded as indirect bases for the executive power to control foreign investment.\textsuperscript{127} For example, the Securities Industry Act 1980 (Cth) was passed for the purposes of regulating securities industry in the Australian Capital Territory. Accordingly, foreign investment in securities industry in the Australian Capital Territory is subject to this Act. Similarly, under the Australian Industry Development Corporation Act 1970 (Cth) the Minister may direct the Corporation with regard to the establishment and development of an industry.\textsuperscript{128} Thus, a government policy in relation to a specified industry invested by foreign interests may be implemented through the

\textsuperscript{125} The Corporations Act 1989 (Cth) was amended by the Corporations Legislation Amendment Act 1990.

\textsuperscript{126} See "Gloves off in company law debate" Aus.Fin.Rev. 2 April 1990.

\textsuperscript{127} For instance, there are the Australian Industry Development Corporation Act 1970 (Cth), the Trade Practice Act 1977 (Cth), and so on (for the manufacturing industry); the Financial Corporations Act 1974 (Cth) and the Management and Investment Companies Act 1983 (Cth) (for non-bank financial intermediaries); the Health Insurance Act 1973 (Cth), the Life Insurance Act 1945 (Cth) and the Superannuation Act 1976 (Cth) (for the insurance industry); the Commonwealth Inscribed Stock Act 1911 (Cth), the Securities Industry Act 1980 (Cth), the Companies (Acquisition of Shares) Act 1980 (Cth), the Companies and Securities Legislation Amendment (Future Industry) Act 1986 (Cth), the Futures Industry Act 1986 (Cth) and the Stock Exchange and National Guarantee Fund Act 1987 (Cth) (for the stockbroking industry although some laws are made for ACT); the Australian Tourist Commission (Transitional Provisions) Act 1987 (Cth) (for tourism); the Australian Apple and Pear Corporation Act (Cth), the Australian Dried Fruits Corporation Act 1978 (Cth) and so on (for primary industry); the Trade Practice Act 1974 (Cth), the Preference to Australian Goods (Commonwealth Authority Act) 1980 (Cth), and so on (for the service industry). The only sector which seems to lack of regulations is resource processing. But it may be argued that some laws on export prohibition, petroleum exploitation and environment protection are relevant to resource procession. In addition, the federal Corporations Act 1989 (Cth) has been passed by the federal Parliament but not yet promulgated for some constitutional reasons. If the federal Government decides to go ahead with the Act and the Act can survive the forthcoming constitutional challenges by some States, the Act will reinforce the power of the Commonwealth Government to control foreign investment in these sectors.

\textsuperscript{128} Section 8A of the Act.
Corporation as far as the matter concerned falls under the scope of the Australian Industry Development Corporation Act.

2.3.2.2. Control in Banking

The Banking Act 1959 (Cth) required a corporation which intends to carry on banking business in Australia to apply for approval to the federal Treasurer. In 1984 the federal Government relaxed policy on foreign banking in Australia. Subsequently, 16 entry rights were granted to foreign banks in 1985. Of them J.P.Morgan did not take up its licence. Today, the Guidelines do not encourage foreign banks to apply for banking licences in Australia, although the Government may approve application of foreign banks to set up representative offices for liaison purpose. The experience in past 5 years suggests that foreign banks do not constitute a threat to Australian banks, in particular in the retail banking sector. As the Australian Financial Review commented, "despite great hopes and ambitions, the experiment [to open Australian financial market] has largely been a failure".

Federal control of banking is sanctioned by the Banking Act 1959 (Cth) and the Banking (Foreign Exchange) Regulations 1946 (Cth). Although the States have power to regulate State banking, their power, in the light of Melbourne Corporation v Commonwealth, seems to be limited to the case where a State, or a person or agency authorized by the State, acts as a banker within the territory of the State. This limitation on state power is also a restriction on the federal power. As suggested in Bourke v State Bank of NSW, federal law relating to banking may be invalid to the extent that it affects state banking. Thus ss 52 and 52A of the TPA are held invalid as far as they are applied to the transaction conducted within New

129 Sections 8 & 9 of the Banking Act 1959 (Cth).

130 Guidelines, supra note 30, at 5.


132 (1947) 74 CLR 31.

133 In Melbourne Corporation v Commonwealth, Latham CJ. states that State banking in his opinion "refers to banks established and conducted by a State or by an authority established under State law and representing a State". Id, at 52. This view is shared by the whole Court.


135 93 ALR 460.
South Wales by the State Bank. But when foreign investment is involved, the federal Government should have prevailing power even if a State bank is also involved in the transaction.136

The federal banking power under the Constitution has been examined by the courts in several cases. The Banking Act 1947 (Cth) was held valid as a whole (although certain sections were regarded as beyond the banking power) in Bank of NSW v Commonwealth.137 In this case, the banking power was construed as extending not only to those regulations which aid, foster and protect banking and the choice of persons engaging in it, but also making of rules which prohibit it. But rules so made are subject to s.92 of the Commonwealth Constitution and cannot hinder free trade within the Commonwealth.138 A similar view was shared by the judges in Melbourne Corporation v Commonwealth.139 The Banking (Foreign Exchange) Regulations 1946 (Cth) were considered in Watson v Lee, where reg.6(1) of the Regulations was decided to have been supported by the Constitution;140 and in Amid Pty Ltd v Beck & Jonas Pty Ltd, where the validity of reg.8(1) of the Regulations was upheld and the plaintiff’s claim, which was decided to be based on an action contravening the Regulations, was dismissed.141 In the light of these cases, it can be concluded that the Banking Act 1959 (Cth) and Banking (Foreign Exchange) Regulations 1946 (Cth) are substantially justified under the banking power, as well as other relevant heads of power. The Guidelines on foreign investment in banking, which are mainly based on the Act and Regulations, as a whole do not go beyond the established judicial interpretation of the banking power.

2.3.2.3. Control in Civil Aviation

136 The Court in Bourke v State Bank of NSW decided that a federal Act cannot apply to State banking not extending beyond a State. (See e.g. 93 ALR 460, at 468.) But, when foreign investment is involved, the matter cannot be regarded as "State banking not extending beyond the limits of a State".

137 (1947-48) 76 CLR 1.


139 (1946-47) 74 CLR 31.

140 (1979) 144 CLR 374, ie, 397-401.

The federal Parliament restricted the issue of international airline licences in Australia in 1960.\textsuperscript{142} Since then an international airline licence is not available to any foreign applicant unless an international treaty exists between the country of the applicant and Australia, e.g. the Air Transit Agreement or other relevant treaties to which both countries are parties. Under the Act, the Governor-General has power to regulate matters concerning the implementation of the Act;\textsuperscript{143} and the Secretary of the Department of Transport is given a discretion to issue or cancel an airline licence.\textsuperscript{144} However, no specific legal rules governing foreign ownership in this sector have been laid down.\textsuperscript{145}

Indeed, the Government has relaxed control of foreign investment in the civil aviation sector. The Guidelines announced that till October 1990 "proposals by foreign interests to establish new business involving total investment of $10 million or more or to takeover existing business with total assets valued at $5 million or more in the civil aviation industry will be approved unless judged contrary to the national interest.\textsuperscript{146} This brings control in the civil aviation to the same base as under FATA. After deregulation, a foreign international is allowed to hold more than 15% of shares in any Australian domestic operator.\textsuperscript{147}

Government policy in this sector is sanctioned by the Air Navigation Act 1920 (Cth) and Air Navigation Regulations 1920 (Cth). Both the Act and Regulations have been repeatedly tested in the High Court in different contexts. In Airlines of NSW Pty Ltd v State of NSW,\textsuperscript{148} several regulations of the Air Navigation Regulations 1920 (Cth) which were made pursuant to the Air Navigation Act 1920 (Cth) were discussed. It was alleged that regs.198, 199, 200B, 320A and 320B interfered with intrastate air navigation and were therefore unconstitutional. But the Court found only reg.200B invalid. Regs.320A and 320B were determined valid by the whole court and regs. 198 and 199 were also found valid by the majority of the court (with Taylor J. dissenting). Thus under reg.198 of Air Navigation Regulations 1920 (Cth) any aircraft, regardless of whether it is engaged in intrastate

\textsuperscript{142} Air Navigation Act 1920-1960 (Cth), s.12.
\textsuperscript{143} Id, s.26.
\textsuperscript{144} Id, s.199.
\textsuperscript{145} The provisions on non-British subjects in the 1920 Act have been repealed.
\textsuperscript{146} Guidelines, supra note 30, at 5.
\textsuperscript{147} Ibid.
\textsuperscript{148} (1965) ALR 984.
or interstate regular public transport operations, must be authorized by the Secretary to the Department of Transport and Communication before commencing operation.  

Generally speaking, the federal powers to legislate for civil aviation are supported and justified by s.51(xxix) the external affairs power, and s.51(i) trade and commerce power, which "includes power not merely to protect but to foster and encourage interstate and foreign trade and commerce." In the context of foreign investment in civil aviation, the federal power to regulate the matter is also supported by s.51(xx) of the Constitution.

2.3.2.4. Control Over the Media

The media covers two sectors: broadcasting (radio and television) and newspapers. The federal power to control foreign investment in the media is mainly derived from s.51(v) of the Constitution, which allows the federal Parliament to pass law with respect to postal, telegraphic, telephonic and other like services; and s.51(xx) which allows the federal Parliament to regulate foreign corporations as well as financial and trading corporations formed within the Commonwealth. Judicial interpretation of s.51(v) extends the application of "other like services" to radio and television. But the federal power to control newspapers, which may indirectly arise from s.51(i) and (xx) of the Constitution, has not been tested in the courts. So far the federal Parliament has not assumed a general power to regulate newspapers, but only a power to legislate on cross media interests, which involve control of a newspaper by a licensee of radio or television station within the service area of the licence. Nevertheless, federal power to regulate foreign investment in the newspaper

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149 Reg. 198 requires all aircraft engaging in commercial operations, which according to reg.197 of the Regulations, include all air transport carried out within the Commonwealth except for "private operations" to be authorized. Therefore, all commercial operations must be authorized by the federal Government. The Secretary may ask an applicant for an aircraft licence to supply information on safety, regularity and efficiency of air navigation, even if the service is intended to operate intrastate. See Reg.199(3) & (4) of the Regulations. In addition, any aircraft is forbidden to land or take off from a Commonwealth aerodrome or fly in controlled airspace in the course of operation unless permission has been given by the Secretary. See Regs.320A & 320B of the Regulations.

150 *Airlines of NSW Pty Ltd v State of NSW* (1965) ALR 984, 994-5, 1017, 1023 & 1033.

151 Id, at 999, 1000 & 1035.

152 Id, at 999.

153 *R v Brislan; Ex P Williams* (1935) 54 CLR 262; *Jones v Commonwealth* (1965) 112 CLR 206; and *Herald & Weekly Times Ltd v Commonwealth* (1966) 115 CLR 418.
business can be supported by s.51(xx) of the Constitution. The federal policy in these two sectors will be discussed separately.

The federal Government assumed power to regulate broadcasting and television under s.51(v) of the Commonwealth Constitution. Section 51(v) of the Constitution vests power to legislate in relation to "postal, telephonic, and other like services" in the Commonwealth Parliament. The meaning of the words "other like services" was investigated in *R v Brislan; Ex Parte Williams* by the High Court, and radio broadcasting was regarded as falling within the meaning of these words. Further, the Broadcasting and Television Act 1942 (Cth) was found to be within the legislative power of the Commonwealth in *Jones v Commonwealth* and *Herald & Weekly Times Ltd v Commonwealth*. In general, federal power to legislate on the broadcasting and television throughout Australia has not since been challenged.

Although the Broadcasting Act was passed as early as 1942, restrictions on foreign investment in the broadcasting and television sector did not exist until 1969 when the Broadcasting and Television Act 1942 (Cth) was amended. Under the amended Act, a foreign person or foreign controlled company was not allowed to hold more than 15% of the voting power or shares in a broadcasting or television company. The Broadcasting and Television Act 1942 (Cth) was further amended in 1981, 1987 and 1988. At present, the Act provides that a foreign person is not allowed to be in a position to control, directly or indirectly, a company holding a radio or television licence. It also restricts two or more "foreign persons" from directly holding or controlling in aggregate more than 20% of the issued capital or voting rights in a licensee company. This provision has been exploited by some foreign companies to hold more than 20% of shares in a broadcasting corporation.

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154 (1935) 54 CLR 262.
155 (1965) 112 CLR 206.
156 (1966) 115 CLR 418.
158 Id. ss.90E & 90G.
159 Broadcasting Act 1942, s.90G. The Guidelines have set up the threshold for control of interest by one foreign person in a broadcasting company as 15% of shares or voting power. The threshold is not directed sanctioned by the Broadcasting Act, but is supported by FATA.
160 Broadcasting Act 1942, s.90G.
through their subsidiaries. The Government has thus indicated its intention to tighten up the 20% rule except when non-voting shares are involved. In general, the federal Guidelines for foreign investment in broadcasting and television sector are supported by the Broadcasting and Television Act 1942 (Cth).162

The Commonwealth Government exercised a degree of control over newspapers by the Post and Telegraph Act 1901 (Cth),163 which was repealed in 1975. But the provisions relating to newspapers did not impose any restriction on the ownership of newspapers, except providing a definition of newspaper for postal purposes. Nevertheless, the federal Government did regulate some aspects of newspapers in that Act. Probably because of the insignificance of the provisions, these provisions, in particular the federal power to do so, were never challenged during the operation of the Act, although a case relating to s.28 of the Act was brought before a Victorian Court in 1903.164 After the Post and Telegraph Act 1901 was repealed, provisions in relation to newspapers were omitted from both the Postal and Telecommunications Commissions (Transitional Provisions) Act 1975 (Cth) and the Postal Service Act 1975 (Cth), which replaced the Post and Telegraph Act 1901. The federal Government had nevertheless restricted foreign investment in newspapers, as indicated in its Guidelines, without formal legislative sanction until 1987, when the Broadcasting and Television Act was amended. Some provisions in relation to registration of newspapers and control of cross-media interests (the same licencsee of television or radio, who also has prescribed interests in newspapers within the area of broadcasting licence) were added.165 Under the present legal framework for foreign investment, foreign takeovers of newspapers fall within the FATA.

Although the Broadcasting (Ownership and Control) Act 1987 gives the ABT power to limit cross media interests involving associate newspapers, this power does not extend to newspapers which are not related to cross-media interests. At present,

161 This is possible under Broadcasting Act. For example, s.90G(4) defines that a company is controlled by a foreign person when more than 50% of its votes or shares are controlled by the person. But a person may control a company even if he does not control of more than 50% of its votes or shares. Thus, foreign ownership in a broadcasting company may exceed 20% bench-mark when several companies where foreign interests hold less than 50% of votes or shares control substantial shares in the company.

162 i.e. sections 90G & 92D of the Act.

163 See ss. 28 & 29 of the Act.

164 See Re Bradshaws Guide; Ex Parte Stillwell (1903) 29 VLR 415.

165 Section 91AAE of the Broadcasting (Ownership and Control) Act 1987 sets up the Associated Newspaper Registration in charge of the registration of newspapers. Other relevant sections are s.91, 91AAB, 92FAB, and 92FAD.
foreign investment in newspapers is controlled only by Government policy, which has been stated as follows:

Foreign investment in mass circulation newspapers is restricted. All proposals by foreign interests to establish a newspaper in Australia or to acquire an existing newspaper business are subject to case-by-case examination irrespective of the size of the proposed investment. Approval is not normally given to proposals by foreign interests to establish ethnic newspapers in Australia, unless there is substantial involvement by the local ethnic community and effective local control of editorial policy.166

In fact, the federal Parliament has never directly exercised legislative power to control foreign investment in newspapers. In the past it regulated in the Post and Television Act 1901 (Cth) only the registration (not operation) of newspapers as part of postal services pursuant to s.51(v).167 In addition, the extent of federal power to legislate in relation to newspapers has never been examined in the courts, although the section concerning the registration of newspapers was considered in Re Bradshaw's Guide; Ex Parte Stillwell.168 As noted earlier, based on the corporations power under the Constitution, the federal Parliament can regulate the newspapers business carried on by foreign or financial and trading corporations formed within the Commonwealth if it chooses to do so. But as the policy stands today, the basis for the federal policy on foreign investment in newspapers can be regarded as a mixture of the statutory power under FATA and the executive power under s.61 of the Constitution.169

2.3.2.5. Control over Mining

Matters involving mining have traditionally fallen within State power. For example, the first Act expressly restricting foreign investment in the mining sector in Australia was the A.C.T. (Uranium Mining Companies) Ordinance 1970 (repealed in 1979), which limited the right of foreign investors to hold shares and voting powers within a uranium mining company formed within A.C.T. But the federal

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166 Guidelines, supra note 30, at 5-6.

167 The repealed Act set forth rules on the registration of any newspaper "known and recognized as a newspaper in the generally accepted sense". Section 20 of the Act.

168 (1903) 29 VLR 415. Hood J. applied s.20 of the Act to the publication in dispute - Bradshaw's Guide to Victoria, and found that the publication lacked "every element of what I shall call a newspaper".

169 When foreign investors propose to acquire interests in existing newspapers, FATA is applicable. But when foreign investors propose to establish a new newspaper, to which FATA is not applicable, federal executive power applies.
Government may regulate foreign investment in this sector to some extent through the control of export licences and the regulation of the conduct of foreign or trading companies.\textsuperscript{170} Statutes made under s.51(i) & (xx) include the Customs (Prohibited Exports) Regulations 1958 (Cth), the Environment Protection (Impact of Proposals) Act 1974 (Cth),\textsuperscript{172} and FATA 1975. As at December 1990, no federal statute expressly dealing with foreign investment in the mining sector had been passed, but State laws on mining and petroleum exploitation do exist.\textsuperscript{173}

Government policy on foreign investment in the mining sector is based on FATA, and to a lesser extent on the Environmental Protection (Impact of Proposals) Act 1974 and the Customs (Prohibited Exports) Regulations 1958 (Cth). FATA addresses control of foreign investment in the mining sector by defining the holding of a mineral right in Australia as carrying on an Australian business.\textsuperscript{174} Accordingly, an acquisition of shares in a company which holds a mineral right in Australia may be subject to FATA.

There is no head of federal legislative power under the Commonwealth Constitution expressly dealing with mining operations. For this reason perhaps, the federal Parliament has not passed any Act in relation to mining in general. But when foreign investment in mining becomes a matter of concern, the federal Parliament is able to regulate the matter under s.51(i) and (xx) of the Commonwealth Constitution. In addition, ss.51(vi), (xxix) & (xxxix) may also provide support to different extents


\textsuperscript{171} For discussion on various heads of power under which the federal Parliament may regulate mining industry, see Prof. Crawford, "The Constitution and the Environment" paper unpublished as at December 1990.

\textsuperscript{172} The constitutional validity of the Customs (Prohibited Exports) Regulations and the Environment Protection (Impact of Proposals) 1974 Act was supported by the High Court in Murphyores Incorporated Pty Ltd v Commonwealth (1976) 9 ALR 199.

\textsuperscript{173} For example, the Mining Act 1973 (NSW), the Petroleum Act 1955 (NSW), the Mining Act 1968 (Qld), the Petroleum (Submerged Lands) Act 1982 (Qld), the Mining Act 1958 (Vic), and the Petroleum (Submerged Lands) Act 1982 (Vic).

\textsuperscript{174} FATA, s.7.
or in various circumstances to a federal Act governing foreign investment in mining.175

The Guidelines emphasize Australian participation in mineral operations which include mineral exploration and exploitation. Mineral exploration rights can be granted by a State government, and are not subject to federal approval. Thus the transfer of mineral exploration rights does not fall under FATA.176 On the other hand, mineral exploitation177 is subject to the federal Guidelines. As at December 1990, the federal Government requires investment proposals of $10 million or more to be approved by the Treasurer. In the examination of a proposal, Australian participation of 50% is usually required unless the Treasurer decides that the proposal is not "contrary to the national interest" or the "Government judges that the unavailability of sufficient Australian equity capital on reasonable terms and conditions would unduly delay the development of Australia's natural resources".178 The Guidelines prohibit the establishment of any new uranium project, although the exploration of uranium is not forbidden.179 A takeover involving existing uranium mining is subject to FATA.

The Guidelines on foreign investment in the mining sector have the same deficiencies as the policies in the newspaper and real estate sectors. The Guidelines purport to direct foreign investment in both the acquisition of interests in an established company and the creation of a new business. Control of takeovers can be sanctioned by FATA, but control over the establishment of a new business seems beyond the ambit of FATA, which does not address issues relating to the establishment of a new business. The establishment of a new business could refer to the incorporation of a company. When the incorporation involves a foreign company or financial or trading corporation, it is subject to federal legislation. In contrast, if

175 For example, mining operations are often associated with international or interstate trades; uranium, as a special kind of mineral, requires special considerations in defence and foreign policy of Australia; and moreover, mining operations often concern environmental protection. These matters may fall within the above-mentioned heads of federal legislative powers. For discussion, see Crawford, supra note 171.

176 Foreign Takeovers Amendment Act 1989 excludes the exploration rights from the "mineral right" which is subject to FATA.

177 It refers to the extraction of minerals and hydrocarbons, or the production of concentrate and initial grading or screening treatment necessary for a mineral to be transformed into a saleable product. Guidelines, supra note 30, at 6.

178 Guidelines, id, at 6.

179 Id, at 7. The existing uranium operations are the Ranger and Nabarlek Projects in NT and the Olympic Dam project in SA.
no foreign or financial and trading corporations are involved, the matter seems to be subject to State jurisdiction. The uncertainty of the federal legislative power in relation to the establishment of a new foreign-related corporation might be the reason for the omission of the establishment of a new mining company in FATA. For the same reason perhaps, the State governments have voluntarily cooperated with the federal Guidelines.

2.4. Examination Procedures for Investment Proposals

Procedural requirements for examining proposals falling within the scope of FATA and the categories of restricted sectors described in the Guidelines are different. According to FATA, the Treasurer must make a decision within a thirty-day period, and notify the applicant within 10 days after a decision has been made. Meanwhile, the applicant is not allowed to proceed with the proposed takeover before the expiration of the forty-day period. If the Treasurer does not respond to the proposal within the forty-day period, the applicant is entitled to proceed.

There is no prescribed form or time limit for proposals falling within the categories of restricted sectors described in the Guidelines other than FATA. During 1988-89, it was said, the average time taken to process all proposals (including those falling under FATA) was 22 days,180 although it has been pointed out that the average time might be longer if calculated in another way.181 In general FIRB has long since indicated an intention of meeting applicants' request for urgent decision for commercial reasons as soon as it can.182

2.5. Control of Foreign Investment by State Governments

2.5.1. Introduction

The State governments do not have special foreign investment regulations or overall guidelines for foreign investment. Due to the effect of ss.51 & 109 of the Commonwealth Constitution, there is practically no room for a State to pass separate laws on foreign investment, given the existence of FATA and a number of other relevant federal Acts and regulations. Nevertheless, some State governments have passed laws on various subjects falling within general State powers, such as the

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181 Kasper, supra note 65, at 63-4.
power to regulate casinos, mining and corporate affairs, which are relevant to foreign investment in some circumstances. The laws so made may apply to foreign investment within the States, provided that the local laws do not contravene the relevant federal laws. These State laws will be examined below. In addition, the local policies of the New South Wales and South Australia governments, which are so far the only States that have announced their own policies on foreign investment in the mining sector, will also be discussed.

2.5.2. Local Control in New South Wales

The New South Wales Government has set forth its own law and policy on foreign investment in the mining and agricultural sectors. Like other States, New South Wales has its own Mining Act. But unlike the laws in other States, the Mining Act 1973 (NSW) clearly spells out that control of a corporation applying for an exploration or mining licence may be taken into account by the Minister in deciding whether to grant a licence.\(^{184}\) This implies that whether a corporation is controlled by local or foreign interests may be an important element in the case of competitive bidding for a licence. To implement its control over foreign investment in the mining sector, the New South Wales Government announced Investment Guidelines for the Mineral Industry in N.S.W. on 21 February 1978.\(^{185}\) These Guidelines require a minimum Australian equity participation of 51% in most situations, except where the exploitation is of exceptional value to the State or the required special technology can only be obtained by majority foreign participation. For a proposal with majority foreign participation, a gradual achievement of majority Australian participation over a specific period may be imposed as a condition.\(^{186}\) The New South Wales Government emphasizes that in case of competition, preference will be given to the venture with higher Australian participation, subject to the consideration of overall benefits to the State.\(^{187}\)

New South Wales Government policy requires that foreign agricultural investment involving land purchase be approved by both the federal and State

\(^{183}\) Hamilton, supra note 43, at 199-205.

\(^{184}\) Mining Act 1973 (NSW), s.61.

\(^{185}\) Flint, supra note 35, at 252.

\(^{186}\) Hamilton, supra note 43, at 201.

\(^{187}\) Id, at 202.
Governments. The federal consent does not necessarily prevail over the State's decision if the State decides against the investment proposal. No specific criterion has been laid down by the State Government, except that it requires that, in order to give priority to Australians, foreign investors can only purchase properties which have been advertised, and foreign investors are not allowed to engage in any speculative acquisition. To date, the State Government has not rejected any project approved by the federal Government, as far as is known.

2.5.3. Local Control in South Australia

The South Australia Government acted in 1979 and 1980 to limit the maximum shareholding by any single shareholder or the associates of the shareholder in two companies. The Santos (Regulation of Shareholding) Act 1979 (SA) prohibited any person or the associates of that person from holding more than 15% of company shares in Santos Ltd. The Executors' Company's Act Amendment Act 1980 (SA) restricted any person or associates of that person from holding more than 1.67% of company share in the Executors' Company. Under the Act, the maximum limit could be changed by regulations made by the Governor of South Australia. These two Acts were not passed directly for the purposes of controlling foreign investment in South Australia. But any foreign interests invested or to be invested in the two companies would be subject to these Acts.

The South Australian Government, like the New South Wales Government, has announced its own guidelines for foreign investment in the mining sector. The power to regulate the mining sector is vested in the State Government by the Mining Act 1974 (SA), which gives discretion to the Minister to grant and cancel mining licences in the State. The South Australian Government requires at least 51% Australian equity participation in new mining projects involving foreign investment. Similar to the practices of the federal and NSW Governments, the South Australian Government is willing to lower the required percentage of Australian participation if the operation is judged to be particularly valuable to the State's economy and local

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188 The NSW Government indicates in its policies that foreign investors "wishing to invest in Australian agriculture must have their proposed agricultural land purchase approved by the Foreign Investment Review Board". Hamilton, supra note 43, at 204. The federal and State governments exercise concurrent power in relation to the purchase of land by foreign corporations. The federal Government may intervene on the basis of s.51(xx) of the Commonwealth Constitution, and the State governments have power to control because s.51 does not specify the power to regulate real estate as an exclusive federal power. Thus by virtue of s.109 of the Commonwealth Constitution, the federal power to control foreign investment in real estate prevails over State power to regulate real estate where foreign investments are involved.

participation is not available, or if the technology needed can only be obtained through majority foreign participation. Again, the possibility of a gradual achievement of majority Australian participation over a specific period is taken into account when such foreign investment proposals are examined.

The South Australian Government has also announced in its Guidelines that uranium exploitation is allowed provided that 75% of Australian equity participation is available.190 The policy to allow the exploitation of uranium conflicts with the federal policy. Due to the importance of uranium to national defence and environment, as well as its significance to world peace and environment, the federal Government seems to have strong constitutional grounds191 and effective control over exploitation of uranium in South Australia. For the time being, the federal Parliament has not passed any Act directly dealing with uranium exploitation, although it has passed the Nuclear Codes Act 1978 (Cth). But the federal Government may exercise control over uranium mining in South Australia or any State by using the power to issue or refuse an export licence under the Customs (Prohibited Exports) Regulations 1958 (Cth), through its power to protect environment under the Environmental Protection (Impacts of Proposals) Act 1974 (Cth), or through its power to control foreign takeovers under FATA, as the case may be. If none of these powers is applicable in the special circumstances of the case, the federal Parliament could always pass an Act on uranium mining under the enumerated powers of the Commonwealth Constitution, such as defence, external affairs, foreign corporations, and overseas trade and commerce. Having regard to the existing federal power to control uranium exploitation, the current federal foreign investment policies seem to have been based on a stronger constitutional ground than the present mining policies of the South Australia Government in relation to foreign investment.

190 This requirement does not have any practical significance, because the federal Government has indicated that uranium exploitation will be limited to the existing projects only. It is impractical that the South Australian Government may give approval to a new uranium exploitation project against the federal policy which is supported in particular by federal power to regulate environment and several Acts or regulations, such as Nuclear Codes Act 1978, Environmental Protection (Impacts of Proposals) Act 1974 and Customs (Prohibited Exports) Regulations 1958. For discussion, see Crawford, supra note 171.

191 A number of enumerated powers may be used by the federal Government, e.g. s.122, (legislative power with respect to federal territories); ss.51(ii), 81-3, and 96 (financial power); s.51(xxix), (external power); s.51(xx), (corporations power) and s.51(i), (commerce power). See Crawford, ibid.
2.5.4. Local Control in Tasmania

The Tasmanian Government has restricted foreign investment in casino operation by the Casino Company Control Act 1973 (Tas), which allows foreign investors to hold no more than 38% of the shareholding in any corporation engaged in the operation of a gambling casino in Tasmania. This Act is based on general State powers which cover areas not enumerated by the federal Constitution. Nevertheless, in the case of a foreign corporation investing in a casino, the Act and FATA may overlap in some circumstances, e.g. foreign takeovers exceeding the limits set out in FATA or transfer of control of a company contrary to the "national interests". By virtue of s.109 of the Commonwealth Constitution, as far as foreign investment is concerned FATA prevails over Casino Company Control Act of Tasmania. Therefore, a foreign corporation proposing a takeover resulting in its control of more than 15% of voting power or issued shares in a casino business is subject to approval by the federal Government, although the takeover may be exempt under the Casino Company Control Act 1973 (Tas). Failure to obtain federal approval by the foreign corporation may result in the prosecution of the foreign corporation under FATA.

2.5.5. Local Control in Queensland

Queensland Parliament passed the Foreign Ownership of Land Register Act in 1988. The Act establishes the Foreign Ownership of Land Register. Its function is to monitor foreign investment in land in Queensland. The Act does not impose restrictions on acquisitions of land in Queensland by foreign corporations and foreign natural persons, but requires foreign persons (including corporations) to disclose their interests in land. There is no contradiction between this Act and existing federal law.

192 The original Act defined foreign corporations broadly, including corporations incorporated in Australia but controlled by foreigners. (See section 4 of the Foreign Ownership of Land Register Act 1988, no. 75) This wide definition of foreign corporations has been abandoned in the Foreign Ownership of Land Register Act Amendment Act 1989 (no.3), where foreign corporations are defined as corporations incorporated outside Australia. This change has brought the Queensland to the same line as the federal position on foreign corporations.

193 "Interests in land" means an estate or interest in land; in a licence or permit granted under Land Act 1962-88, under Harbour Act 1955-87, under Mining Regulations of 1971; in a business area or residential area defined under the Mining Act 1968-86; in a miner's lease granted under the Miner's Homestead Lease Act 1913-88; in a lease granted under the Mining Titles Freeholding Act 1980-86; and a special mining lease granted under the Commonwealth Aluminium Corporation Pty Ltd Agreement Act of 1965 or the Aurukun Associates Agreement Act 1875. Sections 4 of Foreign Ownership of Land Register Act 1988-89 (Qld).
The Queensland Government has also, reportedly, exercised executive power, through government agencies, such as the State Government Insurance Office and the Port of Brisbane Authority, to influence takeovers of local companies by interests outside the State, or to prevent potential competitors from other States or overseas from threatening the interests of local companies. The influence of the Government was often indirect, subtle and of an executive nature. In this case to invoke s.92 of the federal Constitution against the activity of the Queensland Government could be a difficult task. It was noted that the State Government Insurance Office had on occasion taken advantage of its position to influence takeovers of Queensland companies, e.g. the takeover of Walker's Ltd and Evans Deakin Ltd and Clyde Industries Ltd, through increasing or threatening to increase its shareholding in the target companies. It was also noted that Queensland Government, for the purpose of protecting the interests of Queensland Cement & Lime Co Ltd, prohibited other companies from having cement storage facilities on the Brisbane River.

These practices are not directly relevant, but they indicate what the Queensland Government might do in case of unwelcome foreign investment proposals. For example, it was reported that after a $443 million Japanese purchase of a stake in the Mirage resort in 1989, the then Premier of Queensland stated that he might introduce restrictions on foreign investment in the State. However, as at December 1990, no such restriction has been enacted.

2.5.6. Local Control in Western Australia

Western Australia does not have any special law for controlling foreign investment, but has reportedly applied legislation which requires any proposed lease of business on Rottnest Island to be approved by the State Minister for Tourism and the Island Authority to foreign takeovers. A case involving the Minister's rejection of a proposal by Victoria Co (Hospitality) Pty Ltd, a subsidiary of the Japanese-owned Victoria Co Australia Pty Ltd which is incorporated in Western Australia, to takeover Lombardo Ltd's business on Rottnest Island was recently commenced in the State Supreme Court on the ground of the federal Racial

195 Id, at 255.
196 Id, at 257.
Discrimination Act 1975. The Minister rejected the proposed takeover on the ground that the State Government encouraged control of Rottnest Island to remain in Western Australia, so as to maintain "its unique Western Australian character".

The case is about the State power to impose limits which are different from FATA on foreign takeovers within its territory, an area in which there is overlapping federal and State legislation but which has not been tested in Australian courts. So far some foreign takeovers which are not subject to FATA have been subject to State examination under various Acts such as the one concerned in this case. FATA may not be directly applicable under s.109 of the Commonwealth Constitution in this case because the State laws under which some foreign investment proposals are rejected are not Acts dealing with control of foreign investment. Rather, like the Western Australian case, the State laws give the State governments discretions which may in fact be used to block foreign takeovers in some cases. If Victoria Co (Hospitality) Pty Ltd's claim on the ground of the federal Racial Discrimination Act is supported by the Court, a practical approach to the settlement of the overlapping between the federal and State laws in relation to foreign investment may be found. However, even if the State Supreme Court would reject the plaintiff's claim, the legal action itself has suggested a possibility of challenging State control of foreign investment.

2.6. Executive Power in the Administration of Foreign Investment

2.6.1. Executive Power in General

The executive power of the federal Government is conferred, but not defined, by s.61 of the federal Constitution, which is "remarkably cryptic; indeed, it has been suggested that it was deliberately left vague". The executive power to execute the Acts of Parliament is evident from s.61, but the language of the executive power "extends to the execution and maintenance of this Constitution", in

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199 The application was dismissed by the Court. The order dismissing the application was not available as at December 1990.

200 Ibid.

201 Renfree argues that executive power is an abstract concept, "connoting that part of sovereignty concerned with executive functions as distinct from legislative and judicial functions". H.Renfree, The Executive Power of the Commonwealth of Australia (Sydney, Legal Books Pty Ltd, 1984) 389.

particular "maintenance", may sometimes raise divergent interpretations, and the term has not yet been clearly defined by the High Court.

Nevertheless, there is a number of cases which throw some light on the meaning of s.61. In the Wooltops Case, Knox CJ. comments that the execution of the Constitution "means the doing of something immediately prescribed or authorized by the Constitution without the intervention of Federal legislation". His view was confirmed by Williams J. in Australian Communist Party v Commonwealth, where he stated that

The maintenance of the Constitution therefore means the protection and safeguarding of something immediately prescribed or authorized by the Constitution without the intervention of Federal legislation. The execution and maintenance of the laws of the Commonwealth must mean the doing and the protection and safeguarding of something authorized by some law of the Commonwealth made under the Constitution.

Both judges give a wide interpretation of "the maintenance of the Constitution", which may give direct or indirect support to executive power. The power seems also to extend to the activities incidental for the exercise and implementation of the constitutional power. However, their view can be compared with the view of Evatt J. who in King v Hush; ex parte Devanny pointed out that s.61 ...

only defines the general limits of the King's executive authority in respect of the Commonwealth and does not determine what the Executive may lawfully do upon any given occasion. Whatever power or duties are conferred or imposed upon the King's executive government, by any section of the Constitution, or by such portion of the Royal prerogative as is applicable, may lawfully be exercised; but sec.61 itself gives no assistance in the ascertainment or definition of such powers and duties.

In the light of these judicial views, Knox CJ. appeared to say that s.61 of the Constitution grants a substantive power to the executive, but Evatt J. seemed to say

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203 Id, at 31-2.
204 Id, at 32.
205 Commonwealth v Colonial Combing, Spinning and Weaving Co Ltd (1922) 31 CLR 421.
206 Id, at 432.
207 (1951) 83 CLR 1.
208 Id, at 230.
209 (1933) 48 CLR 487.
210 Id., at 511.
that s.61 only confirms powers which are vested in the executive under other sections of the Constitution or any particular law.

The essential difference between these judicial views is whether or not the executive may exercise power under s.61 of the Constitution without the "intervention of federal legislation". Knox CJ. seemed to say that an executive can do so as long as the act is authorized under the Constitution or is carried out for "safeguarding" the Constitution. By contrast, Evatt J. seems to insist that an act of the executive must be judged in a particular circumstance in accordance with law but not under s.61 in general. The former view supports the existence of a discretionary power which may be exercised by the executive for the purposes of maintaining the Constitution without direct authorization by the Parliament; the latter takes a cautious position and denies the existence of such general power. The two views may be consistent in some cases where an executive act is supported by either legislation or the prerogative, but they contradict when an executive act is not supported by any legislation, case law or royal prerogative other than s.61 itself as construed by Knox CJ.

In sum, the executive power of the federal Government includes three limbs. First, it includes the power to execute the laws of the Parliament and delegated legislation as authorized by these laws. Secondly, it contains executive power granted in s.61 of the Commonwealth Constitution; extending to the powers enumerated under the heads of the federal legislative power and sometimes the royal prerogatives for the purposes of maintenance of the Constitution. Thirdly, it involves specific executive powers prescribed in various sections of the Constitution. Therefore, s.61 is the main (but not the only) provisions for the executive power of the Commonwealth Government. A number of other provisions, such as ss.5, 21, 32, 33, 56, 57, 62, 64, 65, 67, 68, 69, 70, 72, 83, 103 and 126, also grant specified power.

211 Australian Communist Party v Commonwealth (1951) 83 CLR 1, 230.

212 Winterton divides federal executive power into four limbs. These are: the execution and maintenance of the laws of the Commonwealth, executive power implied in s.61 of the Commonwealth Constitution, the execution of the Constitution, and the maintenance of the Constitution. Id, at 31. But the distinction between executive power implied in s.61 and the "maintenance of the Constitution" which itself is derived from s.61 can hardly be clearly made. See discussion on the "Maintenance of the Constitution" in Winterton, supra note 202, at 31-8.
either to the Governor-General\textsuperscript{213} or to the Governor-General in Council\textsuperscript{214}. But most powers in relation to substantial matters are actually exercised by the Executive. Renfree states that the Governor-General in Australia is "the image, in little, of a constitutional King, introducing measures to the legislature, conducting the executive, distributing patronage, in name only, while all these functions are in reality performed by his councillors."\textsuperscript{215} In the context of the above-mentioned three limbs of the executive power, sometimes the Governor-General is granted a specified power (such as the power to make regulations in relation to foreign exchange control under the Banking Act 1959 (Cth)), sometimes a Minister is given a power to implement a particular Act (such as the Treasurer's power to approve or reject a foreign takeover under FATA). However, it is the federal Ministers who exercise substantial or most of the executive power. As observed by Winterton, executive power conferred by s.61 is exercisable by the Governor-General "means that all power conferred by s.61 is exercisable on the advice of Commonwealth Ministers."\textsuperscript{216}

2.6.2. Executive Power to Regulate Foreign Investment

As mentioned earlier, the Executive exercises power under Acts of Parliament and delegated legislation, as well as under the prerogative incorporated into the Constitution although the latter is of limited relevance here. This characteristic is important in understanding the federal executive power to regulate foreign investment. The authority is clear in most cases when the Government controls foreign investment pursuant to statutes and delegated legislation, such as the power vested in the Treasurer by FATA and Banking (Foreign Exchange) Regulations 1946

\textsuperscript{213} The Governor-General, according to the Commonwealth Constitution, is appointed by the Queen as her majesty's representative in the Commonwealth. His main responsibilities are to grant or withhold assent on behalf of the Queen to a proposed law passed by the Parliament under s.58, to convene sessions of the Parliament, prorogue Parliament, dissolve the House of Representatives under s.5, and dissolve the Senate and House of Representatives under s.57. He also performs a number of other functions vested in him in the Commonwealth Constitution. The relationship between the Queen and the Governor-General is now more or less of symbolic nature. Thus, Renfree argues that "Governor-General should indeed have the status of a viceroy" in Australia. Renfree, supra note 201, at 149.

\textsuperscript{214} The Council refers to the Federal Executive Council established under s.62 of the Commonwealth Constitution. The power granted to the Governor-General in Council means, according to s.63 of the Commonwealth Constitution, the Governor-General should act with the advice of the Federal Executive Council.

\textsuperscript{215} Quick and Garran, supra note 134, at 388.

\textsuperscript{216} Winterton, supra note 202, at 27.
(Cth), the power given to the Minister for Transport by the Air Navigation Act 1920
(Cth) and the powers granted to the TPC by the TPA and to the ABT by the
Broadcasting and Television Act 1942 (Cth). But the authority is far less clear when
the Government controls foreign investment through a policy which has nor express
statutory basis, although in the light of some judicial views the executive
Government may justify its policy on the ground of maintaining the Constitution.

Confusion arises from the policy unsupported by legislation. Under the
Commonwealth Constitution, legislative, executive and judicial powers are separated,
although not to the same extent as the separation of powers in the United States.
This implies that the Executive cannot exercise the power designated to the
Parliament without parliamentary authorization. On the other hand, some judicial
views, which have not been expressly rejected so far, suggest that the Executive may
for the purposes of maintaining the Constitution under s.61 of the Constitution
protect and safeguard "something immediately prescribed or authorized by the
Constitution without the intervention of Federal legislation".217 This implies that the
executive power may extend beyond the specified executive power under the
Constitution. Otherwise the Judges should not have qualified their views by stating
"without the intervention of Federal legislation". But in the context of the
Commonwealth Constitution, this judicial view of s.61 should be limited to special
circumstances. Although the Judges do not indicate how extensive the executive
power under s.61 should be, they could not have meant that the Executive may
exercise legislative powers without limitation or qualification. This assumption is
contrary to the rule of law and the Constitution as a whole. For this reason perhaps,
only a very small portion of federal foreign investment policies, such as establishing
a new newspaper by foreign investors, are unsupported by any existing federal
legislation. Presumably, such policy is based on a limited application of the judicial
view of s.61 as given in Wooltops Case.

When a federal policy is not directly supported by legislation, there are two
ways to implement the policy without resorting to legislative power. One is to rely
on relevant legislation which may give the Executive effective control over the
matter concerned. For example, there is no federal legislation governing the
establishment of a new mining operation by a foreign corporation in Australia.218
The federal investment policy requires foreign investment proposals involving more
than $5 million to be examined by the federal Government. If a proposal involves

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217 Wooltops Case (1922) 31 CLR 421, per Knox CJ. at 432; and Australian
Communist Party v Commonwealth (1951) 83 CLR 1, per Williams J. at 230.

218 The federal Corporations Act was not promulgated as at December 1990.
sole foreign investment, it falls under the corporation power of the federal Parliament. But there is no federal law governing the establishment of Australian companies by foreign corporations, except the law relating to foreign takeovers. If a proposal involves both foreign and local corporations, the matter is currently still subject to State law. But in either case, the federal Government is able to use its power under other relevant laws, such as export control regulations, to make the operation of a unapproved project uneconomic or impossible. This possibility may be the reason for voluntary cooperation from foreign investors, although they literally do not have obligation to do so.

Another way to support the policy is to rely on the existing federal legislative power, which under the system of responsible government is subject to the influence of the executive Government. Restriction on foreign investment in newspapers is an example. The federal Guidelines require that foreign investment in newspapers must be examined by the federal Government regardless of the amount involved. This policy is not directly supported by any legislation.\(^{219}\) Nor is there any express power under the Constitution which enables the federal Parliament to regulate newspapers in general. But when foreign corporations and trading or financial corporations are involved, the federal Parliament may regulate newspapers under either s.51(i) (commerce power) or s.51(xx) (corporation power). Accordingly, when a newspaper is established by sole foreign investment, the federal Parliament is able to legislate if it chooses to do so. The existence of this power does not make the policy legally enforceable, but the possibility may be enough to encourage voluntary cooperation from foreign investors. So is the case when a newspaper is invested by both foreign and local corporations, because the federal Parliament is able to regulate the operations of foreign corporations and trading or financial corporations formed within the Commonwealth.

The legality of a federal foreign investment policy and the applicability of the policy are different matters. The question of legality does not arise unless the enforcement of the policy becomes an issue. The federal foreign investment policy unsupported by legislation would be illegal if the Government intended to enforce it

\(^{219}\) The federal Parliament has dealt with some aspects of newspapers in two separate laws: FATA and Broadcasting Act. The FATA may apply to foreign takeovers in newspapers business regardless of the amount of investment involved, because the Treasurer has power to decide the applicability of the Act even if the amount involved does not satisfy the requirement set forth in the Act. But as have been noted, the FATA does not apply to the establishment of a new business. The Broadcasting Act 1942 restricts cross media interests. But the Act is applicable only when "cross media interests" are involved. Similarly, it does not apply to the case when a new business which has no association with any existing broadcasting licence is established.
through the court or by taking direct action. However, it is legal if the policy calls only for voluntary cooperation. Requirements unsupported by law, no matter how strict the terms may be, do not constitute legal obligations. It is up to foreign investors to decide whether to accept or not, although a legally warranted right, which may be achieved by a litigation-minded foreign investor in an Australian court, to set up a business in Australia often does not guarantee the profitability of the business. The Australian Government may simply use its various powers to make the business unprofitable, such as in the case of export control. Therefore, a theoretical voluntariness of the federal investment policy does not always reflect the practical enforceability of the policy.

2.6.3. State Power to Regulate Foreign Investment

As we have seen, some States have announced their own foreign investment guidelines in the mining sectors and passed laws which may occasionally affect foreign investment in particular areas of the economy. Inevitably, a constitutional issue - namely the relationship between the federal and State powers in the field of regulating foreign investment - arises from the existing State laws and policies on foreign investment, as well as the exercise of State legislative and executive powers to regulate foreign investment in the future. The issue can be further examined in two aspects: first, what is the relationship between the federal laws and State laws which affect foreign investment in the same area or on the same subject, such as the relationship between FATA or TPA and Tasmanian Casino Company Control Act 1973; and secondly, what is the relationship between the federal executive power and State executive power, such as the relation between the federal investment Guidelines and the Guidelines in the mining sector announced by the New South Wales and the South Australia Governments.

Most of the enumerated heads of federal legislative powers under s.51 are concurrent rather than exclusive.\(^\text{220}\) The powers to regulate foreign investment, such as ss.51(i), (ii), (v), (xii), (xiv), and (xx),\(^\text{221}\) are not exclusively exercised by the federal Parliament. In the case of direct inconsistency between the federal and State laws, s.109 of the Constitution applies, and thereby the State law "to the extent of the

\(^{220}\) As Crawford comments that the fundamental point of understanding the Commonwealth Constitution is that "with few exceptions, the Constitution creates no exclusive powers, either for the Commonwealth or the States". Crawford, supra note 171.

\(^{221}\) By contrast, ss.51(iv), (xxiv), (xxx), (xxxii), (xxxiii), (xxxvi) and (xxxviii) are generally regarded as exclusive federal powers, see R.D.Lumb, The Constitution of the Commonwealth of Australia Annotated (Sydney, Butterworths, 1986) 78.
Inconsistency is invalid. In the case where a federal law explicitly or implicitly indicates an intention to cover a particular field exclusively, the State law infringing upon such exclusiveness of the federal law would be invalid. These are the so-called tests - direct inconsistency (collision) and covering the field (cover-the-field) - for deciding the inconsistency between the federal and State laws. In the context of the present State law, only the Tasmanian Casino Company Act 1973 may conflict with the federal FATA. The others, such as Queensland Foreign Ownership of Land Registration Act 1988 and Mining Act in each State, do not directly contravene any federal legislation and some inconsistency, i.e. in the Victoria Co Case in Western Australia, arises from only the exercise of discretion by the State governments. In the latter case, the federal Government has not passed any Act in respect of the matters dealt with by the State laws. However, in both cases, direct or indirect conflict between federal and State laws may make the business involved uneconomic, and eventually limit the effect of the state law with regard to the matters of disagreement. In this sense, the federal law prevails over state law, although they overlap only in their extended, but not direct, applications.

The relationship between the federal foreign investment Guidelines and the Guidelines of the New South Wales and South Australian Governments in the mining sector is not clear in the case of inconsistency between them. The difficulties arise from the fact that the federal policy in mining sector does not have direct and express statutory authority. Thus, it is impossible to apply s.109 to this case if an inconsistency exists between the federal policy and the policy of New South Wales or South Australia. However, the federal policy still appears to have stronger constitutional ground in the sense that it would ultimately prevail over the State policies. The prevalence of the federal policy is not based on existing legislation, but on the availability of federal legislative power and the possibility of applying the power by the federal Parliament. For example, s.51(xx) is available to the federal

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222 The Constitution, s.109.

223 R v Brisbane Licensing Court (1920) 28 CLR 23, Colvin v Bradley Bros Pty Ltd (1943) 68 CLR 151, Clyde Engineering Co v Cowburn (1926) 37 CLR 466, and Blackley v Devondale Cream (Vic) Pty Ltd (1968) 117 CLR 253.


225 The "mineral right" was mentioned in FTA 1975 and redefined in the Foreign Takeovers Amendment Act 1989. But neither Act spells out the rules relating to the establishment of a new mining project by foreign investors.
Parliament. Under this power, although the State governments seem to have general power to regulate mining in the States, the federal Government has prevailing power to control foreign corporations engaging in mining operations in a State. Had the federal Parliament chosen to pass an Act in relation to the operations of foreign corporations, or financial and trading corporations, in the mining sector, the federal policy sanctioned by such Act would prevail over the State policies supported by State laws. For this reason, even if the federal Guidelines in relation to foreign-invested new projects in mining are not directly supported by federal Act, they still have a stronger position against the State Guidelines, having regard to the availability of the federal legislative power. The effect of s.109 in this case is indirect. Having regard to this possibility, as the present form of the federal control over foreign investment in the mining sector stands, the potential inconsistency between the federal and State policies is more likely to be resolved through cooperation between the federal and State governments, in particular the acknowledgement of the existence of the federal policy by the State governments. In fact, the relationship between the federal and State policies in relation to foreign investment in mining industry is rather based on voluntary cooperation. It is reached between the federal and State governments in view of a practicability of controlling foreign investment for the purposes of developing Australian economy at both national and State levels, and of ultimate enforceability of the federal policies on foreign investment in mineral industry.

2.7. Conclusion

Section 51 grants the federal Government extensive power to control foreign investment in Australia. The issue is not whether the federal Government can control, but how it exercises that control. The most unequivocal but not necessarily the most effective means of control is legislative control. The surety of legislative control forms contrast with policy which may or may not be based on an authorization from the legislature. Policy is often relatively vague, flexible and unenforceable in the courts. But surety may not always guarantees efficiency. They

The Governments of the New South Wales and South Australia indicates that their policies in relation to foreign investment in the mineral industry are prepared "with recognition of the published policies of the Commonwealth Government relating to foreign ownership in the mineral industry". Hamilton, supra note 43, at 200 & 203. By contrast, the federal Government only recognizes the existence of State law with regard to mineral exploration. Accordingly, the federal Guidelines state that "assignments and transfers of interests in petroleum exploration permits and licences are required to be approved under State, Territory or Commonwealth petroleum legislation". Guidelines, supra note 30, at 6. With regard to the exploitation of minerals, the Guidelines fail to acknowledge the existence of State laws.
are different issues. A clear and practical law may provide great efficiency. By contrast, a clear but impractical law (e.g. inflexible or incomprehensible) may have achieved its clarity at the expense of efficiency. Efficiency can be lost because either the law fails to address questions it should have, or fails to respond to changes of circumstance. In addition, a federal law governing the establishment of a financial or trading company by foreign interests (or the operation of mining companies involving foreign and trading or financial corporations) or a federal foreign investment Act which is intended to cover all aspects of foreign investment may not be particularly efficient, because many areas to be regulated are also subject to state power.

A federal law to that effect without an appropriate solution to the disputes between the federal and state jurisdiction over the matters concerned will be inefficient for several reasons. First, the constant power struggle between the federal and State governments will inevitably affect the application of such legislation. Secondly, the federal Parliament does not have express power to regulate some areas, such mining and newspapers, although it may legislate as to the operation of foreign or trading corporations. This may result in overlapping of laws and unnecessary complexity of administration if a federal law in these areas is passed. Thirdly, even if there is no constitutional problems as to who has proper power to regulate these matters, there may still be administrative difficulties in the implementation of a lengthy and perhaps inflexible piece of legislation. Lengthiness is often a result of specification and comprehension. Both reduce the degree of flexibility which is needed for dealing with indefinite varieties of operational forms of foreign investment and conflict between national and foreign interests inspired and affected constantly by the changing economy. In addition, foreign investment matters, like taxation matters, require prompt response from the legislature. This may be an extra burden to the Government, and if so may reduce the efficiency of administration. Having regard to these problems, a combination of law and policy seems to be a more economic and convenient way for the federal Government to administer foreign investment.

The Foreign Investment Guidelines in a sense are the result of the unsettled constitutional dispute regarding power to regulate foreign investment between the federal and State government. The federal Parliament has power to regulate foreign corporations, or financial and trading corporations formed within the Commonwealth. But this power, according to the majority of the High Court in \textit{NSW v Commonwealth},\textsuperscript{227} "is not a power to bring into existence the artificial legal persons

\textsuperscript{227} (1990) 8 ACLC 120.
upon which laws made under the power can operate". 228 If what the majority of the Court said is the test for the exercise of s.51(xx), the federal Parliament will have trouble in regulating the incorporation of any venture which involves only unincorporated foreign investors. 229 But the federal Parliament should be able to legislate on the formation and incorporation of a venture participated by foreign corporations, or financial and trading corporations formed within the Commonwealth. 230 Given that the federal Parliament has power to regulate "artificial legal persons" after they have been established under foreign or State laws, it is still unclear how far the power can extend to the areas traditionally dominated by State laws, such as mining, real estate and newspapers. It seems that the federal Government has to anticipate a lengthy, and perhaps costly, legal battle with State governments in winning formal recognition from the High Court of its authority to exercise prevailing power in these areas, which are not clearly defined by the Constitution. The past has shown that such victory does not come easily both in financial terms and in terms of their cost to federal State relations. Probably for such pragmatic considerations, the federal Government has adopted the Guidelines, backed by particular statutory power under several existing Acts, as the main means of control. The Guidelines appear in a more informal and negotiable form. Voluntary cooperation, rather than compulsory acceptance, is required from the States, although the cooperation is supported, but not without disputes, by the constitutional powers vested in the federal Government. In this way, the federal and State governments may often reach a kind of compromise whenever conflict can be seen between the existing federal law (or policies) on foreign investment and the laws of the States. This perhaps is also the reason why the State governments have not made any formal challenge to the federal Guidelines for foreign investment, although the State governments do play some role in examining foreign investment proposals within their territories. 231

228 Id. at 124.

229 For discussion on unincorporated foreign investors, see Flint, supra note 35, at 29.

230 For various situations where foreign investment may be involved, see id. at 27-9.

231 It was reported that the Queensland Government made recommendations regarding some foreign investment proposals received by the federal Treasurer. It is not clear whether Queensland legally requires foreign investors to apply for its approval before, or at the same time as, a investment proposal is submitted to the federal Treasurer for examination. Aus.Fin.Rev. 27 April 1990.
The Guidelines are voluntary. In theory, they provide foreign investors with constructive guidance and assistance for their business decisions. An investment proposal may be rejected if inconsistent with the Guidelines. In such case, if the refusal is supported by power under an Act, the authority of the Guidelines is irrelevant; if the refusal is based on the Guidelines only, the decisions of the Treasurer which are based on the policies that do not expressly indicate their legal bases may theoretically become a cause for litigation. However, for practical reasons, the authority of the Guidelines is unlikely to be challenged by foreign investors. This conclusion does not in theory exclude the possibility that a foreign investor may be able to challenge the Guidelines on the ground of his rights which have been provided under Australian laws.

To sum up, the policies on foreign investment could be more authoritative if the federal Government incorporates them into a comprehensive foreign investment Code. But the practicability of such Code is dubious because of the existing or potential disputes on the jurisdiction over some aspects of foreign investment between the federal and State government and the possibilities of administrative inconvenience in implementing a lengthy and complex Act. In addition, the Guidelines also have advantages of flexibility in the process of amendment (policy change), compared with an Act. Having regard to the fact that the Guidelines have received positive cooperation from foreign investors and the State governments, it seems unnecessary for the federal Parliament to venture a formal investment Code, at least for the time being.
Chapter 3 The Administration of Foreign Investment in China

3.1. An Overview

Foreign investment began to flow into China since 1840 when its door was forced open in the First Opium War by Western countries. Precise statistics of foreign investment in China between 1840 and 1949 are not available, but many foreign investment and interests operated in China under various privileges and concessions, e.g. immunity from direct Chinese tax, low tariff for imports and exports, or right of coastal and inland navigation. The existence of these privileges and concessions could be seen in the extraterritorial jurisdiction exercised by some foreign governments in China. However, this thesis does not deal with issues relevant to foreign investment in China prior to 1949 because the history of foreign investment in China prior to the PRC does not affect the development of foreign investment in the PRC either in political or economic terms. Politically, although regulations and legal institutions governing foreign participation in China's economic activities had considerably developed since 1840, in 1949 the Government of the PRC explicitly denied any connection or continuity between the new legal system of the PRC and the previous legal tradition of China. Even today, despite the fact that some connection can be seen between the present legal system of the PRC and

1 As early as the mid-17th century, the Dutch began to trade with China. But the trading between the Chinese and foreigners were limited and subject to the conditions set up by the Chinese Government. No foreign investment was made in China. After the first Opium War (1839-1842), foreigners began to enjoy many privileges which were not based on reciprocity between the Chinese Government and their governments. For a review of foreign trade history of China after the end of the second Opium War, see W.P. Alford & D.E. Birenbaum, "Ventures in the China Trade: An Analysis of China's Emerging Legal Framework for the Regulation of Foreign Investment" (1981) 3 Northw. J. Int'l L. & Bus. 56, 61-4.

2 These and a number of other privileges are direct results of extraterritorial jurisdiction enjoyed by the then major Western countries, including Japan, which forced China to accept a number of unequal treaties by force. The extraterritoriality was formally renounced in 1943. For a detailed discussion of extraterritorial jurisdiction in China, see J. Vincent, The Extraterritorial System in China: Final Phase (Harvard University, East Asian Research Centre, 1970).

3 For discussions on foreign involvement in China's economy after 1840 and the development of the laws and practice concerning status and privileges of foreign nationals or governments in China, see W. Willoughby, Foreign Rights and Interests in China (2nd edn, republished in Taiwan by Cheng-Wen Publishing Co, 1966); for discussions of the laws or regulations concerning foreign investment between 1927 and 1949 when the Nationalist Government of the Republic of China (ROC) ruled the mainland of China, see J.Y. Lu, "The Legal Status of Foreign Companies in China" (1937-40) 10 China L.R. 147, and T.Y. Wang, The Status of Alien and Foreign Enterprises in China (Chungking, China Institute of Pacific Relations, 1945, China's Council Series No.4).

the Chinese legal tradition, the predominant legal opinion in the PRC, which follows and represents the official position of the Chinese Government, still insists on distinguishing the legal system of the PRC from the previous legal institutions in Chinese history. In terms of economic connection, the history of foreign investment law before 1949 has not in fact affected the development of foreign investment law in the PRC. The Government of the PRC insists that it succeeded neither to the rights nor the duties arising from the economic contracts of the previous Kuomintang Government. This position has been upheld by the Chinese Government, despite the fact that it is probably not justified in international law and is not expressly accepted by most Western countries. Since the development of foreign investment law in China is mainly a domestic event controlled by the Government, the omission of consideration of investment history prior to 1949 does not substantially affect the discussion in this thesis.

In 1949, when the present Chinese Government was established in Beijing, there were not many foreign businesses remaining in China. Having foreseen the inevitable political change in China, most foreign businesses had transferred their assets out of China by the end of 1949. According to the statistics of the new Chinese Government, only 1,192 foreign enterprises remained in China after the 1949 Liberation, and the assets of these enterprises were estimated at 1.21 billion.


6 The attempt to distinguish the legal system of the PRC from previous Chinese legal institutions can be seen in many Chinese law textbooks. Two schools of thoughts in relation to the continuity of legal tradition in China can be identified. The conventional opinion denies any connection or continuity between the present system and previous systems, e.g. L.P.Yin & Others, Concise Jurisprudence (Jian Ming Fa Xue) (Liaoning University Press, 1986, in Chinese) 105-9. The new opinion treats the issue of continuity more flexibly, and argues that some connection exists between the different systems. The continuity is regarded as existing in two forms: positive inheritance and negative inheritance. Positive inheritance takes place when the present legal system borrows legal concepts and terminology from the previous legal systems; and negative inheritance can be identified when the experience of the previous legal system, both successful and unsuccessful, is considered by the new legal system in order to deal with similar problems. An example of the latter school can be found in M.Cui, Essays on Jurisprudence (Fa Xue Wen Ji) (Beijing, Mass Publishing House, 1986, in Chinese) 80-4.

7 Some forms of foreign investment, e.g. processing of exported and imported materials for the purposes of trade, can be seen in earlier Sino-foreign trade which began to grow significantly in 17th century. Detailed statistics of various forms of trade is not available. But data on trade between China and selected countries in some periods of history have been collected. For example, between 1818 and 1833, the average import to China by the United Kingdom and United States together reached US $25,125,774; and export was US $23,033,046. See, H. Morse, The International Relations of the Chinese Empire: the Period of Conflict 1834-1860 (Shanghai, Kelly and Walsh Ltd, 1910) 92.
Renminbi.\(^8\) No doubt these few remaining foreign enterprises were uncertain whether they could, even if they hoped to, survive under the new political regime of China.

The policies of the new Chinese Government regarding foreign investment were not clear during the first few years after 1949. The 1949 Common Program of the Chinese Political Consultative Conference which served as the first constitutional document of the PRC did not provide specific guidelines for treatment of foreign enterprises. On the one hand, Article 3 of the Common Program declared that the "People's Republic of China must abolish all the prerogatives of imperialist countries in China.\(^9\) According to the theories of Marxism-Leninism, foreign-owned enterprises might well be classified as the "prerogative" of imperialist countries. Thus, the provision (Article 3) seemed to indicate that foreign enterprises would not be allowed to continue in China. On the other hand, Articles 26 and 30 basically recognized the existence of private capital in the new socialist economy, provided that adequate control over private capital was imposed in accordance with the State plan.\(^10\) Thus these provisions appeared to suggest that foreign enterprises might be allowed to exist under some conditions in China's centrally-controlled economy, because they fell within the definition of private capital.\(^11\) In addition, Article 57 of the Common Program stated that China may "develop commercial relations with foreign governments and people on the basis of equality and mutual benefit."\(^12\) This suggested that the continuing operation of foreign enterprises was possible if China was able to develop foreign trade under the so-called "equality and mutual benefit" principle.

In fact, the Chinese Communist Party did not plan to abolish foreign enterprises immediately after 1949. "The policies adopted at the Second Plenary

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\(^8\) S.Liu & Q.Wu, China's Socialist Economy- An Outline History 1949-1984 (Beijing, Beijing Review, 1986) 58. The authors do not provide the exchange rate of these Renminbis at the time of calculation. Renminbi has devalued considerably since 1986 when the book was published.

\(^9\) Blaustein, supra note 4, at 36.

\(^10\) Id., at 43, & 44-5.

\(^11\) Some articles written by the late Chinese leaders may also support this proposition. Foreign enterprise might be accepted for a certain period of time and under certain conditions in the PRC. For example, Liu Shaoqi, who was the President of the PRC before the Cultural Revolution, in his article "Guiding Principles for New China's Economic Development", stated that "we shall gradually nationalize imperialist-run enterprise in China, or put them under state supervision". See the Editorial Committee on Party's Documentation of the Central Committee of the CCP, ed. Selected Works of Liu Shaoqi vol.1 (Beijing, Foreign Language Press, 1984) 424, 426.

\(^12\) Blaustein, supra note 4, at 53.
Session of the Seventh Party Central Committee stipulated that the Chinese Government would, after the founding of new China, allow the remnant imperialist economic forces to continue to exist for a certain period of time under government supervision and control.\textsuperscript{13} It may be that foreign enterprises might have continued to operate in China for an unspecified period of time if other political causes, such as the Korean War, had not arisen in the 1950s.

China adopted a discriminatory policy against foreign enterprises, in particular those owned by the nationals of the United States and United Kingdom, in 1950. Following Chinese involvement in the Korean War, on 16 December 1950, the U.S. Government decided to take control of all Chinese Communist assets within United States' jurisdiction, and to prohibit any ships of United States registration from calling at Chinese ports.\textsuperscript{14} In response to the U.S. policy, the Chinese Government issued an order to take control of all property of the U.S. Government and of some of its citizens situated within Chinese jurisdiction.\textsuperscript{15} A similar policy was adopted by the Chinese Government against British property following the participation of the United Kingdom in the Korean War. The Chinese Government ordered the requisition of the British-owned Shell Company in China on 30 April 1951.\textsuperscript{16} Consequently, many American and British companies were confiscated by the Chinese Government. Some Chinese writers imply that some compensation was paid to these requisitioned foreign enterprises.\textsuperscript{17} Even if this was true, the compensated amount probably fell well below the acceptable international standards of fair and reasonable compensation, because the Chinese Government refused to accept these standards in the 1950s.\textsuperscript{18} In 1953, only 563 of the 1,192 foreign enterprises remained in China, with assets totalling 450 million RMB.\textsuperscript{19}

Foreign enterprises ceased to exist altogether following the completion of the so-called "Socialist Transformation" in the 1950s. The basic functions of this program were to transform privately-owned enterprises into State or collectively-

\textsuperscript{13} Liu, supra note 8, at 57.
\textsuperscript{15} Id, at 686-7.
\textsuperscript{16} Id, at 688-9.
\textsuperscript{17} Liu, supra note 8, at 57-8.
\textsuperscript{18} No information on claims raised by foreign companies is available. In practice, the Chinese Government "persuaded" some foreigners to surrender their properties voluntarily to the Chinese Government, because these properties were regarded as examples of exploitation of Chinese people and thus should be "returned" to the people. As to the Chinese view of compensation, see chapter 6 of this thesis.
\textsuperscript{19} Liu, supra note 8, at 58.
owned enterprises in the cities, to replace private ownership of land in rural areas with collective ownership, and eventually to change the "semi-feudal" and "semi-colonial" economy into a "state planned socialist economy". The transformation was gradually achieved in a period of 6 years, and by the end of 1956 only a small fraction of private ownership remained in the sectors of small retailing and small family businesses.\textsuperscript{20} It is not clear when the last remnant of foreign enterprises was finally nationalized. However, it is possible that the final blow came in 1956 when the private capital which had been incorporated into joint State-private enterprises was evaluated, and the previous private owners were compensated at a fixed rate of 5\% per year of the assessed capital. In 1966, the ownership of the assessed capital was formally transferred to State ownership, and the State thus stopped paying interest to the previous owners of the capital.\textsuperscript{21} It can therefore be assumed that the remnants of foreign enterprises were treated in the same way as Chinese domestic private enterprises.

Systematic laws and policies on foreign investment had not developed before 1978, although China had to deal with issues of overseas borrowing and foreign technological assistance, which came mainly from the Soviet Union, in the 1950s. Given their similar ideological positions, China and the Soviet Union had a close relationship during the early 1950s. In 1950, China borrowed from the Soviet Union a development loan of US $300 million at 1\% interest, and in 1954 China received another loan equivalent to US $130 million from the Soviet Union.\textsuperscript{22} It is estimated that the total of Soviet credits to China in the 1950s, including credits for economic development, financing trade deficits, purchasing Soviet shares in joint stock companies and providing military aid, ranged between US $1.37 billion and US $2.24 billion.\textsuperscript{23} During the 1950s, Russia also agreed to assist the Chinese to build or transform 156 industrial projects.\textsuperscript{24} These assistance projects and borrowing from the Russians might be regarded as a specific form of foreign investment in China. However, due to the short duration of these borrowings and projects, and the political considerations behind them, the Chinese Government did not develop any systematic policy which might be regarded as providing for control over foreign investment. Possibly, there were some government or Party policies regarding

\textsuperscript{20} For the discussion on the measures of the transformation, see Liu, supra note 8, at 54-160.
\textsuperscript{23} Ibid; and Chinese source estimates the loans totalled 1.40 billion roubles, see Liu, supra note 8, at 125.
\textsuperscript{24} Liu, supra note 8, at 124-5.
foreign loans and Russian-aided projects, but no adequate information in this area is available.

Foreign exchange control was formally adopted in 1950 by the Decision on the Unification of the State Financial and Economic Work, promulgated by the Government Administrative Council on 3 March 1950.\(^{25}\) Item 8 of the Decision granted the People's Bank exclusive power to control foreign exchange in China, and thus any transaction involving foreign currency had to be handled by the People's Bank.\(^{26}\) Although this measure was introduced initially for dealing with the scarcity of foreign exchange in the 1950s, the measure has been continuously used since then.

There was no comprehensive law on exchange control and most measures of control were announced in separate Orders or Regulations. For example, drawing on deposits by American firms and individuals was said to be restricted in 1951.\(^{27}\) This suggests that some local regulations on foreign exchange control may have existed. Though the original regulations are not available, two public apologies, published in a Shanghai newspaper by two foreign enterprises for their negligence in not following the foreign exchange control regulations, evidenced the existence of Temporary Regulations Governing Exchange Transaction in the East China Region and other similar regulations.\(^{28}\) In fact, measures of foreign exchange control were not specified in the forms of law or regulations in China until 1980, although foreign exchange control was adopted in 1950.

The development of China's foreign trade during the 1960s and 1970s resulted in the emergence of regulations regarding the status of foreign experts and the import of foreign technology. From 1949 to 1976 China expanded its foreign trade relations from about 40 countries or regions to about 160.\(^{29}\) Meanwhile, the "total volume of foreign trade rose 11.9 times from 1.132 billion to 13.435 billion U.S. dollars (inflation not considered)".\(^{30}\) China also hired experts from Western countries to assist it in operating new equipment imported from abroad and in constructing new projects. As a result, regulations regarding the treatment of foreign experts and

\(^{25}\) The English translation of the Decision can be found in id., at 501-8.

\(^{26}\) Id., at 506.

\(^{27}\) Cohen, supra note 14, at 688.

\(^{28}\) These two apologies are collected in Cohen, id, at 694.


\(^{30}\) Id, at 677.
technicians were formulated. But strictly speaking, these regulations were not for the purposes of government control over foreign investment, and could not be appropriately regarded as part of foreign investment law.

From 1949 to 1979 very few regulations or policies regarding foreign investment were formulated or publicly accessible. Some regulations on the requisition of foreign enterprises, which revealed China's attitude toward foreign investment, ceased to operate as soon as the foreign enterprises were nationalized in the 1950s. The only area in which regulations and policies regarding foreign investment continued to exist was foreign exchange control. However, most regulations and policies took the form of "internal" documents, and were thus not available to the public.

Government control over foreign investment has rapidly developed since 1979. The first major law regulating foreign investment is the Law of the PRC on Joint Ventures Using Chinese and Foreign Investment, passed on 1 July 1979 by the Second Session of the Fifth National Peoples' Congress. Subsequently, laws and regulations concerning joint and foreign ventures, foreign taxation, and exchange control have been formulated one after another, by both the central and local governments.

Like the administration of foreign investment in Australia, the administration of foreign investment in China raises a number of constitutional or administrative

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31 For example, see the Circular of the State Council on the Approval of the Report by the National Construction Commission and the Department of Foreign Trade on the Problems and Suggestions Concerning the Treatment of Technicians and Experts from the Capitalist Countries, delivered on 29 Sept. 1975; the Chinese text can be found in the Legal Enactment Bureau, the State Council, Collection of Current Laws and Regulations of PRC 1949-85: Foreign Relations and Trade (Zhong Hua Ren Min Gong He Guo Xian Xin Fa Gui Hui Bian 1949-85: Wei Shi Wei Jing Mou Jue) (Beijing, People's Publishing House, 1987, in Chinese) 14-6.

32 Beside those regulations mentioned earlier, there is another example. The Order of the State Council for Implementation of the Policies Regarding the Protection of Foreign Currencies of Overseas Chinese was promulgated on 23 Feb. 1955 for dealing with foreign exchange brought into China by overseas Chinese. This Order suggests China's position on foreign exchange control. The Chinese text of this Order can be found in id, at 397-400.

33 It was reported that by the end of 1988, about 16,325 contracts involving a total foreign capital of US $79.168 billion had been signed, and of these, US $47.34% billion had been actually put into use. 32:10 Beijing Rev. 6-12 March 1989, at 22.

issues. At least two of these issues - the power of the executive to regulate foreign investment and the power of local governments (in Provinces, Municipalities directly under the central Government, Autonomous Regions, and municipalities in Special Economic Zones (SEZs)\(^{35}\) or specified coastal or open cities\(^{36}\) to legislate on foreign investment - are broadly comparable with the issues arisen in Australia. Contrasts and similarities can also be seen in the practices of Australia and China. This chapter will discuss Chinese approaches to the administration of foreign investment in that country.

Strong and extensive government control of foreign investment is preferred in China. The economic, legal and ideological bases on which the PRC was established largely account for this approach. In China's economic system, although Sino-foreign joint ownership, foreign ownership and private ownership have considerably increased since 1978, the State plan still plays an essential role not only in the direction of Chinese enterprises but also in its administration. Thus the present Chinese economy can be described as a State-planned economy, where central control has been greatly eased and various forms of ownership (State, collective, private and foreign) co-exist. In its legal system, China has in theory (and in theory only) adopted two principles as the bases of its Constitution. These are the supremacy of legislature over executive (at a given administrative level), and supremacy of the central Government over local governments. Thus, the central Government has substantial and prevailing power to control foreign investment under the Constitution and the special authorization by the NPC.\(^{37}\) In terms of ideology, the Communist Party, as the ruling party, is well known for its preference for Marxist-Leninist theories of State-controlled economy, which encourage a government to manipulate the economy toward a designed goal. This practice has been followed by the Chinese Government in the administration of foreign investment. All these factors have affected the administration of foreign investment in China.

\(^{35}\) These are cities of Shenzhen, Shantou, Zhuhai and Fujian. The Chinese Government hopes to develop experience in utilizing foreign investment and has given these cities extensive autonomy in dealing with foreign investment for experimental purposes.

\(^{36}\) These are 14 coastal cities which do not have as much as autonomy as the SEZs but have more independent power in dealing with foreign investment than inland cities.

\(^{37}\) Decision of the Third Session of the Sixth NPC on Vesting the State Council with Power to Form Provisional Regulations or Rules on Economic Reform and Open-door Policy, the Chinese version can be found in Dept. of Legislation Supervision and Review, Law Enactment Bureau, the State Council, ed, Selected Chinese Laws on Encouragement of Foreign Investment (Zhong Guo Gu Li Wei Shang Tou Zi Fa Gui Xuan Bian) (Chinese University of Politics and Law, 1987, in Chinese) 3.
The present system of control over foreign investment is a result of the open-door policy. Foreign investment, while it greatly boosted China's economy, has constantly put pressure on the Chinese Government by demanding a more deregulated and less controlled Chinese market. The past experience of foreign investment in China has shown a subtle and delicate process of compromise between the Chinese Government and foreign investors, during which all the parties concerned appeared to be cautious in balancing their mutually beneficial, but yet sometimes conflicting, interests. Today, how to operate successfully in China, taking into account China's difficulties in improving its administrative system (the reform of the system has been noticeably slowed down since the disastrous political set-back of June 1989) is a pressing issue faced by foreign investors in China. By contrast, how to create an appropriate legal climate for the development of foreign-related enterprises, taking into account the policy adjustments which have further strengthened the role of central control (an adverse factor to foreign investment), is a high priority for the Chinese Government which, somehow, still officially clings to its open-door policy. The present administrative system of foreign investment in China bears the marks of all these events.

3.2. Mechanisms for Controlling Foreign Investment in China

3.2.1. Power of the State Council

The controlling mechanisms in China operate at two levels: central and local government. The central Government controls foreign investment through the State Council, responsible Ministries such as the Ministry for Foreign Economic Relations and Trade (MOFERT) and special governmental bodies such as the People's Bank of China. Local governments usually control foreign investment through a special commission set up by provincial or municipal governments, although sometimes a department of a local government deals with foreign investment matters directly.

The State Council does not directly process foreign investment proposals. Its power to control foreign investment is seen in its general and broad delegated legislative power under the Constitution and the special authorization by the NPC. Thus the State Council may regulate foreign investment matters whenever it considers this necessary. No specific delegation is needed as long as the regulations so made are relevant to foreign investment and economic reform and are consistent with the laws of the NPC. A wide discretionary power is thus vested in the State Council.

38 In the sense that the Chinese Government had to give up many conventional practices (such as prohibiting the existence of foreign ownership in the Chinese economy and forbidding the existence of market-oriented pricing) and that foreign investors had to learn Chinese way of business dealings, in particular, to put up with the inefficient and corrupted administration.
The State Council has actively exercised its power with respect to foreign investment. Several important regulations, such as the State Council Provisions concerning Encouragement of Foreign Investment, the Interim Regulations of the PRC Concerning Control of Resident Offices of Foreign Enterprises, and the State Council Regulations Concerning the Balance of Foreign Exchange Income and Expenditure by Sino-Foreign Joint Equity Ventures, have been passed. In addition, the State Council has made various policy statements on foreign investment, such as the Statement of the Spokesman for the State Council on the Policy Concerning Fourteen Newly Opened Coastal Cities, and the State Council Decision on a Better and Faster Development of SEZs.

The power exercised by the State Council to regulate foreign investment is comparable, in some respects, with the power of the federal Treasurer in Australia. Both are policy makers in relation to the administration of foreign investment. But the State Council exercises far broader power, in particular in its delegated legislative power, than its Australian counterpart.

3.2.2. Power of the Ministry for Foreign Economic Relations and Trade to Control Foreign Investment (MOFERT)

3.2.2.1. Introductory

MOFERT is the principal authority of the central Government in charge of the administration of foreign investment. It was created in 1982 as a result of a merger of Ministry of Foreign Trade, Ministry of Foreign Economic Relations, the Foreign Investment Control Commission and the State Import-Export Commission. In relation to examination of foreign investment proposals, the Ministry has similar responsibilities to the Department of the Treasury in Australia, but it differs from

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40 CCH, China Laws for Foreign Business para.7-500.
41 CCH, China Laws for Foreign Business para.6-590.
43 Id. at 84.
44 The State Council in terms of its administrative status is equal to the Cabinet in Australia, in which the federal Treasurer is a member. However, in terms of their capacity to formulate overall policy on foreign investment, the functions of the State Council in China and of the Treasurer in Australia are comparable.
the Treasurer in that it examines proposals itself rather than through an agency such as Foreign Investment Review Board (FIRB). MOFERT has delegated legislative power to make regulations in relation to foreign investment, but does not initiate overall policy on foreign investment, which is within the functions of the State Council.

The power of MOFERT to control foreign investment is granted by various statutes. The Joint Venture Law requires all foreign investment proposals purporting to establish Sino-foreign joint ventures to be approved by the Foreign Investment Commission. Article 5 of the Law on Co-operative Enterprises specifies that all applications to establish Sino-foreign co-operative enterprises are to be submitted for examination to the State Council department in charge of foreign economic relations and trade, which for the time being is MOFERT. The Foreign Enterprises Law states that an application to establish a solely foreign-owned enterprise is to be examined by the State Council department in charge of foreign economic relations and trade, which is again MOFERT.

The statutory criteria under which MOFERT decides whether to approve or reject a foreign investment project are general and broad. In practice, "approval will depend upon the degree to which a joint venture assists the PRC in its modernization". The Joint Venture Regulations set up the following requirements for the establishment of joint ventures:

1. they shall adopt advanced technical equipment and scientific management which enable the increase of the variety of products, the raising of quality and output, and the saving of energy and materials;

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47 Art.3 of the Law. The Foreign Investment Commission was incorporated into MOFERT in 1982. On 5 March 1983, the Standing Committee of the NPC made a Decision, allowing MOFERT to exercise all powers vested in the Foreign Investment Commission under the Joint Venture Law. A Chinese version of this Decision can be found in Dept. of Legislation Supervision and Review, supra note 37, at 7.


50 Art.6.


(2) they shall provide benefits in terms of technical renovation of enterprises and result in less investment, quicker returns and bigger profits;

(3) they shall enable the expanded production of products for export and result in increasing income in foreign currency;

(4) they shall enable the training of technical and managerial personnel. Proposals falling within one of these categories would normally be approved. However, these requirements are not self-evident. Except where the products are to be exported immediately or involve very advanced technology, most proposals would be very much dependent upon the discretions of MOFERT. Terms such as "the raising of quality", "technical renovation", and "enable the training of technical and managerial personnel" are open to varying interpretations. Thus the application of these criteria involves considerable uncertainty. Moreover, not every proposal which superficially satisfies these minimum criteria will be approved. For foreign investors, sometimes these criteria may appear easy to satisfy, sometimes not, depending on the general demand on foreign investment on Chinese markets, and on the availability of the proposed technology in China. The recently approved joint venture between Australian Solar International Holdings and the North China Industries Commission is an example. The venture is a hard resin lenses manufacturer aiming at the Chinese domestic market, presumably the first such venture in China. The technology provided by the Australian company may be advanced but the product itself is not a priority for development in China. No doubt China's great need for foreign investment after June 1989 is the main reason for the approval of this project. Otherwise, China normally does not accept a foreign investment planning to sell to the Chinese domestic market for foreign currency. This is a concession made by the Chinese side, because the Australian company's rights to convert its profits into foreign currency are protected by the Australia-China Investment Protection Treaty.

The Regulations also enumerate specific circumstances under which a proposal can be rejected. In general, MOFERT will reject a proposal if it is satisfied that a proposal falls one of the following situations:

(1) it is detrimental to China's sovereignty;

(2) it is a violation of Chinese law;

53 Id. Art.4.
54 The Australian 1 June 1990.
55 See chapter 7 of the thesis for discussion of the Australia-China Investment Promotion and Protection Treaty.
(3) there is nonconformity with the requirements for the development of China's national economy;

(4) there is obvious inequity in the agreements, contracts and articles of association signed, impairing the rights and interests of one party.66

The authority to interpret these criteria is vested in MOFERT,57 which, however, has not published any official interpretation of these rules so far. Perhaps MOFERT would prefer to keep these criteria at an abstract and general level, so that a broad discretionary power can be exercised by it. Unlike Australia, the Chinese courts do not provide assistance in the interpretation of these criteria. There are two reasons for this. First, the law does not allow an unsuccessful applicant a right to take a court action against the administrative decision of MOFERT. Secondly, assuming nonetheless that a case may be brought to a court, the Chinese court would be reluctant to interpret these criteria because the authority to interpret them literally belongs to MOFERT. The vagueness of these criteria cannot therefore be clarified by resorting to judicial interpretation. Furthermore, even if the court were willing to do so, the validity of its decision would be dubious because a general authority to interpret law rests in the Standing Committee of the NPC rather than in any court.58

Since there is no implementing rule for either the Law on Co-operative Enterprises or the Foreign Enterprise Law, the tests for examining proposals involving these enterprises are even more general and vague. The laws mention briefly that the State encourages the establishment of export-oriented or technologically advanced joint ventures and solely foreign owned enterprises,59 provided that enterprises must be established in accordance with Chinese law and must benefit the development of the Chinese economy.60 Probably, proposals involving these enterprises will be examined by analogy to the criteria set forth in the Joint Venture Regulations, except where wholly foreign owned enterprises are involved. In the latter cases stricter criteria may apply, because solely foreign-owned enterprises are normally expected to export all or most of their products.61

3.2.2.2. Criteria for Decentralizing the Power of Approval

56 Joint Venture Regulations, Art.5.
57 Id., Art.117.
58 The Constitution, Art.67. But the Chinese National Supreme Court may issue circulars with regard to the application of some laws whose construction is not designated to any other bodies.
59 Co-operative Enterprises Law, Art.4, and Foreign Enterprise Law, Art.3.
60 Co-operative Enterprises Law, Art.2, and Foreign Enterprise Law, Art.3.
61 Foreign Enterprise Law, Art.3.
At present, the power to examine foreign investment proposals is considerably decentralized.\(^\text{62}\) Article 8 of the Joint Venture Regulations specify two conditions under which MOFERT may authorize a competent department or a provincial government to approve certain types of investment proposal. First, if an investment proposal falls under the monetary limits prescribed by the State Council and the financial resources of the Chinese participants have been ascertained, the proposal may be approved by a provincial government or an authorized body. Secondly, if no additional allocations of raw materials by the State are required and the national balance of fuel, power, transportation and foreign trade export quota is not affected, the project may be approved by either the Ministry in charge or by a local government. These two conditions are the bases on which the power to approve foreign investment proposals has been decentralized.\(^\text{63}\)

The monetary limits regarding foreign investment, set by the State Council, may be adjusted from time to time. As at the end of 1986, the limits were as follows:

1. Guangdong and Fujian Provinces were allowed to examine proposals with a total investment amount of less than 1 billion Renminbi (RMB). (as on 31 March 1990, US$1 = 3.52 RMB according to China Daily, English Edition)

2. Shanghai and Tianjin Municipalities, which are directly under the central Government, were allowed to review proposals with a total investment amount of less than US $30 million.

3. Beijing, another Municipality directly under the central Government, Liaoning Province, and Dalian (an open port city) were authorized to approve projects involving less than US $10 million in total.

4. Other provinces, autonomous regions, departments belonging to the State Council, and fourteen coastal cities may approve projects which are less than US $5 million in total.\(^\text{64}\)

Although the monetary limits of local jurisdiction over foreign investment were set forth, it is not clear from the language of the Regulations whether a local

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\(^{63}\) However, Moser commented that in practice precisely "what level of approval - local or central - is required for different types of projects has been the source of much confusion for foreign investors". The reason for this confusion, he observed, "lies in the fact that there is as yet no national legislation which comprehensively spells out the approval procedures for investment projects" M.J.Moser, "Foreign Investment in China: the Legal Framework" in Moser ed, Foreign Trade, Investment, and the Law in the People's Republic of China (2nd edn, HK, Oxford University Press, 1987) 90, 91.

\(^{64}\) Zheng, supra note 45, at 262. The thresholds may have been increased or decreased since the data were collected in 1986.
government or a responsible department can examine proposals falling under the prescribed monetary limits on their own initiative, or whether they may so do only with the specified authorization of MOFERT. Article 8 of Joint Ventures Regulations seems to suggest that the power may only be exercised under the express authorization of MOFERT. Moreover, it is not clear whether the authorization is to be granted with regard to a category of proposals or a particular proposal only. Thus literally, MOFERT has a discretion in determining if any local government has power to approve proposals falling within the exempted category under Article 8 of Joint Venture Regulations; or if a given proposal is to be referred to other departments or local governments for examination. The uncertainty in the legislation is echoed by the uncertainty shown in the practice of local governments. For instance, some local governments in the SEZs and open coastal cities have stated in their local legislation that foreign investors may apply directly to the local Administration Commission or the government for approval of a business within the jurisdiction of the local government concerned, without specifying the type and conditions of the proposals they may examine. These local regulations may not conform with the conditions set forth in the Joint Venture Regulations.

3.2.3. Power of Other Departments and Statutory Bodies to Control Foreign Investment

Other governmental departments and bodies may also give approval to foreign investment proposals falling within their jurisdiction as determined by statute or authorized by MOFERT. For example, according to Art. 4 of the Interim Regulations of the PRC Concerning the Control of Resident Office of Foreign Enterprises, a banking or insurance institution intending to establish an office in China must seek approval from the People's Bank of China, a maritime shipping operator or maritime shipping agent must apply to Ministry of Communications, an air transport enterprise to the General Administration of Civil Aviation, and other enterprises to the competent Commissions, Ministries or Bureaus.

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65 Article 8 states that the establishment of a joint venture must be approved by MOFERT; however, MOFERT may entrust local governments or competent Departments of the central Government to examine and approve proposals which satisfy conditions set forth in this Article.

66 For example, Provisional Measures on Application and Registration Administration for Economic and Technological Development and Construction Enterprises of Beihai Municipality, CCH, China Laws for Foreign Business para. 82-016, Art.2; and Measures of the Dalian Economic and Technological Development Zone on the Administration or the Registration of Foreign Investment Enterprises, CCH, China Law for Foreign Business para. 83-003, Art.3.
A competent Ministry or other government body may formulate detailed rules for implementing the laws of the NPC and regulations of the State Council. There are several ways in which specific rules can be made. First, a Ministry may make detailed rules under an express authorization by either the NPC or the State Council. For example, Article 33 of the Provisional Regulations for Foreign Exchange Control of the PRC,\(^67\) issued by the State Council, states that detailed rules for implementation of the Regulations should be formulated by the State Administration of Exchange Control (SAEC). Under this authorization SAEC passed, for instance, the Rules for the Implementation of Foreign Exchange Control Relating to Foreign Representation in China and their Personnel.\(^68\)

Secondly, a Ministry may make rules under an implied authorization. For instance, the State Administration for Industry and Commerce (SAIC) passed the Provisional Regulations on the Confirmation and Handling of Invalid Economic Contracts,\(^69\) in pursuance of Art.51 of the Economic Contract Law of the PRC,\(^70\) which authorize SAIC to supervise and examine economic contracts, and to establish a system of control. It may thus be argued that the Regulations are the exercise of the power to establish a system of control.

Thirdly, a Ministry may make rules on its own initiative provided that the rules so made are consistent with the Constitution and the relevant laws and regulations. The Regulations of the PRC on the Financial Control of Sino-Foreign Joint Equity Enterprises\(^71\) and the Provisional Measures of the People's Bank of China on Foreign Exchange Secured Reminbi Loans for Foreign Investment Enterprises\(^72\) are examples. The former was made by the Ministry of Finance allegedly pursuant to the Joint Venture Law, which, however, does not give any hint of the authorization alleged by the Ministry. The latter was made allegedly in pursuance of the State Council Regulations Concerning Encouragement of Foreign Investment, which too does not clearly authorize the People's Bank of China to make the Measures.\(^73\) It seems that the two bodies assumed power to make the relevant

\(^{67}\) CCH, China Laws for Foreign Business para 8-550.
\(^{68}\) CCH, China Laws for Foreign Business para.8-590.
\(^{69}\) These regulations set forth specific rules on how to deal with contracts which are deemed to be void under the Contract Law. CCH, China Laws for Foreign Business para.5-560.
\(^{70}\) CCH, China Laws for Foreign Business para.5-500.
\(^{71}\) CCH, China Laws for Foreign Business para.6-598.
\(^{72}\) CCH, China Laws for Foreign Business para.8-694.
\(^{73}\) Rather Art.17 of the Regulations demands generally that governments at various levels should improve their efficiency in the administration of foreign investment. The only article concerning the People's Bank of China is Art.14, which authorizes
regulations on their own initiative. This is allowed in the Chinese legal system as long as the regulations so made are not in the contravention of the Constitution and relevant laws.

3.2.4. Power of Local Authorities to Control Foreign Investment

3.2.4.1. Introduction

Every province, autonomous region, municipality directly under the central Government and designated open city or special economic zone has its own foreign investment control authority, operating under various names. These authorities are government bodies. Their powers to control foreign investment are derived from the authorization of the central Government, which delegates power to local governments either by legislation or policy statements, as the case may be. For example, the Regulations of the PRC on Special Economic Zones in Guangdong Province establish the SEZs for foreign investment and set up a Provincial Administration of the Special Economic Zones which manages foreign investment on behalf of the Guangdong Provincial Government. The State Council Regulations for the Encouragement of Investment in the Development of Hainan Island grant greater autonomy to the Hainan Government in approving and managing foreign investment on the Island. These two laws respectively form the basis for the Guangdong and Hainan Governments to administer foreign investment in their local areas. Other local governments are given power to control foreign investment within their jurisdiction to different degrees by the State Council through administrative measures, which often take the form of State Council approval of applications for opening the local economy to foreign investment, filed by the local government. The authorization through executive order is an extension of the State Council statutory power to control foreign investment.

According to the extent of the openness and the degree of the local government's autonomy, the investment climate in China varies. The SEZs and Hainan Province are the areas where the least restrictions exist, followed by the fourteen coastal cities which are given more autonomy in dealing with foreign
investment than other areas of the country. The investment climate in the rest of the country depends upon the attitude of the local governments and the power to examine foreign investment given to them by the central Government.

3.2.4.2. Local Legislation in SEZs

The SEZs are Shenzhen, Zhuhai, Shantou, and Xiamen. In April 1980, the Guangdong Provincial Administration of Special Economic Zones was set up under the Regulations of the Standing Committee of the NPC. Shenzhen, Zhuhai and Shantou are consequently subject to the unified control and direction of this Provincial Administration. Xiamen was approved by the central Government as an SEZ eight months later, although no special law confirming the approval has been passed by the central Government. This suggests the variety of Chinese practice in the administration of foreign investment. Law and regulations on foreign investment in Xiamen have been passed by both the Fujian Provincial People's Congress and Xiamen Municipal Government. In 1986, the Xiamen Municipal Leading Group of Foreign Investment was established by the Xiamen Municipal Government for the purpose of coordinating foreign investment matters. However, investment proposals are still subject to examination by the responsible Departments of the Xiamen Government.

The SEZs provide special treatment to foreign investors. This includes the local government's freedom to give approval to projects involving a relatively large amount of money; lower income tax rates, longer tax-exempt and tax-reduced

79 The first three are situated in Guangdong Province and the last in Fujian Province. For a general discussion of SEZs, see E.Pow & M.J.Moser, "Law and Investment in China's Special Investment Areas" in Moser ed, Foreign Trade, Investment, and the Law in the People's Republic of China (2nd edn, HK, Oxford University Press, 1987) 199.
80 People's Daily, supra note 42, at 920.
81 Regulations of Xiamen SEZ for the Improvement of Its Foreign Investment Climate CCH, China Laws for Foreign Business para.76-519, Art.1.
82 In December 1990 the enterprise income tax was only 15%. Provincial Regulations on Reduction and Exemption of Enterprise Income Tax and Consolidated Industrial and Commercial Tax for the Fourteen Coastal Cities and SEZs China Laws for Foreign Business para.70-845, Div.1, Art.1.
periods which are available to exporting enterprises, technologically advanced enterprises, enterprises engaged in industry, communications and transport, forestry, agriculture and animal husbandry, and companies investing US $5 million or more in service industries for a period of more than ten years. As a result of this special treatment, the total output value of SEZs in 1986 was said to be US $1.84 billion.

3.2.4.3. Concurrent Power of Central and Local Governments

Local governments at various levels have on occasion exercised concurrent power to regulate foreign investment in SEZs. For example, of the 16 laws and regulations uniformly operating within Shenzhen, Zhuhai and Shantou SEZs in December 1990, one was approved by the Standing Committee of the NPC; two

83 An exporting enterprise is, as described by Chinese law, an enterprise "whose products are primarily exported and which have a foreign exchange surplus after deduction from their total annual foreign exchange income their annual operational foreign exchange expenditure and the foreign exchange required to remit dividends earned by foreign investors". (State Council Regulations 1986, Art.2(1)). If such enterprises invested in industry, communications and transport, agriculture, forestry and animal husbandry in SEZs for a period of more than five years, they are entitled to a two-year tax holiday commencing from the first profit-making year and a 50% tax reduction for three years following the tax holiday. After expiration of these tax free and reduced periods, an exporting enterprise enjoys a 50% tax reduction in any year in which its exporting value amounts to 70% or more of its annual product output. But the lowest tax rate applicable to exporting enterprises after the reduction is 10% of enterprise income.

84 A technologically advanced enterprise is an enterprise "in which a foreign investor provides advanced technology to develop new products or upgrade products, increasing export and generation of foreign exchange or replacing imports". (State Council Regulations 1986, Art.2(2)). If invested in industry, Communications and transport, agriculture, forestry and animal husbandry in SEZs for a period of five year or more, such enterprises are not only given the same tax holiday and tax-reduced period as those given to exporting enterprises, but also allowed an additional three years of tax reduction at a rate of 50%. The 10% lowest tax rate also applies to technologically advanced enterprises.

85 Enterprises engaging in these sectors are given a two-year tax holiday and three years of 50% tax reduction, beginning from the first profit-making year.

86 These enterprises are given one-year tax holiday and two year tax reduction at a rate of 50%.


88 These three cities also have their own local regulations on foreign investment, which are operative only within each of these cities.

89 As collected in CCH, China Laws for Foreign Business.

90 Regulations of the PRC on SEZs in Guangdong Province, CCH, China Laws for Foreign Business para.70-800.
were made by the State Council;\(^{91}\) one was approved by the State Council and promulgated by the General Administration of Customs;\(^ {92}\) five were passed by the Standing Committee of the Provincial People's Congress;\(^ {93}\) four were made by the Provincial Government;\(^ {94}\) one was approved by the Provincial Congress and promulgated by the Provincial Government;\(^ {95}\) one was formed by the Department of Finance of Guangdong Government;\(^ {96}\) and one was promulgated without clearly indicating the authority which made the Regulations.\(^ {97}\) The ambit of concurrent power is thus not clear. Does this mean that all powers in relations to the regulation of foreign investment in SEZs (or any province) are concurrent? Or is there any matter which can be regulated only by a special authority or a government at a particular level? The Chinese Constitution fails to address these issues at all, and in practice a considerable amount of discretion appears to be exercised by local governments, in particular Provincial Governments, in relation to who should

\(^{91}\) Provisional Regulations on Reduction and Exemption of Enterprise Income Tax and Consolidated Industrial and Commercial Tax for the Fourteen Coastal Cities and the SEZs, CCH, China Laws for Foreign Business para.70-845; and Regulations Governing Foreign Banks and Joint Chinese-Foreign Banks in SEZs, CCH, China Laws for Foreign Business para.70-850.

\(^{92}\) Regulations of the General Administration of Customs of the PRC Governing Control of Goods, Means of Conveyance, Luggage and Postal Articles Entering or Leaving SEZs, CCH, China Laws for Foreign Business para.70-861.

\(^{93}\) Provisional Regulations on the Registration of Enterprises in SEZs of Guangdong Province, CCH, China Laws for Foreign Business para.70-820; Interim Entry and Exit Regulations for SEZs in Guangdong Province, CCH, China Laws for Foreign Business para.70-840; Regulations on Trade Unions in Enterprises in SEZs in Guangdong Province, CCH, China Laws for Foreign Business para.70-855; Regulations on Foreign Related Companies in SEZs in Guangdong Province, CCH, China Laws for Foreign Business para.70-865; Labour Regulations Governing SEZs in Guangdong Province, CCH, China Laws for Foreign Business para.70-885.


\(^{95}\) Regulations for Control of Accounting of Foreign Related Enterprises in SEZs in Guangdong Province, CCH, China Laws for Foreign Business para.70-858.

\(^{96}\) Provisional Regulations of Guangdong Province on Several Issues Concerning the Financial Administration of Sino-Foreign Joint Equity Enterprises, CCH, China Laws for Foreign Business para.70-877.

\(^{97}\) Regulations of Guangdong Province on Labour Management in Foreign Investment Enterprises, CCH, China Laws for Foreign Business para.70-887. Presumably the Regulations were made by the Provincial Government.
regulate what. As a result, confusion arises in deciding when the local legislature should act and when the local executive should. In addition, confusion is also found in the practice of approving a law by one authority and promulgating it by another. The Constitution does not require such a procedure when it grants law-making power to the State Council,98 Departments of the central Government,99 or local governments,100 except in the cases of local governments in autonomous regions.101 No attention has been given to these issues in Chinese constitutional law studies.

The practice of exercising concurrent power and the resultant confusion with respect to who has power to regulate what can also be found in the laws and regulations effective within each city of the SEZs in Guangdong Province. Of the 18 local regulations operating as at December 1990 in Shenzhen,102 six were made by the provincial authorities, either the Congress or Government;103 eight were passed by Shenzhen Municipal Government;104 one was approved by the Guangdong Provincial Government and promulgated by Shenzhen Municipal Government;105 one was made by the Shenzhen Branch of the People's Bank of China;106 and two by Kowloon Customs.107 Of the three local regulations effective as at December 1990 in Zhuhai city,108 2 were made by the Municipal Government,109 and one was approved by the General Administration of Customs and promulgated by the Gongbei Customs.110 Of the two local regulations operating in Shantou city as at

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98 Art.89.
99 Art.90.
100 Arts.99, 100, & 107.
101 Art.116.
102 As collected in CCH, China Laws for Foreign Business.
103 The names of these regulations are omitted. For details, see CCH, China Laws for Foreign Business paras.73-500, 73-505, 73-510, 73-516, 73-521 & 73-540.
104 For details, see CCH, China Laws for Foreign Business paras.73-511, 73-519, 73-524, 73-527, 73-528, 73-529, 73-544 & 73-547.
105 For details, see CCH, China Laws for Foreign Business para.73-513.
106 For details, see CCH, China Laws for Foreign Business para.73-530.
107 One was approved by the General Administration of Customs and promulgated by Kowloon Customs, see CCH, China Laws for Foreign Business para.73-535, and the other was formed by the Kowloon Customs alone, see CCH, China Laws for Foreign Business para.73-537.
108 As collected in CCH, China Laws for Foreign Business.
109 For details, see CCH, China Laws for Foreign Business paras.74-500 & 74-504.
110 See CCH, China Laws for Foreign Business para.74-528.
December 1990,\textsuperscript{111} one was made by the Municipal Government,\textsuperscript{112} and the other was approved by General Administration of Customs and promulgated by the Shantou Customs.\textsuperscript{113} As this suggests, the subject matters regulated by the provincial and municipal governments overlapped,\textsuperscript{114} and it is difficult or even impossible to draw a boundary between provincial legislative power and municipal legislative power by reference to the matters concerned.

3.3. Sectors Open to Foreign Investors

The sectors open to foreign investors suggest the types of foreign investment proposals likely to be approved in China. Unlike the sectors specified in the Australian policy, which suggest the areas where control has been imposed, the sectors open to foreign investors in China indicate the areas in which government control has been relaxed. In another words, in Australia control does not exist in sectors which are not specified by laws and policies, whereas in China control has been eased in specified sectors and areas but not in the areas unspecified.

The sectors open to foreign investors are largely determined by the law of the central Government. But in some cases local legislation has to be considered when investing in a Province, city or zone, because local governments may set up their own preferential priority for developing certain sectors. Article 3 of the Joint Venture Regulations enumerates the following sectors of the economy in which joint ventures are encouraged:\textsuperscript{115}

(1) development of energy resources and construction materials, and chemical or metallurgical industries;

(2) machine manufacture, instrument and meter industries, and manufacture of equipment for off-shore oil exploitation;

(3) electronics, computers and manufacture of communication equipment;

(4) light, textile, foodstuffs, medicine and medical apparatus and packaging industries;

\textsuperscript{111} As collected in CCH, China Laws for Foreign Business.

\textsuperscript{112} See CCH, China Laws for Foreign Business para.75-100.

\textsuperscript{113} See, CCH, China Laws for Foreign Business para.75-104.

\textsuperscript{114} For instance, the Provincial Congress promulgated the Regulations of the Shenzhen SEZ on Land Management in 1987, CCH, China Laws for Foreign Business para.73-500; but the Shenzhen Municipal Government already in 1984 made the Measures on Readjusting Land Use Fees and Preferential Reduction of and Exemption from Land Use Fee in Shenzhen, CCH, China Laws for Foreign Business para.73-519. The two laws overlapped over some matters.

\textsuperscript{115} A Sino-foreign co-operative enterprise and a solely foreign owned enterprise are expected to refer to this law for guidance, because as at December 1990 no special rule has been made for them.
(5) agriculture, animal husbandry and aquaculture;
(6) tourism and service industries.\textsuperscript{116}

It is clear from these categories that some sectors of the economy, such as civil aviation (domestic airlines), radio, television, newspapers, insurance, banking and financial institutions are generally closed to foreign investment. But since 1985, foreign banks or joint Sino-foreign banks are allowed to operate in the SEZs,\textsuperscript{117} and also in Hainan Island in 1988.\textsuperscript{118} Although education and public health are specified in the Regulations, it is possible that proposals in these areas might be allowed by some local governments within the SEZs or Special Economic and Technological Zones (also known as Open Port Cities or Open Coastal Cities). For example, in the regulations concerning land used by foreign-related enterprises in Xiamen and Dalian city, the land used for the purpose of education and public health is mentioned.\textsuperscript{119}

Given the variety of the practices, it is necessary for a foreign investor to consult both the central and local governments if he is interested in investing in sectors which are not specified by law.

It is a common feature of Chinese law and policy that the rules regarding the sectors open to foreign investors, and the conditions for approval or disapproval of a foreign investment proposal, are often abstract and general. The governments at every level have discretions in the application of these rules. The flexibility resulting from discretions enables the administrators to interpret the rules broadly according to whatever policies are decided, but may pose difficulties for foreign investors who are not so familiar with the Chinese legal tradition, its bureaucratic system and culture. Foreign investment can thus be discouraged because of the unpredictable application of these rules. An effort to define the rules and policy more clearly and specifically seems to be in China's interests.

\textsuperscript{116} Joint Venture Regulations, Art.3.
\textsuperscript{117} Regulations Governing Foreign Banks and Joint Chinese-Foreign Banks in the Special Economic Zones of the PRC, CCH, China Laws for Foreign Business para.70-850.
\textsuperscript{118} State Council Regulations on Hainan.
\textsuperscript{119} Article 6(5) of Regulations for the Administration of Land Use in the Xiamen Special Economic Zone states that the land use period for projects involving education, public health, scientific research and cultural purposes is sixty years. CCH, China Laws for Foreign Business para.76-503. Article 12 of Measures of the Dalian Economic and Technological Development Zone on the Administration of Land Use states that the land use fee for the land used for educational, scientific research, cultural, medical treatment or hygiene purposes shall be reduced in accordance with the actual circumstances. CCH, China Laws for Foreign Business para.83-012.
3.4. Application Procedures

In China, application procedures for joint Sino-foreign ventures and for wholly foreign owned enterprises differ according to the type of venture involved. In the case of a joint venture, the procedures for applications are stipulated by law and the foreign participant should always rely on the Chinese participants to apply for approval. In the case of a wholly foreign-owned enterprise, the application procedures are not specified by law and may be followed by analogy to the procedures for a joint venture. However, the foreign investor must apply in person.

The application procedures described by Article 9 of the Joint Venture Regulation consist of two steps. First, the Chinese participant in a joint venture must submit to the responsible governmental department to which it belongs a report on the proposed project and a preliminary study. After the report has been approved, the participants in the project may proceed with their discussion and enter into an agreement, contract, or articles of incorporation. Secondly, the Chinese participant in the project must submit formal documentation (including an application for the establishment of the enterprise, a feasibility study, the agreement or contract, the names of the director or deputy directors, and a written opinion given by the department in charge or the provincial government concerned, in which the proposed enterprise will be located) to MOFERT or another appropriate authority. Evidently, Chinese participants are required to take the responsibility for applications.

The time allowed for this application is three months. A competent authority must make a decision within three months after receiving the complete application. However, Chinese law does not specify what is the effect of the application when the time limit has expired. Thus, it is not clear whether a proposal is deemed to be approved if an authority fails to make a decision within the three-month period. Given the reluctance of the Chinese Government to specify clearly the effect of the application after the termination of the time limit, the application probably should not be regarded as having been approved automatically, even if the official time limit has elapsed.

120 For discussion of the approval procedures, see Moser, supra note 63, at 91-4.
121 In the Chinese economic system, State-owned enterprises are controlled by government departments at a municipal, provincial and central level. In turn, each enterprise controlled by a local authority can always trace its ultimate superior at the central Government level.
123 Joint Venture Regulations, Art.10.
3.5. Delegated Power and the Administration of Foreign Investment

3.5.1. Introduction

Constitutional issues in relation to the administration of foreign investment in China have not received much consideration in the literature on Chinese foreign investment law. Considerable attention has been given to the development of the Chinese legal framework for foreign investment, but little to the constitutional implications of these foreign investment laws and regulations, whether enacted by central or local governments. As have been seen, the State Council has formulated large volumes of regulations with respect to foreign investment, but the ambit of the State Council's power to regulate foreign investment has not yet been clearly defined. In addition, the status of local legislation, which makes up about half of the existing foreign investment laws and regulations in China, and the relationship between the central and local governments with respect to the regulation of foreign investment, are issues not yet considered in detail by Chinese or foreign legal scholars. For the purposes of comparison with the administration of foreign investment in Australia, this chapter will discuss these issues. Moreover, other issues, such as the process of delegating or re-delegating powers within the hierarchy of the government and its constitutional implications, as well as the impact of local legislation on the development of national laws on foreign investment, will also be discussed.

3.5.2. Hierarchical Power Structure in the Constitution

The sub-delegation of delegated power to other bodies by the State Council is a common practice in China, where the central government has ultimate supremacy over local governments, and the executive branch, at both central and local levels, has been given extensive powers to make delegated legislation. Power can be delegated to subordinate governmental organs by the State Council within the limits of its authority, which is vaguely defined in the Constitution but was explicitly reinforced by Decisions of the NPC in 1986.

The Chinese Constitution contains a hierarchical power structure in the State system. Three levels of legislative power exist in China: the NPC and its Standing Committee, the State Council, and local governments. There are also vertical and horizontal connections within the power sharing structure. In general, the NPC and

124 For example, neither of the two most recently published books on Chinese commercial and investment law, H.R. Zheng, China's Civil and Commercial Law (Singapore, Butterworths, 1988), and G. Wang, China's Investment Laws: New Directions (Singapore, Butterworths, 1988), gives appropriate attention to the constitutional issues with respect to foreign investment law in China.

125 Dept. of Legislation Supervision and Review, supra note 37, at 3.
its Standing Committee exercise the highest legislative power nation-wide.126 At the
next level, the State Council may make administrative orders and regulations in
accordance with the Constitution and the laws of the NPC and its Standing
Committee,127 and Ministries or statutory bodies may issue orders and rules within
the limits of their authorities given by the NPC or the State Council.128 At the
third level, Provincial People's Congresses may pass local legislation provided that it
is consistent with the Constitution, the laws of the NPC and regulations of the State
Council;129 and in addition, provincial governments may, for the purposes of
administering their local affairs, issue decisions and orders provided that the
regulations so made are consistent with the law of the central Government.130 The
power of local governments to pass local laws and regulations in relation to the
administration of local affairs extends to a county government.131 These
arrangements suggest a vertical connection within the hierarchy. In other words,
throughout China a government at a higher level has prevailing authority over a
government at a lower level.132 Accordingly, the State Council may delegate its
power to regulate foreign investment to its Ministries and local governments.

On the other hand, there is a horizontal connection as well. This connection
can be seen within every level of the governmental administration, such as central,
provincial and county governments. No matter how many levels exist, the
legislature always in theory has higher authority than the executive at the same level.
The relationship between the legislature and executive is illustrated by several
features. First, the Premier and the members of the State Council (including Vice­
Premiers, State Councillors, Auditor-General and the Secretary-General) must be
appointed or approved by the NPC.133 Secondly, the Standing Committee of the
NPC supervises the work of the State Council and has power to annul State Council
regulations and orders.134 Thirdly, a local People's Congress may appoint and
remove the heads of the local government (governors, mayors, or heads of a county
government)135 and thus the local government is accountable for the local People's

127 The Constitution, Art.89.
128 The Constitution, Art.90.
129 The Constitution, Art.100.
133 The Constitution, Art.110.
134 The Constitution, Art.62(5).
135 The Constitution, Art.67(7).
Congress. The horizontal connection suggests that regulations made by a local executive government must be subject to the supremacy (not necessarily authorization) of the local legislature at the same level, whose power is in turn, virtually, subject to the supremacy of the central Government. But the Constitution does not address the hypothetical situation where a local executive government makes regulations in contravention of the law of the local legislature that had passed the law in contravention of a central Government law. Whether the inconsistency of a local law passed by a local legislature with the law of the central Government allows a local executive a power to make regulations, which are contrary to the local law but consistent with the law of the central Government, is an issue which has not been considered in Chinese law.

3.5.3. Conditional Legislative Power of the State Council

The power of the State Council includes both executive and legislative power which may be regarded as a "conditional" legislative power in the sense that the power is vested in it on certain conditions by the Constitution. This "conditional" legislative power (though the power is almost too wide to be regarded as conditional in a strict sense) can perhaps be regarded as an equivalent to delegated legislative power in Australian law. Compared with the Australian Government, the Chinese Government exercises a wider delegated legislative power. The width of this power is also evidenced by the fact that the regulations or decisions of the State Council are regarded as a source of law in China. The only limit on the delegated legislative power is that the regulations must accord with the Constitution and laws of the NPC. This abstract and flexible restriction can at most be interpreted as that no regulations of the State Council may contravene the Constitution and the existing laws of the NPC and its Standing Committee. Accordingly, the State Council may always justify its regulations when the NPC has not passed a law with regard to the matter

136 Ibid.
137 The condition is that the rules and regulations made under this power cannot contravene the Constitution and the laws of the NPC and its Standing Committee.
138 Evidently, the State Council may exercise a general executive power to issue orders and documents which are not rules of law. The Constitution fails to distinguish when the State Council is exercising delegated legislative power and when it is exercising executive power. A discretion is left to the hands of the State Council.
139 This restriction becomes obscure when regulations of the State Council concern issues which have not been clearly dealt with in the Constitution and law of the NPC. For example, Art.18 of the Constitution in a broad term allows foreign investors operate in China; thus no real restriction is imposed in this Article and any State Council regulations dealing with foreign investment issues which have not been dealt with by the NPC can be justified.
deal with by the State Council, because if the condition "in accordance with the Constitution" applies, the Constitution has granted the "conditional" legislative power to the State Council, and if the condition "in accordance with the law" applies, there is no law prohibiting the State Council from doing so.

The conditional legislative power of the State Council is "constitutional" in the context of the Chinese Constitution, where neither the doctrine of the separation of powers as adopted in the United States nor the modified Westminster model of responsible government as adopted in Australia applies. While recognizing the ultimate supremacy of the legislature in theory, the Chinese Constitution rejects a strict separation of power between the legislature and executive. The alleged supremacy of the NPC is supported by two arguments: first, that the NPC is the highest power of the State; and secondly, that the Constitution and laws, both made by the NPC, prevail over regulations of the State Council and of local governments. The question whether or not these arrangements have effectively protected the alleged supremacy of the NPC in China is a matter which goes beyond the scope of this thesis, although the answer must be negative. However unsatisfactory the basic constitutional principles in the Chinese Constitution are, the State Council exercises an extensive and discretionary power with respect to the administration and regulations of foreign investment, as the present Constitution stands.

3.5.4. Delegated Power of Other Departments

Governmental Departments, such as MOFERT, and special bodies, such as the State Administration of Industry and Commerce (SAIC), may exercise power to regulate foreign investment pursuant to the authorization by the NPC or its Standing Committee, and the State Council. The rules, regulations and orders so made are recognized legal norms, although they are subordinate to the law of the NPC and regulations of the State Council. Unlike the State Council's power to regulate foreign investment, the power of various governmental Departments or bodies is relatively certain and specific. It is usually exercised pursuant to a special authorization of the

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140 The Westminster model of the responsible government has been modified in the sense that the model has been applied to a federal system, rather than a unitary state system like England, where the model was created.

141 Art.57 of the Constitution states that the NPC is the highest authority of the State power.

142 The supremacy of the legislature is dubious. The NPC has been obviously and decisively influenced, if not controlled, by the Chinese Communist Party and the State Council. An example of such connection between the NPC and the Party can be seen in the events taken place following the nation-wide crack-down on the pro-democracy moment in China. In June 1989, while Martial Law was still in force in Beijing, the NPC passed a law prohibiting any pro-democracy demonstration pursuant evidently to the Party's policy.
NPC or the State Council, but has occasionally been exercised on a Department's own initiative.\textsuperscript{143} The dependence of the power on the authorization by the NPC or the State Council is the reason why in this thesis the power is called a "delegated power", one which bears similarities to delegated power in Australia.

Rules of Departments and other bodies are usually made for assisting the implementation of the laws of the NPC or regulations of the State Council. For example, the Provisional Regulations of SAIC on the Confirmation and Handling of Invalid Economic Contracts were made by SAIC, the Commission in charge of the administration of industrial and commercial enterprises, for the purposes of implementing the Economic Contract Law passed by the NPC. The Provisional Measures of the People's Bank of China on Foreign Exchange Secured Renminbi Loans for Foreign Investment Enterprises were intended to assist in the implementation of the State Council Regulations Concerning Encouragement of Foreign Investment. Sometimes these rules give detailed interpretations of the laws of the NPC and regulations of the State Council. Detailed Rules of SAEC on Violation of Foreign Exchange Control are such an example.\textsuperscript{144}

In Chinese practice, the State Council often authorizes other Departments\textsuperscript{145} or local governments\textsuperscript{146} to develop detailed rules for the implementation of its regulations. In the sense of delegating power, the State Council exercises similar power as the NPC. This is another feature of delegated power in China.

3.5.5. Local Legislative Power In Relation to Foreign Investment

In this thesis, local legislative power refers to the power exercised either by local legislatures or executives. It is limited by the principle that the laws so made must be consistent with the Constitution, the law of the NPC and regulations of the State Council. However, this limitation seems rather too abstract and loose, and thus doubtful. First, like legislative power exercised by the central executive, the authorization of legislative power to the local executive is not specific and

\textsuperscript{143} The Constitution states ambiguously that the Departments should form rules in accordance with the authorization. The expression "in accordance with" (gengju) in Chinese means either "pursuant to a specific authorization" or "in pursuance of the principles (not direct authorization) of a relevant law". Some Departments have on occasion formulated rules without having a direct authorization from the NPC and State Council.

\textsuperscript{144} CCH, China Laws for Foreign Business para.8-675.

\textsuperscript{145} e.g. the State Council authorizes SAEC to form detailed rules for the implementation of the Exchange Control Regulations.

\textsuperscript{146} e.g. the State Council implicitly directs local governments to formulate relevant rules or measures for implementing its Regulations Concerning Encouragement of Foreign Investment.
certain. Secondly, a local executive may exercise legislative power pursuant to the laws of the central Government, the laws of a superior government or the law of the People's Congress at the same level. Accordingly, the Shenzhen Municipal Government has made rules in pursuance of either the law of the central Government, or of the law of the Guangdong Provincial Government or Congress. Thus the restriction on the exercise of local legislative power appears to be too wide to be an effective restriction.

The ambit of local legislative power with respect to the regulation of foreign investment raises constitutional problems. First, the scope of local legislative power, in particular the subject matters to be legislated for, is not clearly defined. Thus local legislation has on occasion exempted foreign investors from taxes which are subject to the regulations of the central Government. Secondly, like the power of the State Council and other Departments in some circumstances, the authority of some local legislation is not unambiguous. Many local governments claim that the local regulations were made in accordance with applicable laws and regulations, but often without specifying which laws or regulations have granted the authorization. In the first case, a local government may well exceed its specific or general authorization. In the second case, a local government frequently does not have specific authorization to make laws, and has to rely on the general and vague authorization in the Constitution.

There is no basis for a local government to exceed its jurisdiction over subject matters in regulating foreign investment, in particular giving excessive tax concessions to foreign investors. This is an abuse of local legislative power and cannot be justified by even vaguely phrased constitutional language. Such an abuse of power mostly occurs in the course of allowing preferential tax treatment to foreign investors, but sometimes arises when a local government makes new regulations which do not have any basis in the law of the NPC, or even worse contravene the law of the NPC. The main taxes, such as the Joint Venture

147 For example, the Standing Committee of the NPC has authorized the People's Congress in Guangdong and Fujian Provinces where SEZs are situated in broad terms to formulate rules and regulations on SEZs. People's Daily, supra note 42, at 921.
148 e.g. Implementing Measures of the Shenzhen SEZ on Individual Income Adjustment Tax, CCH, China Laws for Foreign Business para.73-528.
149 e.g. Detailed Implementing Rules of the Shenzhen SEZ on Land Registration and the Issue of Certificates, CCH, China Laws for Foreign Business para.73-547.
150 For example, Measures of the Dalian Economic and Technological Development Zone for the Administration of Economic Contracts Involving Foreigners, CCH, China Laws for Foreign Business para.83-006.
151 For example, Guangdong Provincial People's Congress passed Regulations on Foreign Related Companies in the Special Economic Zones in Guangdong Province, CCH, China Laws for Foreign Business para.70-365. But as at December 1990, the
Income Tax, Foreign Enterprise Income Tax, Individual Income Tax, Consolidated Industrial and Commercial Tax and Urban Real Estate Tax are subject to the national legislation. The others, such as Vehicle and Vessel License Plate Tax, a national tax whose rate is fixed by provincial governments with the approval of the central Government, may be regulated by local governments. But the exemption of foreign investment enterprises from the national taxes must be a matter for the central Government to decide. Local governments may do so only if authorized by the central Government. Thus many existing local preferential tax treatment that exceed the limits of local jurisdiction are virtually unconstitutional.

But unconstitutionality does not automatically render these questionable local regulations unenforceable. Many of these local regulations are still operative within the jurisdiction of the local governments, although the Chinese Constitution states that the Standing Committee of the NPC and the State Council may annul local legislation which is contrary to national law. Probably due to practical difficulties, such as the rapidly growing volume of local laws, the insufficient number of personnel in charge of legislative review, and the well-known inefficiency of the Chinese administration, some questionable local laws are virtually not touched, although the State Council issued a statement in 1989 announcing that all preferential treatment inconsistent with laws of the central Government was void. In this situation, the responsibility for checking the validity of local laws seems to rest on foreign investors themselves. Whether any remedy exists for possible losses suffered by a foreign investor under the influence of a constitutionally invalid local legislation is a question which has not been tested in any Chinese court.

The central Government's attitude to local laws contravening national law has been inconsistent. Some local laws, though they infringed upon areas prohibited by

NPC has not passed any comprehensive company Act apart from disparate laws on joint ventures and solely foreign-owned enterprises.

152 CCH, China Laws for Foreign Business para.33-500.
153 CCH, China Laws for Foreign Business para.32-500.
154 CCH, China Laws for Foreign Business para.30-500.
155 CCH, China Laws for Foreign Business para.31-500.
156 CCH, China Laws for Foreign Business para.39-500.
157 CCH, China Laws for Foreign Business para.34-500.
158 Art.67(8).
159 Art.89(14).
160 It was reported that the State Council in January 1989 passed a resolution, stating that the national taxation law must be strictly observed and that local tax laws inconsistent with the national laws are void. see People's Daily, (English Edition) 7 Jan.1989.
the Constitution or national law, were first tacitly accepted, then expressly adopted, resulting in the amendment to the Constitution. The transfer of land use rights is an example. But some local laws which are deemed to be inconsistent with national laws, such as above-mentioned local preferential tax treatment, have at least in theory been rejected by the central Government.

The vague provisions of the Constitution on the power of local governments to make rules of law sometimes do not provide sufficient direction in deciding whether a particular local law is constitutional or not. This is particularly true when a new area of law is involved. Presently, takeovers involving private or foreign companies have not been regulated by the central Government. But the Guangdong Provincial People's Congress has passed the Regulations on Foreign Related Companies, the first of this type of law in China, governing takeovers and mergers between foreign, joint enterprises and private businesses. It is difficult to judge the constitutionality of this law in the context of the Constitution and national laws, because the latter do not address these issues. In effect, the central Government has again given its tacit consent. It may well be that the local law will once more lead to a new development of the national law in the area of company regulation.

161 Land use rights were first allowed to transfer in Shenzhen, when the Constitution of China still prohibited the transfer of land between private parties. But the central Government did not challenge the theoretically illegal regulations of Shenzhen. Rather it gave an acquiescence to the Shenzhen Government. Eventually, the Constitution was amended in 1988, allowing land use rights be transferred between private parties.
Chapter 4. Executive Power and Foreign Exchange Control

4.1. An Overview

Foreign exchange, as the term suggests, refers to foreign currency used as a medium of payment in international trade. For historical, political, and more importantly economic reasons, only the currencies of a few industrialized countries are generally accepted as a medium of payment in international trade. As a result, countries which must purchase the so-called hard currency of other countries to pay for imports constantly face a problem of foreign exchange imbalance, and often have to resort to control measures for the purposes of maintaining their foreign exchange reserves at a reasonable level. Foreign exchange control has therefore been introduced in many countries. But foreign exchange control can sometimes serve other purposes, such as stabilizing domestic financial markets, accumulating capital and tax screening.

Depending on the circumstances, the extent and effect of exchange control vary. Generally speaking, a country whose currency is accepted internationally has no need to reserve a hard currency fund merely for the purposes of foreign trade payments. Similarly, a country whose economy is closely related to the international economy is less inclined to adopt a tight control over foreign exchange. By contrast, a country with a less developed economy often has to adopt a stricter policy in relation to foreign exchange. The questions of foreign exchange control in Australia and China today are examples of these quite different models. However, the history of exchange control in the two countries, in particular in Australia which had a controlled foreign exchange market until the 1980s in spite of its currency being internationally acceptable, is an indication that exchange control may be adopted for some other reasons as well.

Australia had exercised exchange control for more than four decades before the 1980s for the purposes of maintaining the "value" of Australian dollars or of

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1 The term "foreign exchange control measures" will be used in this chapter to refer to policies and regulations governing transactions in foreign currency in and outside the country in question, exchange rates between local and foreign currency, and measures designed to encourage or discourage foreign capital inflow.

2 Government control over foreign exchange has been largely deregulated since 1983, when the Treasurer announced that the Australian dollar would be allowed to float.

3 The value of Australian dollars was then fixed artificially by the Reserve Bank, which determined the exchange rates between Australian dollar and the trade-weighted average of nominated currencies ("basket of currencies").
restricting foreign borrowing, than reserving foreign exchange for trade payments. Although exchange control was initially adopted as an emergency war time measure, it continued to exist under the Banking (Foreign Exchange) Regulations 1946 (Cth) which were promulgated under s.29 of the Banking Act 1945 (Cth) after the end of the Second World War, in particular in the 1970s when a Variable Deposit Requirement (VDR) was introduced to restrict foreign borrowing. The 1981 Campbell Report, which strongly criticized most control measures and recommended a less controlled exchange market, led to the suspension of most exchange control measures in Australia. Today, the Banking (Foreign Exchange) Regulations still

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4 For history of exchange control, see D.Flint, Foreign Investment Law in Australia (Sydney, Law Book Company, 1985) 273-8.

5 Section 51(vi) of the Constitution vests the Commonwealth Government with defence power and s.51(xxxix) with incidental power. Under these powers, the federal Parliament passed the Defence Act 1903 (Cth) and the Defence (Monetary Control) Regulations 1939 (Cth), imposing control over the transfer of currency out of Australia. These measures substantially affected some aspects of foreign investment, including the transfer of overseas assets owned by Australians. The Defence (Monetary Control) Regulations 1939 were replaced one month later by the National Security (Monetary Control) Regulations (Cth) in September 1939. In the same year, the National Security (Securities) Regulations (Cth) were promulgated. These regulations were meant to control the transfer of various securities out of Australia. The National Security (Monetary Control) Regulations 1939 and the National Security (Securities) Regulations 1939 were consolidated into the National Security (Exchange Control) Regulations 1940 (Cth), as later amended in 1943.

6 The Banking Act 1945 (Cth), after a series of changes and amendments, was replaced by the Banking Act 1959 (Cth). See Flint, supra note 4, at 273; and M.Sexton & A.Adamovich, The Regulation of Foreign Investment in Australia (Sydney, CCH, 1981) 40-1.

7 In 1972 the federal Government adopted a Variable Deposit Requirement (VDR) scheme which required a certain percentage of a transaction involving overseas borrowing to be deposited in the Reserve Bank, which was established as the central Bank of Australia in 1959. The VDR scheme was occasionally used to adjust the inflow of foreign currencies into Australia in the 1970s, but was suspended after 1978. Broadly, this measure was used to discourage the inflow of foreign capital into Australia. For example, when the Government considered the capital inflow was too high, such as in December 1972, October 1973 and January 1977, a certain percentage of interest-free deposit from overseas borrowing was required by the Reserve Bank; and when the proportionality of foreign capital inflow was adjusted to a degree satisfactory to the Government, the VDR was modified and often no such deposit was required.

exist, but most measures of control are no longer operative, except for some provisions of the Regulations relating to tax screening for which the Reserve Bank has designed two categories: A and B. Category A refers to monetary transactions to a number of specified tax havens, and transactions involving emigrants from Australia in an amount of more than $50,000, either in a single or an accumulated amount, within the previous twelve months. For Category A transactions, a tax clearance certificate is required. Category B transactions, which refer to other transactions of over $50,000 at a single amount, require no tax clearance certificate, but a tax declaration form. In a narrow sense, exchange control in Australia today is used as a general support to the Government's exchange rate policy, which in turn is adopted for the purpose of maintaining a desirable non-market exchange rate for a specific period. The history of foreign exchange control in Australia suggests that apart from reserving foreign exchange, exchange control may sometimes be used for the purposes of reinforcing the value of the national currency and supporting government monetary policy. In time of war, it may serve the purposes of gathering money and preventing the flow of money into enemy countries.

Unlike Australia, exchange control in China exists mainly for the purpose of conserving and retaining foreign currency, which has been a constant problem in China's economic development from the day when the PRC was established. For political reasons, the PRC was economically isolated from the most of the Western world until 1978, when China adopted a more realistic approach to its economic

9 The federal Treasurer and the Reserve Bank have issued orders, a power vested in them under the Banking (Foreign Exchange) Regulations, to suspend the application of most provisions of the Regulations which impose substantial control. The only "substantive" control over foreign exchange which is still effective is the rules about authorized dealing in foreign currency. The Reserve Bank still exercises power to authorize foreign exchange dealers according to the Banking (Foreign Exchange) Regulations 1946 (Cth). At the end of August 1987, there were 88 authorized dealers in Australia. Reserve Bank of Australia, Functions and Operations (Sydney, 1987) 10.

10 These are Bahamas, Bermuda, British Channel Is, British Virgin Is, Cayman Is, Gibraltar, Grenada, Hong Kong, the Isle of Man, Liberia, Liechtenstein, Luxembourg, Nauru, Netherlands Antilles, Panama, Switzerland and Tonga. In addition, some specific transactions to Vanuatu are classed as category A transactions. R.Hamilton, ed., Foreign Investment and Exchange Control (Sydney, Prospect Publishing, loose leaf service) 12-3.

11 Ibid.

12 For discussion, see Flint, supra note 4, at 278-281.

development. The isolation, in conjunction with the poor industrial and economic conditions of China, created tremendous foreign exchange shortage problems for the newly established Chinese Government in the 1950s, which was forced to centralize the power to handle foreign exchange in the hands of the People's Bank of China. The Bank became the sole dealer in China in foreign exchange. Foreign exchange control, like most policies in China, was then implemented through administrative measures, which may be translated as "regulations" but nevertheless often did not have direct authorization from the legislature. This situation remained very much the same until 1978. During the 1980s, the system of exchange control was established on the basis of formal legislation. Although at the end of the 1980s control measures were relatively relaxed, in the sense that some autonomy in the use of their exchange quota has been given to Chinese enterprises, extensive measures of control still exist. Apart from conserving foreign exchange, exchange control in China is also part of the state economic development plan to stabilize Chinese financial markets. This is another function of exchange control, which in a sense (in the sense of the effect of control but not the form - e.g. a state plan) may be compared with the Australian policy of maintaining the value of Australian dollars artificially in the 1960s and 1970s. Both are designed to implement government monetary policy.

Foreign exchange control usually covers a number of different aspects which may or may not be directly related to foreign investment. Control measures which have direct impacts on foreign investment include control over the flow of foreign


15 For example, drawing on deposits by American firms and individuals was said to be restricted in 1951. This suggests that some local regulations on foreign exchange control may have existed. Though the original regulations are not available, two public apologies, published in a Shanghai newspaper, by two foreign enterprises for their negligence in not following the foreign exchange control regulations, suggested the existence of Temporary Regulations Governing Exchange Transaction in the East China Region and other similar regulations. See J.Cohen, & H.Chiu, People's China and International Law (Princeton, Princeton University Press, 1974) 688 & 694.

16 An Chen argued that the "policy and decree relating to foreign exchange in China has two goals. As a socialist State, China must exercise strict control on foreign exchange; as a developing country encouraging foreign investment, China must assist foreign participants - investors as much as possible". By stating that "socialist system" is a reason for strict exchange control, Chen probably meant that the State-panned economy in China demands foreign exchange to be subject to the State plan. See An Chen, "To Open Wider, or To Close Again: China's Foreign Investment Policies and Laws (1984) 6:1 N.Y.L.S.J.Int'l & Comp.L. 1, 24-7.
capital out or into a country, control over the repatriation of profits deriving from investment in a country, and control over the conversion of local money into foreign currency. Of these, restrictions on the repatriation of profits and restrictions on foreign borrowing often have a crucial impact on foreign investment.

Some measures of control are less significant to foreign investment than others. For example, sending or taking local currency in notes or coin out of Australia is limited to a specified amount, but no amount of Chinese currency is allowed to be taken or sent out of China at all. Such restrictions on the transfer of local currency do not have any significant impact on foreign investment in the two countries. Similarly, exchange control over imports and exports has little impact on foreign investment, unless foreign investors are engaged in or dependent on imports and exports. At present, exchange control over imports and exports has a more significant effect on foreign investment in China than in Australia, not only because Australia has exempted the application of most provisions (including import measures) of the Banking (Foreign Exchange) Regulations 1946 (Cth), but also because China has indicated a strong preference for enterprises which may increase exports and has scrutinized closely imported goods which require foreign exchange payments.

While Australia has substantially deregulated its foreign exchange market, China has passed a considerable amount of legislation on foreign exchange control. As at December 1990, 31 regulations in relation to foreign exchange control have

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17 As at December 1990, a single amount of less than $5000 is allowed. See the Reserve Bank, Banking (Foreign Exchange) Regulations Tax Screening and Other Requirements.

18 Provisional Regulations for Control of Foreign Exchange of the PRC, CCH, China Laws for Foreign Business para.8-550, Art.30, hereinafter referred to as Exchange Control Regulations.


been made by the central Government, and about 5 by local governments. A special feature of foreign exchange control in China is that none of these laws have been passed by the NPC. The Exchange Control Regulations made by the State Council may be regarded as the basis of the legal framework for foreign exchange control, which consists of regulations and rules made by the State Administration of Exchange Control (SAEC), the Bank of China, the People's Bank of China, the People's Bank of China together with the General Customs Administration, and local governments. The State Council's power to regulate foreign exchange is derived from the Constitution and the special authorization by the Standing Committee of the NPC. The powers of other authorities to regulate foreign exchange control are in theory based on the Constitution and on authorization by the State Council, which has occasionally granted approval to rules made by departments and special bodies of the central Government.

The measures of exchange control in China can be divided into two basic categories: control over Chinese organizations and individuals, and control over foreign-related enterprises and individuals. Generally speaking, control measures applicable to Chinese enterprises are stricter than those applicable to foreign-related enterprises. Compared with their Chinese counterparts, foreign investors are allowed much more freedom in utilizing their foreign exchange reserves. The measures

21 As collected in CCH, China Laws for Foreign Business.

22 These are Provisional Measures of Zhuhai Municipality for Control of Foreign Exchange Adjustment, CCH, China Laws for Foreign Business para.74-504; Trading and Administrative Rules of the Shanghai Foreign Exchange Adjustment Centre, CCH, China Laws for Foreign Business para.91-042; Regulations of Shanghai Municipality for Foreign Exchange Control in the Leasing Trade, CCH, China Laws for Foreign Business para.91-058; Provisional Regulations of Shanghai Municipality in Foreign Exchange Mortgage Loan Administration, CCH, China Laws for Foreign Business para.91-061; and Provisional Measures of Beijing Municipality on Foreign Exchange Control for Foreign Investment Enterprises, CCH, China Laws for Foreign Business para.96-316.

23 SAEC was established in 1980 under Exchange Control Regulations. Its original name was the State General Administration of Exchange Control (SGAEC).

24 Decision of the Third Session of the Sixth NPC on Vesting the State Council with Power to Form Provisional Regulations or Rules on Economic Reform and Open-door Policy, the Chinese version can be found in Dept. of Legislation Supervision and Review, Law Enactment Bureau, the State Council, ed. Selected Chinese Laws on Encouragement of Foreign Investment (Zhong Guo Gu Li Wei Shang Tou Zi Fa Gui Xuan Bian) (Beijing, Chinese University of Politics and Law, 1987, in Chinese) 3.

25 For example, Rules for the Implementation of Control of Foreign Exchange Relating to Individuals, made by SAEC and approved by the State Council, CCH, China Laws for Foreign Business para.8-630.
concerning Chinese enterprises may sometimes indirectly affect the operation of foreign-related enterprises, in particular when a foreign-related enterprise engages in transactions with Chinese enterprises which are bound by tight control measures.

Australian and Chinese Governments have taken different approaches to the administration of foreign exchange markets. This chapter will examine some common issues faced by the two governments in dealing with the question of foreign exchange control, such as how they use exchange control to support their foreign investment policies, what are the constitutional restraints on their power to deal with exchange control in the context of their respective Constitutions, and how the relationship between the Reserve Bank and the Australian Government differs from the relationship between the People’s Bank of China and the Chinese Government. Undoubtedly, the differences in their legal traditions, State systems and economic backgrounds have affected the laws and policies of the respective Governments regarding foreign exchange control.

4.2. Constitutional Issues Relating to Exchange Control
4.2.1. Status of the Competent Authorities

Governments exercise control over foreign exchange market through a mechanism which is suitable for performing the functions of control. The form or organization of the mechanism is affected by the principles adopted in a Constitution or the model of executive government recognized in the Constitution. The Australian and Chinese Governments today exercise foreign exchange control in very diverse extents, although the differences between the measures of control before the 1980s in Australia and the system of control in China at present could be relatively smaller than they are today. The present measures of control over foreign exchange in Australia and China are virtually incomparable since Australia has suspended all substantial measures of control over foreign exchange market. But the forms of control, such as the status of competent authorities dealing with exchange control matters, may be studied in a comparative context, simply because the regulation of foreign exchange markets is an issue which faces both governments. Two distinctive features can be seen in the process of dealing with foreign exchange markets in Australia and China. These are the differences in the regulatory powers exercised by the competent authorities in charge of exchange control and the differences in the independence of central banks in dealing with foreign exchange matters.

The competent authorities to administer foreign exchange in Australia are the Governor-General, the federal Treasurer and the Reserve Bank. In China they are the State Council, the SAEC, the People’s Bank of China and, to some extent including the Bank of China. The Governor-General, the Treasurer, and the State
Council or SAEC are respectively part of the executive governments in the two countries. By contrast, the Reserve Bank and the People's Bank of China may be regarded as special bodies performing the functions of the central banks in Australia and China, although the two banks have different levels of independence. As far as foreign exchange control in China is concerned, the Bank of China may also be regarded as a competent authority which engages specifically in foreign exchange banking in China. Thus the functions of a central bank in managing foreign exchange matters in China are shared in a sense by the People's Bank of China and the Bank of China.

Of the three authorities involved in exchange control in Australia, the Governor-General may be regarded as the highest in sense that he has delegated power to regulate exchange control. Neither the Treasurer nor the Reserve Bank has the same power, although the Treasurer may determine the matters for which tax clearance certificates are required and the Reserve Bank has power to grant or refuse to grant authority to do an act or thing which is subject to taxation clearance. These authorities in theory exercise their functions described by law independently. But the Treasurer may sometimes influence the power of either the Governor-General or the Reserve Bank under the laws of exchange control. For instance, the Treasurer may advise the Governor-General in the exercise of his power, including of course the Governor-General's power to regulate exchange control under the Banking Act. He may also direct the Reserve Bank in the exercise of its power under the Banking (Foreign Exchange) Regulations 1946 (Cth). The Treasurer's influence raises several constitutional or administrative issues: is the

26 Part III of the Banking Act 1959 (Cth), entitled "Foreign Exchange, Foreign Investment, Etc", grants the Governor-General power to make regulations where he considers expedient to do so for a number of purposes as specified in s.39 of the Act.

27 Section 39 of the Banking Act.

28 Section 39B of the Banking Act.

29 The relationship between the Treasurer and the Governor-General is defined in the Commonwealth Constitution, where the Governor-General, as the symbolic head of the executive Government must act on the advice of either the Executive Council or Ministers. In Renfree's words, the former is "the manner in which the Government acts formally", and the latter reflects "the principles of responsible Government" which is implied in the Commonwealth Constitution. H.Renfree, The Executive Power of the Commonwealth of Australia (Sydney, Legal Books, 1984) 176.

30 The relationship between the Treasurer and the Bank is defined by reg. 38 of the Banking (Foreign Exchange) Regulations 1946 (Cth), which states that the Bank's power to exempt the application of the provisions of the Regulations is subject to the direction of the Treasurer.
Treasurer's influence consistent with the Westminster model adopted in the
Commonwealth Constitution? how does the Bank maintain its independence given the
possible influence of the Treasurer? and what are constitutional restraints on these
authorities of exchange control? These questions will be discussed in the following
subsections.

Of the authorities of exchange control in China, the State Council, the SAEC,
and sometimes the People's Bank of China, may exercise delegated legislative power.
The State Council exercises delegated legislative power under the Constitution or by
the authorization by the NPC. But the SAEC and the People's Bank of China (both
are attached to the State Council) derive their power to make regulations from either
their status as agencies (departments or commissions) of the State Council or direct
degregation in the regulations of the State Council. Delegated legislative power
sometimes extends to the Bank of China, whose power to make delegated legislation
is, however, unclear as a matter of legal theories. This is because the Bank of China
is a commercial bank whose administration is largely subject to the direction of the
People's Bank of China. Although the Articles of Association of the Bank of China
are approved by the State Council, it is not clear in the Articles themselves, nor in
Chinese legal theory, whether an approval by the State Council of the Bank's
establishment makes the Bank equivalent to a State Council department. The
Constitution allows departments or commissions of the central Government to make
regulations on their own initiative. Therefore, if the Bank of China is not a
department of the State Council, it can exercise delegated power only under
degregation from the State Council. But in practice, the Bank has made some
regulations without direct authorization by the State Council, thus causing some
confusion about the power of the Bank to make delegated legislation. Such
confusion, however, does not affect the role of the Bank in the administration of
foreign exchange. In practice it is able to implement its measures (even in the form
of policy) through its unique position as the most powerful foreign exchange dealer
in the country.

The relationship between SAEC, the People's Bank of China and the Bank of
China, is not clearly defined by law. The SAEC and the People's Bank of China do
not have any administrative connection, although the SAEC was a department of the
People's Bank of China until 1983. These two authorities may be regarded,

31 The Articles were approved by the State Council on 22 Sept. 1980, CCH, China
Laws for Foreign Business para.8-500.

32 H.Zheng, China's Civil and Commercial Law (Singapore, Butterworths, 1988) 89,
footnote 2.
However, as separate bodies, more or less equal, directly under the State Council. The SAEC has no administrative connection with the Bank of China either. Nor has it any power to interfere with the administration of the Bank of China or of other financial institutions engaged in foreign exchange dealings. The influence of the SAEC on the Bank of China and other financial institutions can be seen in its power to direct the Bank of China and other foreign exchange dealers in their foreign exchange dealings. Thus, their relationships are limited only so far as foreign exchange matters are concerned. Unlike the SAEC, the People's Bank of China is the central bank of the country, and may direct the Bank of China and any bank or non-banking financial institution on its administrative matters. The People's Bank of China has authority to grant licences to any financial institution which intends to engage in banking in China. The relationships between the People's Bank of China and other banks and non-banking financial institutions are that of superior and subordinate. In the light of these powers and relationships, the questions to be asked are what is the constitutional restraint on the power of these authorities to make regulations, and how does a central bank operate in China where independence of a statutory body is unknown? This will lead to a comparison between the regulatory power of the executive bodies in the two countries, and the respective roles of the central bank in Australia and China.

The status of the competent exchange control authorities in Australia and China differs in several respects. First, in Australia, the authority to regulate foreign exchange matters is conferred on the Governor-General - the symbolic head of the Government, but in China on the State Council and its departments or agencies, i.e. the executive branch of the government. The fact that the exercise of Governor-General's power is subject to the advice of the Treasurer makes the conferral of power to the Governor-General a mere formality. Secondly, the Treasurer's influence on the exercise of power by the Governor-General is supported by constitutional convention rather than the Banking Act 1959 (Cth) which delegates power to the Governor-General. This is contrasted with the possible influence of the State Council on the exercise of power by the SAEC, the People's Bank of China and the Bank of China. In the latter case, the State Council may either make regulations directing the exercise of power by the SAEC or banks, or issue policy to guide the SAEC and the banks, because of its general responsibilities as a department of the State Council to administer financial matters. The differences, which are seen in the ways the federal Treasurer and the State Council influence other exchange control authorities, result from the different principles adopted in the Australian or Chinese

33 Id, at 88.
Constitution. Thirdly, the Reserve Bank is clearly defined as an independent body in Australia, but the People's Bank of China and Bank of China are not, although they are established or authorized under special legislation. This reflects the different positions of the Australian and Chinese Government with regard to the use of an independent government agency. The Australian Government accepts the notion that an independent body can provide "a degree of specification and flexibility of management not normally attainable within a department" and can also provide advantages of distancing policy-making from party politics and representing sectional interests in the community. By contrast, the "independent agency" is not regarded as an issue at all in Chinese law, partly because the Executive in China exercises very broad power and partly because the Chinese Government insists that party policy should guide Government policy and that sectional interests in the community should be subject to the so-called national interests of the country. The use of an independent agency and the contrasts in Australian and Chinese legal theories will be further examined in subsection 4.3. of this chapter.

4.2.2. Constitutional Restraints and the Exercise of Delegated Power

The Governor-General in Australia and the State Council (whose delegated power may extend to the SAEC and the People's Bank of China) in China have delegated legislative power. The exercise of this power is subject to constitutional restraints in both countries. The apparent restraints are that the Governor-General must exercise his power under the advice of the Executive Council (and the Ministers) and that the State Council may make regulations under either a direct authorization by the NPC (or the State Council in the case of regulations made by the SAEC and the People's Bank of China) or pursuant to general principles of law (provided that the delegated regulations are not inconsistent with the Constitution and the law). The differences between Australian and Chinese practices do not reflect the ordinary contrasts between the common law and Chinese law: rather they suggest the distinct features of Australian law, which is a modified version (or combination) of the British legal system, the U.S. legal system and Australian

34 The Articles of Association of the Bank of China were approved by the State Council. Although the People's Bank of China was established in the 1950s, its functions and responsibilities are restated in the Provisional Regulations of the PRC on Control of Banks, Arts.5-11, CCH, China Laws for Foreign Business para 8-690.

federalism, and the Chinese legal system. Apart from the differences in dealing with State system (federalism vs. centralism) and monarchical sovereignty, the differences in dealing with issues of the separation of powers in the Australian and Chinese Constitution are also attributable to the contrasts in the constitutional restraints on the exercise of the delegated power by the Governor-General in Australia and by the State Council in China.

The marriage between the Westminster model of the "responsible government" and Queen's position as a symbolic head of the federation, led to the arrangement that the executive power of the Australian Government should be exercised by the Governor-General under the advice of the Ministers. If the executive power is exercised by the Governor-General alone, the principles of "responsible government" which require the Ministers to be accountable to the Parliament would be contravened. On the other hand, if the executive power is exercised by Ministers alone, the Queen's sovereignty which is deemed to have been passed to the Australian Government upon the federation would be denied. This constitutional restraint results in the power to regulate foreign exchange being delegated to the Governor-General and implies that the Treasurer may advise the Governor-General in the exercise of his power. The grounds which result in the distinct way of exercising delegated legislative power in Australia do not exist in China. Thus, "delegated" legislative power may be exercised by the State Council, the SAEC or the People's Bank of China. A common feature of the power exercised by the Chinese executive is that the power may be exercised either under direct authorization by the NPC or the State Council (in the case of the SAEC or the People's Bank of China exercising delegated power) or on the initiative of the executive. In the former case, the power so exercised can be regarded as delegated. But in the latter case the power may be regarded as subordinate, because the only constitutional restraint here is that none of the regulations so made is contrary to the Constitution and the law of the NPC. The delegated legislative power and subordinate legislative power in China differs in the sense that the latter is not based on direct delegation of power by a competent authority. Since the Chinese Constitution does not recognize the exclusiveness of legislative power, the executive is generally allowed to exercise delegated legislative power. The "legislative power" of the executive is regarded as "delegated" only in the sense that the regulations made under this power are secondary to the law of the NPC. This constitutional restraint imposes limitation on the effect of the executive's regulation but places no restriction on the manner in which the power is exercised.

The restraint in turn results in a contrast between the Australian and Chinese

Constitution in the exercise of delegated legislative power. In addition, the extensiveness of the delegated legislative power in China is also attributable to the way in which the powers are separated in the Chinese Constitution. The issues of separation of powers and their implication on the exercise of regulatory power in Australia and China will be discussed in the following subsection.

4.2.3. Separation of Powers and the Regulatory Power of the Competent Authorities

Delegated legislation is made by the executive in both Australia and China. Although both countries broadly accept that regulations made by the executive are dependent on and enforceable only within the authorization of legislature, they delegate legislative power to the executive in different ways. The Australian Government may make delegated legislation under authorization from the Commonwealth Parliament, which is usually required to be specific and certain. Sub-delegation, which refers to an executive body at a higher level delegating its delegated legislative power to another executive body at a lower level, is comparatively rare in Australia. By contrast, the executive Government in China has been granted general legislative power. An example is the authorization of the NPC to the State Council to make regulations or rules regarding foreign investment and economic reform. The State Council has thereby been granted a broad discretion to formulate new regulations for the purposes of promoting foreign investment in China. The only condition which restricts the exercise of delegated legislative power by the State Council is that none of the regulations of the State

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38 P.Lane, Lane’s Commentary on the Australian Constitution (Sydney, Law Book Company, 1986) 311.

39 Generally speaking, under the maxim *delegatus non potest delegare*, a person "who himself is a delegate of a certain power cannot further delegate the exercise of the power to a sub-delegate". E.Sykes, Cases and Materials on Administrative Law (4th edn, Sydney, Butterworths, 1982) para.2.10. See also *Sambell v Cook* [1962] VR 450. But there are exceptions: when a statute granting delegated power specifically allows the power to be sub-delegated (*Esmonds Motors Pty Ltd v the Commonwealth* (1970) 120 CLR 476) and when the delegated power is plenary (*Nelson v Braisby* (No.2) [1934] NZLR 559). See Pearce, Delegated Legislation in Australia and New Zealand (Sydney, Butterworths, 1977) para.508.

40 Decision of the Third Meeting of the Sixth Session of the NPC on Granting the State Council Power of Making Provisional Regulations and Rules on the Reform of Economic System and Open-door Policy, supra note 24.
Council should be inconsistent with the Constitution and laws made by the NPC. The State Council may not only exercise a broad delegated legislative power, but also delegate similar power to ministries or commissions attached to the State Council and provincial governments. This hierarchical structure of delegated legislative power is recognized by the Chinese Constitution. The delegation of delegated legislative power by the State Council to its subordinate departments and provincial governments is a distinct feature of Chinese legal system.

Foreign exchange control in China is principally based on the Exchange Control Regulations, and Provisional Regulations of the PRC on Control of Banks. These Regulations authorize the SAEC and the People's Bank of China to formulate detailed rules. The orders or rules made by the SAEC and the People's Bank under the Regulations are regarded as sources of law according to the Chinese Constitution. In this sense, the Chinese executive has been given a broader delegated legislative power than its Australian counterpart.

The contrast in the ambit of delegated power in Australia and China results partially from their different attitudes towards the separation of powers doctrine. Neither country has expressly accepted the doctrine in its Constitution, but both Constitutions deal with issues of separation of powers. The separation of powers doctrine assumes that the organs of a government, whether legislative, executive or judicial organs, collectively share the functions of government, but that no one is entitled to exercise the functions of the others. In another words, the "three must share the reins of control", but no one should become dominant. However, this

41 Ibid.
43 CCH, China Laws for Foreign Business para.8-690; hereinafter referred to as Bank Control Regulations.
44 Exchange Control Regulations, Art.33; and Bank Control Regulations, Art.5.
45 Constitution of the PRC, Art.90, CCH, China Laws for Foreign Business para.4-500. This Article recognizes the power of the departments or commissions of the State Council to issue orders, directives and regulations within the jurisdiction defined by law of the NPC and regulations of the State Council. The SAEC and the People's Bank of China are regarded as equal to a special commission of the State Council and therefore, the regulations of the SAEC and the People's Bank of China are regarded as law.
doctrine also recognizes the necessity of delegation of power by one organ to another, in particular, the delegation of law-making power to the executive.\textsuperscript{47}

The Australian Constitution assigns legislative power, executive power and judicial power respectively to the Commonwealth Parliament, the Governor-General and Commonwealth ministers, and the High Court, other federal courts, State courts and other specialist courts.\textsuperscript{48} Although the British model was not the only one considered at federation,\textsuperscript{49} it was decided that the ministers of the Commonwealth Government should be required to be members of the Parliament.\textsuperscript{50} Thus the legislative and executive powers in Australia are not meant to be absolutely separate. This arrangement is based on the idea of "responsible government".\textsuperscript{51} It has been accepted that in order to perform functions of government effectively, some functions of one branch of government should be exercised by another branch, and the executive may thereby be authorized by the Parliament to make secondary rules within the jurisdiction granted by legislature.\textsuperscript{52} The delegation of law-making power to executive must be limited by the Parliament, although sometimes by a very broad limit.\textsuperscript{53}


\textsuperscript{48} The \textit{Australian Constitution}, ss.1, 61 & 71. The federal judicial power may be invested in State courts. See J.Crawford, \textit{Australian Courts of Law} (2nd edn, Melbourne, Oxford University Press, 1988) 33-7.

\textsuperscript{49} Many aspects \textit{US Constitution} were noticeably adopted by the \textit{Australian Constitution}. J.Crawford, supra note 36.

\textsuperscript{50} The \textit{Constitution}, s.64.

\textsuperscript{51} Howard, supra note 47, at 231.

\textsuperscript{52} Id, at 231-2. Pearce suggests four arguments supporting the use of delegated legislation. These are to save pressure on parliamentary time, unsuitability of some legislation (too technical or detailed) for parliamentary consideration, needs for dealing with rapid change or uncertain situations, and necessity of legislative action in the case of emergency. D.Pearce, \textit{Delegated Legislation in Australia and New Zealand} (Sydney, Butterworths, 1977) 4-7.

\textsuperscript{53} Professor Lane comments that, in the context of s 51 of the Constitution, "mere width of the delegated power should not spell invalidity". Supra note 37, at 415.
The Chinese Constitution rejects the idea of the separation of powers as adopted in the U.S. Constitution. Rather it separates powers among the legislature, executive and judiciary in a way which superficially supports the notion of legislative supremacy but substantially allows the existence of an executive "supremacy". Under the Chinese Constitution, the NPC is the highest organ of "state power", exercising the legislative power of the State; the State Council, the highest organ of state administration, is the executive body of the highest organ of "State power"; and the People's Courts and People's Procuratorate are the judicial organs of the State. A hierarchical structure which is characterized by the NPC being the highest organ is thus established. The State Council as the executive body of the NPC is equal to the National Supreme Court, but both are under the guidance of the NPC. These facts suggest that the separation of powers doctrine, even as adopted in Australia in an attenuated form, does not exist in China.

However, although not exactly by way of a "separation of powers", state powers in China are separated. The separation can be seen in several respects. First, legislative, executive and judicial power are separate. The "separation" of powers exists in China only to the extent that legislative, executive and judicial powers are named, but not exclusively assigned to the separate branches of the Government.

Three main reasons have been given by persons who insist that the Chinese Constitution cannot adopt the separation of power doctrine. First, these persons insist that China has adopted a system of People's Congress which is suitable for the situation in China. Therefore, there is no need to change it. In addition, they argue that the adoption of the system of People's Congress, which applies the democratic centralism and legislative-executive collaborationism as basic principles to its organization and activities, denies the separation of power doctrine. Secondly, they argue that although the system of People's Congress has many weakness and shortcomings, the political reform in China must be carried on for the purposes of preserving this system. Therefore the separation of power doctrine whose inception will fundamentally change the present system cannot be introduced. This argument does not from legal perspective answer why the present system "must" be preserved except for political considerations. Thirdly, they argue that the harmful tradition of feudalism in China differs from other countries and this pernicious influence can be removed only through the reinforcement of political and ideological education and through the enforcement of law. Therefore, the separation of powers cannot be adopted. H.He, "On the Impossibility of the Separation of Powers in China" (1990) 39:1 Law Review (Fa Xue Pi LUN, in Chinese, with "Table of Contents" in English) 1-6. The reasons given here represent the conservative views of Chinese legal scholars, consistent with those of the Party and Government. These reasons are clearly political. They neither give legal explanation for why the separation of powers doctrine cannot be adopted in China, nor have they evidenced that the system of People's Congress suits China better in its pursuit of modernization.

The Chinese Constitution, Arts.57 & 58.

Id, Art.85.

Id, Arts.123 & 129.
This is not the same as the Australian system, because the State Council and courts are subordinate to the NPC. In addition, Chinese courts do not have power to determine a law of the NPC to be unconstitutional, although the courts may declare regulations made by the executive and local governments invalid. Secondly, the Chinese Constitution states that the People’s Congress exercises legislative power, but the executive may also exercise delegated legislative power under varying conditions, depending on the administrative level of an executive body. Thus Chinese law generally recognizes that the law of the NPC is superior to the regulations of the State Council, which in turn prevail over local legislation. Although the State Council and local governments may make regulations, orders and decisions regarding matters within their jurisdiction, the regulations of the State Council and local governments are secondary and subject to authorizations and limitations contained in the Constitution, and to the direction of the law of the NPC. In this sense, executive law-making is similar in Australia and China. But the similarity is only partial, and some fundamental rules for exercising delegated legislative power, such as certainty and specification, are ignored in China. In Chinese practice, sometimes the State Council is given a wide authorization, such as the power to make regulations on economic reform and foreign investment; and sometimes the State Council or its departments are delegated to make regulations on specific issues, such as the Income Tax Law of the PRC Concerning Joint Ventures with Chinese and Foreign Investment. But occasionally, the State Council assumes legislative power on its own initiative according to the Constitution, which allows the State Council to do so on the condition that none of its regulations is inconsistent with the Constitution and law of the NPC. In this respect, Australian and Chinese practices also differ.

One may conclude that the separation of powers does not exist in China for two reasons. First, theoretically the legislature is regarded as the highest organ of the country and has power to interfere in the actions of the executive and the judiciary. Secondly, in practice the executive government exercises almost unlimited executive and legislative powers. The executive, through the organization of the Party, may interfere with the performance of the People’s Congress and the courts.

58 Article 89 of the Constitution states that regulations or orders of the State Council must be consistent with the Constitution and law of the NPC. Thus in theory the courts may declare the regulations of the State Council invalid. As at December 1990, no court case concerning the validity of the regulations had been heard.

59 Article 17 of the Law authorizes the Ministry of Finance to form detailed rules for the implementation of the Law. CCH, China Laws for Foreign Business para.33-550.

60 The Chinese Constitution, Art.89.
This wide and uncontrolled executive power destroys the nominal "separation" of powers set forth in the Constitution. Although this observation reflects the reality in the present-day China, abuse of executive power may not be what was aimed at by the Constitution, which might as well be interpreted differently to provide a foundation for a better-controlled executive power.  

4.3. Independence of the Central Banks and Exchange Control  

4.3.1. Constitutional Restraints and the Australian Reserve Bank  

The Reserve Bank is the central bank of Australia. Under the Banking Act 1959 (Cth), the Reserve Bank does not have a general discretionary power to deal with issues of foreign exchange control, although it may require other banks to transfer an amount of foreign exchange to it from time to time. The power to control foreign exchange is vested in the Bank by the Banking (Foreign Exchange) Regulations 1946 (Cth), which extend control to the purchase of foreign exchange, the transfer of either Australian or foreign currency out of Australia, the proceeds of exports, and the disposal of securities.

The Bank is a statutory authority. Although it is argued that a statutory authority is usually established to perform some government function which cannot be performed by the government because "restrictions imposed by the normal departmental structure", the objectives of the Bank do not seem to suggest any goal which cannot be achieved by a normal governmental body. However, the

61 The flexibility of the constitutional principle that none of the regulations of the State Council should be inconsistent with the Constitution and the laws of the NPC provides discretions to the State Council which may exercise more limited delegated power in accordance with a narrow interpretation of the principle.

62 It is established by the Reserve Bank Act 1959 (Cth), replacing the Commonwealth Bank as the central bank of Australia. Banking Act 1959 (Cth), ss.12, 13, 14 & 16. For a review of the history of the Reserve Bank, see H.Coombs (Governor of the Reserve Bank from 1949 to 1968), Trial Balance (Melbourne, The Macmillan Company of Australian Pty Ltd, 1981) 141-182.

63 Id. s.33.

64 In addition, a statutory body may provide several advantages over a governmental department. These are managerial flexibility and specification, detachment from direct influence of party's policy and representation of sectional interests in the community which may not be achievable within the formal executive structure. Lewis, supra note 35, at 351.

65 The basic purpose of the Reserve Bank is, according to the Reserve Bank Act and the Financial Corporations Act 1974 (Cth), to assist the Australian Government to manage the financial system effectively in the interests of the people of Australia. This has several aspects:

(1) to stabilize the Australian economy and currency;
independence of the Bank from the immediate influence of party politics, and its neutrality in forming its policy are rather convincing reasons for its existence.

The Reserve Bank implements independently its goals of maintaining a desirable exchange rate and a stable foreign exchange market favourable to the Australian economy by participating actively in the exchange market. When the exchange rate is thought too low or too high, the Bank sells or buys foreign currency, mainly US dollars, thereby influencing the interest rate of Australian dollars in the domestic market. During 1986 and 1987, the Reserve Bank sold US dollars twice, in July-August 1986 and January 1987, totalling about US $2.4 billion. The exchange market was consequently restored to a "desirable level". The so-called "desirable level" of exchange rate is judged by the "desire" of the Bank. This reflects the independence of the Bank in determining its monetary policy for the purpose of implementing the general goal stated in the Reserve Bank Act 1959 (Cth). Although the Bank forms its policy independently, it does take government financial policy into consideration when so doing, provided that this is consistent with its goal stated in the Act. For instance, during 1988-89 the emphasis of the Bank's policy was on restraining domestic spending. This coincided with the Treasurer's policy. For the purposes of implementing this policy, when Australian dollars fell sharply in February 1989 following the announcement of inflation figures and the current deficit in Australia, the Bank "saw advantage in the breaking of the close nexus between high interest rates and a rising currency" and "aided the currency's depreciation through sales of Australian dollars in the market". The depreciation of Australian dollars was seen by the Bank as a compensation to the "loss of

(2) to maintain full employment in Australia;

(3) to allocate efficiently productive resources, and;

(4) to promote the economic prosperity and welfare of the people of Australia.

See the Reserve Bank Act (Cth), s.10(2), and Financial Corporation Act 1974 (Cth), s.3.

66 The propriety of an exchange rate is rather arbitrary. The Reserve Bank holds that exchange rate between Australian dollar and major foreign currencies should be "correct" and reasonably stable. By its view, in general, "a sharp fall in the exchange rate can be inflationary whilst a strongly rising rate can erode competitiveness". Reserve Bank, Annual Report 1986-87, at 13.

67 Id, at 16.

competitiveness by the currency's rise during 1988.69 During that time, the Bank's role was "to keep order in the foreign exchange market and to discourage any tendency towards an excessive loss in Australian dollars".70 Although the policies of the Treasurer and the Bank coincided, the independence of the Bank can be seen in measures to restrict the domestic spending, the time of implementing these measures, and the amount of currency involved. These matters were decided solely by the Bank.

The independence of the Bank is subject to constitutional restraints which can be seen in the Parliament's power to set up any agency (or body) to exercise the executive functions of the Government,71 or in the Westminster model of government accepted in the Constitution which "requires that any exercise of executive power can only take place under the general oversight of ministers who are responsible to Parliament".72 When all state powers are regarded as having been divided among the three branches of government, the acts of the Reserve Bank, which are executive actions by nature, must be subject to the ultimate supervision of the Executive (the federal Cabinet), in particular, the Treasurer in this case, who is accountable to the Parliament for financial matters in Australia. The same conclusion is also reached in the context of the US Constitution. Strauss, although he argues that the Congress can define the relationship between the President, who is the ultimate head of the executive, and any statutory body,73 notes the constitutional restraint that the work of a statutory authority must be "under the supervision of a unitary, politically accountable chief executive".74 In Australia, the "chief executive" is the federal Executive. As far as financial matters are concerned, the ultimate supervision of the federal Executive is normally exercised through the federal Treasurer. Therefore, the Reserve Bank, while exercising executive power vested in it by the federal Parliament, is inevitably under the supervision of the executive Government, in particular the Treasurer. This is why the Bank's power to exempt the application of some exchange control measures under the Regulations is subject

69 Id, at 14.

70 Ibid.

71 Heiner v Scott (1914) 19 CLR 381, and Baxter v Ah Way (1909) 8 CLR 626.

72 Lewis, supra note 35, at 369.

73 Strauss even seems to favour the proposition that the "Congress is free to choose between placing ultimate responsibility for decision with the President and giving that responsibility to those to whom it has initially assigned the work of administration". Strauss, supra note 46, at 605.

74 Id, at 667.
to the direction of the Treasurer despite that the Bank is independent from the Treasurer.  

The independence of the Bank is defined, protected and also limited by the Reserve Bank Act 1959 (Cth). Section 11 of the Act deals with the relationship between the Bank and the Government in case they disagree on questions of policy. Although the executive government in Australia includes both the Governor-General and Ministers, the term "government" in this Section seems to refer to the federal Treasurer only. Under the Act, the Bank is an independent authority, which should "from time to time, inform the Government of the monetary and banking policy of the Bank." The relationship between the Treasurer and the Bank is not of superior and subordinate. The Treasurer and Bank are required to "endeavour" to resolve the differences in their policies, through, presumably, the method of consultation. Thus the Act not only defines the relationship between the Treasurer and the Bank, but also protects the independence of the Bank by restricting the Treasurer from exercising executive power directly over the Bank. The limitation on the independence of the Bank is seen in s.11(4)-(6), which reinforce the ultimate control of the Government over the Bank's policy. Under this section, differences between the Treasurer and the Bank should be ultimately resolved by the Governor-General who is after all a part of the executive Government. In addition, as if to ensure the contribution of the Treasurer in the decision-making, the Governor-General is expressly required to make his decision with the advice of the Federal Executive Council. This, as observed by Renfree, can only mean that the Governor-General "is expected to act on the advice of Ministers, and the cooperation of the Executive Council is not then necessary to ensure that the Governor-General is acting with constitutional propriety". Thus the Bank is within the ultimate control of the executive Government, although it is not under the direct supervision of the Treasurer.

The independence of the Reserve Bank can neither be ignored nor exaggerated. The independence is absolute and unconditional when the Bank exercises power to formulate its policy. The Treasurer cannot directly interfere with

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75 Section 38 of Banking (Exchange Control) Regulations.

76 The Reserve Bank Act, s.11(1).

77 Id, s.11(2).

78 The restriction on the Treasurer's direct influence on the Bank is also seen in s.11(4) which requires the Treasurer to submit a recommendation to the Governor-General with regard to the differences between the Treasurer and the Bank.

79 Renfree, supra note 29, at 176.
the process of policy-making, nor is the Bank obliged to take the Treasurer’s policy into account, such as required of some departmental officers. But the independence does not prohibit the Bank from taking the Treasurer’s policy into account provided that the decision so reached does not contravene the duties of the Bank under the Reserve Bank Act. Moreover, the mere coincidence between the Bank’s and Treasurer’s policy does not often raise question of the independence of the Bank as long as the coincidence is consistent with the objectives of the Bank stated in the Reserve Bank Act, although it is noted that the Treasurer has influenced the policy of the Bank in some circumstances, e.g. the high interest rate adopted between 1989-90. On the other hand, the independence of the Bank exists only within the model of responsible government as adopted in Australia. Under this model, the executive government is required to be accountable to the Parliament with regard to the administration of law. Although the Parliament may perhaps pass a law requiring a statutory body which exercises executive power to be directly accountable to the Parliament, the Reserve Bank Act does not grant the Bank a special status outside the system of responsible government. Thus, in the case of disagreement between the Government and Bank, the Australian Government has ultimate power under the Reserve Bank Act "to direct (and take responsibility for) the Bank to pursue the

80 Ansett Transport Industries (Operations) Pty Ltd v Commonwealth (1977) 139 CLR 54, per Barwick CJ at 61, per Gibbs J at 62 and per Murphy J at 87.

81 For example, Kitto J Commented that it "may be conceded that where the law confers a power of discretionary decision upon an officer of the civil service in his official capacity Government policy is not in every case an extraneous matter which he must put out of consideration". R v Anderson; Ex Parte Ipec-Air Pty Ltd (1965) 113 CLR 177 192.

82 See "Hands off the Reserve: banker" SMH 16 July 1990. This article demands that the "Reserve Bank should have greater independence from the Treasurer".

83 In Ansett Case, Murphy J stated that the system of responsible government requires the discretionary power of a governmental department be exercised in accordance with the direction or policy of the Minister, unless "the language of legislation (including delegated legislation) is unambiguously to the contrary". (1977) CLR 54, at 87.

84 This was noted by the Campbell Report in 1981, which stated that:

If the Bank believes it is being pushed beyond reasonable limits it has the discretion and obligation to hold firmly to its view and ensure its concerns are brought to the attention of the Parliament. Ultimately, however, the Bank cannot rise above the source of its powers - government and Parliament - and must be responsive to the direction which governments may deem fit to give.

supra note 8, at 21. This is also noted by the public, e.g. SMH 11 Feb, 1989, at 17.

85 Section 11 of the Act.
Government's choice of policy". This power of the Government was considered necessary and the Campbell Report recommends the continuation of this arrangement.

4.3.2. Constitutional Restraints and the People's Bank of China

The People's Bank of China was officially nominated as the central bank of China accountable to the State Council in 1983. It is a subordinate agency of the State Council (rather than an independent body) in charge of the administration of China's financial system, but does not engage in commercial banking itself. One of its functions is to issue or revoke banking licences of banks and other financial institutions, including foreign-related banks and financial institutions. At present, foreign banks are allowed to carry on banking business in the SEZs and, to a restricted extent, to open branches in other cities outside the SEZs. As far as foreign exchange control is concerned, the People's Bank may determine the

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86 Campbell Report, supra note 8, at 17.
87 Id. at 21.
88 H. Zheng, supra note 32, at 89.
89 Article 5 of the Provisional Regulations of the PRC on Control of Banks states that the "People's Bank of China is the State organ through which the State Council leads and controls the fiscal affairs of the nation". CCH, China Laws for Foreign Business para.8-690.
90 Provisional Regulations of the PRC on Control of Banks, Art.11, CCH, China Laws for Foreign Business para.8-690, hereinafter referred to as Bank Control Regulations.
91 Id., Art.8.
92 Foreign-related banks and financial institutions refer to wholly foreign-owned and sino-foreign joint banks or financial institutions allowed to operate in China. These banks and financial institutions may operate in the SEZs of China and may also set up representative offices in other parts of China. See Regulations Governing Foreign Banks and Joint Chinese-Foreign Banks in Special Economic Zones of the PRC, CCH, China Laws for Foreign Business para.70-850, hereinafter referred to as Foreign Bank Regulations; and Interim Regulations of the PRC Concerning Control of Resident Offices of Foreign Enterprises, CCH, China Laws for Foreign Business para.7-540, hereinafter referred to as Interim Regulations.
93 Foreign Bank Regulations, Art.6.
94 It was reported that the People's Bank of China may approve certain foreign banks opening branches outside the SEZs, but the number was restricted. It was also noted that some local legislation allows foreign banks to operate within the local jurisdiction. Baker & Mckenzie, (Oct.1988) China Law Quarterly 2. However, the local legislation which is not authorized by the NPC or State Council may be regarded as unconstitutional by the central Government.
exchange rate between RMB and foreign currency, control foreign exchange, bullion and gold reserves, grant banking licences to financial institutions, and supervise their operations. In order to administer the financial system and coordinate the activities of financial institutions, the People's Bank of China is authorized to propose policies on the financial system and to draft specific regulations for financial activities. Compared with the SAEC, the People's Bank of China has more general responsibilities in administering the financial system but only limited involvement in foreign exchange control.

Whether there is any constitutional restraint on the status of the central bank of China is a complicated and virtually unanswered question in Chinese law. Literally, the Chinese Constitution does not prohibit the NPC from passing a law to establish a statutory body. But on the other, the notion of "statutory authority", and its functions and status, are totally unknown in Chinese law. This may partly explain why the People's Bank of China is set up as a dependent "agency" of the State Council, rather than a statutory body. Apart from the foreignness of the notion of "statutory authority" to Chinese law, the system of government adopted in the Chinese Constitution, which implies that all executive powers must be subject to the supervision of the State Council, discourages the establishment of a statutory body which is independent from the State Council.

The character of central banks is affected by the systems of government adopted in Australia and China. Australia adopts the Westminster model of responsible government which allows ultimate supervision of the Executive over the Reserve Bank. China does not have a system of responsible government, whose essence is the accountability of the executive to the legislature and the capacity of the executive to influence decisions of the legislature, but allows the State Council to exercise direct control over the People's Bank of China although the Bank itself is set up as a dependent "agency" of the State Council. However, the People's Bank of China, however, plays a crucial role in granting banking licence to foreign-related banks, which are not required to apply for a separate foreign exchange licence. Foreign Bank Regulations, Art.6.

Article 85 of the Constitution states that the State Council is the highest executive authority of the country, implying that all authorities exercising executive power must be subject to the direction of the State Council.
up by law. The Chinese system of government, however, bears partial and superficial resemblances to the "model of responsible government" in the sense that the executive - the State Council - is required to be accountable to the NPC.\textsuperscript{102} The Chinese system differs from the Australian system in the sense that (although this is not the only dissimilarity between them) the members of the State Council (Ministers) are not required to be members of the NPC.\textsuperscript{103} Despite that the Chinese Government is not based on the Westminster system or anything like it, the central bank in China, like the Reserve Bank in Australia, is subject to the direct supervision of the executive government. This coincidence results from the separation of state power in the Chinese Constitution. As we have seen, although China does not accept the separation of powers doctrine, State powers are generally divided into three branches (the NPC, the State Council, and judiciary: the National Supreme Court and National Supreme Procuratorate) in its Constitution. The Executive exercises wide and substantive power. The doctrine of separation of powers is rejected in the sense that the Executive has been granted very extensive power. But the impact of the separation of power doctrine can be seen when the Chinese Constitution categorizes all state powers into legislative, executive and judicial. Based probably on the presumption that a state power must be exercised by one of the established branches, and assisted by the notion of central control that all executive powers must be thoroughly subject to a uniform central authority,\textsuperscript{104} the Chinese Constitution seems to be intended to leave no space for any suggestion that a statutory body independent of the State Council could have a place in the institutional structure of the State. This indicates how a system of government may affect the status of central banks, although the system is not based on responsible government.

However, it was reported that a proposal to separate the People's Bank of China from the direct control of the State Council was made to the Government in July 1988.\textsuperscript{105} The proposal was made by a group of economists, who suggested that the traditional role of the People's Bank of China as a "teller's desk for the Finance Ministry" should be changed for the purposes of controlling the issue of currency, which was said to be one of the major reasons for the serious inflation occurring in

\textsuperscript{102} Article 92 of the Constitution states that the State Council is accountable to the NPC and should report its works to the NPC or the Standing Committee of the NPC.

\textsuperscript{103} Neither the Constitution, nor any legal institution (convention) has addressed this issue.

\textsuperscript{104} Section 85 of the Chinese Constitution.

early 1988. According to the proposal, the Bank should be independent from the Ministry of Finance and non-governmental Bank branches should be established to replace the existing governmental branches in provinces.\textsuperscript{106} The details of the proposal were not reported, but the intention of these economists is clear. If this proposal is adopted, the difference between the Australian Reserve Bank and the People's Bank of China will be greatly reduced.

4.3.3. The Central Bank and Government Policy

A central bank of a Western country is more likely a statutory body (e.g. the Australian Reserve Bank), which enjoys broader independence. A central bank in a socialist or communist country is often a governmental body, which is created under executive power of the government. The People's Bank of China is an example. However, the common role of a central bank is to formulate (with varying degrees of independence\textsuperscript{107}) and execute monetary policy,\textsuperscript{108} including determination of exchange rates. Given the variations of the status of central banks and their common role, central banks may be regarded as national financial institutions which formulate and implement national economic policies in accordance with their statutory or executive duties through their limited involvement in financial markets.

Independence of central banks varies even in Western countries which believe in the same \textit{laissez-faire} economy. The United Kingdom Committee to Review the Functioning of Financial Institutions\textsuperscript{109} studies the relationship between government and central bank and concluded that except central banks in Western Germany and Switzerland central banks in other countries are either subject to direct governmental control (by general or specific approval) or indirect control (by imposing a duty to inform government).\textsuperscript{109} This suggests that independence of a central bank is determined by the role of the bank designed by legislature. Thus, when a legislature attempts to designate a power to manage monetary system or financial market to an independent body, it would give the body necessary independence. In contrast, if a legislature regards direct government control of financial market desirable, it would

\textsuperscript{106} Ibid.

\textsuperscript{107} In some countries, banks are required to keep governments informed, e.g. in Australia and China. But the central banks in Germany and Switzerland are largely independent of government in pursuit of their statutory duties.

\textsuperscript{108} e.g. Provisional Regulations of PRC on Control of Banks, Arts.5-7; the Reserve Bank Act (Cth), s.10(2).

\textsuperscript{109} The result of the survey is reprinted in Australian Financial System, supra note 8, at 35-50.
allow less independence to the body in charge. Australian and Chinese practices form a clear contrast in this regard.

The Australian Reserve Bank is based on the model of the Bank of England which was created in 1694.\textsuperscript{110} Both are set up as independent bodies, but yet are subject to the direction of government. In England, the Treasurer may, after consultation with the Governor of the Bank, direct the policy of the bank when s/he thinks necessary in the public interest.\textsuperscript{111} In Australia, the Reserve Bank is required to "inform the Government of the monetary and banking policies of the Bank".\textsuperscript{112} This arrangement provides assurance that the Reserve Bank's policies would be broadly consistent with the federal Treasurer's. A superficial comparison of the relationships between the central bank and government in England and Australia reveals that even in countries with similar legal tradition degree of central bank's independence varies.

"The essence of central banking is discretionary control of the monetary system".\textsuperscript{113} Having regard to this characteristic of central banking, a discretionary power to control the monetary system is, however, exercised by either a governmental department or a statutory body. The need for "discretionary control" does not suggest a preference for either form of the administration. But at least in Australia, Lewis has suggested several reasons for the preference for an independent Reserve Bank.\textsuperscript{114} Various arguments may be raised to support the independence of the Reserve Bank, including the neutrality of the Bank,\textsuperscript{115} the institution of a


\textsuperscript{111} Bank of England Act 1946, s.4(1).

\textsuperscript{112} The Reserve Bank Act (Cth), s.11(1).


\textsuperscript{114} Lewis, supra note 35, at 368.

\textsuperscript{115} The neutrality of a central bank is also a commonly accepted belief in establishing an independent authority. Neutrality is needed for detaching the independent authority from immediate influence of the party's policy and of a special interest group. The limitation of this argument has been noted by Lewis, who argues that while "central banks are capable of an apolitical stance", "the consequence of their actions are inevitably political". Lewis, ibid. His conclusion is supported by the Campbell Committee, which stated that "ultimate determination of, and responsibility for overall economic policy - including monetary policy - cannot be effectively divorced from government and Parliament". supra note 8, at 20.
central bank in Australia and increasing demands for the Bank's participation in the financial market. These arguments, in particular the neutrality of the Bank (albeit limited) and market participation by the Bank, do suggest a need for an independent central bank to carry on functions that cannot be performed by a normal governmental department.

It may be further argued that if a central bank is not required to carry on these special functions, the independence of the bank may not be a crucial issue. This is particularly true in China, where the People's Bank of China is not designed to be an independent authority of the central Government. The Chinese Constitution reflects the influence of the Chinese Communist Party on the law, policy and all branches of the Government. Thus, there is no need, and it is not even permissible, to set up an independent authority for the purposes of detaching the authority's policy from the immediate influence of the Party. Although in practice the ultimate control of the Party will ensure consistency between any authority's policy and the Party's policy, for merely political reasons, the Chinese Government is afraid of any limited detachment an independent authority may have from the Party's overall policy. This may, from both practical and constitutional perspectives, explain why the People's Bank of China is not meant to be an independent authority. The participation of the market is not an issue for the People's Bank of China, because the Banking Control Regulations do not allow it to carry on any banking business. Rather, it exercises control over the financial market merely through its policy and power to grant or withdraw banking licences. Compared with the functions of the Reserve Bank, the People's Bank of China actually does not perform the full functions of a central bank. This may explain why a totally dependent central bank in China has not raised too much concern over its capacity to perform a central bank's duties, which usually require the bank to manage the market in a neutral and commercial manner.

116 Lewis argues that the "theory of central banking has become much less pedagogic and much more instrumental (and arguably the reality has always been so)". He observes that successive "Royal Commissions and inquiries have accepted that, insofar as monetary policy is concerned, a government's economic and social objectives are best facilitated by allowing central bank policy to be flexible and responsive to changes in economic conditions". Lewis, ibid.

117 Lewis, ibid.

118 The Preamble of the Constitution states that all Chinese people will be continuously led by the Communist Party and guided by the Marxism, Leninism and Mao Zedong Thought. This virtually makes an anti-Party and anti-Maoism activity a crime.
not exclude cooperation between the central bank and the government. The notion of independence itself does not deny the ultimate control of a government over the bank, because the separation of functions between the executive and central bank is no more than a power-sharing arrangement within the executive agencies of the State.

Despite the difference in the level of independence enjoyed by the Reserve Bank and People's Bank of China, some limited similarities can be found in their relationships with government. The People's Bank of China may draft policy, guidelines and regulations itself (independently), although the exercise of the power is subject to final approval by the State Council. This is perhaps comparable with the cases where the Reserve Bank's policy is modified to satisfy the Treasurer's requirements through the directive of the Governor-General. The difference between the Reserve Bank and the People's Bank of China is that the effect of the Reserve Bank's policy is not subject to approval, but the latter's is. The similarity between them can be seen when the Reserve Bank is forced to implement the Governor-General's decision in the case of disagreement between the Treasurer and the Bank. In the latter case, both banks are subject to ultimate supervision of the governments. Thus it may be argued that independence of the People's Bank of China exists when the Bank deliberates its policy, but the independence of both Reserve Bank and the People's Bank of China is limited when the proposed policies contravene the relevant government policies.
An essential difference between the Reserve Bank and the People's Bank of China is the Reserve Bank's ability to formulate an independent policy. The Reserve Bank is free of immediate interference from the Treasurer in the process of policy-making. The freedom of the Bank within the ambit of its authority indeed provides an opportunity for developing policies which are most appropriate for performing the Bank's obligations. The suitability of a policy may be argued between the Bank and Treasurer on the basis of limited equality in the case of disagreement between them, or supported respectively by them in the case of agreement. This arrangement reflects the basic ideas of a \textit{laissez-faire} economy where government's interference with the economy has been greatly restricted and government's functions to control economy have been largely decentralized. These features are missing in the Chinese system. In addition, the unfounded presumption that the Party is able to represent the interests of the people and only under the guidance of the Party can the Government make a correct policy are perhaps the political reasons why Chinese constitutional theories do not support the existence of an independent authority.

The purposes of central banks seem to suggest that certain cooperation between the banks and their governments are necessary. In practice, a central bank is a vehicle through which government monetary policy can be implemented. As the Campbell Report observes:

> In most Countries central banks are either required to keep government informed of their policies or subject to general directions of government or must obtain specific government approval for particular policies. Only in West Germany and Switzerland is the central bank largely independent of government in pursuit of its statutory duties. In the United States, the central bank can set and implement its own monetary objectives and largely operates independently of the Executive; however, it is ultimately accountable to, and subject to direction from, Congress.\(^{119}\)

This suggests that although central banks in different countries enjoy various levels of independence from governments, no central bank has been, or should be, absolutely independent from government. Since, as noted by the Campbell Report, a "common role of central banks is substantial responsibility for the formulation and execution of monetary policy (including, in many cases, exchange rate and some other aspects of external policy)\(^{120}\), a central bank is expected to formulate policy according to its judgment as to what is for the best interests of the country, and to cooperate with government policy which is virtually formed for the same purposes. Moreover, the purposes of a central bank to pursue the better management of a country's financial system and to ensure an efficient approach to financial issues, do

\[^{119}\text{Campbell Report, supra note 8, at 18-9.}\]
\[^{120}\text{Id, at 18.}\]
Chapter 5 Some Issues of International Taxation in Australia and China

5.1. An Overview

The taxation of foreign investors serves the same purposes as the taxation of nationals of a recipient country. Similarly, revenue collecting, economic growth and wealth redistribution are probably the main concerns in the taxation of foreign investment. Foreign investors benefit from the human or natural resources of a recipient country. They are, like nationals of the recipient country, liable to contribute to the operation of the government and the social or economic welfare of the local community. However, the functions of taxation to promote economic development and wealth redistribution are more crucial in the context of foreign investment than in the background of domestic taxation, because foreign investment is originally accepted by a host country for the purpose of developing the national economy and furthermore, the making of high profits by foreigners may arise nationalistic sentiment in the recipient country. This is particularly true in Australia, but less evident in China.

Australia has relied heavily on foreign investment in developing its economy. Today, foreign investment operates in Australia in various forms, such as solely

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1 The term "international taxation" may refer to taxation of either foreign investment in a host country or overseas investment by nationals of the host country. For example, in Hamilton & Deutsch, Understanding Australian International Taxation (2nd edn, Sydney, CCH, 1988), the term refers both to taxation of foreign investment in Australia and to the taxation of Australians investing overseas. Since overseas investment by either Australian or Chinese nationals is not the major concern of this thesis, the term "international taxation" in this thesis will be used to refer only to the taxation of foreign investment in Australia and China. The expression "international aspects of taxation" can also be used in the same sense as "international taxation", e.g. D.Flint, Foreign Investment Law in Australia (Sydney, Law Book Company, 1985) and Taxation Review Committee, Full Report 1975 (Canberra, AGPS, 1975). Again, in this thesis only those aspects of taxation which are relevant to foreign investment in Australia and China will be discussed.

2 Taxation, in a general term, serves a number of purposes, such as raising revenue, maintaining price stability, promoting economic growth, increasing employment, redistributing wealth and other particular objectives specified by governments. See Sommerfeld & Others, An Introduction to Taxation (NY, Harcourt Brace Jovanovich Inc, 1972) 10-6.

3 Such as commented by Quick and Garran that taxation is an "exaction of money or revenue, by the authority of a State, from its subjects or citizens and others within its jurisdiction, for the purposes of defraying the cost of governments, promoting the common welfare, and defending it against aggression from without". Quick & Garran, The Annotated Constitution of the Australian Commonwealth (Sydney, Legal Books, 1976) 550.

4 In China these features are not obvious because the Chinese market is not fully open to foreign investors and also the profits made by foreign investors from exports are not something which could otherwise have been obtained by Chinese enterprises.
foreign-owned companies, joint ventures, Australian subsidiaries of foreign corporations, Australian companies controlled by foreign interests, and Australian companies with foreign portfolio investment. The Government imposes different measures on residents and non-residents for the purposes of encouraging or discouraging certain types of foreign investment. For instance, the thin capitalization rule is intended to prevent the abuse of portfolio investment by non-residents or by residents through a non-resident agent, because dividends or interests paid to a non-resident are subject to a lower tax rate (10%-30% withholding tax) than business profits of a resident or non-resident (39% company tax). One of the effects of the rule is to prevent Australian companies from massive overseas borrowing that increases the foreign debt of Australia. Similarly, the Australian Government treats residents in the same way regardless of whether they are foreign or local investors because the fairness so reached is the best way in Australia to encourage foreign investment.

The "open-door" policy adopted by the Chinese Government since 1978 emphasizes strongly the role of foreign investment in the modernization of Chinese economy. Today, foreign investments are allowed to operate in various forms, such as solely foreign-owned enterprises, joint ventures or cooperative ventures. Taxation of foreign investment became an issue in Chinese law after 1978 when many foreign-invested enterprises were established. But there was in fact no income tax law in China until two years later, when the Income Tax Law of PRC concerning Joint Ventures Using Chinese and Foreign Investment was passed, despite Article 7 of the Joint Venture Law which stated in 1979 that the profits of joint ventures should be taxed by Chinese tax law. The inflow of foreign investment, which mostly comes from the Western countries with laissez-faire economies, forced the Chinese Government to adopt a taxation system comparable to that accepted in these Western countries. As a result, a new tax system governing the taxation of foreign-related


enterprises and foreign individuals has been developed. The development of the legal framework for the taxation of foreigners has in turn promoted the regulation of Chinese domestic tax matters.

One of the contrasts between Australian and Chinese tax laws is seen in the body of tax legislation. In Australia, the same tax law applies to foreign and local companies. But in China, tax law consists of three classes of legislation: laws governing the taxation of foreigners, laws governing the taxation of Chinese citizens, and laws applicable to both foreigners and Chinese. The laws governing the taxation of foreigners (such as the JVIT Law and the Income Tax Law of the PRC on Foreign Enterprises) and tax laws applicable to both foreigners and Chinese (e.g. the Provisional Regulations of the PRC on Real Estate Tax) are relevant to this study. The tax laws on Chinese domestic enterprises and Chinese nationals, such as the Provisional Rules of the PRC on Construction Tax and the Provisional Rules of the PRC on Individual Income Adjustment Tax will not be considered in this thesis.


A considerable volume of tax legislation dealing with domestic tax matters has been passed in China since 1980. Examples of these laws can be found in CCH, China Laws For Foreign Business.

These laws and regulations were mostly passed before 1978, e.g. the Regulations of the Consolidated Industrial and Commercial Tax of the PRC (Draft) passed by the Standing Committee of the NPC in 1958 (see CCH, China Laws For Foreign Business para.31-500, hereinafter referred to as CICT Regulations), the Provisional Regulations Concerning Vehicle and Vessel License Plate Tax (see CCH, China Laws For Foreign Business para. 34-500, hereinafter referred to as VVLPT Regulations) and the Provisional Regulations Governing the Urban Estate Tax (see CCH, China Laws For Foreign Business para.39-500, hereinafter referred to as URET Regulations) made by the Administrative Council of the central Government (the predecessor of the State Council) in 1951. These Regulations were extended to foreign-related companies and foreign persons after 1978.

CCH, China Laws For Foreign Business para.32-500, hereinafter referred to as FEIT Law.

CCH, China Laws For Foreign Business para.39-505, hereinafter referred to as RET Regulations. It must be pointed that real estate in China excludes land, and mainly refers to property in the form of buildings and house. See the General Tax Bureau (GTB) of the Ministry of Finance Circular on Several Questions Concerning Explanation of RET and Vehicle and Vessel Utilization Tax, (1987) 1:9 China Law and Practice (CLP) 23.

CCH, China Laws For Foreign Business para.31-704.

CCH, China Laws For Foreign Business para.30-524.
Another difference between Australia and China can be seen in the types of taxes imposed in the two countries. Although foreign investments are subject to income tax in Australia and China, the types of taxes imposed on foreign investments in Australia and China differ in their details. In Australia, a foreign investor may be subject to company tax,\(^{14}\) personal income tax,\(^{15}\) withholding tax\(^{16}\) or capital gains tax,\(^{17}\) as the case may be. Apart from these federal taxes, a foreign investor may also be subject to several State taxes, such as payroll tax, land tax, real estate tax or stamp duties, which, however, do not substantially affect the operation of foreign investment.

\(^{14}\) It is 39% of taxable income for year of 1990-91.

\(^{15}\) During 1990-91 income year, the income tax rates for resident individuals range as follows: no tax is levied on taxable income of less than $5,100; a rate of 21% applies to income of over $5,100 but under $17,650; a rate of 29% applies to income of over $17,650 but under $20,600; a rate of 39% applies to income of over $20,600 but under $35,000; a rate of 47% applies to income of over $35,000. No tax-free threshold is given to non-resident individuals and they therefore are required to pay tax at a rate of 29% on the first dollar up to $20,600. Thereafter, the same tax rates as applicable to resident individuals apply to non-residents.

\(^{16}\) Withholding tax is levied on certain categories of income, such as dividends or interest, derived from Australian sources by non-resident companies. Dividends paid by a resident company to a non-resident company, except franked dividends, are subject to a tax rate of 30% of gross dividends (see the ITAA, s.128B(1) and Income Tax (Dividends and Interest Withholding Tax) Act 1974, s.7). But a rate of 15% applies to dividends paid to residents of Papua New Guinea, (see the ITAA, s.128B(4) and Income Tax (Dividends and Interest Withholding Tax) Act 1974, s.7) and of countries with which Australia has double taxation treaties. Interest deemed to be outgoings of an Australian business is subject to a 10% withholding tax, payable on the gross amount of interest paid to a non-resident company (see the ITAA, s.128B(2), (6), (7), (8) & (9), and Income Tax (Dividends and Interest Withholding Tax) Act 1974, s.7).

\(^{17}\) A capital gains tax was introduced by the Income Tax Assessment Amendment (Capital Gains) Act 1986, which inserted Part IIIA into the ITAA. The tax was imposed on income derived from disposition of assets acquired on or after 20 September 1985. Capital gains form a separate category of income, but do not attract an independent tax rate. Rather, capital gains are taxed according to the tax rate applicable to each taxpayer in a particular circumstance. Thus, in cases where progressive tax rates apply, only 1/5 of net capital gains (taxable income) should be taken into account in determining the appropriate tax rate applicable to the taxpayer. This is intended to avoid the situation where a taxpayer may be subject to a much higher tax rate than when net capital gains are not included into his/her taxable income.
investment. In China four basic taxes are presently imposed on foreign investors.\(^{18}\)

\(^{18}\) However, Moser and Zee divide Chinese taxes into seven categories: the individual tax, the joint venture tax, the foreign enterprises tax, the consolidated industrial and commercial tax, the real estate tax, the vehicle and vessel licence tax and customs duties. M.J.Moser & W.K.Zee, China Tax Guide (Oxford, Oxford University Press, 1987) 2-3. The categories adopted in this thesis include all these taxes except the customs duties, which are excluded because they are neither subject to the tax law nor collected by the taxation authorities in China.
They are income tax,\textsuperscript{19} CICT,\textsuperscript{20} VVLPT\textsuperscript{21} and RET.\textsuperscript{22} Generally speaking, an

\textsuperscript{19} Income tax includes enterprise income tax, which can be further divided into FEIT and JVIT, and individual income tax (IIT). First, FEIT applies to solely foreign-owned enterprises which may either have or not have establishments in China. Currently, a foreign enterprise which has an establishment in China is liable to pay tax on any income derived from Chinese sources at progressive rates (Art.3 of FEIT Law). They are as follows: a rate of 20\% applies to annual income below 250,000 RMB, a rate of 25\% applies to income over 250,000 RMB but below 500,000 RMB, a rate of 30\% applies to income over 500,000 RMB but below 750,000 RMB; a rate of 35\% applies to income over 750,000 but below 1 million RMB, and a rate of 40\% applies to income above 1 million RMB. An additional local tax at a rate of 10\% of taxable income is also payable by the foreign enterprise. Secondly, JVIT which contains an income tax and a local surtax applies to Sino-foreign enterprises established under Chinese law. According to Art.3 of JVIT Law, the income tax is 30\% of taxable income of a joint venture, and the local surtax is 10\% of the tax payment assessed at the rate of 30\% of the taxable income. It should be noted that the local surtax payable by a joint venture differs from the local tax payable by a foreign enterprise in the sense that the latter is 10\% of the foreign enterprise’s taxable income. Joint ventures engaged in petroleum operations or exploitation of other natural resources are intended to be subject to special tax rates, which, however, had not been promulgated as at December 1990. Thirdly, IIT applies to foreigners who receive income from sources in China. Under Art.3 of Individual Income Tax Law of the PRC, (hereinafter referred to as IIT (Individual Income Tax) Law, CCH, China Laws For Foreign Business para.30-500) two kinds of tax rates apply to individual income. Progressive rates ranging from 5\% to 45\% apply to salaries and wages, and a flat rate of 20\% applies to remuneration from specified professions, royalties, interest, dividends, rentals, and other specified classes of income. The details of the progressive rates are as follows: monthly income of 800 yuan and less is exempted from tax; that part of monthly income from 801 yuan to 1,500 yuan is subject to a 5\% tax; that part of monthly income from 1,501 yuan to 3,000 yuan is subject to a 10\% tax; that part of monthly income from 3,001 yuan to 6,000 yuan is subject to a 20\% tax; that part of monthly income from 6,001 yuan to 9,000 yuan is subject to a 30\% tax; that part of monthly income from 9,001 yuan to 12,000 yuan is subject to a 40\% tax; and that part of monthly income from 12,001 yuan above is subject to a 45\% tax (see IIT Regulations, infra note 62, endnote). However, at present the above-mentioned progressive tax rates have been reduced by 50\% while applying to foreign individuals working in China (see Provisional Regulations of the State Council concerning the Reduction of IIT on Wages and Salaries of Foreign Nationals Working in China, CCH, China Laws for Foreign Business para.30-528), resulting in effective tax rates for salaries earned by foreign nationals and overseas Chinese in China being from 2.5\% to 22.5\%.

\textsuperscript{21} This is levied on any person or enterprise engaging in import business, manufacture of industrial products, purchase of agricultural products, retailing, communications, transportation, and commercial services (including advertising agency operated by foreign enterprises, see Levying CICT and FEIT on Advertising Agency Fees Obtained by Foreign Enterprise Permanent Representative Offices Circular, issued by the GTB on 2 December 12 1988. Summary of the Circular can be found in (1989) 35 CLP 7.) in China. CICT would be applicable to foreign-related enterprises in most situations. In special cases where CICT is not required by law, a foreign-related enterprise may be liable to pay the Stamp Duty, which was initially replaced by CICT in 1958 (see CICT Regulations, Art.1), but was reintroduced as a separate tax on specific transactions in 1988 by the Provisional Rules of PRC on Stamp Duty (see CCH, China Laws for Foreign Business para.31-712). Thus, a foreign-related enterprise engages in the prescribed transactions is
individual is liable at least to income tax, and an enterprise to income tax and CICT. But VVLPT and RET are payable by an enterprise or person who has a prescribed vehicle or is an owner or tenant of prescribed property.

General comparisons may also be made in other aspects of international taxation in Australia and China. For example, both countries impose income tax, such as company tax (enterprise tax), personal tax (individual tax), withholding tax, stamp duty and real estate tax, but adopt different tax rates. Differences can also be seen in the taxation power of local governments (e.g. stamp duty is imposed by a State government in Australia, but none of the Chinese local governments has imposed any tax on their own initiative), and the imposition of some taxes, e.g. capital gains tax in Australia and CICT in China, which are not comparable between the two countries. Generally speaking, the similarities are based on the fact that both Governments use taxation as a means of revenue raising. The differences arise mainly from the differences in their economic systems, the proprietary rights recognized under their laws and the taxation powers prescribed in their Constitutions which result in that no local government in China has imposed its own tax and that Australian States have introduced their own taxes according to the arrangements with the federal Government.

liable to the Stamp Duty even if it is not subject to CICT. For discussion of CICT, see Moser, supra note 18, at 64-71.

21 Although it is imposed by the central Government, it is in fact a registration fee paid to local governments in the form of a national tax.

22 It actually includes two separate taxes: the URET and RET. Both are imposed by the central Government but are actually administered by local governments, which may make detailed rules for the implementation of the Regulations imposing these taxes. RET is a charge on owners of houses or buildings. But other persons, such as a tenant or a caretaker of the property, may also be liable to pay the tax on owner’s behalf.

23 If one government does not use taxation as a means of revenue collection, such as the Chinese practice before the 1970s, no similarity whatever would exist between taxation systems in Australia and China.

24 For example, the Australian Government imposes the same tax rates on its nationals and foreign investors but the Chinese Government imposes higher taxes on foreign investors. This is because the Chinese believe that its economic system already gives a foreign investor many privileges which are not available to an ordinary Chinese.

25 This can explain why the Australian Government introduces capital gains tax, but Chinese Government does not. Chinese law does not allow individuals to own land and only recently provided protection to buyers of houses or buildings. Therefore capital gains are not a concern in Chinese tax law.
5.2. Features of Taxation Power in Australia and China

5.2.1. Concurrent Taxation Power in Australia

The Australian and Chinese Constitutions and the State systems adopted in the Constitutions have a direct impact on the exercise of taxation power in the two countries. In Australia, the federal and State governments exercise concurrent taxation power under the Commonwealth Constitution. While the federal Parliament has power to make laws with regard to taxation, it must not discriminate between States or parts of States.26 State governments also have power to legislate on local tax matters.27 Because the federal and State taxation powers deal with different matters,28 a direct and express conflict between these powers is "seen as an impossibility".29 Although the State taxation power was confirmed in several cases,30 State governments have since 1942 not exercised their taxation powers with respect to income tax,31 due initially to legal, and more recently political, considerations.32 However, some local taxes, such as land tax and stamp duties, are collected by every State.

26 Commonwealth Constitution, s.51(ii).
28 This proposition is based on two grounds. First, the federal and State taxation powers deal with different matters in the sense that the federal power applies to the Commonwealth and the State power operates only within a State. But the concurrence of the power results in possible overlapping and duplication between the federal and State taxes, e.g. between 1915 and 1942. Thus the second ground is that the federal and State taxation powers deal with different matters according to the arrangement made between the federal and State governments. In theory, State governments still have concurrent taxation power. But the exercise of this power would be impractical both politically and economically. Therefore, in a practical sense, federal and State taxation power deal with different matters.
29 Victoria v Commonwealth (1957) 99 CLR 575, per Fullagar J. at 657.
30 For example, Victoria v Commonwealth (1957) 99 CLR 575.
31 Before federation in 1901, some Australian colonies had introduced income tax. For example, the South Australian Government introduced a tax on land and also the first income tax in Australia in 1884. Victoria and New South Wales imposed similar taxes in 1895. State governments continued to regulate taxation after the Commonwealth was created in 1901. Tasmania introduced a land and income tax in 1902, Western Australia in 1907; and Queensland introduced an income tax in 1902 and a land tax in 1915. See Woellner, Vella & Chippendale, Australian Taxation Law (Sydney, CCH, 1987) 7-8).
32 See Woellner, id., at 62-3; and Baxt & Others, Cases and Materials on Taxation (2nd edn, Sydney, Butterworths, 1980) 3. Baxt and others state that "if the State government continued to impose income taxes of their own they would lose the Commonwealth grants and subject their electors to the additional State tax burden.
The federal Government introduced its own income tax in 1915. From 1915 to 1942, the federal and State income tax laws co-existed. In 1942 the income taxation system was unified under the pressure of the War. A Uniform Tax Scheme, which included four Acts - the Income Tax Act, the Income Tax Assessment Act, the State Grants (Income Tax Reimbursement) Act and Income Tax (War-Time Arrangements) Act - was then passed. State governments, although some of them challenged the validity of the federal tax scheme on separate occasions, have not levied income tax since then.

The federal taxation power is limited by the Constitution. Four restrictions on the federal taxation power have been generally recognized. First, a federal tax law cannot discriminate between States or parts of States. This requires that a federal tax law must apply to taxpayers in every State on a basis of equality. But "equality" in this context refers to direct equality as stated in a law rather than indirect or consequential inequality resulting from the operation of the law in different circumstances. Secondly, a federal law imposing a tax should deal with the imposition of the tax only. This is merely a restriction on the means through which a tax may be collected.

No government, irrespective of its popularity, could hope to remain in power if it adopted such measures.

33 The Income Tax Assessment Act 1915 (Cth).
34 A uniform income tax Bill was proposed in 1917 following the discussion between the federal and State ministers. But no uniformity was achieved. In 1932 a Royal Commission on Taxation was formed to investigate Australian taxation system. According to the recommendation of the Commission, a uniform income Act was passed by the federal Parliament in 1936.
35 Woellner, supra note 31, at 61-2.
36 e.g. South Australia v Commonwealth (1942) 65 CLR 373, and Victoria v Commonwealth (1957) 99 CLR 575.
37 Fairfax v F.C. of T. (1965) 114 CLR 1, 16.
38 Commonwealth Constitution, s.51(ii).
39 In Cameron v D.F.C. of T. (1923) 32 CLR 68, regs 46 and 46A of the Income Tax Regulations 1917 (Cth), imposing different duties on chickens produced in different States, were held invalid as being an infringement of s.51(ii) of Commonwealth Constitution.
41 Commonwealth Constitution, s.55, and Re.Dymond (1959) 101 CLR 11.
which the taxation power under s.51(ii) is exercised. Traditionally there have been
two separate Acts whenever a federal tax was imposed, with one imposing the tax
and the other prescribing measures for its implementation. The Income Tax Act
1936 (ITA) and the Income Tax Assessment Act 1936 (ITAA) are examples of this
function. Thirdly, a federal law imposing taxation must deal with only one subject
of tax. This constitutional requirement restrains the federal Parliament from
imposing a number of distinct taxes in one Act. Like the second restriction, this is
intended to prevent the House of Representatives from passing a tax law without the
Senate's full understanding and support. As a result, the legal framework for the
taxation of foreign-related businesses consists of several independent Acts, which
separately impose income tax, resource rent tax and other specific taxes. However,
this restriction does not apply to laws imposing customs duties or excises. Although
duty and exercise must be dealt with separately, an Act may be concerned with
several different duties or excises at the same time. Fourthly, a federal tax law
cannot "impose any tax on property of any kind belonging to a State", nor can a State
law "impose any tax on property of any kind belonging to the Commonwealth". But
the immunities extend neither to the importation of goods by a State, nor to
the pay-roll tax imposed on State governments by the federal Government.

5.2.2. Exclusive Taxation Power in China

Unlike Australia, the taxation power in China exclusively belongs to the
central Government. Although there is no special provision relating to the taxation
power in the Chinese Constitution, the taxation power of the central Government can
be supported by Art.62(3) which gives the NPC extensive legislative power to pass
and amend criminal law, civil law, administrative law and other basic laws. The
taxation power in relation to foreign investment is further reinforced by Art.18
which recognizes the existence of foreign investment in China, and Art.32 which
states that Chinese law applies to all foreigners in China. On the basis of these

43 Commonwealth Constitution, s.55. This section, in particular what are regarded
as different subjects of tax, was discussed in Resch v F.C. of T. (1942) 66 CLR 198.
44 Woellner, supra note 31, at 57.
45 Commonwealth Constitution, s.114.
46 Attorney-General of NSW v Collector of Customs for NSW (1908) 5 CLR 818.
47 McTiernan J, held that it is "not unconstitutional to tax equally payment of
salaries or wages or other remuneration by private employers and State governments
as such". State of Victoria v Commonwealth (1969) 122 CLR 353, 386.
provisions, the NPC and State Council may pass any law and regulations on the
taxation of foreign investment. Apparently, these three provisions are also the basis
for the central Government's general power to regulate foreign investment.

Both the NPC and the State Council have exercised legislative power to
regulate the taxation of foreign-related enterprises and foreign persons. In fact, the
IIT, JVIT, FEIT and CICT are imposed by the NPC whilst the VVLPT, URET, and
RET are the exercise of the State Council's delegated (or subordinate) legislative
power. A common feature of these State Council regulations is that local
governments are clearly responsible to varying degrees for the implementation of
these regulations.48

Local governments in China do not have express constitutional power to
regulate the taxation of foreigners. But they may in theory make subordinate tax
regulations under the provisions dealing with general local legislative power, such as
Arts.93 and 100 of the Constitution, subject to the same condition that none of their
laws is inconsistent with the Constitution, the law of the NPC and regulations of the
State Council. So far, Chinese local governments have not imposed any formal local
tax.49 Political impracticability is probably the reason which prohibits local
governments from entering into the taxation forum.50 Nevertheless, local
governments have been very active in providing tax reductions and exemption to
foreign investors at the expense of national revenue.51

48 For example, rates of VVLPT should be fixed by a provincial or municipal
government and the details should be reported to the Ministry of Finance (VVLPT
Regulations, Art.9); the implementing rules for URET Regulations should be made
by a provincial or municipal tax office, approved by the provincial or municipal
government and reported to the GTB (URET Regulations, Art.17); and the
implementing rules for RET Regulations should be made by a provincial or
municipal government and filed in the Ministry of Finance (RET Regulations,
Art.10).

49 However, disguised forms of levies were adopted by some local governments.
These levies became extra financial burden of Chinese and foreign enterprises. The
State Council made Provisional Regulations Prohibiting Solicitation of Funds from
Enterprises in 1988 to curb these informal levies imposed by local governments at
various levels. The English text of the Regulations can be seen in the Statutes and
Regulations of the PRC vol.5 (HK, UEA Press Ltd & Institute of Chinese Law

50 Since taxation matters are sensitive to both foreign investors and Chinese
nationals, the imposition of any local tax would definitely affect the implementation
of national law and policy. To prevent this, the central Government may always
invalidate any local tax law on the basis that the law is not consistent with the basic
aims of the existing law of the NPC and regulations of the State Council, or pass new
law to nullify the controversial local legislation.

51 This practice has become a highly controversial issue in Chinese foreign
investment law. More discussion on this will follow in this chapter.
5.3. Features of Taxation Authorities in Australia and China

5.3.1. Defining the Tax Authorities

In the context of Australian and Chinese tax laws, the tax authorities are the Taxation Office in Australia, and the Ministry of Finance or the General Tax Bureau (GTB) in China. A contrast can be seen in the status of the tax authorities in the two countries. The Australian Tax Office is a statutory body, but the Ministry of Finance and GTB are executive bodies of the Chinese Government.

Several reasons may explain why the Ministry of Finance in China must be regarded as one of the tax authorities. First, the Ministry of Finance has not only the power to make and interpret tax regulations, but also discretion in dealing with specific tax matters, such as giving approval to accelerated depreciation \(^{52}\) and determining whether a particular item is taxable.\(^ {53}\) Secondly, the GTB is a Department of the Ministry of Finance. In the exercise of its discretion under tax laws, the GTB is directed by the policy of the Ministry of Finance. Thus the policy of the GTB is often the Ministry's. In fact the administration of taxation in China is shared between the Ministry of Finance and GTB. In the sense that the Ministry of Finance can either exercise or delegate its power to the GTB, the Ministry of Finance and the Commissioner of Taxation in Australia bear similarities to each other. The GTB, on the other hand, handles routine administrative matters and exercises discretion delegated to it under tax laws passed by the NPC and under regulations made by the State Council or Ministry of Finance.

The federal Treasurer in Australia is not regarded as a tax authority because tax law does not expressly grant the Treasurer power to administer taxation. Although the federal Treasurer in fact exercises an influential power through his policy statements or budget papers in the administration of taxation, the power to do so has no express statutory basis. Instead the Treasurer's policies are based on the general executive power of the Government, and are enforceable through the cooperation (either voluntary or compulsory) of the Taxation Office, which may be "bound" (either legally or practically) by government policy in performing its

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53 Id., Art.27.
functions,\textsuperscript{54} and of taxpayers who may do so having regard to the certainty that the
policies would be incorporated into law in due course. The roles of the federal
Treasurer and that of the Ministry of Finance in China are in clear contrast. The
latter is authorized by law to administer taxation. Since statutory authorization rather
than the actual influence is the test for identifying the tax authorities in this thesis,
the federal Treasurer is excluded from this discussion.

5.3.2. The Commissioner’s Discretions in International Taxation

In the area of taxation, the Australian Government’s control of foreign
investment is assisted by the Commissioner’s discretions under the ITAA. In general,
the Government may implement its policies in relation to foreign investment through
either legislation or executive power. But in the context of taxation, the
Commissioner of Taxation is granted power to administer matters arising from the
ITAA. Although the Commissioner’s discretions are statutory powers by nature, the
exercise of his power may sometimes be affected by the government policies.

The influence of the Government on the exercise of the Commissioner’s
discretion can be seen in two respects. Theoretically, the Commissioner’s power falls
under the executive functions of the Government. Under the Australian
Constitution, the functions of the Government are divided into three basic categories:
legislative, executive and judicial functions. The Commissioner’s discretionary power
is neither judicial nor legislative (although in some cases it may be delegated
legislative power\textsuperscript{55}). Thus it must be executive. It is vested in the Commissioner by

\textsuperscript{54} Murphy J. supported by the majority of the High Court in \textit{Ansett Transport
Industries (Operations) Pty Ltd v Commonwealth} commented that the system of
responsible government adopted in the Australian Constitution requires that the
departments of the Government are guided by government policy. (1977) 139 CLR
54, at 87. In contrast Mason J. in the same case observed that a Minister cannot
without statutory authority “direct an officer in whom a statutory discretion is
reposed”; at 83. The issue concerned here is how should the Taxation Office which
has been given a statutory discretion to administer the ITAA exercise its power when
the Treasurer’s policy is concerned. It appears that if the view of the majority of
the High Court in \textit{Ansett Transport Industries (Operations) Pty Ltd v Commonwealth}
prevails, the Taxation Office is bound by the Treasurer’s policy; and if the view of
Mason J. (supported by the majority in \textit{Queen v Anderson; Ex parte Ipec-Air Pty Ltd}
(1965) 113 CLR 177)) is accepted, the Taxation Office is not bound by the policy but
should consider the relevant government policy in exercising its power. The need to
consider but not to be bound by government policy can be seen in the comments
made by Mason J. (1977) 139 CLR 83 and, inter alia, Kitto J. (1965) 113 CLR 193.

\textsuperscript{55} Barwick CJ in \textit{Giris Pty Ltd v FCT} held that when the Commissioner of Taxation
may choose to assess an income under one section rather than another, he exercises “a
legislative discretion”. Barwick CJ also commented that in some cases when the
Commissioner is required to make a decision without being provided with guidance
by the legislature, the Commissioner’s discretion “is in truth a function of the
the Parliament for the purposes of implementing tax law and policy. The independent status of the Commissioner does not change the nature of the power exercised, although an intention on the part of the Parliament to separate the exercise of this power from the exercise of other executive powers is clear. The Commissioner's power is subject to the guidance of the Executive. This is because the Parliament did not make the Taxation Office an independent body accountable directly to the Parliament, although it has power to do so. In fact, when the exercise of legislative power is strongly influenced by the government policies through the arrangement that the Ministers of the Government are the members of the legislature, the exercise of the statutory power by the Commissioner cannot be free of influence of government policies, given that the Commissioner is appointed by the Government. There is no direct conflict between the statutory provisions which require the Commissioner to perform his duties in a specified manner and the influence of the government policies. When the law is specific and non-discretionary, the Commissioner must implement the law in the manner prescribed by law. However, when the law grants a discretion to the Commissioner, he may take government policies into account as he thinks fit. This is implied in the act of granting discretion. Thus, foreign investment policies which are based on the notions of fairness, equity and natural justice may be taken into account by the Commissioner.

56 The Parliament's power to do so has received judicial recognition. See Baxter v Ah Way (1909) CLR 626 and Heiner v Scott (1914) 19 CLR 381.

57 Indeed judicial opinion seems to suggest that an official exercising statutory power should be directed by the government policy which is consistent with law. The Queen v Anderson Ex parte Ipec-Air Pty Ltd (1965) 113 CLR 177, and Ansett Transport Industries (Operations) Pty Ltd v the Commonwealth (1977)139 CLR 54.

58 In Giris Pty Ltd v FCT, Windeyer J. held that when exercising discretions, the Commissioner "is to be guided and controlled by the policy and purpose of the enactment, so far as that is manifest in it". (1969) 119 CLR 365, 384. This opens a possibility that the policy so referred to can be the policy announced when the provisions of law are made or the policy formed after the enactment of an Act for the purposes of explaining the provisions which have not be clearly defined in the Act. This also pragmatically extends to the policy announcing forthcoming changes to tax laws. Judicial confirmation of the legality of taking policy into consideration when exercising the Commissioner's discretions can be seen from another angle. In the same case, Barwick CJ. did not agree that the Commissioner is bound by policy. But he noted the varieties of factors that may be considered by the Commissioner. Thus, he commented that he found in ss.99A and 99 "considerations of a kind upon which a legislature acts in deciding whether an enactment or its particular terms are or are not unreasonable having regard to the interests of the public generally, of the citizen to be affected, of the revenue and of the requirements of those policies, political, economic and fiscal which the parliament is prepared to sanction". (1969) 119 CLR 365, 372.
In practice, the influence of government policy on the exercise of the Commissioner's discretions is even clearer. No statute of the federal Parliament has given the federal Treasurer power to administer taxation. But the Treasurer has frequently issued news releases and policy statements regarding various taxation matters. The power of the Treasurer can be supported by the executive power of the Government for the "maintenance of the Constitution". The issue concerned here is what is the relationship between the Treasurer's policy statements and the ITAA, in particular the Commissioner's discretions under the Act. Two situations may occur in relation to the effect of the Treasurer's policy. When the Treasurer's news release announces an amendment expected to be made to tax legislation in the future, the statement may be treated in the same way as the announcement on the changes expected for the Foreign Takeover Act 1975 (Cth) in the Guidelines. The policy forecasting the changes in legislation is not enforceable in a court of law, but is practically applicable because of the certainty of the legislative changes and the difficulties of challenging it at a court. In this case, although the policy is literally inconsistent with the language of an Act (e.g. the tax rates announced in advance for each tax year by the Treasurer in his Budget Paper) the Commissioner seems to have followed the Treasurer's policy regardless of any technical inconsistency with the Act. When the Treasurer issues a policy in relation to the matters which are subject to the discretion of the Commissioner, the policy not only directs the Commissioner in the exercise of the discretion, but also prevails over the Commissioner's decisions which are inconsistent with the policy. The prevailing effect of government policy has been seen in many occasions when the Commissioner decided "how the law should be applied to particular types of arrangements".

In relation to control of foreign investment, the Commissioner's discretion is an essential means through which government policy is implemented. As have been seen, although the Treasurer can announce government policy in relation to taxation

59 Given the certainty of the proposed changes becoming law, a legal action to challenge the policy may soon lose its legal basis by the time of the court hearing, in particular when a retrospective provision to the plaintiff's disadvantage has been inserted into the Act.

60 For example, the Treasurer announced that FBT is not applicable to local governments councillors; and that the Government would refund the tax payments which had been collected from them in accordance with the Taxation Ruling No. MT2035. This resulted in the withdrawal of the Ruling by the Taxation Office which did so after a declaratory order was issued by the Federal Court in August 1989. See Butterworths, (1990) Weekly Tax Bulletin para.149.

61 M.Leibler, "The Policies of Tax Administration" (1990) 19:1 Australian Tax Rev. 9, 12. Examples with regard to Taxation Ruling IT2512 and IT2546 are given in this article, at 12-3.
of foreign investment, the policy must be implemented by the Commissioner through his power to administer taxation. Therefore, in the context of international taxation, the Commissioner is bound (politically rather than legally) to consider the government policies. The connection between them is voluntary in a legal sense but mandatory in a practical sense.62

5.3.3. Power of the Ministry of Finance in the Taxation of Foreign Investment

Unlike Australia, China has not passed any special law dealing with the administration of taxation. Rather, various tax laws authorize the Ministry of Finance to act as the Ministry responsible for the interpretation of tax law,63 and the GTB or its local branches to act as the taxation offices in charge of the administration of taxation.64

Generally speaking, the power of the Ministry of Finance to interpret taxation and make regulations for the implementation of tax law is granted by the law of the NPC,65 and on occasion by regulations of the State Council.66 Its regulations have the force of law. The power of the Ministry of Finance does not automatically extend to the GTB.

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62 In theory, the Commissioner is not bound by government policy except where the law so states. But in practice, the Commissioner may voluntarily cooperate with government policy for several reasons. First, judicial opinion seems to support that an officer exercising statutory power should take government policy into account provided that the policy does not contravene the law. (See Queen v Anderson Ex parte Ipec-Air Pty Ltd (1966) 113 CLR 177, Ansett Transport Industries (Operations) Pty Ltd v the Commonwealth (1977)139 CLR 54, and Giris Pty Ltd v FCT (1969) 119 CLR 365, 384.) Secondly, the Commissioner is a political appointment. The Government must be certain that the appointee would understand government policy before making the appointment. Thirdly, Treasurer's policy often suggests likely legislative changes in future. A rigid refusal of a Treasurer's policy by the Commissioner may often reduce efficiency in the administration of tax law, especially when the policy becomes law with retrospective effect.

63 For example, IIT Law, Art.26; CICT Regulations, Art.18; FEIT Law, Art.18; and JVIT Law, Art.17.


65 e.g. IIT Law and FEIT Law.

66 e.g. the State Council Regulations Concerning Encouragement of Foreign Investment, CCH, China Laws For Foreign Business para.13-509.
The Ministry of Finance plays an important role in the regulation of tax matters. It has power to make rules implementing the CICT Regulations, IIT Law, JVIT Law and FEIT Law, and to supervise the implementation of the VVLPT Regulations, URET Regulations and RET Regulations, whose implementing measures are intended to be made by local governments. Regulations of the Ministry of Finance are usually made under direct authorization of the NPC, such as IIT Regulations and JVIT Regulations. Sometimes, they are made allegedly pursuant to specific provisions which, however, do not expressly authorize the Ministry of Finance to do so. This practice of the Ministry could probably be supported by its general delegated power to make implementing and interpreting rules for tax laws, granted by a number of tax legislation. After all, the Ministry may justify its regulations by the Chinese constitutional principle, that the executive may make regulations according to the Constitution and the law of NPC provided that the regulations so made are not inconsistent with the Constitution and the law of the NPC.

5.3.4. Power of General Taxation Bureau in the Taxation of Foreign Investment

The GTB, which is a department of the Ministry of Finance, is the head of the taxation offices in China. It has provincial branches in each province and local offices at various lower administrative levels, which extend to counties in rural areas and districts in urban areas. The main responsibilities of the taxation offices are to collect taxes, examine tax returns and investigate activities involving tax avoidance. On various occasions the GTB has released explanatory documents (notices or circulars) to its branches on specific issues regarding taxation of foreign-related enterprises. A similar practice is also followed by several local offices.

67 Local governments have not formulated formal rules in relation to the implementation of URET Regulations, RET Regulations and VVLPT Regulations.

68 For Example, the Ministry of Finance stated that it made the Provisional Regulations for Collection of CICT and Enterprise Income Tax from Resident Representative Offices of Foreign Enterprises (see CCH, China Laws for Foreign Business para.31-600) in accordance with Arts.2 and 8 of CICT Regulations, Art.1 of the FEIT Law, Arts.2 and 4 of the FEIT Regulations, and Art.9 of the Interim Regulations of the State Council Concerning Control of Resident Representative Offices of Foreign Enterprises. But none of these provisions directly authorizes the Ministry to make these Regulations.

69 Including local governments in municipalities directly under the central Government and autonomous regions, which are equivalent to provinces.

70 For example, Notice of the GTB of the Ministry of Finance concerning Several Regulations Relating to the Levying of Income Tax on Sino-foreign Joint Equity Enterprises, and Co-operative Production Enterprises and Enterprises With Sole Foreign Investment, CCH, China Laws For Foreign Business para.33-515; hereinafter
such as the Beijing Municipal Taxation Office, which issue notices to explain the regulations of the Ministry of Finance. Presumably, these notices are effective only within the areas designated by the GTB or within the authority of the relevant local office. It can be argued that even if these notices are not a recognized form of law, they are enforceable so long as they are consistent with the applicable laws and regulations. In practice, these notices may be regarded as the internal instructions of a superior tax authority to its subordinate offices, directing the application of tax law in specific situations.

5.4. Discretionary Power of the Tax Authorities
5.4.1. Features of Discretion

A discretionary power is a power (legislative, executive or judicial) that allows "the power-holder a certain degree of choice as to what he will do or as to what decision he will reach". The essential feature of a discretionary power is twofold: first, the power is granted by an authority, and secondly, the holder of the power has varying degree of autonomy in exercising the power. For the purposes of this thesis, judicial discretion will not be examined.

To delineate the boundary of a discretionary power is a very difficult task. Often, subjective rather than objective criteria are needed in determining what is or is not a discretionary power. For instance, the difference between a discretionary power and a duty under a statute is usually clear. A duty-holder does not have any choice as to what he will do. The cause and consequence are prescribed by law. The duty-holder can only act in accordance with what has been clearly prescribed in law. But sometimes a duty to decide a question of fact or of law requires an active contribution from a duty-holder who thus has to decide why this fact but not the

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71 e.g. Notice on the Question of Income and Payment of Income Tax by Sino-foreign Joint Equity Enterprises, and Co-operative Production Enterprises and Enterprises With Sole Foreign Investment, issued by Foreign Tax Division, Beijing Municipal Tax Bureau, CCH, China Laws For Foreign Business para.33-518. Other examples can be found in CLP.

72 The Chinese Constitution allows departments of the Government (including local governments) to make regulations, which are enforceable upon the approval of appropriate authorities.


74 This is a matter of definition. A "duty" to exercise a discretion is treated here as a discretionary power rather than a "duty".
other, or why this provision but not the other, is relevant. The process involves both the interpretation of laws and the identification of facts. During this process, the duty-holder actually makes decisions as to the fact or law and has a choice as to what he thinks fit although the degree of such choice is always circumscribed. In this case, the duty-holder may also be a power-holder, and the boundary of discretionary power is blurred. But, as noted by Cane, "powers to decide questions of fact or law are usually not labelled as discretionary power".

Apart from the essential point that a discretionary power is a kind of autonomy to act as the holder thinks fit, a discretionary power has several features. First, a discretion requires that the holder must act in accordance with the purposes of the discretion and "settle upon the policies and strategies for achieving them". The discretion is seen in identifying and interpreting the purposes and in applying the policies and standards, or in the procedure to reach the purposes. Secondly, the boundary of discretions varies. A discretion can be wide and unstructured, or specific and structured. In each case, the ambit of a discretion is limited by the terms granting the power. Thirdly, a discretion requires the holder not to generalize the application of his power. The holder may formulate general measures and standards for exercising the discretion, but must react to each particular case.

75 For example, the Commissioner of Taxation in Australia can decide who is or is not a resident in Australia. The tests for residence are described in the ITAA and common law. In a simpler case when a company or individual satisfies a test, it or he is a resident in Australia. The Commissioner thus has no power but a duty to treat the taxpayer as a resident. But in a complicated case when there are several facts relating the residence of a taxpayer, the Commissioner may choose one of the facts and apply a test he thinks fit. A discretion is exercised in this process.

76 Cane, supra note 73, at 63.


78 Ibid.

79 In this case the law granting discretion to an executive arm of the state does not describe criterion or conditions for the exercise of the power. For example, the ITAA, s.263, which allows the Commissioner of Taxation in Australia to have free access to all buildings, places, books, and documents for any purposes of the Act. If the Commissioner decides to exercise this discretion himself, no condition is set out as to how the discretion should be exercised. Similar example is Art.44 of FEIT Regulations in China, which allows tax offices in China to impose a fine up to 5,000 yuan on foreign enterprises which violate Arts.8, 9, 10 & 12 of the FEIT Law. No criterion is set forth as to how the power should be exercised.

80 In this case some criteria and standards in relation to the application of the discretion, which may vary in degree of precision and clarity, have been attached to the authorization. For example, the ITAA, s.99A(3) and FEIT Regulations, Art.41.
individually. This is a requirement for the administration of discretion. However, the appropriateness and applicability of the measures in a given case is, in a circular way, again dependent upon the discretion of the holder. This fact may defy the purposes of the requirement. This is part of the reasons why supervision of discretionary power is necessary.

5.4.2. Defining the Tax Authorities' Discretion

The tax authorities' discretion is a specific type of power vested in the Taxation Office in Australia and the Ministry of Finance or GTB in China by the tax law of each country. Under that authorization, the tax authorities have power to make decisions in accordance with the purposes of the law, the criteria set forth in the law and policies relating to the implementation of the law. Like discretionary power in other areas of law, the tax authorities' discretion is necessary "in the interests of fairness to the taxpayer, or to facilitate the administration of the Act." As will be seen, most discretionary powers of the tax authorities concern the interpretation of provisions and the application of general rules to varieties of situation which can never be enumerated and specified in a tax Act.

In exercising their discretions, the Commissioner of Taxation in Australia and the Ministry of Finance or GTB in China are bound by law, and by natural justice. This important characteristic of the tax authorities' discretion was noted by the Australian Taxation Review Committee in 1975. The Committee then pointed out that:

The possession of a discretion by the Commissioner does not mean that he is completely at large in its exercise. It is not his private opinion that he is to express. He must act according to law and reason and to the justice of the

81 Galligan, supra note 77, at 22.

82 K. Ryan "Curbing the Commissioner's Discretionary Power" in R. O'Neill & Others eds, Tax Essays vol.1 (Sydney, Butterworths, 1979) 1, 2.

83 In Australia, restrictions on the manner in which the Commissioner exercises his discretion are found in common law principles. See Padfield and Others v Minister of Agriculture, Fisheries and Food & Others [1968] AC 997, 1047 & 1049; Perpetual Executors Trustees and Agency Co (WA) Ltd v FCT (1935) 3 ATD 132, 135. In China, the restrictions can be seen in the Constitution which prohibits the executive to make any regulations or decisions in contrary to the Constitution and the laws of the NPC. The Chinese Constitution, Art. 90.

84 Padfield and Others v Minister of Agriculture, Fisheries and Food & Others [1968] AC 997, 1007.
case and not arbitrarily or capriciously or upon inadmissible or irrelevant grounds.\(^{85}\)

Similar but less unambiguous views are expressed by Chinese legal scholars. They argue that executive power is subject to "legal conscience", which is perhaps a Chinese version of natural justice, and "administrative law" which refers to a body of law governing the exercise of executive and judicial power in China.\(^{86}\) Thus the tax authorities' discretion is subject to supervision (either judicial or administrative) in Australia and China.

5.4.3. The Necessity for Tax Authority Discretions

Taxation is highly sensitive (in the sense of its impact on the life of ordinary people), complicated (in the sense of its wide variety of factors that affect the fairness of tax law) and crucially important (in the sense of its financial impact on national revenue and economy). It is thus difficult for legislators to pass a law which can solve every specific case of taxation with simplicity, clarity, precision and effect such that every taxpayer would be able to discern the precise limits of liability and no one would be able or want to avoid liability by tax schemes which are not clearly prohibited by law. Therefore, tax authorities must have discretions, although the scope of discretions granted to them may vary.

The necessity of tax authorities' discretions has been clearly recognized in both Australia and China. In Australia, the Commissioner's discretion is regarded as the "only practical means" to reach a fairness in taxation "so that the Revenue should not obtain more than in all fairness it is entitled to" and "the taxpayer should not, at the expense of his fellow taxpayers, escape payment of his just liabilities".\(^{87}\) In addition, the Commissioner's discretion is also a "feasible alternative" to lengthy and complex legislation, and an "effective way to deal with certain tax avoidance scheme".\(^{88}\) The Chinese view of tax authorities' discretion can be seen in its recognition of the importance of executive discretion in general. For instance, some textbook writers argue that because of the highly developed economy and complicated variety of social divisions today, a legislative discretion is necessary.\(^{89}\)


\(^{87}\) Taxation Review Committee, supra note 85, para.22.6.

\(^{88}\) Ryan, supra note 82, at 2.

\(^{89}\) Pi, supra note 86, at 86.
They further argue that if there is no executive discretion (used narrowly to refer to discretion other than power to make regulations), the legislative discretion would be meaningless. According to this argument, legislative discretion refers to delegated (or subordinate) legislative power exercised by the executive branch of the Government. Since the broad regulation-making power of the Chinese Executive Government is exercisable by the executive in Australia under the authorization by the Parliament, the so-called "legislative discretion" is to some extent comparable with executive discretion in Australia. Due also to the extensiveness of the regulation-making power in China, many executive discretions under Australian law are regarded as an exercise of "delegated legislative power" in China. This further suggests that the "legislative discretion" is often comparable with executive discretion in Australia, in particular in the area of taxation. As suggested in the Chinese arguments, such discretion is needed for dealing with complicated and varying economic and social issues, which in the context of tax law refer to such matters as fairness in taxation, complexity of law and the variety of tax avoidance schemes. Chinese scholars hold that discretion is necessary both in the process of making rules to tackle those issues and in the process of implementing these rules.

5.4.4. Functions of Tax Authorities’ Discretions

The tax authorities’ discretions have two basic functions: the administration of taxation (administrative discretion) and the elimination of tax-avoidance schemes (anti-avoidance discretions). Administrative discretion refers to power conferred upon the Commissioner in Australia or the Ministry of Finance and GTB in China to determine matters which are not involved with tax-avoidance schemes. Determining whether an item which is not specified in law is taxable or whether an accelerated depreciation should be allowed are examples. Anti-avoidance discretions are powers exercised by the Commissioner or his counterpart in China to control any act or scheme which is performed or made for the purposes of avoiding the taxpayer's legal liability. Articles 43 and 44 of the FEIT Regulations in China and ss.46(3) & 202BF of the ITAA in Australia are examples. Sometimes the distinction between the two functions is blurred. For example, in China the Ministry of Finance may determine

90 Id, at 111.

91 For example, the GTB has discretion in interpreting many provisions of tax law. It may exercise discretion in each particular case or may issue circulars or notices dealing with a given category of issues. In the latter case, the circulars and notices of the GTB may be treated as a source of law in China. By contrast, the Rulings of the Australian Taxation Office are not in theory regarded as a source of law but are enforceable under its discretions. In this context, the difference between the "legislative discretion" and "executive discretion" is rather nominal than substantial.
an item which is not specified in law to be taxable. This power can be used either unspecifiedly for the purposes of tax assessment, or particularly in the case of tax-avoidance. Similarly, in Australia s.263 of the ITAA gives the Commissioner a free access to documents and information, which can be used either for ordinary administrative purposes or for anti-avoidance purposes.

5.4.5. Categories of Tax Discretions

Discretion can be either structured or unstructured. Structured and unstructured discretions are distinguished according to whether any objective criterion, which can be regarded as a limitation on the tax authorities' discretion, has been laid down, regardless of how abstract the criteria may be.92 Structured discretions refer to any discretions whose exercise is subject to some objective criteria, whether brief or exhaustive, laid down in law as guidelines. An example of briefly structured (or "partially structured" in Grbich's words93) discretions in Australia is s.27H(3) of the ITAA.94 An example of exhaustively structured ("fully structured"95) discretions in Australia is s.51AE(13) of the ITAA.96 On the other hand, unstructured discretions refer to discretions for which no criterion (or no clear criterion) for the exercise of the power has been laid down. Section 82EK(1) of the ITAA97 is an example in Australia. Similar discretions can be found in

92 For example, Art.41 of FEIT Regulations requires officials from tax offices to carry identification cards while investigating financial, accounting and tax affairs of foreign enterprises. "Carrying an identification card" is the criterion for exercising the power; but issues, such as what is the "identification card", whether the tax offices have free access to all documents, whether the tax offices may copy or move documents away from the taxpayers' possession, are to be determined by the tax offices which carry out the investigation, or by the Ministry of Finance or GTB if they think necessary to do so.


94 It allows the Commissioner, while determining a deductible amount, to take into account not only "the terms and conditions applying to the annuity", but also "such other matters as the Commissioner considers relevant".

95 Grbich, supra note 93, at 22.

96 It specifies that, if under an agreement a taxpayer incurs a loss or outgoing and also non-deductible entertainment is provided to the taxpayer or another person, the Commissioner may allow the loss or outgoing to be deducted to such extent as he considers reasonable.

97 It allows the Commissioner to determine the amount payable in respect of the acquisition or construction of the unit of eligible property under the circumstance specified in the section without actually laying down any amount.
ss.103AA(4)(e) and 103AA(7) of the ITAA. In China, Art.34 of JVIT Regulations\textsuperscript{98} and Art.29 of JVIT Regulations\textsuperscript{99} are examples.

The difference between unstructured discretions exercised by the Commissioner in Australia and the Ministry of Finance and GTB in China is a matter of degree. The Chinese tax authorities often exercise a wide legislative discretion, which, however, has been vested in the Commissioner in Australia only when he is in a position to apply one section of the ITAA rather than the other as he thinks it reasonable to do so.\textsuperscript{100} The contrast between their discretions is that the Chinese tax authorities may usually make legally enforceable regulations without specific authorization, but the Commissioner in most cases may only explore the potential applicability of an existing provision when applying the provision to a given case.

The provisions granting structured or unstructured discretion to the tax authorities in Australia and China are worded differently. For example, s.24N(2) of the ITAA, which allows the Commissioner to treat a prescribed company as a Territory company for the purposes of ss 24F, 24G, 24J and 24L "if he considers it reasonable in the circumstances to do so", is a wide (unstructured) discretion although the matter concerned is a fairly narrow one. The Commissioner is not bound by any specified criterion or consideration while determining whether a prescribed company is a Territory company, although he must take into account specified facts while determining the amount of income of the company in the year concerned.\textsuperscript{101} In contrast to a wide discretion, an example of specified discretions can be found in s.99A(3) of the ITAA, which specifies "matters to be considered by the Commissioner" when taxable income of certain trusts is concerned. The Commissioner is bound to consider these matters while exercising his discretion under s.99A.

\textsuperscript{98} It gives the Ministry of Finance a general power to interpret all provisions of JVIT Regulations.

\textsuperscript{99} It allows the tax offices to impose fine up to 5,000 \textit{yuan} on joint ventures which violate Arts.25 and 26 of the Regulations.

\textsuperscript{100} Per Barwick CJ. in \textit{Giris Pty Ltd v FCT} (1969) 119 CLR 365, 372.

\textsuperscript{101} S.24N(2) further states that when the Commissioner determines the prescribed company to be a Territory company, the income of the company in that year is "so much only of any income derived by the company during that year of income that is income to which section 24F or 24G applies is exempt from income tax as the Commissioner considers reasonable having regard to the extend to which Territory residents were the beneficial owners of shares in the company at the time when the income was determined". The second half of the section grants the Commissioner a specified discretion.
Although in the context of Australian tax law discretions may be divided into as many as seven categories, in the context of Chinese tax law discretions are either unstructured or only slightly structured. In fact, a wide discretion is exercised by the Ministry of Finance and GTB. Often, criteria set out by law in structured discretions are simple and vague.

5.5. Assessing the Tax Authorities' Discretions
5.5.1. Discretions, Legal Rules and Fairness

One of the purposes of vesting discretions in tax authorities is to achieve fairness in taxation. The Australian Taxation Review Committee expressed the following view in 1975:

The only practical means, on the one hand, of coping with the cases of hardship and providing an equitable result for the inevitable departure from the norm so that the revenue should not obtain more than in all fairness it is entitled to and, on the other, of ensuring that at the same time the taxpayer should not, at the expense of his fellow taxpayers, escape payment of his just liabilities, in many instances is by the exercise of a discretionary judgment to reach the solution called for by the particular circumstances of the case.

A similar view has been expressed by Chinese scholars. One writer asserts that one of the basic principles of taxation is fairness. In order to implement these provisions, a competent authority designated by law should have flexible power with regard to matters such as the determination of taxable items, the application of tax rates, and the reduction of or exemption from tax. The competent authorities in China are the Ministry of Finance and GTB, in particular GTB.

Fairness in relations to discretions in general, as argued by Galligan, has two meanings. Under some circumstances, it concerns the "principles upon which benefits and burdens are distributed among the members of society". But

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102 These are unstructured discretions, partially structured discretions, fully structured discretions, discretions with over-riding duties, discretions deemed to have binding effect, anti-avoidance provisions with vague objective criteria, and mini-anti-avoidance formulas. Grbich, supra note 93, at 22-4.

103 Australia Taxation Review Committee, supra note 85, para.22.6.

104 "Fairness" here, according to the writer, means that the liability of various taxpayers should be fair and reasonable under tax law, so that the conditions in which taxpayers compete with each other are relatively equal. S.M.Sun, An Introduction to Taxation (Shui Shou Jian Jie Beijing, Chinese University of Politics and Law, 1986, in Chinese) 15.

105 Id, at 20.

106 Galligan, supra note 77, at 152.
sometimes, it refers to procedural fairness.\textsuperscript{107} In the context of taxation, although "it is an ideal of exceeding difficulty to define and harder still to measure",\textsuperscript{108} fairness in relation to taxation may broadly have three meanings. First, fairness means that tax should be collected according to one's ability to pay. This task, as noted by the Taxation Review Committee, is "a difficult objective to achieve in view of the infinite variety of circumstances which attends even those with comparable grades of income."\textsuperscript{109} Secondly, fairness requires that a distinction must be drawn between a lawful scheme which minimizes tax liabilities and an illegal scheme which avoids tax liabilities. Thirdly, fairness requires that fair, equal, and unprejudiced procedures should be provided so that taxpayers may properly exercise their rights.

Fairness in taxation is an aim to be fulfilled by exercising discretions. But sometimes the aim, and the means through which the aim is to be reached, may conflict. It has been argued that unfairness occurs when there are no clear standards to guide the executive in the exercise of discretions.\textsuperscript{110} This results in either inconsistencies or unpredictability in the exercise of discretionary power. Both create unfairness. Thus, it is suggested that "fairness requires the formulation and notification of the standards\textsuperscript{111} under which discretions are exercised. But, in the context of taxation, the exercise of a discretion sometimes denies the existence of precise "standards" which are intended to guide the discretion. If a tax law granting a discretion is specific and complicated, the discretion will be too rigid to be a discretion. The restraints defy the purpose of discretion and fairness in taxation will not be achieved. If the "standards" are too brief and wide, the exercise of discretions may result in abuse of the power, resulting unfairness in taxation. Thus the purpose of discretion is also denied. Ideally, there should be a balance between the unfairness likely to be caused by the absence of discretions and the abuse of power which may result from the exercise of discretions. But pragmatically, the existence of discretion often excludes the presence of precise and clearly applicable legal norms. Having regard to this contradiction, it should be noted that a discretion, when its existence is crucial to fairness in taxation, does need to be properly constrained if it is to perform its functions.

\textsuperscript{107} Id., at 153.
\textsuperscript{108} Australia Taxation Review Committee, supra note 85, para.3.7.
\textsuperscript{109} Id., para.22.5.
\textsuperscript{110} Galligan, supra note 77, at 154-5.
\textsuperscript{111} Ibid.
Australian tax law has taken notice of unfairness likely to be caused by the exercise of unguided discretions. Based on the recommendation of the Taxation Review Committee, the most provisions in the ITAA granting discretions are structured discretions, although the clarity and precision of these provisions vary.

Australia and China have adopted different views of fairness and discretions. The tension between fairness and discretion undoubtedly exists in both countries. But unlike Australia, China has not conducted any formal study or inquiry into this issue. The differences between the two countries are reflected in their tax legislation. In Australia, most provisions in the ITAA which grant discretions are structured; but in China, most provisions are unstructured or poorly structured. This has given the tax authorities in China, as mentioned earlier, very wide and general discretions.

Australia and China have different legal traditions with regard to the exercise of discretions. It is well known that the executive in China has traditionally exercised a wide discretion, which was often neither authorized nor restricted by statutes. The influence of this tradition is so deep that even today the issue whether executive discretions should be appropriately guided by statutes has not been given any attention by administrative law lawyers in China. Chinese scholars generally agree that executive discretions should be scrutinized and supervised, but do not expressly accept that the formulation of detailed rules as guidance for discretions is a

112 Australia Taxation Review Committee made the following recommendation:

Whenever the law gives a discretion to the Commissioner, it should at the same time indicate the principle to which the Commissioner is to give effect in the exercise of the discretion; if the principle is not otherwise evident, it should be possible to infer it from any guidelines included in the section giving the discretion.

supra note 85, para.22.9.

crucial means of constraining discretions. This is because Chinese intend not to see fundamental differences in the values of fairness represented by the rules, that are made by legislature, and given by the executive, either through regulation-making power or executive discretions. Therefore, the existence of detailed guidance for the exercise of executive discretions seems unimportant.

The different legal traditions of Australia and China can also be seen in the style of legislation. Compared with Australian law, Chinese law always seems more general, abstract and vague. Its application largely depends on the interpretation given by the executive and, in some cases, the judiciary. Because of this tradition, the absence of detailed or structured guidance for the tax authorities in China is probably not regarded as a ground for dissatisfaction. If legislators in a country believe that the executive should have wide power to interpret and implement statutes, there is probably no reason to believe why the executive should be guided strictly by the legislature. This may, from another angle, explain why controlling the

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114 Chinese textbook writers argue that measures and conditions are necessary for ensuring the legality, fairness and validity of administrative activities. The legality, fairness and validity are ensured through three basic means: legal conscience in administrative law (spiritual assurance), supervision through "administrative law and order", and supervision through litigation procedures. Legal conscience in administrative law is an important part of legal conscience and a common term referring to one's ideas, views and mentality towards administrative law and social phenomena to which administrative law applies. Legal conscience in administrative law requires the persons who have discretions to increase their knowledge of administrative law, assess their attitude to administrative law and adopt law-abiding mentality towards administrative law. (This is a modified version of the "law-abiding-spirit" in the 1950s which called on Party members to "obey the Party Constitution and to observe their obligations as Party members by setting an example in strictly keeping the law". A.Tay, "Law in Communist China - Part 2" (1968-71) 6 Syd.L.Rev. 335, 353.) Supervision through "administrative law and order" is hardly explained by these writers. In a vague way, the writers appear to imply that the supervision through the "administrative law and order" means that all discretions, (including legislative discretions, executive discretions, and judicial discretions) should be controlled by all walks of the society, such as the Party, governmental branches, enterprises, social organizations, mass organizations and ordinary citizens. See, Pi, supra note 86, at 150-78. Supervision through litigation procedures has different meanings in China. Broadly, it means any litigating process or dispute resolution conducted by executive, judiciary, administrative courts or legislature. Narrowly, it refers to judicial process of dispute resolution carried out in the court of law. See Luo, id, at 406. None of these controlling measures is directly relevant to control of discretions through the formulation of detailed rules.

115 Chinese lawyers argue that the executive in China has seven different executive powers. These are power to make regulations, power to make discretionary decisions, power to allow or disallow a certain activity, power to compel the performance of certain duty, power to execute executive orders, power to punish a certain activity and power to arbitrate certain disputes. It appears that all these powers except the general power to make regulations may fall within the scope of executive discretions as understood in Australia, where regulation-making power of executive is not as wide as the similar power in China.
tax authorities' discretions by the formulation of detailed legal rules has not received any attention in China.

Popular legal opinion in China appears to believe that the formulation of detailed legal rules is not a crucial part of preventing the abuse of the tax authorities' discretions and guaranteeing procedural fairness, although it emphasises general supervision (including judicial supervision) over the exercise of executive power.\(^{116}\) However, the means of supervision adopted in China seems to represent a more complicated but less effective system of supervision. As a matter of fact China has not developed any practical means of combating the abuse of executive discretions. Various measures discussed in the textbooks can hardly be implemented. For example, supervision of the exercise of executive discretions by the Party or the executive itself leads to the replacement of one executive discretion by another.\(^{117}\) An impartial means of supervision seems necessary. The impracticability of the system can also be seen in the means of supervising the executive by mass organizations, a factually meaningless label, and by judicial authorities (such as the procuratorate and the courts), which are almost powerless because they lack both detailed rules of supervision by which legality and illegality could be determined and ideas of equality between ruler and ruled. Fairness in taxation in China is in fact not supported by procedural fairness and thus is incomplete.

Australia has given considerable attention to possible abuse of Commissioner's discretions, and regards the formulation of detailed legal rules and judicial supervision as effective means of reducing unfairness caused by a possible abuse of discretions. By contrast, China has not seen the abuse of the tax authorities' discretions as an issue at all. Activities which may be regarded as abuse of executive

\(^{116}\) For example, in the discussion of supervision on the executive, some argue that the executive should be supervised by legislature (in particular, including the supervision on the exercise of delegated legislative power, examination of governmental budgets, enquiry into government policies, and appointment or removal of governmental officials), the executive at various levels (in the sense of supervising individuals by the offices), procuratorate and courts. Luo, supra note 113, at 340-74. Some argue that activities of executive should be examined through four basic means: improving individuals' (both officials and ordinary people) understanding and knowledge of administrative law, supervising the executive by external authorities (such as the Party, legislature, judiciary, mass and social organizations), and supervising the executive by internal authorities (such as examining local governments by the Central Government, criticising the Central Government by local governments, supervision between different branches of government, and supervision by the Audit Authority). Pi, supra note 86, at 150-78.

\(^{117}\) Such replacement cannot prevent and correct the abuse of executive discretions, because both the Party and executive are affected mainly by Party and government policies, which do not often coincide with the notion of fairness held by taxpayers. But the taxpayers' view of fairness is always the basis on which an allegation against the abuse of power is made.
power by Australian standards may be regarded as reasonable in China, where the executive has exercised a wide discretion.

5.5.2. The Exercise of Tax Authorities' Delegated Power

Discretions are delegated to the tax authorities in Australia and China in different ways. In Australia, the discretion of the Commissioner of Taxation is granted by the ITAA and TAA. The latter vests the Commissioner with a power to delegate his power under the ITAA to other proper persons. In China, the Ministry of Finance is given power to make tax regulations by the law of the NPC, and GTB is granted discretion by both the law of the NPC and regulations of the State Council (including its Department - the Ministry of Finance). Although no law has specified that the Ministry of Finance may delegate its power to others, GTB has in fact exercised legislative discretion, which under law should be exercised by the Ministry of Finance, in interpreting tax laws and regulations. Many Circulars and Notices explaining tax laws and regulations have been issued by the GTB and its local offices. Evidently, the link between the Chinese tax authorities in delegating discretionary power seems not as clear as the process of delegating power in Australia. The reasons for this difference will be probed below.

A fundamental difference between Australian and Chinese laws in dealing with tax authorities' discretions can be found in a common belief that the executive may according to law assume regulation-making power on its own initiative, a belief adopted in the Chinese Constitution. Under the Chinese Constitution, the executive at various levels (county and above) may issue orders, rules and regulations, which may be regarded as rules of law. These executive-made rules are enforceable as long as they do not contravene the Constitution, the law of the NPC, regulations made according to law by the State Council and by any local government which is superior to the executive making the rules. This practice suggests that China regards the legislature as the highest, but not the sole, legislative authority in the country. This view has been commonly held by many Chinese textbooks on constitutional or administrative law. Since legislative power is not deemed to belong to the NPC exclusively, a specific authorization for the transfer of legislative power from the legislature to the executive is not needed in Chinese law. The authority of the NPC, which is claimed as the highest, is ensured by the principle that no regulation of an

118 See China Law and Practice for example.

executive and no law of a local government can be inconsistent with the Constitution and law of the NPC. This may explain why Chinese law does not adopt the special provisions found in Australian law, which authorize the Commissioner to delegate his power under the Act to other persons.

The different attitudes towards executive discretions adopted in the two countries are another reason for the differences in the process of delegating power. As observed earlier, the possible abuse of the tax authorities' discretions is considered an issue in Australia, but not in China. A precise and certain procedure for the delegation of Commissioner's power reflects Australia's efforts to prevent the abuse of discretions. The importance of following the prescribed manner to delegate power has been confirmed by the courts in several cases. But, in China executive discretion (including tax authorities' discretion) is regarded as effective as judicial power for the purpose of implementing tax law. The tax authorities' discretions are not different from ordinary executive discretions, which are part of the inherent power of the executive. This is why no procedural requirements for delegating tax authorities' discretions are needed in China. How to exercise discretions, including the delegation of power, is a matter to be determined by the tax authorities. In practice, the Ministry of Finance may issue circulars or notices authorizing the GTB to make some further interpretation of the law; sometimes, the GTB and its branches issue circulars and notices without indicating how the power to do so has been passed to them.

5.5.3. Judicial Control of Discretion

The tax authorities' discretions can be reviewed by the judiciary in both Australia and China. In Australia, the judiciary in this context includes both the court of law and the Administrative Appeal Tribunal (AAT), which has quasi-judicial functions. In China, the judiciary in this context includes only the courts of law. The power of the judiciary in the two countries to review the tax authorities' discretions is granted by law. However, in Australia, the AAT may review

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120 For example, the validity of the Taxation Office's activities is dependent upon whether the Taxation Office has followed the provisions on the delegation of the Commissioner's power correctly. See Allen Allen & Hemsley v FCT (1989) 20 ATR 321 and FCT v Citibank ltd (1989) 20 ATR 292.

121 In Australia, the power of AAT is granted by the ITAA, AAT Act, and Tax Administration Act, and the power of the courts is mainly based on the Administrative Decision (Judicial Review) Act. In China, the power of the court to review tax offices' decisions is granted by tax law.
certain decisions on their "merits" whereas the Federal Court can review a decision merely on the ground of error of law.122

A detailed comparison between the practices of the judiciaries in relation to the tax authorities' discretions is not possible, for such cases are rarely heard in Chinese courts.123 Nevertheless, judicial review has been accepted in theory in both Australia and China as a means of supervising executive discretion. A comparison on their views of judicial control of discretion may reveal the attitudes of the two legal systems towards the tax authorities' discretions and suggest the roles of executive and judiciary as perceived in the two countries.

Judicial review has a different status in Australia and in China. In Australia, it is the only and ultimate means of correcting the abuse of the Commissioner's discretions; whereas in China, it is only one of the proposed means to control executive discretion. Although this difference between the two countries is not revealed in the language of the laws,124 it arises from the different roles played by the judiciaries in, but not only in, the administration of taxation in the two countries. As the sole means of external control, the AAT and courts in Australia


123 A few cases involving the exercise of the tax offices' discretion have been briefly reported in Chinese sources. For example, a case involving a farmer and a local tax office was reported in Gazette of the National Supreme Court. A Mr. Zhi leased a brickkiln from a Mr.Fu who leased the brickkiln from the local Government. The parties agreed in their contract that Mr.Fu was responsible for Product Tax payable for the production of bricks. The local tax office ignored the contract and insisted that the tax should be paid by the producer of the products, in this case by Mr.Zhi. Mr.Zhi did not accept the decision and appeal to the Tax Office of Miyan county. But the county Tax Office confirmed the local office's decision. Mr.Zhi took a legal action against the tax office's decision in the county court, which, however, upheld the decision of the tax office. The case was consequently appealed to the Intermediate Court in the region. The Intermediate Court construed the law differently and decided that under both the relevant provisions of law and the contract concerned Mr.Fu not Mr.Zhi was responsible to pay the tax. The Court also ordered the judgment of the local court and decision of the tax office be withdrawn and the local tax office to compensate economic loss suffered by Mr.Zhi at a mount of 1,000 RMB. 2 Gazette of the National Supreme Court of the PRC (Zhong Hua Ren Ming Gong He Guo Zui Gao Fa Yuan Gong Bao 1989, in Chinese) 37-38. The report does not give detailed judgment, thus is not very helpful to any detailed study. But it is an example that Chinese courts do exercise judicial power to control tax authorities' discretion in some cases.

124 Both countries adopt similar arrangement regarding the review of tax offices' decisions. The tax offices are required to reconsider their decisions on the request of taxpayers as the first step of the review systems. After that, taxpayers who are still dissatisfied with the decisions may take legal action in the AAT or courts, as allowed in Australia, or in the courts as described in Chinese law.
have been extensively involved in the interpretation of tax legislation. Thus the judiciary in Australia has contributed creatively to the development of tax law. As a result, either new meanings have been given to the existing provisions of the Act, or new provisions have been added to the Act following directions suggested by judgments of the courts. But Chinese courts have neither been widely involved in, nor contributed to, the development of tax law. Because of the existence of other options, disputes involving the discretions of the tax authorities are usually resolved before resorting to court proceedings.

Although literally in China taxpayers dissatisfied with the tax offices' decisions may take the matter to a court of law, the legal remedy is in practice an improbability. The power of the courts to review tax decisions appears to be more of a cosmetic effect or a symbolic assurance added to the Chinese tax system than an effective means of controlling the abuse of the tax offices' discretions. Since both Chinese legal tradition and contemporary legal opinions do not regard litigation as a desirable means of settling disputes, in particular those involving executive discretions, the power of courts to review seemingly represents the efforts of China to change its image as a country which had not had any formal "law and order" until late 1970s. An emphasis on judicial review of the tax authorities' discretions may be seen as psychologically providing some assurance to foreign investors who are used to legal proceedings as a basic means of dispute resolution. Although the efficacy of the courts' power is hard to assess, the existence of the remedy alone may help ensure the confidence of foreign investors. But in practice courts have been rarely used in settling disputes involving taxation matters. More often than not a tax office takes a taxpayer to a court,125 but not the other way around. The reluctance among Chinese to resort to court proceedings and the lack of experience of the courts in dealing with tax matters may be the reasons for the so far limited use of legal proceedings as means of settling taxation disputes.

Different legal traditions and their impacts on Australian and Chinese societies again must be taken into account in understanding the differences between the roles of courts in Australia and China. The courts have traditionally had different images in the two societies. In Australia, the courts of law are until

125 A few cases concerning avoidance of tax liabilities have been reported by official sources. For example, a shop owner in Longhai county, Fujian Province, refused to pay tax on some of his business income, valued at RMB 26,000, earned in a period of time after March 1982. The Tax Office of Longhai county took the matter to the county court which ordered the shopowner to pay the amount of RMB 2,666.36 due for the tax payment plus a fine equal to the payment due. The case is reported in X.L.Zhang & T.J.Jia eds, Annotated Cases on Economic Law (Jing Ji Fa An Li Xun Jiilin, Jiilin People's Publishing House, 1986, in Chinese) 476-7. Another example is Mao Anmin case, (1989) 3:7 CLP 37.
recently the preferred and the ultimate forum of dispute resolution, although disputes are often resolved through voluntary compromise between the parties concerned prior to the trial or by the recommendation of the courts. By contrast, Chinese people treat the courts as an inferior means of dispute resolution. Before 1911 when the last feudal dynasty in China was overthrown, the judicial and executive functions of the government were in fact inseparable, and the courts of law were rarely the ultimate forum for dispute resolution. After 1911, Western legal theories, which were introduced into China at the end of 19th century, were gradually put into practice and the courts enhanced their status in the process of dispute resolution. Nevertheless, the impact of legal tradition on Chinese culture still generally affects the attitudes of ordinary Chinese towards the role of courts. In addition, the disappointing performance of the judiciary, which was a political tool of the Chinese Communist Party,¹²⁶ has in the past decades given Chinese people unhappy memories. These old and new experiences with the courts, which have not been established and guided by the same principles as those adopted in Australia, have discouraged people from resorting to the judiciary for resolution of disputes.

Judicial review of the tax authorities' discretions has been literally accepted by Australia and China as a legal remedy to taxpayers who are the alleged victims of the abuse of executive discretions. Australian courts have played an very important role in examining and controlling the Commissioner's discretions, as well as in the development of taxation legislation. But Chinese courts have hardly had any practical significance in the supervision of the tax authorities' discretions and in the development of tax law in China. Chinese legal tradition, and generally the unfavourable attitude of ordinary people towards the role of judiciary in the process of dispute resolution, apparently suggest that the claimed legal remedy is merely a comforting measure to foreigners and a lip-service to Chinese.¹²⁷

5.6. Residential Tests and International Taxation

5.6.1. Significance of the Residence Test

¹²⁶ The Party may affect the appointment of judges. The existence of the Party within the judicial system also gives privileges to judges who are party members over those who are not, e.g. access to internal documents and chance of promotion. These means of control ensure that the judiciary is dependent upon the Party.

¹²⁷ The judiciary has never been a preferred means of settling disputes on tax matters to Chinese. Even if foreign investors insist on resorting to the courts of law for settlement of disputes, Chinese courts will never play a decisive role, as played by Australian courts, in reviewing the tax authorities' discretions for lacking of appropriate case reporting system and attention to legal precedents.
The residential status of a taxpayer is crucial in determining one's liabilities. While a resident is liable to pay tax on income derived from both in and outside Australia and China, a non-resident in these countries pays tax only on income derived from sources within these countries. Similarly, deductions allowed to foreign investors vary depending on their status. The profitability of an investment project may be affected by the legal status of a taxpayer.

Although residence has been adopted by Australia as the criterion for determining a taxpayer's tax liability, the term is not formally accepted in Chinese law. Rather the Chinese Government assumes taxation power over foreign investors by the fact that any foreign or joint enterprises operating in China must be approved before beginning operation. The incorporation of an enterprise under Chinese law or the registration of a foreign company in accordance with Chinese law may be regarded as a test for determining residence of the enterprise. But the test of incorporation in Chinese law does not have the same implication as in Australian law. For example, a joint venture established under Chinese law, like a resident company in Australia, is liable to pay tax on income derived from its overseas operations. But a foreign enterprise established under Chinese law is not

128 For tax purpose, joint ventures refer to various Sino-foreign enterprises which are independent legal entities created by either the Joint Venture Law or the Law of PRC on Sino-foreign Cooperative Enterprises (CCH, China Laws for Foreign Business para 6-100, hereinafter referred to as the Cooperative Enterprises Law). A cooperative joint venture established under the Cooperative Enterprise Law but with its participants operating separately in their own right are not "joint ventures" for tax purposes. The foreign partner in such cooperative operations is taxed separately under the FEIT Law. Art.1 of FEIT Law states that the Law applies to foreign enterprises which have establishments in China and engage in independent operations or cooperative operations. FEIT Regulations further provides that foreign parties to a cooperative production or business operation shall be subject to FEIT Law unless other provisions of law apply. The "other provisions" can be found in the Cooperative Enterprise Law. Article 2 of the Cooperative Enterprise Law states that any cooperative enterprise which satisfies the conditions to be a legal person may acquire the status of a Chinese legal person. In light of these relevant provisions, it can be concluded that if a new legal person is created under the Cooperative Enterprise Law, JVIT Law should apply; and if no legal person is created under the contract, FEIT Law applies to the foreign party to the contract.

129 JVIT Law, Art.1.

130 For tax purpose, foreign enterprises, except those which do not have establishments in China (these enterprises are subject to withholding tax, Art.11 of FEIT Law) are foreign companies, enterprises, and other economic organizations which have establishments (referring to offices, places of business operations, or agents of foreign companies, FEIT Regulations, Art.2) and engage in independent business operations, co-operative production or joint business operations in China (FEIT Law, Art.1). The implication of "foreign enterprises" under tax law is wider than that of the "solely foreign-owned business" as defined in the Law of the PRC Concerning Enterprises With Sole Foreign Investment (CCH, China Laws For Foreign Business para.13-506, hereinafter referred to as Foreign Enterprise Law) which includes only those solely foreign-owned enterprises established under Chinese law.
expressly required to pay tax on income derived from its overseas operations.\textsuperscript{131} In fact the Law does not address taxation issues relating to income of a solely foreign-owned enterprise derived from sources outside China. Such income is thus not taxed by the Chinese Government. This practice differs from Australian law which requires all resident companies (incorporation is a test for determining residence of a company) in Australia to pay tax on income derived from foreign sources. Having regard to the differences in Australian and Chinese laws, the discussion of residence tests in this chapter is to be mainly based on Australian law. The Chinese practice will be compared wherever relevant materials are available.

The major consequences of a taxpayer's residential status on his or her liabilities are outlined below. Under Australian tax law, a resident company is allowed to apply for foreign tax credits on taxes paid to a foreign government on its assessable income derived from sources in that country; a resident company may deduct from its income losses and carry forward the losses as allowed in law; and a resident company is also eligible for the intercorporate dividend rebate. In addition, a resident individual is eligible for the tax free threshold under which no tax is collected. By contrast, while a non-resident is not eligible for the intercorporate dividend rebate and tax free threshold available to a resident, he/she does not pay tax to Australian Government on foreign income either.\textsuperscript{132} A foreign investor may exploit the rules with regard to residential status to minimize his/her tax liabilities. But one's ability to choose under the Act is limited by the discretions of the Commissioner in applying the tests to determine the status of a taxpayer. In China, the significance of residence tests is seen in the operation of joint ventures which are required to pay tax on their foreign income and entitled to foreign tax credits on the tax paid on their foreign income.\textsuperscript{133}

5.6.2. Tests for Determining Residence of Company

\textsuperscript{131} Art.1 of FEIT Law states that income of a solely foreign-owned enterprise derived from sources in China is subject to this law.

\textsuperscript{132} A non-resident is also subject to a number of provisions, such as "branch profits", (ITAA, Div. 11B), which impose specified tax liabilities on non-resident companies.

\textsuperscript{133} JVIT Law, Art.16.
As we have seen, "resident/non-resident company" is a concept used in Australian law but unknown in Chinese law. In Australia, the residential status of a foreign-related business for taxation purpose is determined principally by three tests. First, if a foreign-related business is incorporated within Australia, it is deemed to be a company resident of Australia.\(^{134}\) Secondly, if a foreign-related business carrying on business in Australia is incorporated outside Australia but its central management and control is situated in Australia, it is seen as a company resident in Australia.\(^{135}\) Thirdly, if a foreign-related business carrying on business in Australia is incorporated outside Australia, but its voting power is controlled by shareholders residing in Australia, it is deemed to be a resident company of Australia.\(^{136}\) By contrast, Chinese law only adopts the first test, and the acceptance of this test is implied and partial. This is implied because tax laws do not specify the test at all. It is partial because the FEIT Law taxes only Chinese income of solely foreign-owned enterprises, although these enterprises are incorporated under Chinese law.\(^{137}\) Even if a solely foreign-owned enterprise is incorporated or registered under Chinese law, its tax liabilities are limited to income derived from Chinese sources.\(^{138}\) Thus, the application of the "residence test" in China is comparable with the use of the "test" in Australia only where joint ventures are concerned. The absence of the second and third test in Chinese law is attributable to the fact that the Chinese market is not fully open to foreign investors. Currently, all foreign investments operate under a close scrutiny of the Government. This practically eliminates possibilities of various tax avoidance schemes. Their operations could be adverse to fairness in taxation had the second and third test not been applied in Australia.

Since Chinese law only implicitly and in a limited way adopts the first test, the discussion of the three tests in this section will be mainly based on Australian law. The first test is self-evident. Any business incorporated under Australian law and all joint ventures incorporated under Chinese law, no matter whether they are controlled by residents or non-residents of these countries, are treated as residents in the respective country for tax purpose, even if their central management and control is located outside these countries. The second and third test are not as simple as the first one, and will be further analysed below.

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\(^{134}\) ITAA, s.6(1).

\(^{135}\) ITAA, s.6(1).

\(^{136}\) ITAA, s.6(1).

\(^{137}\) JVIT Law, Art.1 & FEIT Law, Art.1.

\(^{138}\) FEIT Law, Art.1.
The "central management and control" test applies to enterprises which are not incorporated under Australian law, but which carry on business in Australia. Carrying on business and having central management and control in Australia are two basic features of this test. But, as noted by some commentators,\textsuperscript{139} "carrying on business in Australia" may sometimes not be regarded as an essential factor in determining the residence of a foreign company because of the decision in \textit{Malayan Shipping Co Ltd v FCT}.\textsuperscript{140} "Central management and control" is the essential feature of the test. This test includes two elements: "central management" and "central control", which are not synonyms.\textsuperscript{141} However, the test has been traditionally treated as a single concept and refers to where the major independent business decisions are made. It usually refers to where directors of a company meet,\textsuperscript{142} but may sometimes refer to where the shareholder meeting is held if the decision to do business is made by the shareholders rather than the directors.\textsuperscript{143} The key factor under this test is who actually makes the decisions. Therefore, even if sometimes the two situations co-exist, "central management and control" is deemed to be situated in the place where the real issues arising in the business are decided or controlled.\textsuperscript{144} Under this test, a foreign-related company carrying on business in

\begin{footnotesize}
\begin{enumerate}
\item[139] Hamilton, supra note 1, at 39.
\item[140] (1946) 71 CLR 156.
\item[141] Hamilton, supra note 1, at 16.
\item[142] \textit{Koitaki Para Rubber Estates Ltd v FCT} (1942) 6 ATD 42.
\item[143] \textit{John Hood & Co Ltd v Magee} (1918) 7 TC 327.
\item[144] For example, in \textit{Esquire Nominees Ltd v FCT} 72 ATC 4076, at 4086, with respect to the question who actually made business decisions: a group of Melbourne accountants or the local directors of the company in Norfolk Island, Gibbs J. commented:
\end{enumerate}
\end{footnotesize}

That firm had no power to control the directors of the appellant in the exercise of their powers or the A class shareholders in the exercise of their voting rights. Although it is doubtless true that steps could have been taken to remove the appellant from its position as trustee of one or more of the trust estates, Messrs. Wilson, Bishop, Bowes and Craig could not control the appellant in the conduct of its business of a trustee company. The firm had power to exert influence, and perhaps strong influence, on the appellant, but that is all. The directors in fact complied with the wishes of Messrs. Wilson, Bishop, Bowes and Craig because they accepted that it was in the interest of the beneficiaries, having regard to the tax position, that they should give effect to the scheme. If, on the other hand, Messrs. Wilson, Bishop, Bowes and Craig had instructed the directors to do something which they considered improper or inadvisable, I do not believe that they would have acted on the instruction. It was apparent that it was intended that the appellant should carry on its business of trustee company on Norfolk Island. It was in my opinion managed and controlled there, none the less because the control was
Australia is considered a resident in Australia if its business decisions are made in Australia either by directors or shareholders residing in Australia.

The test of "controlling shareholders" refers to a situation where the voting power of a foreign corporation carrying on business in Australia is controlled by shareholders who are residents of Australia, regardless of whether the head office of the company is situated in Australia. To satisfy this test, certain special conditions must be met. First, whether a foreign company is carrying on business in Australia should be decided in the context of indications such as repetition or intended repetition of the business transaction, continuity and system of the business organization, commercial significance of the activities and profit motive. 145

Secondly, "shareholders" in this test refer to persons whose names are entered or to be entered on the register of members as the holders of shares in the company. By contrast, persons who are beneficial owners of the shares but whose names are not entered on the register of shareholders are not "shareholders" for this purpose. 146

Thirdly, "voting power" refers to the entire voting power (including the voting power attached to an office holder) not merely the voting power attached to shares. 147

Lastly, "control" seems to refer to majority control (more than 50%) of the voting power at general meetings of the company. 148 However, control must be de facto and not be merely a capacity to control. 149 This may therefore extends to actual control of a company by Australian residents who may not hold more than 50% of voting power.

5.6.3. Tests for Determining Residence of Individuals

Australian and Chinese law take different approaches to the residence of individuals. The Australian ITAA sets forth four tests for determining whether a taxpayer is a resident in Australia. First, a taxpayer is regarded as a resident of Australia if he falls within the common law definition of residence. Secondly, a

exercised in a manner which accorded with the wishes of the interests in Australia. The appellant was, in my opinion, a resident of Norfolk Island.

145 Hamilton, supra note 1, at 41.

146 Patcrop Investments Ltd & Ors v FCT 76 ATC 4225, 4235 & 4239.

147 Kolotex Hosiery (Australia) Pty Ltd v FCT 75 ATC 4028.

148 Mendes v Commr. of Probate Duties (Vic.) (1967) 122 CLR 152.

149 Hamilton, supra note 1, at 42.

150 ITAA, s.6(1). Residence according to ordinary concepts accepted in common law is deemed to be incorporated in s.6(1). Hamilton, supra note 1, at 32.
person whose domicile is in Australia is deemed to be a resident of Australia, unless the Commissioner is satisfied that his permanent place of abode is outside Australia. Thirdly, a person who has actually been in Australia for more than one-half of an income year is deemed to be a resident, unless the Commissioner is satisfied that his usual place of abode is outside Australia and that he does not intend to take up residence in Australia. Lastly, a person, who is an eligible employee for the purposes of the Superannuation Act 1976 or is the spouse or a child under 16 years old of such a person, is deemed to be a resident.

In China, although the Law does not formally distinguish residents and non-residents of China, the residential period of a taxpayer in China does affect his/her tax liabilities. A person who has resided in China for a full year (365 days) pays tax on his/her income derived from sources both in and outside China. But a taxpayer who has resided in China for less than 365 days in the year of income pays tax only on his/her income derived from sources in China. In terms of tax liability, the person who resides in China for 365 days in a tax year is comparable to a "resident in Australia". Therefore, such persons in China may be regarded as "residents in China", although Chinese law does not adopt this expression. For the purposes of comparison, in this thesis, a person residing in China for 365 days in a tax year will be treated as a "resident in China", whilst, a person who resides in China for less than 365 days will be regarded as a "non-resident in China".

The test to decide residential status of a taxpayer in China, as mentioned earlier, is whether he has resided in China for a total of 365 days in a tax year. The test is poorly defined. Neither law nor the documents of the Ministry of Finance or GTB have explained what is "residing in China". Moreover, Chinese courts have never attempted to interpret this test. The application of the test has inevitably been left in the hands of the tax offices. It can be assumed that "residing

151 ITAA, s.6(1); Case H10, 76 ATC 45, and FCT v Applegate 79 ATC 4307.
152 Ibid.
153 Easson and Li observe that when calculating days of residence "the Chinese authorities have in the past taken a stricter view, and presence in China for any period of 365 days, even though spanning two years, has sufficed to constitute residence". Easson and Li, supra note 7, at 47.
154 IIT Law, Art.1.
155 The same view is expressed in Easson and Li, supra note 7, at 48.
in China" means actual physical presence of a person in China, because in the case of determining if a person has resided in China for more than 90 days, the period of time during which a person holding a multi-entry visa is absent from China is allowed to be subtracted.\(^{157}\) This implies that the domicile and permanent residence of a person may not be taken into account in determining residential status.

5.7. Source Tests and International Taxation

5.7.1. Classification of Sources

In general, sources of income are divided into domestic sources and foreign sources. Domestic sources (i.e. Australian sources or Chinese sources) mainly refer to sources within Australia or China but sometimes include those specified classes of income which are related to sources in these countries.\(^ {158}\) Foreign sources refer to sources outside Australia or China, which do not fall under the categories of Australian income specified in the Act or common law or of Chinese income as defined in Chinese law.

The sources of income are classified in accordance with the geographical connection of an income, or of an act or property from which an income is derived. The connection reflects the relationship between an element which produces a given item of income and the locality of the element. In producing a particular income, many elements may be relevant. However, under Australian law, only the "locality at which the substantial elements exist or occur will be the source (or sources) of the income".\(^ {159}\) When several elements exist, "the courts have tended to concentrate upon where the formal aspects of a transaction have taken place, rather than on where the economic activity which gave rise to the income occurred".\(^ {160}\) Accordingly, when a contract is the decisive source of income, the place where the contract is made is seen as essential in determining the source of income concerned, such as an annuity payable under a contract, salary and professional fees deriving

\(^{157}\) IIT Regulations, endnote.

\(^{158}\) For example, under Australian law interest paid upon money secured by mortgage of any property in Australia unless paid on debentures by a permanent establishment abroad and natural resource payment to non-residents is treated as Australian income. ITAA, ss.25(2) & 6CA. In China, a person who has resided in China for more than 90 days is liable to pay tax on his income derived from his works in China even if the money was paid outside China. IIT Regulations, Art.5.

\(^{159}\) Hamilton, supra note 1, at 50.

\(^{160}\) Ibid.

\(^{161}\) CCH, Australian Federal Tax Reporter para.15-570.
from special knowledge, and business profits deriving substantially from the making of contracts. By contrast, when the performance of acts or service is the main element, the place where the contract is performed or where the service is provided is the test for determining the source of the income. In the case of dividends, the transaction of payment is not essential. Rather, the source of income is determined by the place where the profits paid in the form of dividends are derived. In the case of royalties, the place where the property, such as a patent, trade-mark, design or mine from which the royalties arise, is situated is the source of the royalty. Thus, the locality of sources from which funds to be paid in the forms of dividends and royalties are derived is the crucial element in determining the sources of income in the cases of dividends and royalties. A similar rule also extends to the determination of the source of a pension.

Besides the general classification of the sources of income, the sources may be further classified according to the geographical distinction between, i.e. Australian or Chinese sources and foreign sources. This practice is common in Australia where the classifications so made are based on statutory and common law rules. Under these rules, firstly, interest paid upon money secured by mortgage of any property in Australia is seen as Australian income except interest paid outside Australia to a non-resident on company debenture issued outside Australia. Secondly, natural

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162 FCT v Mitchum (1965) 39 ALJR 23.

163 C of T (NSW) v Cam and Sons Ltd (1936) 36 SR (NSW) 544, and Premier Automatic Ticket Issuers Ltd v FCT (1933) 50 CLR 268. This is also accepted in China, in particular when a contract of joint production is involved.

164 FCT v French (1957) 98 CLR 398, C of T (NSW) v Cam and Sons Ltd (1936) 36 SR (NSW) 544, and Thorpe Nominees Pty Ltd v FCT 88 ATC 4886. This is also broadly accepted in Chinese law. For example, Art.2 of JVIT Law regards income derived from various business operations in China as Chinese income, including services provided in China by foreign investors.

165 Esquire Nominees Ltd v FCT 73 ATC 4114, and Parke Davis & Co v FCT 91959) 101 CLR 521. Art.2 of JVIT Regulations.

166 Besides the statutory definition of royalties provided in s.6 of the ITAA, the Australian Taxation Office has issued guidelines for classifying royalties, see Hamilton, supra note 1, at 52-4.

167 ITAA, s.6C.


169 ITAA, s.25(2). Interest paid upon money secured by mortgage consisting of both Australian and non-Australian properties is deemed to be Australian income as well. See Broken Hill South Ltd v C of T (NSW) (1937) 56 CLR 337.
resource income\textsuperscript{170} received by a non-resident is deemed to be an Australian income regardless of where the payment is actually made. Thirdly, when a royalty paid or credited to a non-resident by another non-resident is an outgoing incurred in carrying on a permanent establishment in Australia, it is deemed to have an Australian source.\textsuperscript{171} These are the main categories relating to sources of income, although several other categories may also be specified.\textsuperscript{172}

5.7.2. Australian Sources and Foreign-Related Resident Companies

Foreign investors may invest in Australia in various forms. A foreign corporation, "a body or person incorporated in a place outside Australia",\textsuperscript{173} is one of them. When a foreign national invests in an Australian company or establishes a company under Australian law, the company is an Australian company even if it is controlled by the foreign investor. Often, a foreign investor has interests in an Australian company but does not have control over the company. This company is foreign-related.

The term "foreign-related company" broadly refers to any business operating in Australia with foreign investment. These companies can be further divided into companies with substantial foreign interests (or foreign controlled companies), and companies without substantial foreign interests. The tax liabilities of these companies vary in some circumstances. For tax planning purposes, foreign investors in a company controlled by Australian interests do not have much option in deciding their strategy for tax planning, except in matters, relating to personal income tax. By contrast, decisions of a company controlled by foreign investors are affected by the status of such investors, who have wider options for tax planning.

Tax law does not define companies with substantial foreign interests or controlled by foreign investors, although it defines "foreign-related company" for the purposes of applying foreign tax credit rules. In this regard, tests for determining whether control exists are borrowed from FATCA in order to provide a reference to the meaning of "substantial foreign interests" or "foreign controlled companies" in Australia in the context of foreign investment.

\textsuperscript{170} According to s.6 of the ITAA, natural resource income refers to income that is derived by a non-resident and is calculated by reference to the value or quantity of natural resource produced or recovered in Australia after 7 April 1986, excluding royalties and income derived under an arrangement made with the Commissioner before 7 April 1986.

\textsuperscript{171} ITAA, s.6C(1)(b).

\textsuperscript{172} For details, see Hamilton, supra note 1, at 49-94.

\textsuperscript{173} Foreign Corporations (Application of Laws) Act 1989 (Cth).
Under FATA, the following types of companies are regarded as foreign-related businesses:

(1) if more than 15% of the voting power or issued shares in a corporation is controlled by a foreign person174 or his/her associates;175

(2) if more than 40% of the voting power or issued shares in a corporation is controlled by two or more foreign persons or their associates;176

(3) if a foreign person or persons, together with their associates, are in a position to determine, or are deemed by the Treasurer to be able to determine, the policy of a corporation;177 or

(4) if a corporation is incorporated outside Australia.

The purpose of defining foreign-related companies in this chapter is to emphasize the fact that the taxation of foreign investment concerns not only foreign corporations but also foreign investors who invest in Australian corporations.

"Company" for tax purposes "includes all bodies or associations corporate or unincorporated, but does not include partnerships".178 Under the ITAA, public trading trusts, a form of public unit trusts, are taxed as companies.179 In 1990-91, the general tax rate applicable to taxable income of companies (both public and

174 "Foreign person" as defined in FATA means: (a) a natural person not ordinarily resident in Australia, (b) a corporation in which a natural person not ordinarily resident in Australia or a foreign corporation holds a controlling interest, or (c) a corporation in which two or more persons, each of whom is either a natural person not ordinarily resident in Australia or a foreign corporation holding an aggregate controlling interest.

175 FATA, s.18(7)(b).

176 FATA, s.18(7)(c).

177 FATA, ss.20(5) & 21(5).

178 ITAA, s.6(1).

179 ITAA, ss.102M - 102T.
private) was 39%,\textsuperscript{180} with the exceptions of certain specified types of companies.\textsuperscript{181} A resident company is liable to pay tax on income derived from both in and outside Australia.

A number of issues relating to the calculation of taxable income of a foreign-related company should be noted. First, the continuity of ownership test and the continuity of business test must be satisfied for a company to apply for allowable deductions for current year losses, bad debts, or carrying forward losses to succeeding years. This is significant to a foreign investor who intends to acquire or transfer interests in a company. The continuity of ownership test requires a company applying for deductions to show that more than 50% of the shares, which carry rights to vote, to receive dividends and capital, were owned by the same person or persons during both the year of losses and the year of recoupment.\textsuperscript{182} The continuity of business test requires that a company must have carried on at all times during the year of recoupment the same business as it did immediately before a substantial change in the ownership of the shares in the company, which disqualified the company from relying on the continuity of ownership test, took place.\textsuperscript{183} This test provides an alternative basis for a company to deduct prior year losses. The latter seems suitable to a foreign investor who has acquired interests in a company. Secondly, losses can be transferred between companies of the same group provided

\textsuperscript{180} Income Tax Rates Act 1986, s.23(2) & (3).

\textsuperscript{181} In the case of registered organizations, such as a non-profit friendly society, a trade union or an employee association which is treated as a public company under the ITAA, a rate of 15% of taxable income applies to the CS/RA component (which, as defined in s.110(1) of the ITAA, means the component of the taxable income determined under s.116CJ for the CS/RA class which further describes that the component of taxable income for a particular class of assessable income is the amount that is left over after the assessable income of that income has been reduced in accordance with ss.116CF, 116CG & 116CH); a rate of 30% applies to the EIB component (which is not defined in the Act); and a rate of 47% applies to the NCS component (which, according to s.110(1), means the component of the taxable income determined under s.116CJ for the NCS class). See Income Tax Rates Act 1986, s.23(4). In the case of a life assurance company, a rate of 15% of taxable income applies to the "CS/RA component", a rate of 39% applies to the "AD/RLA" (which, again as defined in s.110(1) of the ITAA, refers to 116CJ for further interpretation) or "non-fund" component, (which refers also to the taxable income for non-fund class determined under s.116CJ); and a rate of 47% applies to the NCS component. See Income Tax Rates Act 1986, s.23(4A).

\textsuperscript{182} ITAA, ss.50H, 63A & 80A(1).

\textsuperscript{183} ITAA, ss. 50D, 63C & 80 E.
that there is 100% common ownership of the two companies.\textsuperscript{184} But the transfer of losses, as a "privilege", can be enjoyed by resident companies only. Thus, a transferor must be an Australian resident in the income year in which the loss is incurred, and the transferee must be an Australian resident in the year of income in which the right to deduct is transferred. This requires a foreign corporation to be a resident in Australia either in the year of the loss or the year of recoupment in order to qualify for the transfer. Since the two relevant companies are not required to be resident companies at the same time when the loss is incurred and the right is transferred, foreign corporations may exploit this rule in tax planning. The amount of losses transferable is limited to the amount of transferee's taxable income,\textsuperscript{185} except in the case of film losses where the sum of net assessable film income and net exempt film income of the transferee is the maximum transferable amount.\textsuperscript{186}

Intercorporate franked dividend rebate is relevant to foreign investment, but it is available only to residents in Australia. Dividends received by foreign-related companies are calculated as part of their assessable income. The companies pay taxes on the received dividends according to an appropriate rate, which varies depending on the types of companies (public, private, registered organizations or life assurance companies) and the categories of income (such as taxable income, undistributed profits of private company, CS/RA component, NCS component and so on). Under the present imputation system,\textsuperscript{187} intercorporate franked dividends are free from tax and thus a company may in effect transfer a tax paid by it on dividends to its shareholders or other companies. In order to be eligible for this benefit, a foreign corporation must satisfy the Australian resident tests.

5.7.3. Australian Sources and Non-resident Companies

The tax liabilities of a non-resident company are limited to taxable income derived directly or indirectly from all sources in Australia.\textsuperscript{188} The same deductions, exemptions and exclusions applicable to a resident company are also applicable to a

\textsuperscript{184} ITAA, s.80G. In addition, the common ownership is satisfied only when either a company is a wholly-owned subsidiary of the other or both are wholly-owned subsidiaries of the same holding company. ITAA, s.80G(2).

\textsuperscript{185} ITAA, s.80G(7).

\textsuperscript{186} ITAA, s.80G(8).

\textsuperscript{187} ITAA, s.46.

\textsuperscript{188} ITAA, ss.25 & 51.
non-resident company, except as specified by law.\textsuperscript{189} The same rates of company tax equally apply to both resident and non-resident companies. But non-resident companies are not entitled to the tax rebate in respect of dividends received from other companies.\textsuperscript{190} Taxes payable by a non-resident company are required to be deducted or paid on the companies' behalf by the person paying income or the company's agents in Australia.\textsuperscript{191}

Apart from ordinary rates of company tax, withholding tax is levied on certain categories of income derived from Australian sources by non-resident companies. Dividends paid by a resident company to a non-resident company, except franked dividends, are subject to a tax rate of 30% of gross dividends.\textsuperscript{192} But a rate of 15% applies to dividends paid to residents of Papua New Guinea,\textsuperscript{193} and of countries with which Australia has double taxation treaties.\textsuperscript{194} Interest deemed to be outgoings of an Australian business is subject to a 10% withholding tax, payable on the gross amount of interest paid to a non-resident company.\textsuperscript{195} This rate is adopted by most Australian double tax treaties, except those with Canada, South Korea, Malaysia, Malta, and Philippines, where a maximum rate of 15% of gross interest is adopted.\textsuperscript{196} Withholding tax is required to be deducted at source by the person or company paying dividends or interest.\textsuperscript{197} Withholding tax is a major concern of foreign investors who are not residents in Australia. Because of

\begin{enumerate}
\item For example, the transfer of loss between companies is available only to residents in Australia.
\item ITAA, s.46(2).
\item ITAA, Eg, ss.221YHZB, 255 & 257.
\item ITAA, s.128B(1) and Income Tax (Dividends and Interest Withholding Tax) Act 1974, s.7.
\item ITAA, s.128B(4) and Income Tax (Dividends and Interest Withholding Tax) Act 1974, s.7.
\item CCH, Australian International Tax Agreements.
\item ITAA, s.128B(2), (6), (7), (8) & (9), and Income Tax (Dividends and Interest Withholding Tax) Act 1974, s.7.
\item CCH, Australian International Tax Agreements. But it must be pointed that as at December 1990 ITAA imposed 10% withholding tax on gross interest, which is lower than the maximum rate adopted in those treaties.
\item ITAA, ss.221YK - 221YR.
\end{enumerate}
the low tax rate of withholding tax, a non-resident may pay less tax than a resident on the same amount of income derived from the same source in Australia. 198

5.7.4. Chinese Sources and Foreign-Related Companies

Chinese law does not provide a general definition of income. In the context of the FEIT Law, income means gains derived by foreign enterprises from production, business and other sources within Chinese territory. 199 Thus, any income, whether in the form of money or of products, 200 which is derived from sources within China by foreign enterprises is subject to FEIT. In addition, "income from production and business", which is further defined in the FEIT Regulations, means income derived from operations in industry, mining, communications, transportation, agriculture, forestry, animal husbandry, fisheries, poultry, farming, commerce, service, 201 and other trades. "Income from other services" is specified as dividends, 203 interest, royalties, 204 and any other gains specified as taxable by the Ministry of Finance. 205

It appears that the criterion of "source basis" is adopted by China to tax income of foreign enterprises. Although the law does not expressly exclude foreign income, the omission of foreign income in the FEIT Law suggests that income of foreign enterprises derived from sources outside China is not taxable in China. Under the "source rule" Chinese law taxes income derived from sources in China by

198 For further discussion of withholding tax, see Hamilton, supra note 1, at 131-60.
199 FEIT Law, Art.1.
200 In cases where the partners in a co-operative production share profits between them by distributing goods produced, or where the partners in an offshore petroleum operation receive crude oil according to their share, the goods and oil so received are regarded as income of the parties involved. The goods and oil are to be converted into RMB according to their prevailing market prices. FEIT Regulations, Art.26.
201 Management fees received by a foreign enterprise for providing managerial services to other foreign or joint enterprises are treated as income of the enterprise. In addition, the fees are also subject to CICT. Notice of the GTB, Item 4.
202 FEIT Regulations, Art.4.
203 "Dividends" refer to the dividends or the share of profits derived from enterprises in China. FEIT Regulations, Art.27.
204 "Royalties" refer to royalties derived from the use of various patents, technical know-how, copyright and trademark interest in China. Ibid.
205 Ibid.
companies which do not have establishments\textsuperscript{206} in the country. These companies can be regarded as non-resident companies, although Chinese tax law does not draw a line between resident and non-resident companies. Compared with Australian law, "resident" has different implication in Chinese law. Even a solely foreign-owned enterprise is regarded as a resident in China by virtue of its incorporation under Chinese law, its foreign income is not subject to Chinese tax. Thus, the different implication is that a resident company in China is not always liable to pay tax on its foreign source income under Chinese tax law.

A general definition of income of joint ventures is not attempted in the JVIT Law either. Rather the law specifies a number of items as taxable income,\textsuperscript{207} Given the great variety of sources, the categories of income cannot be fully enumerated. Thus, the Ministry of Finance and GTB constantly exercise a discretion in determining the taxable income of joint ventures. Since these ventures are residents of China for tax purposes,\textsuperscript{208} their income from both Chinese and foreign sources is subject to Chinese tax.\textsuperscript{209}

5.7.5. Australian Sources and Foreign Individuals

Foreign individuals residing in Australia are subject to the same rules as are applicable to Australian nationals residing in Australia. A resident of Australia pays tax at a progressive tax rate.\textsuperscript{210} Foreign investors not resident in Australia are taxed on income derived from sources in Australia. Unless specified by law, the deductions available to resident individuals apply also to non-resident individuals. But tax rates applicable to non-resident individuals differ from the rates applicable to resident individuals to some extent.\textsuperscript{211} In addition, a non-resident individual is

\textsuperscript{206} For the meanings of the establishment in Chinese law, see Easson and Li, supra note 7, at 84-7.

\textsuperscript{207} These include gains derived from production and business operations in industry, mining, communications, transportation, agriculture, forestry, animal husbandry, fisheries, poultry farming, commerce, tourism, catering, service and other trades. The concept of income also extends to dividends, interest, bonuses, transfer of property, patents, technical know-how, trademark interest, copyright and any specified items. JVIT Regulations, Art.2.

\textsuperscript{208} These prescribed joint ventures are regarded as residents in China because they are created under Chinese law.

\textsuperscript{209} JVIT Law, Art.1.

\textsuperscript{210} See supra note 15.

\textsuperscript{211} Ibid.
not entitled to claim rebates for his dependents or medical expenses. Non-resident individuals are subject to the same withholding taxes as those applicable to non-resident companies.

5.7.6. Chinese Sources and Foreign Individuals

The IIT Law specifies six classes of income which are subject to IIT. First, "wage and salary" refers to earnings from personal exertions. Secondly, "remuneration for personal service" refers to earnings from certain professional services. Thirdly, "royalty" refers to income derived from the transfer of patents or copyrights, the right to use technical know-how and other similar rights. Fourthly, "interest and dividend" refers to interest on deposits, loans and various kinds of securities and dividends from investment. Fifthly, "income from lease of property" refers to income from the lease of houses, machinery, equipment, motor vehicles, ships, and other kind of property. The last category includes any other income specified as taxable by the Ministry of Finance. Income falling within these categories is subject to IIT, regardless of whether it is received by a resident or non-resident of China.

On the other hand, IIT Law specifies nine classes of income which are exempted from IIT. These are prizes and awards for scientific, technological or cultural achievements; interest on savings deposits in State banks and credit

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212 ITAA, s.159J.
213 ITAA, s.159P.
214 These include wages, salaries, bonuses, year-end extras, earned from work in offices, schools, enterprises, organizations or other services. But prizes and awards for scientific, technological or cultural achievements are excluded from aforementioned bonuses. IIT Regulations, Art.4(1).
215 These are designing installation, drafting, medical treatment, law practising, accounting, consultation, lecturing, news reporting, broadcasting and television, contribution to publications, translation, calligraphy and painting, sculpture, cinema, drama and opera, music, dancing, acrobatics, ballad singing and comic talk, sports and technical services. Id, Art.4(2).
216 Id, Art.4(3).
217 Id, Art.4(4). But, dividends derived from joint ventures or cooperative organizations in urban and rural areas are exempt from IIT, id, Art.5(2).
218 Id, Art.4(5).
219 These include prizes and awards given to individuals by the Chinese Government and by Chinese or foreign scientific, technological or cultural organizations for inventions or creations in the field of science, technology and culture. IIT Regulations, Art.8.
cooperations of the PRC; welfare benefits, survivors’ pensions and relief payments; insurance indemnities; military severance pay to servicemen for the end of the service; pensions, or lump sum payments for an early retirement of cadres, staff members, and workers; salaries of diplomatic officials of foreign embassies and consulates in China; exempted income as specified by international conventions or treaties of China; and any other income which may be specified by the Ministry of Finance.

In general, a person who resides in China for 365 days in a tax year must pay IIT on income from both Chinese sources and foreign sources. But the IIT Law in fact adopts a flexible policy toward income derived from sources outside China. It requires only those persons who reside in China for more than 5 years to pay tax on their foreign income from the sixth year of their residence. When a person resides in China for less than 5 years but more than 1 year, he only pays tax on that part of foreign income which is remitted to China. Apparently, if there was no remittance, there is no tax on foreign income, even if a foreign national may be regarded as a resident in China by virtue of his physical presence in China. This suggests that China has not fully adopted the "residence basis" as a test to determine tax liabilities of taxpayers.

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220 This exemption also applies to interest on deposits in foreign currency in the said banks or institutions; and extends to dividends from investment by individuals in local construction (investment) companies in China, provided that the dividends do not attract bonuses and are not higher than the interest on savings deposits in the said banks or institutions. IIT Regulations, Art.9.

221 It is not clear whether this exemption applies to foreign employees working in foreign or joint ventures, because the terms "cadres, staff members and workers" are normally used as special terms referring people who work in Chinese State enterprises or collective enterprises. However, if a taxation office refuses to apply this exemption to a foreign individual who applies for exemption under this provision, the refusal would be disputable because of vaguely defined terms in the IIT Law.

222 IIT Regulations, Art.10. The exemption is subject to reciprocity and the Vienna Conventions of the Treatment of Diplomats, to which China is a member.

223 IIT Law, Art.4.

224 Id, Art.1.

225 By analogy to the method used to compute whether a person has resided in China for more than 90 days, (IIT Regulations, endnote), it can be assumed that the five-year rule here means the actual days of residence.

226 IIT regulations, Art.3.

227 Ibid.
Persons who reside in China for less than 1 year are required to pay tax only on their income derived from Chinese sources. A number of issues should be mentioned. First, the term “Chinese sources” seems to refer to both financial sources and the activities from which an income is derived. Thus, in the case of a person working in China but being paid by an employer outside China, earnings from activities in China are subject to IIT unless the accumulated stay in China is less than 90 days in a tax year. Secondly, “90 days” is a threshold to determine how to compute tax on income of a person who resides in China for less than one year.

5.7.7. Issues of Foreign Tax Credits

Both Australian and Chinese laws allow foreign tax credits on tax paid to a foreign country on income derived from sources within that country. But different restrictions have been imposed on the application for foreign credits.

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But some foreign lawyers noticed that Chinese tax officials have treated "all wage and salary income earned by an over-ninety-day resident of China "as gained or sourced in China". This means that the income of a holder of a Chinese visa of longer than 90 days is subject to Chinese tax even if the income is paid outside China and derived from sources unrelated to services in China, as long as the person has stayed in China for more than 90 days. See T.A. Gelatt & R.D. Pomp, "China's Tax System: An Overview and Transactional Analysis" in Moser ed, Foreign Trade, Investment, and the Law in the People's Republic of China (2nd edn, HK, Oxford University Press, 1987) 42.

IIT Regulations, Art.5(1) exempts persons residing in China for less than 90 days from paying IIT on income paid by an employer outside China. This suggests that income paid by an employer outside China to a person residing in China for more than 90 days is subject to Chinese tax law.

When a person has resided in China for more than 90 days in succession or in aggregate in a tax year, his tax should be assessed in accordance with the amount of income from wages (including those paid by employer outside China) received during the period of actual residence in China. In particular, the formula for such calculation is:

\[
\text{tax amount} = \text{income from wages for a specific month} \times \text{applicable tax rate} - \text{fast calculation deduction} \times \frac{\text{number of days of actual residence in China during the month}}{\text{number of days of the month}}
\]

When a person stays in China temporarily (this means the visit to China is a single trip and does not include a person who holds a multi-entry visa to China, see Calculating Individual Income Tax of Foreign Personnel During the Month in Which They Take or Leave Office Circular, issued by the GTB on 4 Nov. 1988, (1988) 3-5 China Law and Practice 8.) for less than a month, a new method of calculation specified by Several Questions Concerning the Levy of and Exemption from IIT in Respect of Personnel Who Comes to China Temporarily According to Their Actual Period of Residence Circular, issued by the Ministry of Finance on 3 May 1988, should apply.
In Australia, the foreign tax credit system described in Div.18 of the ITAA has several basic features. First, not every foreign tax paid by a resident of Australia is eligible for credit against Australian tax. To be eligible for tax credit, a tax must be imposed not only by the law of a foreign country, but also on one of the specific categories of income, such as profits, gains, interest, dividends, and offshore banking income. "Credit absorption tax" and "unitary tax" are not eligible for credit against Australian tax. The Commissioner has provided a country by country list of creditable foreign taxes in Taxation Ruling IT 2507. Secondly, different classes of income, such as interest, offshore banking income, or other foreign income, are "quarantined". This means that each class of income is assessed separately and losses within one class can be deducted only from the same class and source. Thirdly, the amount of foreign tax credit allowed to be claimed is determined by considering either the minimum amount of tax payable on the foreign income under Australian tax law, or the minimum amount of tax possibly payable on the foreign income under the foreign tax law which applies to the assessable income. Fourthly, credit is allowed for the underlying foreign tax paid by the

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231 "Foreign country" refers to a foreign government at a national, state, or local level. ITAA, s.160AE(1).

232 ITAA, s.160AE.

233 This is "a tax imposed by a law of a foreign country to the extent that the tax would not have been payable if the taxpayer concerned or another taxpayer has not been entitled to a credit in respect of the tax under Div. 18 of Part III". ITAA, 6.6AB(6).

234 "Unitary tax", according to s.6AB(6), means a tax imposed by a law of a foreign country, being a law which, for the purposes of taxing income, profits or gains of a company derived from sources within that country, takes into account, or is entitled to take into account, income, losses, outgoings or assets of the company (or of a company that for the purposes of that law is treated as being associated with the company) derived, incurred or situated outside that country, but does not include tax imposed by law if that law only takes those matters into account:
- (a) if such an associated company is a resident for the purposes of that law;
- (b) for the purposes of granting any form of relief in relations to tax imposed on dividends received by one company from another company.

ITAA, s.6AB(6).

235 ITAA, s.160AF(1). The amount of Australian tax is calculated by applying the average rate of Australian tax to the adjusted net foreign income (both are defined in s.160AF(8) of the ITAA) and deducting any rebate available to the taxpayer.

236 ITAA, s.160AF(2).
related foreign company\textsuperscript{237} on that portion of its profits from which the dividend is paid. The amount of credit allowed is subject to possible tax relief available under the tax law of the foreign country.\textsuperscript{238} Fifthly, excess foreign credit, except excess credit in relation to offshore banking income,\textsuperscript{239} may be transferred during the year of income in which the excess credit arises, from a resident company to another resident company in the same group,\textsuperscript{240} provided that the two companies have 100% common ownership or both are 100% owned by a foreign parent company during the year of income.\textsuperscript{241} Lastly, losses incurred in the course of gaining foreign income may be deducted and carried forward only against foreign income of the same class which is also from the same geographical source, in the order of years in which the losses are incurred, and within the limit of the gross income of a particular year.\textsuperscript{242} These provisions form the foreign tax credit system.

In China, foreign tax credits are available only to joint ventures. A unilateral tax imputation system has been adopted in the JVIT Law. Under the system, if a foreign income has been taxed by a foreign country, the foreign tax so paid may be credited against Chinese tax. The maximum tax credit allowed cannot exceed the tax amount payable under Chinese law on the foreign income concerned.\textsuperscript{243} This means that if foreign tax payments exceed the payments on the foreign income due under Chinese law, the excess of the foreign tax cannot be credited against income from Chinese sources; and if the foreign tax payment is less than the payment due under Chinese law, the venture is required to pay the difference to the Chinese tax authority. Unlike Australian tax law, the JVIT Law and Regulations do not specify whether the foreign tax credits of a joint venture can be transferred between ventures within the same group. Although Chinese law fails to address several issues which have been dealt with expressly under the Australian ITAA, this does not mean that these issues do not arise under Chinese law.

\textsuperscript{237} The "related foreign company" is defined in s.160AFB of the ITAA. Briefly, an Australian company is deemed to be related to a foreign company or a group of foreign companies, if it has more than 10% of the voting power of a foreign company, or if it has more than 5% of the voting power in a foreign company that belongs to the group of companies which the Australian company is a member.

\textsuperscript{238} ITAA, s.160AFC(8).

\textsuperscript{239} ITAA, s.160AFE(8).

\textsuperscript{240} ITAA, s.160AFE.

\textsuperscript{241} ITAA, s.160AFE(2), (3) & (4).

\textsuperscript{242} ITAA, s.160AFD.

\textsuperscript{243} JVIT Regulations, Art.32.
Presumably, tax offices in China have discretions in determining whether a credit should be allowed to a particular foreign tax. It is possible that a tax paid on "credit absorption tax" and "unitary tax" as defined in Australian law would not be allowed tax credit under Chinese law, because a notion of unfairness is associated with such taxes. But, classes of taxes as defined in Australian law, e.g. tax on dividends or income, may not be an issue in China, because Chinese law does not emphasize the differences between tax on income and tax on dividends. This approach may have resulted in the disregard of "classes of income" in Chinese law.

5.8. Issues Arising Under the Australian-Chinese Double Tax Treaty
5.8.1. The Australian-Chinese Treaty and the OECD and UN Models

The OECD model refers to the OECD Double Taxation Convention on Income and Capital. It was initially drafted by the Fiscal Committee of the Organization of Economic Cooperation and Development in 1946 and, subsequently redrafted in 1963 and revised in 1977. The Model provides basis for countries, in particular, developed countries, to negotiate double tax treaties.244

The UN model refers to the United Nation Model Double Tax Convention on Income and Capital, published in 1980. The Convention provides alternatives for those developing countries which consider some provisions of the OECD Model unacceptable because the provisions ignore the needs of developing countries. It is usually used, sometimes in conjunction with the OECD Model, as basis for negotiating double tax treaties between developing and developed countries.245

Most double tax treaties signed by Australia are based on the OECD Model, and most treaties signed by China are based on both the OECD and UN Models.246 The Australian-Chinese Double Tax Treaty appears to be a combination of OECD and UN Models. However, some modifications have been made to both Models. A comparison of the Australian-Chinese Double Tax Treaty and the OECD and UN Models will be carried out below.

The provisions of the Australian-Chinese Treaty can be divided into several categories according to the degree of similarity between the Treaty and the


245 For a brief discussion of the UN Model, see J.Phillips, id, at xvi-xviii.

When the provisions of the Models are identical, some provisions of the Australian-Chinese Treaty adopt the language of the Models without any significant change (such as Arts.1, 2, 15, 18, 19, 26, 27 & 28); whilst some add new meanings to the language of the Models. When the texts of the OECD and UN Model vary, three different practices are adopted in the Treaty. First, the Treaty combines the OECD and UN Model. Secondly, the provisions of the Treaty may be mainly based on OECD Model. Thirdly, the provisions of the Treaty may be mainly based on UN Model. A common feature of the above-mentioned categories is that they all basically follow the Models, although the degree of similarity varies. Apart from aforesaid categories, another category can be ascertained. It includes all provisions, to which considerable changes or modification have been made in contrast to the texts of the Models. Some provisions of the Treaty are almost totally different from the texts of the Models.

In the context of the Models and Treaty, a basic feature of the Australian-Chinese Treaty is that only a few provisions of the Treaty adopt the exactly same language of the Models. More often, additional meanings have been incorporated into the provisions in the Models. But as a whole, the Australian-Chinese Treaty must be regarded as a combination of the OECD and UN Models, because the basic structure of the Treaty and fundamental principles in most provisions of the Treaty are identical to those recommended in the Models.

5.8.2. Issues of Residence
5.8.2.1. Tests For Determining Residence Adopted in the Treaty

The Australian-Chinese Treaty seemingly suggests leaving the residential status of taxpayers to be determined by domestic law. Although the language adopted in the Treaty for determining residence of taxpayers is more or less along the same line as those proposed in the Models, no specific criterion has been agreed in relation to tests for determining residence in each domestic law. In fact the Treaty deals with the issues of residence in two steps: first allowing each State to determine the residence of taxpayers by its own law, and secondly, setting forth agreed rules to resolve cases of dual residence of taxpayers.

247 It should be noted that the texts of Models differ in a number of provisions.

248 For example, Art.7 of the Treaty.

249 For example, Arts.16 & 24 of the Treaty.

250 For example, Arts.5, 10-14, 21 & 22 of the Treaty.

251 For example, Arts.9, 12, 13, 17, 20 & 23.
Although the Treaty does not suggest positive tests for residence which are to be adopted in the domestic law of Australia and China, it sets out a negative test for determining residence of the taxpayers. Art.4(1) of the Treaty states that whether or not a taxpayer is a resident of a contracting State should be determined by the country concerned; and Art.4(2) states that a taxpayer can not be treated as a resident of a contracting State merely because the taxpayer is liable to pay tax on income derived from sources within that State. These provisions suggest that if the issues of dual residence and double taxation do not arise, the criteria for determining residence of taxpayers should be decided solely by domestic law. But the contracting countries agree not to adopt the "source test" as the sole criterion for determining residence.

With regard to issues of dual residence, the Treaty sets forth several general and undefined criteria for determining residence.252 In the case of individuals, the test of permanent home should be first considered. If this is not possible, the test of close economic and personal relation should apply. However, since the meanings of these tests are not defined in the Treaty, these tests may have different meanings in their application in Australia and China. For example, China has not yet formally defined the meanings of "permanent home" or "close economic and personal relation". Such uncertainty may result in disagreement on the meanings of these tests between Australia and China in the future. In the case of companies, two commonly used tests ("place of effective management" or "head office") are agreed on in the Treaty.

252 Article 4(3) of the Treaty deals with the residence of individuals. It states:

Where by reason of the preceding provisions of this article a person, being an individual, is a resident of both Contracting States, the status of the person shall be determined in accordance with the following rules:

(a) the person shall be deemed to be a resident solely of the Contracting State in which a permanent home is available to the person;
(b) if a permanent home is available to the person in both Contracting States, or in neither of them, the person shall be deemed to be a resident solely of the Contracting State with which the person's economic and personal relations are the closer.

Article 4(4) deals with the residence of companies. It states:

Where by reason of the provisions of paragraph(1) a person other than an individual is a resident of both Contracting States, then it shall be deemed to be a resident solely of the Contracting State in which its place of effective management or head office is situated. However, where such a person has its place of effective management in a Contracting State and its head office in the other Contracting State, the person shall be deemed to be a resident solely of that other State.
If both tests are applicable, the test of "head office" prevails over the test of "place of effective management". But, because the Treaty lacks clear definitions, conflict on the meanings of these tests may also arise between Australia and China. It also should be noted that the agreed principle with regard to dual residence of companies seems to be inconsistent with the common practice adopted in Australia, where effective management is deemed decisive. The potential conflicts in relation to these undefined criteria for determining residence will be further analysed in the following subsections.

5.8.2.2. Issues of Individual Residence

Australia and China have adopted different criteria for determining the residence of individuals. In Australia, a person who has a domicile in the country, or has continuously resided for more than one-half of a tax year, or has been an eligible employee for the purpose of the Superannuation Act 1976, is deemed to be a resident in Australia. These criteria may be further divided into four tests, including "the residence according to ordinary concepts rule", "the domicile rule", "the 183 day rule", and "the Commonwealth Superannuation Fund

253 For example, Malayan Shipping Co Ltd v FCT (1946) 8 ATD 75.

254 ITAA, s.6.

255 "Ordinary concepts" refer to some basic factors of residence, which have been generally recognized in common law. In particular, the factors to be considered as relevant to residence are place where taxpayer's home is situated, physical presence of a taxpayer in Australia, a taxpayer's residential backgrounds, nationality, frequency and regularity of movements, the purpose of visits to Australia, the nature of a taxpayer's business, a taxpayer's family and social ties in Australia, and a taxpayer's intention to stay in Australia. For detailed discussion, see Hamilton, supra note 1, at 32-4.

256 This test is the extension of the negative limb of the statutory tests - "unless the Commissioner is satisfied that his permanent place of abode is outside Australia" - for determining residence. This test approaches the issue of residence from an opposite direction and determines that a taxpayer would be an Australia resident if he does not have a permanent place of abode outside Australia. Two elements are considered for this purpose. First, length of time in which the taxpayer is absent from Australia. Secondly, the intention of the taxpayer to return to Australia. For more information, see Hamilton, id, at 34-5.

257 This is a statutory test. It must be considered in the light of three specific factors, which are whether a taxpayer has spent more than 183 days in Australia in the year of income, whether the taxpayer does not have a permanent place of abode in Australia, and whether the taxpayer intends to take up residence in Australia. If a taxpayer can be treated as a resident under other tests, "the 183 day rule" would be unnecessary. See Hamilton, id, at 36.
These four tests, though needing further definition in their application, provide the criteria for determining residence as adopted in Australia.

In contrast, China has not set forth any clear definition of residence. With respect to tax liability, Art.1 of the IIT Law states that a taxpayer who has resided in China for 365 days in the year of income is fully liable to pay tax on his income derived from sources in China and outside China; whilst a taxpayer who has resided for less than 365 days in China in a tax year is liable to pay tax only on income from Chinese sources. Since the Australian-Chinese Treaty expressly states that a "person is not a resident of a contracting State for the purpose of this Agreement if the person is liable to tax in that State in respect only of income from sources in that State", it can be assumed accordingly that the "365 day rule" (not the "source rule") is adopted in China as the sole test for determining residents of China.

Double taxation may arise from the criteria adopted in Australia and China. But the tax liability of a foreign person who has resided in China for 365 days in a year of income is further limited by a "5 year rule", which states that a taxpayer who has not resided in China for more than 5 years is liable to tax, apart from his income from Chinese sources, only on that part of his foreign income which has been remitted to China. Thus, no double taxation arises if an Australian, who is fully liable to pay tax on all his income under Chinese law, does not remit his Australian income to China. This additional criterion on the tax liability of foreign taxpayers reduces potential conflicts between Australian and Chinese tax laws in relation to the residence of a taxpayer. As a result, double taxation on individuals may occur only when an Australian resident, who has resided in China for 365 days but less than 5 years, has remitted his Australian income to China or when he has resided in China for more than 5 years.

The Treaty, in order to resolve the conflict, provides two tests for determining residence. The "permanent home" test appears incapable of determining the status of a taxpayer in most cases of dual residence, because while China treats persons residing in China for 365 days in a year of income as having a permanent home in China, Australia does not always regard a person who is away from

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258 This is a statutory test as well. It is applicable to Australian governmental officials and employees working abroad. See Hamilton, id, at 37.

259 Australian-Chinese Treaty, Art.4(2).

260 Although Chinese law does not expressly state so, it implies that a person residing in China for 365 days in an income year is treated as a resident of China, and therefore is regarded as having a permanent home in China.
Australia for 365 days as having a place of abode outside Australia. As a result, an Australian who works in China for one or two years but does not intend to leave Australia permanently, may be regarded as having his permanent home in the two countries. Thus, the second test, "close economic and personal relation" must be considered. But neither Australia nor China has explained clearly the meaning of this test, and difficulties may arise from its application.

The concept of "economic and personal relation" or "centre of vital interests" is an expression used in the OECD and UN Models. Presumably, the concept refers to those relevant factors, which vary in different legal systems, to be considered in determining the permanent home of taxpayers. The "economic relation" of a taxpayer to a country could include all factors which are relevant to how the taxpayer makes his living, such as his place and means of business, his business ties and the location of his employer. These factors have usually been taken into account in determining a taxpayer ordinary residence in common law. "Personal relation" could refer to all factors which are relevant to a taxpayer's social ties to a country, such as nationality, physical presence in the country, marital status and family ties. All these factors, however, are to be considered in determining residence according to ordinary concepts in common law. Although they have not been formally considered in Chinese domestic law, it is certain that for the purposes of implementing the Treaty these factors will be treated as relevant in determining the residence of taxpayers in

261 In such a case, whether an Australian taxpayer has abandoned his place of abode in Australia and whether he has intended to leave Australia permanently are decisive factors in determining his residential status in Australia. In FCT v Applegate 79 ATC 4307 (Federal Court), the taxpayer is regarded as a non-resident. The fact that he has no place of abode in Australia was an important consideration in determining his status as a non-resident in Australia. The importance of the fact whether a taxpayer has maintained a place of abode in Australia in determining his residential status for tax purpose is further evidenced in several cases, such as Case Q68 83 ATC 343, where a taxpayer, who was sent to work overseas for two years but had maintained his Australia home and no intention to stay longer in his overseas post, was not deemed to have a permanent home overseas; and Case Q33 83 ATC 139, where a taxpayer working in Saudi Arabia for 9 months and expressing an intention to return to Australia was treated as a resident in Australia. In contrast, Case S19 85 ATC 225, suggests that even if a taxpayer had maintained an Australian home but had expressed clearly an intention to leave Australia permanently, he was not treated as a resident in Australia for tax purposes. In the context of Australians working in China, an intention to stay in China permanently is usually unlikely.

262 Hamilton, supra note 1, at 32, and CCH, Australia Federal Tax Reporter para.11-565.

263 Ibid.
China where dual residence exists. Thus, China will have to construe the meaning of "economic and personal relation" in case of disputes. Differences between Australia and China may arise when they have to determine the concept of "economic and personal relation", the order of the "economic relation" and "personal relation" if the two "relations" suggest inconsistency, and the order of all relevant economic and personal factors if the application of these relevant factors results in disagreement. It appears that the undefined tests for determining residential status of taxpayers in the case of dual residence imply potential disagreements between Australia and China and, therefore, negotiation, though it is not mentioned as a means of dispute resolution in the Treaty, may have to be used to resolve the disagreements between the contracting parties in some cases of difficulty.

5.8.2.3. Issues in Relation to Residence of Companies

Australia and China have adopted similar criteria for determining the residence of companies, although Chinese criteria appear to be simpler than Australian ones. In Australia, a company can be a resident by virtue of its incorporation in Australia, or where, although not incorporated in Australia, it carries on business and has either "central management and control" in Australia, or is controlled by residents of Australia. In China, a company is a resident by virtue of its incorporation or of approval under Chinese law. Potential disputes may arise when a foreign company, which has been approved to operate in China, is controlled by residents of Australia, or when a company incorporated in China has branches carrying on business in Australia.

The Treaty provides two criteria - the tests of "place of effective management" and of "head office" - for determining residence of companies. In the case of dual residence, one of the criteria should be considered. If the "place of effective management" and the "head office" tests are applied, the relevant test should be determined by the relevant tax authorities in each state of residence.

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264 In China, international treaties signed by China not only have the same effect as domestic law, but also prevail over domestic law in case of inconsistency.

265 ITAA, s.6(1).

266 "Incorporation" refers to the establishment of a joint venture or a wholly foreign-owned enterprise under Chinese law. "Approval" seems to be similar to "registration" of foreign companies in Australia, but may be more selective and restrictive than the "registration". Foreign companies, which wish to operate in China in their established names, may seek approval from the Chinese Government. But the approval is not automatic. In this sense, the process of "approval" in China is selective. The difference between the "incorporation" of a foreign-related company and "approval" of a foreign company in China is that "incorporation" creates a new legal entity under Chinese law but "approval" does not. As far as taxation is concerned, Chinese law does not distinguish between companies allowed to operate in China through these two processes.
effective management" and "head office" are not situated in the same country, the "head office" test prevails over the "place of effective control" test.\(^{267}\) The provisions of the Treaty in relation to dual residence of companies differ from the language of the Models, which suggest only the "place of effective management" as the criterion for resolving the conflicts of dual residence. The Treaty also differs from Australian practice, which usually regards the "place of effective management" rather than "head office" as the decisive factor.\(^{268}\) It appears that the provisions on dual residence of companies are a compromise between Australia and China, although the provisions bear more similarities to Chinese practice than Australian practice. This is probably because Chinese tax law does not impose tax on income derived from sources outside China by solely foreign-owned enterprises.\(^{269}\) As a result, Australian income of an Australia company, which has branches in China, is not subject to Chinese tax, and no double taxation arises. As to Chinese income of the Australian company, provisions on business profits, such as permanent establishment rule,\(^{270}\) and on withholding tax apply. Thus, there is no need to resort to the tests for determining the residence of companies. In addition, joint ventures, which involve Australian investment, established under Chinese law, are unlikely to operate in Australia as Chinese companies. Therefore, as far as Australian tax is concerned, no conflict may arise between the test of the "place of effective management" and the test of "head office" in relation to Australian-participated Chinese joint ventures.

\(^{267}\) Australian-Chinese Treaty, Art.4(4).

\(^{268}\) For example, in *Malayan Shipping Co Ltd v FCT*, (1946) 8 ATD 75, the registered office and the directors of the company concerned were in Singapore, but the company and directors were controlled effectively by an Australian; and therefore, the company was treated as an Australian resident by the High Court. Similar view was held by the Court in *Esquire Nominees Ltd v FCT* 72 ATC 4076 (Gibb J.), 73 ATC 4114 (full High Court), where the company concerned was determined to be a resident of Norfolk Island not because the company was registered in Norfolk Island but because it was in fact controlled by directors on Norfolk Island.

\(^{269}\) FEIT Law fails to address the issues of tax on foreign income earned by solely foreign-owned enterprises established under Chinese law and branches of foreign companies approved according to Chinese law. In contrast to JVIT Law which allows foreign tax paid by joint ventures on their foreign income to be credited against Chinese tax, it appears that Chinese law does not tax foreign income of wholly foreign-owned enterprises and of branches of foreign companies.

\(^{270}\) In applying the "permanent establishment" rule, Chinese tax authorities may require the company concerned to have "a high order of presence or activities in China". Thus, representative offices engaged in information-gathering or liaison activities for their head offices or others are unlikely to be regarded as permanent establishment, not even an "establishment" sometimes. See Gelatt, supra note 228, at 51.
In the actual conditions of the Australian and Chinese economic relations, the potential differences in the application of the "place of effective management" test\(^{271}\) and "head office" test\(^{272}\) may not be significant in most cases.\(^{273}\) In some others, they may have theoretical significance only.\(^{274}\) No double taxation in relation to dividends received by an Australian resident who does not have establishments in China may occur.\(^{275}\) It would be rare for a joint venture established under Chinese law, which is the only form of resident company in China in the sense comparable to resident company in Australia,\(^{276}\) to have its central control and management in Australia as well. In another words, it is practically unlikely, at least today, that any company operating in Australia and falling within the concept of resident in Australia would also fall within the definition of resident company in China.

5.8.3. Tax Sparing Provisions

"Tax sparing" refers to a situation where State A gives tax credits to its resident's foreign income which is derived from State B and also has forgone tax under the law of State B. Art.23(4)-(7) of the Treaty include "tax sparing" provisions, which give tax credits to income containing Chinese forgone tax, as if the Chinese tax forgone has been paid. These provisions effectively ensure that the concessions given by the Chinese Government to Australians investing in China will

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\(^{271}\) Chinese authorities have not clearly expressed their views of the "place of effective management" test, which, arguably, could be open to several interpretations, such as where the general meeting of shareholders is held, where the directors' meeting is held, or where the real business decisions are made.

\(^{272}\) It may refer to registered office, place of directors' meeting, or headquarter of a company.

\(^{273}\) For example, in the case of business profits, a contracting State may have taxing authority merely by virtue of the fact that the company concerned has a permanent establishment, from which the profits concerned are derived, in the State.

\(^{274}\) For example, in the case of dividends, dual residence may never emerge as an issue, because Chinese law imposes withholding tax only on those dividends paid by a resident in China to a foreign person who does not have any establishment in China.

\(^{275}\) In this case, China will not treat an Australian who does not have establishments in China as its resident. It also should be noted that withholding tax on dividends in China has special meaning, which only refers to dividends paid to non-resident.

\(^{276}\) A wholly foreign-owned company in China is not fully comparable to a resident in Australia, because Chinese law does not tax income of wholly foreign-owned enterprises derived from source outside China.
be exempted also from Australian tax, so that the tax incentives granted to foreign investors in China will not lose their attraction.

"Tax sparing" provisions are not a new phenomenon in double tax treaties signed by either Australia and China. For the Chinese Government, these are crucial measures to attract more foreign investment. For the Australian Government, these provisions are more or less concessions made to its treaty partners from developing countries, which have used tax incentives to various extents to encourage the development of foreign investment in their countries. At present, "tax sparing" provisions are also found in the treaties signed by Australia with Singapore, the Philippines, Malaysia and South Korea, but only interest and royalties are dealt with in these treaties. By contrast, the Australian-Chinese Treaty has so far the most extensive "tax sparing" provisions in all the double tax treaties signed by Australia. Not only exemption or reduction on interest and royalties, but also exemption and reduction on dividends, business profits and other specified income are spared from Australian tax. Thus, the amount of income received by an Australian taxpayer from Chinese sources will be assessed together with the other income of the taxpayer, and a tax credit equal to the Chinese forgone tax will be allowed to the Australian taxpayers.

These provisions appear to be a small victory for China, which has made extensive tax concessions to foreign investors in China for the purpose of attracting more foreign investment. Although most treaties signed by China contain "tax sparing" provisions, the Australian-Chinese Treaty certainly is one of the most detailed and extensive ones. Nevertheless, the "tax sparing" provisions, which may be incentives to Australians who are interested in investing in China, seems harmless to Australian tax law and policies. This is because encouraging more Australians to invest in China now coincides with the interests of Australia, considering the potential of the extensive Chinese market and the perceived roles of Australia in Asia-Pacific economy.

5.9. Some Miscellaneous Issues

5.9.1. Issues of Controlled Foreign Companies (CFC)

The Australian Government proposed in 1988 an accruals tax system, which is designed to tax foreign income at the time when it is derived by a foreign company. Under the accruals tax system, countries are classed as either low-tax countries or comparable tax countries. Most income derived from low-tax countries

277 The accruals tax system is proposed for discussion by the federal Treasurer in his Economic Statement of 25 May 1988, see P.Keating, Economic Statement, May 1988 (Canberra, AGPS, 1988).
through either trusts or foreign companies controlled by Australian residents will betaxed in Australia on an accruals basis. On the other hand, most income derivedfrom substantial (or non-portfolio) interests in companies resident in comparable-taxcountries will be exempt from both the accruals tax and tax on dividends paid toAustralian corporate shareholders. Although the federal Treasurer announced thatthe accruals tax system would take effect from the 1990-91 income year, the Billhad not passed the Parliament as at December 1990.

Together with the accruals taxation system, rules governing CFC areproposed. Generally, a CFC has the following features. First, the company concernedmust have been incorporated outside Australia. Secondly, the company concerned may or may not carry on business in Australia, but definitely carries onbusiness outside Australia. Thirdly, Australian residents concerned may beAustralian nationals, or foreign investors who reside in Australia. This feature maysubject many foreign investors to the CFC rule. Lastly, a 50% threshold of controlmust be held by less than five persons who are Australian residents under the taxlaw. Under this rule, when five or less than five foreign investors (companies orindividuals) who are Australian residents for taxation purposes hold more than 50%interests in a foreign corporation operating in a low-tax country, subject to certainexceptions, their income derived from the operation is subject to the accruals taxsystem.

The CFC rule is designed to catch foreign companies controlled by Australianresidents who receive unjustified tax benefits from a listed country. When a CFCderives income from a listed country where the CFC neither is a resident nor has apermanent establishment, the accruals tax measures are applicable. In some caseswhen the CFC is a resident in a listed country from which the income concerned isderived, the accruals taxation measures also apply. The abuse of tax havens by

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278 Taxation of Foreign Source Income - an information paper, forming part of theTreasurer's Economic Statement (Canberra, AGPS, 12 April 1989) iii.

279 Ibid.

280 For example, when a CFC satisfies the test that it has a permanentestablishment in its country of residence, it has acceptable accounts and it has lessthan 50% of its total income in the form of "tainted income", some or all of itsincome will not be attributable to Australian resident shareholders. CCH, 1990Australian Master Tax Guide para.21-210.

281 The permanent establishment test must be read in conjunction with the tests forthe an acceptable account and 50% "tainted income".

282 The specified situations are when a CFC derives income from a designated taxconcession (subject to de minimis exemption), when a CFC's income derived fromanother country is not taxed by the listed country where the CFC resides, and when
Australian residents is a target of the CFC rule. Thus, the transfer of profits from a tax haven to a listed country which does not tax the transaction is subject to the CFC rule. However, the CFC rule does not apply to a CFC which derives income through a permanent establishment in a tax haven.

The CFC rule has important implications for foreign investment. A foreign corporation can be treated as a resident in Australia by virtue of its central management. A company controlled by a foreign investor can be seen as an Australian resident by virtue of its incorporation under Australian law. Moreover, a foreign individual can be regarded as an Australian resident by virtue of his domicile, of his continuous presence in Australia or of Superannuation Act 1976. These foreign investors may have extensive connections outside Australia, and thus may often be subject to the CFC rule.

5.9.2. Thin Capitalization Rules and Foreign Investment

The thin capitalization rules are designed for the purposes of preventing non-resident investors financing their investment excessively by in-house debts. Such excessive in-house debts are a cause of potential revenue loss in Australia, because the interest payment on the debts are currently subject only to a 10% withholding tax. To take advantage of withholding tax on interest is certainly a motivation for a non-resident, or a resident through a non-resident agent, to invest in loans rather than equity.

283 A.Gotterson, "Thin Capitalization by Non-resident" CCH, Australian Federal Tax Reporter para.98-700.
To avoid excessive in-house debts, the thin capitalization rules require an Australian company, partnership, or trust which has a foreign controller\textsuperscript{284} to have a specified foreign equity product.\textsuperscript{285} According to these rules, a company, partnership or trust which has a foreign controller is not allowed to deduct that part of the interest payment on foreign debts which exceeds three times the foreign equity in the company, partnership or trust. Similarly, a financial institution with a foreign controller is not allowed to deduct that part of the interest payment on foreign debts which exceeds six times its foreign equity. In these rules, a foreign controller is synonymous with a non-resident. Thus, the thin capitalization rules do not apply to companies, partnerships or trusts financed by foreign investors residing in Australia.

Under the thin capitalization rules, the term "foreign investor" has a special meaning. Section 159GZA defines a foreign investor as a non-resident who derives assessable income from sources in Australia, other than solely in the capacity of a trust estate. Thus the term "foreign investor" appears to have a narrow meaning under this section. But in the context of foreign investment law in Australia, the term "foreign investor" generally refers to any foreign national or company that

\textsuperscript{284} The meanings of foreign controllers vary in the cases of a company, a partnership or a trust. In the case of a foreign-related company, a foreign controller refers to a non-resident (other than an Australian-owned non-resident company) who, either alone or together with associates, has substantial control of the voting power in the company, is beneficially entitled to receive at least 15% of dividends or distribution of capital made by the company, or is capable of gaining such control or entitlement. A foreign controller also exists when the resident company or its directors are under an obligation (including a reasonable expected obligation) to act in accordance the direction of a non-resident and his associates. (ITAAs.159GZE(1)). In the case of a partnership, a foreign controller means a non-resident who, either alone or together with associates, has substantial control of the voting power in the partnership, has a beneficial interest in at least 15% of the capital or profits of the partnership, or is capable of gaining such control and interest. This extends to the situation where the partners are or may be under an obligation to act in accordance with the direction of a non-resident and his associates. (ITAAs.159GZE(2)). In the case of a trust, a foreign controller is a non-resident who is the trustee of the trust, or who either alone or with associates has substantial control of the voting power in the trust, has a beneficial interest in at least 15% of the corpus or income of the trust, or is capable of gaining such control or interest. Similarly, a foreign controller exists when the trustee is, or may be, under an obligation to act in accordance with the direction of a non-resident and his associates. (ITAAs.159GZE(3))

\textsuperscript{285} Foreign equity product means that the equity and debt ratio of a resident company, trust or partnership should be 1:3 and the equity and debt ratio of a financial institution should be 1:6. See the ITAA, s.159GZA. This means that allowable deductions of a company cannot exceed 3 times of its foreign equity and allowable deductions of a financial institution cannot exceed 6 times of its foreign equity.
invests in Australia regardless of its residential status under local tax law or how it derives its Australian income.

5.9.3. Issues of Tax Concessions - Inconsistency Between the Central and Local Governments in China

5.9.3.1. Disputable Local Concessions

China is a unitary State where the Central Government has higher authority than local governments. This higher authority, however, is by no means exclusive. In fact, local governments may exercise legislative power in many fields which are not reserved for the Central Government by the Constitution. The limitation on local legislative power that no local legislation can be inconsistent with the laws of the Central Government is general, wide and unspecific. Local governments thus may pragmatically make local regulations in relation to various matters, which are not reserved by the Central Government. Taxation is one of these matters.

Local governments in the SEZs, fourteen coastal cities and COEZs have granted many tax concessions, which are not based on any direct authorization from the Central Government, to foreign investors. Some of these concessions appear to be disputable. Since the tax law and regulations of the Central Government neither directly authorize nor clearly prohibit local governments from making tax concessions, the validity of these disputable concessions can only be determined in the context of particular concessions and the relevant laws and regulations of the Central Government.

The disputable concessions given by the local governments may be divided into several categories, such as CICT concessions, IIT concessions, enterprise tax (including FEIT and JVIT) concessions, and incentives relating to depreciation of assets. At present, the CICT concessions are given by the Beihai, Dalian, Guangzhou, Shanghai, Tianjin, Shandong, and Shenzhen Governments, which exempt foreign-related enterprises from paying CICT either at their initial stage of production or when they purchase exportable goods in China for resolving their foreign exchange shortage problems. The IIT concessions are granted by the Beihai, Lianyungang, and Jiangsu Governments, which unconditionally exempt foreign income of foreigners working in China. The enterprise tax concessions refer to exemption

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286 Although the Chinese Constitution has not expressly reserved any power for the Central Government, some areas can be deemed to be reserved for the Central Government. For example, local governments obviously do not have power to make international treaties under the Chinese Constitution.

287 The laws of the Central Government include the Constitution, the law of the NPC and regulations made by the State Council. Such limitation can be found in Arts.100, 107 & 116 of the Constitution.
and reduction of either FEIT or JVIT, which are granted by several local
governments (such as Shenzhen, Zhuhai and Guangzhou Governments) according to
criteria that were not authorized by the Central Government. The incentives relating
to depreciation of assets can be found in Shenyang, which is the only municipal
government as at December 1990 in China to give such incentives. These concessions
are analysed below.

5.9.3.2. Illegality of the CICT Concessions

It is clear that CICT is a national revenue which can only be exempted or
reduced by the Central Government or on its authorization. The Central Government
grants CICT exemptions and reductions to foreign enterprises operating in designated
areas under specified circumstances. \(^{288}\) But none of these concessions is identical
with the exemption given to foreign-related enterprises at their initial stage of
production and with the purchased goods for export. Apparently, the local
governments which granted these CICT concessions cannot support their concessions
by resorting to any of the existing tax incentives given by the Central Government.

Although under the Chinese Constitution, local governments may make
regulations in accordance with the basic principles (or spirit of law) adopted in the
law of the NPC, the above-mentioned CICT concessions cannot be justified on this
ground either. First, the CICT Regulations do not vest local governments with power
to vary the implementing rules for the CICT Regulations, although the Regulations
allow provincial governments to lay down detailed implementing rules in relation to
CICT on farmers and small traders.\(^{289}\) The CICT Regulations were made in 1958
when there was no foreign investment in China. The authorization given to local
governments with regard to the formation of detailed rules cannot be construed as an
authorization to make local CICT concessions to foreign-related enterprises, because
foreign investment was certainly not in the mind of the legislators in 1958.
Secondly, there are provisions implying that power to exempt or reduce the CICT is
reserved in the Central Government unless specified by law.\(^{290}\) Thus local

\(^{288}\) For example, imported goods, products and materials, except those specified by
law, are exempted from CICT, so are the exported products manufactured by
foreign-related enterprises.

\(^{289}\) Art.17 of the CICT Regulations states that a provincial government may lay
down detailed rules for collecting CICT from people's communes and their members,
individual farmers, or remnant capitalist business (including private business other
than small traders which ceased to exist soon after 1958, individual handicraft, small
traders and peddlers); and should report the rules so made to the State Council.

\(^{290}\) Art.2 of the CICT Regulations states that all enterprises and individuals
engaging in the specified traders in the country are subject to the Regulations, and
governments cannot exempt or reduce CICT without direct authorization from the Central Government. Thirdly, the contents of the local governments’ concessions are not consistent with the principles of the laws and regulations on CICT made by the Central Government. Since the imposition of CICT in both situations was arguable at first instance, the exemptions of CICT in the two cases may in fact function as a measure to reduce potential disputes, although this function is not stated in Chinese law. The concessions given by Shenzhen, Guangzhou and other local governments exempting foreign-related enterprises from CICT at their initial stage of production do not bear any similarity to other laws and regulations of the Central Government. Nor does the exemption given by Shandong Government to goods purchased by

Art.3 of the Regulations states that the change of any taxable items or tax rates must be decided by the State Council.

Most CICT concessions given by the Central Government are found in the State Council Regulations 1984, which exempt either imported materials used by foreign-related enterprises for production purposes or exported products manufactured by foreign-related enterprises.

CICT is imposed on enterprises or persons engaging in the production of industrial products, the purchase of agricultural products, the importation of foreign goods, commercial retailing, communications and transportation, and all other service trades. See Art.2 of the CICT Regulations. The application of CICT Regulations to imported materials for production and exported products can be challenged in two aspects. First, the meaning of "enterprises and persons engaged in importation of foreign goods" (Art.2 of the Regulations) is not clear. The question is whether it refers to import business only, or includes import business and general goods imported for the purposes of production and consumption by persons or enterprises which do not especially engage in import business. The language of Art.2 in Chinese can be interpreted in either way. But it appears to be logical if the provision is construed as applicable to import business only. This proposition is supported by the general function of CICT, which seems to be imposed on specified professionals who regularly engage or perform the specified transactions, rather than specified transactions carried out by persons who do not regularly engage in the specified business activities. If CICT was imposed on specified transactions regardless of the person involved, it would be payable by any person who incidentally purchases a chicken from a farmer, or a person who brings a TV set into China as a gift to a friend. As a result it is impossible to implement CICT in the case of a person buying some foods from farmers for personal consumption; and there is no difference between CICT and customs duties imposed on TV set brought in China by an individual. Secondly, it is not clear at all in Chinese practice whether CICT on exported products is imposed on the manufacture, or the exportation, of the products concerned. The tax on manufacture of products is imposed in the CICT Regulations, but the tax on exported product is not mentioned in the Regulations. In the context of the State Council Regulations 1984, the exempted CICT seems to be imposed on exported products not the manufacture of the exported products, and thus, exempting exported products made by foreign-related enterprises from CICT on exports actually frees foreign-related enterprises from a tax which the foreign-related enterprises are not liable to pay at the first instance. However, given the vagueness of the Regulations, the rationality of the exemptions concerned depends heavily on the interpretation of the Regulations by the Ministry of Finance or GTB which have power to do so under Chinese law.
foreign-related enterprises, which face foreign exchange shortage, for export.\textsuperscript{293}

The latter exemption appears to exempt from tax an activity which should not be subject to CICT at all in the circumstance described by the local regulations!

5.9.3.3. Illegality of IIT Concessions

The IIT Law has not authorized any local government to exempt or reduce IIT of foreigners working in China. The only IIT concession granted by the Central Government is a 50% tax reduction to foreign persons working in China.

The IIT concessions given by the Beihai, Lianyungang and Jiansu Governments are vaguely phrased. For example, Art.4 of the Regulations of Beihai Municipality states that all foreigners working in Beihai Municipality, who carry out an assignment or engage in business, will be exempt from paying individual income tax on income derived from sources outside China. Art.8 of the Regulations of Lianyungang Municipality and Art.8 of the Regulations of Jiansu Province states respectively that foreign income of foreigners working in foreign-related enterprises are exempted from IIT regardless of whether or not it is remitted to China. These provisions are only partially consistent with the IIT Law.

As has been seen, IIT Law treats foreign income of foreign individuals working in China in three different ways. Foreign persons residing in China for less than 1 year is exempted from IIT on their foreign income. Foreign persons residing in China for more than 1 but less than 5 years pay IIT on the part of foreign income remitted to China. Foreign persons residing in China for more than 5 years should pay IIT on all their foreign income. But none of the local regulations has noted the residential requirements set forth in the IIT Law.

In the context of the IIT Law, it is obvious that the concession granted by Beihai does not contravene the provisions of the IIT Law if the foreign individuals concerned has not resided in China for more than 1 year; or if the person does not remit his foreign income to China even if he has resided in China for more than 1 but less than 5 years. It is also apparent that the provisions of Lianyungang and Jiansu are consistent with the IIT Law in the case where a taxpayer resides in China for less than 1 year. But inconsistency arises in the case where a foreigner who has resided in China for more than 1 year remits his foreign income to China, or where a taxpayer has resided in China for more than 5 years. The exemption from IIT foreign income of persons who have resided in China for more than 5 years or less

\textsuperscript{293} In relation to this exemption, one can ask why a foreign-related enterprise should pay CICT on the purchase of goods rather than agricultural products. This concession appears to be based on a misunderstanding of the CICT Regulations by the Shandong Government.
than 5 but more than 1 year is unauthorized and virtually rootless. These local concessions are either partially useless,294 or illegal.295

5.9.4. Illegality of Concessions On Enterprise Taxes

5.9.4.1. Exemption of Withholding Tax in Shenzhen

Concessions on enterprises taxes are granted by some local governments in the following forms: exempting interest paid by a foreign bank branch to its head office from withholding tax,296 income tax exemption and reduction granted to enterprises which have US $2 million investment,297 and a 40% refund of reinvested amount by solely foreign-owned enterprises.298 The bases of these concessions will be analysed in turn.

The exemption from withholding tax interest which is not higher than the international interbank rate paid by a foreign bank branch to its head office is not consistent with any exemption ever given by the Central Government. As at December 1990, the Central Government has granted an exemption from withholding tax to interest on loans to designated Chinese banks and financial institutions, or the China National Off-shore Oil Corporation by foreign banks at an interest rate no higher than the rate of international interbank loans;299 interest on deferred payment provided by foreign sellers at an interest rate no higher than that on the Chinese party's buyer credit;300 interest on deposit of foreign banks or individuals in

294 In the case of a foreigner residing in China for less than 1 year, or less than 5 years but remitting no foreign income to China, the IIT is not payable on foreign income. Thus, the local provisions add nothing.

295 In the cases where a person working in China for more than 5 years, or where a person who has been in China for more than 1 but less than 5 years remits his foreign income to China, the tax can only be exempted by the Central Government.

296 Supplementary Regulations on Tax Reduction and Exemption for Enterprises in Shenzhen SEZs, reg.4, CCH, China Laws for Foreign Business para.73-529.

297 Regulations of Zhuhai Municipality for the Provision of Further Preferential Terms for Foreign Investors, reg.5(1), CCH, China Laws For Foreign Business para.74-500.


299 Provisional Regulations of the Ministry of Finance Regarding the Reduction and Exemption of Income Tax Relating to Interest Earned by Foreign Businesses from China, reg.2(1)&(2), CCH, China Laws For Foreign Business para.32-600. Hereinafter referred to as the Interest Exemption Regulations.

300 Id, reg.2(3).
designated Chinese banks when the interest rate on such deposit is lower than the interest rate on deposits in the country of the depositors;\(^301\) and interest derived from counter-trade.\(^302\) In addition, the Central Government also vests the local governments in the SEZs and fourteen coastal cities with power to exempt and reduce withholding tax on interest, royalties, dividends, and rentals derived from the provision of investment and equipment on terms favourable to China, or of advanced technology provided that the recipient does not have an establishment in China.\(^303\) These exemptions are available to enterprises engaging in specified transactions, and cannot be extended to enterprises which do not involve the transactions specified by the provisions.

The concession on withholding tax made by Shenzhen Government is not analogous to the exemptions granted by the Ministry of Finance, because the foreign bank branch is not one of the banks and financial institutions specified in the Interest Exemption Regulations. Although the interest rate in the Shenzhen provisions satisfies the same requirement (no higher than that on international interbank loans) as described in the Interest Exemption Regulations, this similarity alone cannot justify the concession given by the Shenzhen Government on withholding tax. Obviously, to be eligible for the exemption granted by the Ministry of Finance, a foreign bank must both provide loans to a specified bank, financial institution or enterprise in China, and provide the loans at an interest rate no higher than the rate on international interbank loans.

The Shenzhen Government cannot support its concession on withholding tax on the ground of the State Council Regulations 1984 either. The State Council Regulations 1984 imply that when a foreign bank, which does not have establishments in China, provides loans on favourable terms to enterprises in China, the local governments in the SEZs or fourteen coastal cities have discretion in exempting or reducing withholding tax on interest derived from such loans. Having no establishment in China is a necessary condition for the exercise of the local governments' discretion. A foreign bank branch can well be regarded as an establishment of its head office in China. Therefore, a foreign bank which receives interest from its branches in China is not the described enterprises, which do not have establishments in China. The Shenzhen Governments, thus, cannot rely on the

\(^{301}\) Id, reg.2(4).

\(^{302}\) Id, reg.2(5).

\(^{303}\) Provisional Regulations on Reduction and Exemption of Enterprise Income Tax and CICT for the Fourteen Coastal Cities and SEZs, Div.1, Art.4; Div.2, Art.4; and Div.3, Art.3, CCH, China Laws for Foreign Business para.70-845, hereinafter referred to as State Council Regulations 1984.
provisions, which grant a discretion to the local governments to exempt and reduce withholding tax on interest, royalties, dividends or rentals received by foreign enterprises that do not have establishments in China.

5.9.4.2. Questionable Criteria for Tax Concessions in Zhuhai

The Zhuhai Government grants a two-year tax holiday and three year 50% tax reduction to foreign-related enterprises which either have more than US $2 million investment, or have advanced technology, a relevant long capital recovery period and a contract life of more than 10 years. Two criteria are adopted by the Shenzhen Government to grant the concessions. These are "US $2 million" test and "advanced technology, long capital recovery period and 10 year contract life" test. In the Chinese text of the provisions, the three components of the second test appear to be inseparable. Like the IIT concessions in Beihai and Lianyungang, inconsistencies between the law of the Central Government and the Regulations of Zhuhai may arise in some cases.

The US $2 million threshold has no foundation in the law of the Central Government, in particular in the relevant regulations of the State Council. It is not clear where the "US $2 million" threshold comes from. Apparently, income tax exemptions and reductions granted by the Zhuhai Government under the "US $2 million" threshold contravene the law of the NPC and regulations of the State Council. Neither of them has authorized the Zhuhai Government to do so or has granted similar concessions to foreign investors, which may be copied by the Zhuhai Government.

The second test adopted by Zhuhai is not as obviously questionable as the first. It concerns several provisions passed by the NPC and State Council. The Central Government gives tax concessions to enterprises with a long contract life (10 years), a long lead time, or which operate in specified sectors (such as agriculture, forestry, animal husbandry, and communications and transportation). But each

304 The Regulations adopt two thresholds: US $5 million for enterprises operating in the service industries within the SEZs, and US $30 million for foreign-related enterprises operating in the "old suburbs" of the fourteen coastal cities. Reg.2 of Division I of the State Council Regulations 1984 states that enterprises engaging in the service industries which have overseas investment exceeding US $5 million and a contract life of 10 years or longer should be exempted from income tax in the first profit-making year and given a 50% reduction in the next two years, upon the approval by the tax authorities in the special zones. Reg.1 of Division of the State Council Regulations states that foreign-related enterprises operating in the old suburbs of the fourteen coastal cities and of Shantou, Zhuhai and Xiamen, which have overseas investment exceeding US $30 million and require a long lead time, are taxed at a reduced rate of 15%.
provision on the concessions has its own limitation on application. In the light of the provisions of the Central Government, it appears that the provision of Zhuhai is vaguely phrased. It blurs the scope of eligibility set forth in the provisions of the Central Government. No question arises when the Zhuhai's provision applies to enterprises which are eligible for the concessions granted by the Central Government. But inconsistencies arise when the Zhuhai provision applies to solely foreign-owned enterprises, which do not engage in the specified productive-type operations. The Zhuhai provision thus appears to be illegal.

5.9.4.3. Questionable Refund on Reinvested Amount in Guangzhou

Art.35 of the Regulations of Guangzhou states that if a foreign investor reinvests his profits in the Development Zone of Guangzhou for a period of more than 5 years, he will receive a tax refund of 40% of the reinvested amount. This provision does not distinguish between foreign investors in a joint venture and foreign investors in a solely foreign-owned enterprise. The latter, except as specified in law, is not generally eligible for this concession.

The JVIT Law grants a refund of 40% of the reinvested amount to participants of a joint venture. But the FEIT Law does not grant similar concession to foreign investors investing in a solely foreign-owned enterprise. Thus, the concession on the tax refund seems inapplicable to wholly foreign-owned enterprises, except those qualified as exporting enterprises or technologically advanced enterprises which are eligible for 100% tax refund on the reinvested amount reinvested in the same (or similar) enterprises for a period of more than 5 years. The tax refund of 40% of reinvested amount given by the Guangzhou Government blurs the line

305 For example, Art. 5 of JVIT Law allows any joint venture which has a contract life of 10 year or longer to have a two-year tax holiday, followed by a 50% reduction of 3 years. But wholly foreign-owned enterprises are not eligible for the concessions. The State Council Regulations 1984 grant a two-year tax holiday and a 50% reduction of 3 years to enterprises (either wholly foreign-owned or joint ventures) operating in the SEZs, which not only engage in specified sectors such as industry, communications and transport, agriculture, forestry, animal husbandry or other productive-type operations, but also have an operational period of 10 years or longer. Enterprises which have a contract life of 10 years or longer but do not engage in the specified productive-type operations are not eligible for these concessions.

306 Some areas in Guangzhou are designated as Development Zones.

307 Art.6 of JVIT Law states that if a participant in a joint venture reinvests his profits in China for a period of not less than 5 years, he may obtain a tax refund of 40% of the reinvested amount.

between a wholly foreign-owned enterprise and a joint venture. The concession is illegal when it is made available to foreign investors in a solely foreign-owned enterprise, except those in exporting enterprises and technologically advanced enterprises.

5.9.5. Illegality of the Concession on Accelerated Depreciation in Shenyang

Shenyang Municipal Government allows foreign-related enterprises to carry out accelerated depreciation of fixed assets. It sets out maximum depreciation rates, which do not have any basis in the law of the Central Government. The Shenyang Government has exercised a power it does not legally have. Both FEIT Regulations and JVIT Regulations have set out standard depreciation periods of fixed assets, and allowed accelerated depreciation only upon approval by the Ministry of Finance. Local governments are not authorized to change the depreciation periods fixed by the law of the Central Government. Therefore, the concession on accelerated depreciation of fixed assets allowed by the Shenyang Government, which is the only local government in China granting such concession, is illegal.

5.10. Conclusion

Australian and Chinese tax laws are at different stages of development. Compared with Australian tax law, Chinese tax law is far broader and vaguer, leaving many particular issues to be dealt with by tax authorities. In this sense, a wider discretion is exercised by the Chinese tax authorities. This wide discretion is one of the reasons for the existence of many inconsistent and obscure tax regulations in China. To reduce, abolish and prevent inconsistencies, codification of tax law seems essential. The Australian ITAA may provide a helpful example for the codification of tax law in China.

The issue of tax concessions in China is twofold. Firstly, the Chinese Government has heavily relied on tax incentives to encourage foreign investment, but seems to have ignored that tax concession is not the only factor affecting foreign investment. The decline of foreign investment in China after June 1989 suggests that political stability, economic prospect and administrative efficiency of China are equally, if not more, important in attracting foreign investment. In fact, tax concessions (no matter how superficially attractive they seem to be) can hardly be incentives at all to foreign investors who have neither confidence in nor approach to

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309 The rates are 15% on buildings, 20% on machine and equipment and 30% on means of transport and electronic instrument. Regulations of Shenyang Municipal Government for the Encouragement of Foreign Investment, Art.5, CCH, China Laws for Foreign Business para.13-514.
the Chinese market. Secondly, the illegality of many local tax concessions created confusion among foreign investors. The co-existence of these local tax concessions and the central Government's express rejection of these concessions seems to imply that the Chinese Government is not liable to protect foreign investors' interests granted by these illegal concessions. Foreign investors may be further confused by the continuous toleration of the central Government towards the existence of these illegal concessions. This situation undermines confidence of investors and defies the purposes of tax concessions. Therefore, the inconsistencies must be removed and the use of tax concessions in China must be carefully re-examined by the Chinese Government if it intends to attract more foreign investment into China.
Chapter 6 Settlement of Foreign Investment Disputes

6.1. Settlement of Commercial Disputes in Australia

6.1.1. An Overview

Foreign investors may run risks which do not exist, or do not exist to the same extent, when they invest in their home countries. These risks can include nationalization of their properties, non-performance of government promises and procedural unfairness when a foreign investor seeks a legal remedy in the recipient country. These issues are certainly concerns of people investing in Australia and China, and in particular of Australians investing in China. Economically, China is a developing country. Politically, China is the largest communist country that has refused to change its deified but yet undemocratic political beliefs. Both factors increase investment risks.

This chapter will look at issues relating to the protection of foreign investment in Australia and China, and examine legal remedies or their alternatives in the case of investment disputes, with an emphasis on disputes involving Australian and Chinese parties.

In Australia commercial disputes are traditionally settled in courts of law. It was reported that in 1975 Australia had the highest rate of civil litigation in the world, averaging 62.06 civil cases per 1,000 persons.\(^1\) The popularity of courts as a forum for commercial dispute resolution is further illustrated by the statistics on civil caseloads in Victoria between 1981 and 1983, during which civil cases commenced in the State averaged over 220,000 each year.\(^2\) If the cases submitted to the Victorian Registrars of the High Court and Federal Court, the Children's Court, and other courts or tribunals are taken into account, the caseloads would be even higher. In practice, more often than not the courts are deliberately used by one or both parties as a forum for "involuntary negotiation" or "compulsory exchange of information".\(^3\) Such use of courts can be seen again in statistics from Victoria, where between 1978 and 1980 only about 1.7% of the 715 civil cases commenced in the Supreme Court

\(^1\) M. Fulton, Commercial Alternative Dispute Resolution (Sydney, Law Book Company, 1989) 24.

\(^2\) Civil Justice Committee, Court Surveys and Studies 1978-1984: concerning the Civil Caseloads of the Supreme Court, the County Court and the Magistrates' Court of Victoria (Feb.1985) 28.

\(^3\) These terms refer to negotiation processes carried out between disputing parties after the commencement of litigation. The process of negotiation here is involuntary in comparison with "negotiation" as a technique of ADR. The exchange of information between the disputants, which most likely forms the basis for settlement prior to the trial, is compulsory under the court rules.
were tried to verdict, the others being either withdrawn or settled before trial. Pre-trial settlement is a feature of judicial proceedings as a means of dispute resolution in Australia.

Australian courts are now based on the parallel existence of federal and State judicial systems. The federal judicial system consists of the High Court, the Federal Court and specialist courts or tribunals, such as the Family Court and the Administrative Appeal Tribunal. The State judicial system consists of Supreme Courts, intermediate courts and inferior courts in each State or Territory. In general, all courts have power to hear commercial disputes. The Supreme Court in each State has also a Commercial Division specially dealing with cases entered into the commercial list.

The judicial system in Australia is an evolution of the English legal system, which has been modified to suit Australian needs, and especially the needs of a country with a federal political system.

The preference for courts of law as forums for dispute resolution seems to have been received as part of Australian culture. But this has not prevented the development of other means of dispute resolution (e.g. semi-judicial means of dispute resolution), alternative to formal court proceedings. The Australian industrial conciliation and arbitration systems may be regarded as representing such efforts.

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4 Civil Justice Committee, supra note 2, at 45.

5 The high percentage of the cases settled after the beginning of legal action but before the commencement of formal trial is partially attributable to the delay in court hearings. The delay itself, on the one hand, is a result of disproportion between the heavy caseloads and insufficient number of judges; but on the other, could be a factor which presses disputing parties to settle their differences as quick as possible in consideration of time and cost built up. In addition, another reason which resulted in a majority cases to have been settled prior to trial, (as observed by a lawyer who believes that about 95% of cases commenced in the Supreme Court in NSW are settled prior to trial), is "that the pre-trial process involving the exchange of pleadings, discovery and interrogatories results in an exchange of information between the legal representatives acting for the parties which enables them to form a more realistic view of the prospects of their clients' cases". H. Werksman, "Negotiation in Commercial Litigation" (1989) 17 A.B.L. 27, 28.

6 A "commercial list" means a list of cases, compiled by the court, arising from commercial causes defined in the court rules of each State.

7 The federal industrial conciliation and arbitration system was established in 1904 and was developed into a two-tier mechanism after 1956, consisting of the Australian Conciliation and Arbitration Commission and the Australian Industrial Court which was later replaced by the Industrial Division of the Federal Court in 1977. The industrial conciliation and arbitration system in each State and Territory was established at various times in the history, with the earliest mechanism being set up in Victoria in 1896. Today, industrial conciliation and arbitration systems in States adopt more or less the same structure as the federal system, consisting of industrial
During the process of conciliation and arbitration, commissions are not bound by normal rules of court proceeding. Thus the mechanisms for resolving industrial disputes represent an effort to develop a less adverse approach to dispute resolution within the formal judicial system.

Today, the trend seems to shift away from the traditional approach to dispute resolution. As a result of the reception of ADR (alternative dispute resolution), which was initiated in the United States in late 1970s and attracted wide attention in the 1980s, courts of law are no longer the sole forum for settling commercial disputes. Although the concept of ADR is still unsettled, many methods of dispute resolution have been developed for resolving disputes without resorting to formal judicial proceedings. The Australian Centre for International Commercial Arbitration (ACICA) in Melbourne, and Australian Commercial Dispute Centre (ACDC) are two facilities established in the 1980s for developing ADR in Australia.

No satisfactory definition of ADR has yet been achieved. People might have assumed that the term is transparent by itself. But "alternative dispute resolution" itself does not suggest to what the alternative is intended. For example, legal practitioners may regard ADR as "an alternative way to settle disputes. The term itself encompasses a variety of procedures outside of conventional judicial adjudication". J.Doyle, "Appropriate Use of A Third Party Neutral" paper presented at a Conference "Cut Litigation Costs and Save Time Through ADR" held in Sydney on 22 July 1988, at 3. This attempted definition of ADR does not tell us more than what the term itself has literally suggested, because the meaning of "conventional judicial adjudication" is not clear. Some methods of disputes resolution, such as compulsory mediation and arbitration, had been closely associated to, or conducted within, the formal judicial system when the concept of ADR was introduced in the 1980s. Thus, the question, which arises therefrom but can only be defined according to subjective criteria, is what is conventional judicial adjudication or formal judicial system.

For example, Australian Commercial Dispute Centre (ACDC) provides the following options to disputants who want to resolve their disputes through ADR: negotiation, mediation, independent expert appraisal, case presentation, conciliation, hybrid arbitration, arbitration, and private judge. "Another Way" Law Reform commission, (1989) 55 Reform 145, 147.

It was set up in 1985 for the purposes of providing arbitration, as well as conciliation and mediation, services to international commercial disputes taken place in and outside Australia.

It was established in Sydney in 1986 for the purposes of providing ADR services to commercial disputes, with emphasis on mediation, conciliation, and other methods of less formal nature.
Commercial disputes have special features. Parties to such disputes often do not want to endure high costs and waste lengthy time against business interests just for the sake of protecting their legal rights. Nor want they to damage their continual business relationships against their business interest for the sake of maintaining legal procedures of an adverse nature. But they do need to resolve their differences for the sake of their business interests. These features require an economic, fast and amicable means of dispute resolution. ADR was thus seen as the best methods of dispute resolution to serve the needs for commercial dispute resolution.

As will be seen, ADR represents a range of innovative techniques for dispute settlement, which provide the opportunity to reduce or avoid the disadvantages of traditional means of dispute resolution. But whether ADR can satisfy the needs of a society depends on the persons who use it. Thus in some cases ADR could be as expensive and time-consuming as court proceedings. Factors which will affect the performance of ADR methods are to be examined in this section.

6.1.2. Courts and Commercial Disputes

6.1.2.1. Jurisdiction of the High Court Over Commercial Disputes

The High Court of Australia is the highest federal court exercising the judicial power vested by the Commonwealth Constitution. Its original jurisdiction is derived from either s.75 of the Constitution itself or legislation passed under s.76 of the Constitution. Its appellate jurisdiction is derived from s.73 of the Constitution, which enables the High Court to act as a general court of appeal throughout the Commonwealth. In this sense, the High Court is the highest judicial power of the Commonwealth and its decisions "on appeal from any jurisdiction bind all courts in Australia."14

In its capacity to act as either a trial court or an appeal court, the High Court may deal with commercial disputes or foreign investment disputes. As a trial court, the High Court may hear various commercial disputes, such as matters relevant to international treaties signed by Australia,15 disputes relating to the Commonwealth Government,16 disputes involving more than one State,17 matters involving the

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13 Crawford, supra note 7, at 157.
14 Id, at 173.
15 The jurisdiction of the High Court over a treaty is derived from the federal legislation which gives effect to the treaty. Id, at 157.
16 Id, at 158.
17 Ibid.
constitutional power of the Commonwealth to control commerce and foreign investment,\textsuperscript{18} and some matters arising under a federal law.\textsuperscript{19} But for practical difficulties, an ordinary commercial or investment dispute can rarely commence at the High Court, given the fact that there are more district courts, Supreme Courts or even Federal Courts to choose from. As a court of appeal, the High Court may examine any case appealed from federal or State courts in accordance with law, including cases involving foreign investment disputes.

6.1.2.2. Jurisdiction of the Federal Court Over Commercial Disputes

"The Federal Court is a superior court of law and equity, with jurisdiction extending throughout Australia, and with judges resident in each State except Tasmania.\textsuperscript{20} It derives its power principally from Chapter III of the Constitution, which allows the federal jurisdiction to be vested in "such other federal courts as the Parliament creates", but specifically from various federal Acts which grant the Federal Court jurisdiction to deal with matters arising under those Acts.\textsuperscript{21}

The Federal Court has both original and appellate jurisdiction. Its original jurisdiction is conferred by various federal laws, in particular the Bankruptcy Act 1966 (Cth), the Trade Practices Act 1975 (Cth) (TPA), the Administrative Decisions (Judicial Review) Act 1977 (Cth).\textsuperscript{22} Its appellate jurisdiction, also based on various Acts, extends to matters dealt with by a single judge of the Federal Court; appeals from judgments of all territories except the Northern Territory; appeal from judgments of State Supreme Courts in relation to property, bankruptcy, taxation and criminal matters; cases stated or referred to the Federal Court by a lower court or tribunal and appeals from the decisions of a federal tribunal, such as Administrative Appeal Tribunal (AAT).\textsuperscript{23} In both capacities, the Federal Court has considerable significance to foreign investors, in particular when the TPA and ITAA are involved.

When cases arise from the TPA and Income Tax Assessment Act 1936 (Cth) (ITAA), the Federal Court would be the main forum for dispute resolution. Under

\textsuperscript{18} The High Court's power to interpret the Constitution is not exclusive. Rather the Constitution questions "can be decided in any court (except a court composed of lay justice)". Id. at 159.

\textsuperscript{19} Ibid.

\textsuperscript{20} Id. at 138.

\textsuperscript{21} Id. at 136-55.

\textsuperscript{22} Id. at 138-40.

\textsuperscript{23} Id. at 141-2.
TPA, the Federal Court has exclusive jurisdiction over matters arising from Pt.IV (restrictive trade practice). Both sections 50 (mergers and other acquisition) and 50A (acquisition outside Australia) are included in Pt.IV. These sections may affect takeovers carried out either in or outside Australia by foreign investors, who carry on business in Australia.\(^{24}\) The Federal Court has also concurrent jurisdiction over matters falling within the ambit of Pts.V and VI of the TPA. In addition, under ITAA, a foreign investor dissatisfied with a Commissioner's decision may appeal to the Federal Court or the AAT. In this case, since the Court does not have power to amend the Commissioner's decision directly,\(^{25}\) the AAT, which has full power and may exercise discretions to the same extent as the Commissioner, may be a more effective forum when the Commissioner's decisions are involved.

6.1.2.3. Jurisdiction of State Supreme Courts

The State Supreme Courts are courts of general jurisdiction. Their original jurisdiction extends to all commercial or investment disputes, "unless expressly excluded".\(^{26}\) But their appellate jurisdiction, varying in each State and Territory, is determined "in a diffuse way" by the laws of the relevant State.\(^{27}\) Because of their general jurisdiction, State Supreme Courts may play a more active role than the Federal Court in dealing with cases involving commercial and investment disputes.

The importance of State Supreme Courts in dealing with cases involving foreign investment can be seen in either their jurisdiction over disputes arising from the FATA and TPA, or power derived from their general jurisdiction.\(^{28}\) Under the FATA, a State Supreme Court (not only a Supreme Court) is invested with power to

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\(^{24}\) For instance, a proposal made by BHP to takeover a New Zealand corporation (NZ Steel) was challenged by the TPC at the Federal Court between Sept.1989 - Feb.1990. But the TPC's challenge was unsuccessful. *TPC v Australian Iron and Steel Pty Ltd & Ors* CCH, ATPR vol.2, para.41-001.

\(^{25}\) The decision of the Court is implemented through the Commissioner who must give effect to the Court's decision within 60 days after the decision entered into force. ITAA, ss.200B.

\(^{26}\) Crawford, supra note 7, at 119.

\(^{27}\) Id, at 125-6.

\(^{28}\) Crawford observes that the "principal characteristic of supreme Courts, unlike any other trial courts in Australia, is that they are courts of general jurisdiction". Thus, "every matter is within the jurisdiction of a Supreme Court unless expressly excluded". Id, at 119.
enforce the federal Treasurer's decisions and to hear cases arising from the Act.\(^ {29}\)

Under the TPA, a State Supreme Court may hear cases referred to it by the Federal Court and may also deal with cases relating to the TPA Pt.V. The general jurisdiction of a State Supreme Court extends to all matters arising from the State law and matters which can be dealt with by it by the investment of federal jurisdiction under the federal law.

Under the Jurisdiction of Courts (Cross-Vesting) Act 1987 (Cth) and relevant State legislation, foreign investors may seek legal remedies at either the Federal Court or a State Supreme Court unless prohibited by specific provisions, e.g. "special federal matters".\(^ {30}\) This cross-vesting scheme of course does not prevent any foreign investor from seeking legal remedy at the High Court. But, more often, they may commence legal actions in either the Federal Court or a State Supreme Court for pragmatic reasons.\(^ {31}\)

6.1.2.4. Jurisdiction of Lower Courts Over Commercial Disputes

The jurisdiction of intermediate and inferior courts is determined by monetary limits prescribed in the law of each State and Territory, with an intermediate court having higher monetary limits than an inferior court in the same State. But the particular thresholds in each States vary. In civil cases, the monetary limits of intermediate courts in Australia range from $40,000 in Queensland to

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\(^ {29}\) For example, Equitcorp Industries Ltd is an Australian company. Half of its shares were held by an Australian company, Equiticorp Tasman Ltd. Another Australian company, Capitalcorp Holding Ltd in turn held 43% of the Equiticorp Tasman Ltd. At the same time, two New Zealand corporations held convertible notes and options in Equiticorp Tasman Ltd and Capitalcorp Holding Ltd. When Equitcorp Industries Ltd purchased shares in ACI International Ltd in 1986 (the purchase increased Equitcorp Industries Ltd's shares in ACI International Ltd from 12.4% to 18.2%), ACI International Ltd refused to register the transfer on the basis of Art.30(1) of its Articles of Association which prohibits foreign persons from acquiring substantial or aggregate interest in the company. The matter concerned FATA to the extent whether the convertible notes and options held by the two New Zealand corporations had formed control in Equiticorp Tasman Ltd and Capitalcorp Holding Ltd in the meaning defined by the Act. The case was brought to the Victorian Supreme Court by Equitcorp Industries Ltd in 1986, first to a single judge and then to a full Court. The FATA was examined by the Court and the convertible notes and options held by the New Zealand companies were decided not forming control defined in the FATA. *Equitcorp Industries Ltd v ACI International Ltd* (1986) 10 ACLR 568; and (1986) 5 ACLR 237.

\(^ {30}\) Crawford, supra note, at 147.

\(^ {31}\) For example, cases arising from some provisions of the TPA must be heard in the Federal Court; and for the convenience of enforcing judgments, disputants may choose the State where possible subjects of execution are situated.
$100,000 in New South Wales and South Australia. Inferior courts have jurisdiction over matters involving sums "between $500 in North Territory Local Courts of limited jurisdiction to as much as $20,000 in Victoria Magistrates' Courts". Sometimes, "for a variety of reasons: for example, lower costs in a lower court, or the increased publicity or higher level of judicial competence in a higher court", parties to a dispute may prefer to commence a legal action in a chosen court. But cases can often be transferred between different courts after an action has been commenced at a particular court.

6.1.2.5. Informal Proceedings Within the Judicial System

Australian courts, as a forum for dispute resolution, provide not only judicial means, but also quasi-judicial means of dispute resolution. Counselling services in the Family Court, court-annexed arbitration in New South Wales and court-conducted conciliation in South Australia are examples of the latter. The counselling services established by the Family Court Act 1975 (Cth) include three functions: reporting, reconciliation counselling and conciliation counselling. The courts have

32 Crawford, supra note 7, at 102. In particular, the jurisdictional limits of intermediate courts in each State are NSW District Court $100,000; Victorian County Court 100,000; SA Local and District Criminal Court $100,000; District Court of Western Australia $80,000; and Queensland District Court $40,000. Based on data in Crawford, supra note 7, at 112; and a change (limit for personal injuries in Victoria has been lifted from $50,000 to $100,000) is made as the law stands in December 1990.

33 In term of civil jurisdiction, inferior courts refer to the Magistrates courts in ACT, Vic and Qld; Local Courts in NSW, SA, NT and WA and the Courts of Requests in Tas. Crawford, supra note 7, at 103.

34 Ibid. The jurisdictional limits of inferior courts are ACT Magistrates Courts, $10,000; NSW Local Courts, $5,000; NT Local Courts of limited jurisdiction, $500, of full jurisdiction, $10,000; Queensland Magistrates Courts, $5,000; SA Local courts of limited jurisdiction, $7,500; Tasmanian Courts of Requests, $5,000; Victorian Magistrates' Courts, 20,000 and $5,000 for personal injury claims; and WA Local Courts, $6,000. Crawford, id, at 113.

35 Crawford, id, at 105.

36 The possibility of choosing legal forum may bring the party or parties advantages, as well as disadvantages, depending on the perceived priority of the disputing parties and the level of cooperation between the disputants. For example, a disputant's choice of forum could be to the disadvantage of the other disputant. In addition, when a dispute can be sued in several jurisdiction, each of them may emphasize different interests of the disputants, (having regard to the limitation of cross-vesting jurisdiction), the disputants have to determine which interest deserves more attention in a given case.

37 Crawford, supra note 7, at 109-111.

38 The definitions of "reconciliation" and "conciliation" are as follows:
a duty to recommend reconciliation or conciliation services to the parties to a family dispute.\textsuperscript{39} The process of reconciliation or conciliation can be conducted by either the court counselling services or any approved independent counselling organization.\textsuperscript{40} The counselling services are characterised by their compulsoriness (in most cases) and close association with the Court.

Court-annexed arbitration, which was introduced into New South Wales by the Arbitration (Civil Action) Act 1983 (NSW), seems to be a simplified litigating proceeding. Under this scheme, the Registrars of the District Court and Local Court have power to refer certain cases to arbitration.\textsuperscript{41} The arbitrators, who are appointed by the Chief Judge of the District Court and the Stipendiary Magistrate from a panel nominated by the Law Society and Bar Association, conduct arbitration according to the procedural rules of the courts, rather than procedures agreed upon by the disputants. In addition, an award of an arbitrator is regarded as an order of the court and may be appealed against. These features distinguish court-annexed arbitration from normal arbitration.

Court-conducted conciliation was introduced into South Australia by the Conciliation Act (SA) 1929. Under the Act, courts have power to initiate a conciliatory process, if they believe that, either from the nature of the case or from the attitudes of the disputants (or their attorneys), a settlement through conciliation is possible.\textsuperscript{42} The courts act as conciliators and assist disputing parties to reach an agreement for settlement. If necessary, the courts may deliver a judgment to confirm the result of conciliation. But the judgment so made must be expressly

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Reconciliation means the process of re-uniting spouses. Conciliation means assisting the parties to deal with the consequence of the established breakdown of their marriage, whether resulting in a divorce or a separation, by reaching agreement or giving consent or reducing the area of conflict upon custody, support, access to and education of the children, financial provisions, the disposition of the matrimonial home, lawyer's fees and every other matter arising from the breakdown, which calls for a decision on future arrangements.


\textsuperscript{39} Family Law Act 1975 (Cth), ss.14 & 16A.

\textsuperscript{40} Id, s.12.

\textsuperscript{41} The District Court has power to refer claims up to $20,000, and the Local Court can refer claims up to $5,000, to arbitration.

\textsuperscript{42} Conciliation Act 1929 (SA), s.3.
accepted by the parties concerned; otherwise it would be invalid. The active but conciliatory role of the courts in the process of court-conducted conciliation is a feature of this conciliation, which is unique in Australia.

Given the popularity and added functions (compared with traditional role of the common law courts) of the courts, Australian courts have been and will continue to be the most important forum for dispute resolution. Courts will always be the forum where an ultimate settlement of disputes under a given legal system can be reached. In particular, foreign investors may always seek legal protection if they wish to settle disputes through litigation rather than ADR.

6.1.3. Alternative Dispute Resolution in Australia

6.1.3.1. Methods of ADR in Australia

ADR is a vaguely defined concept, which includes all means of dispute resolution except formal court proceedings where judges play the role of adjudicators. Many methods or techniques of dispute resolution could be brought within the scope of the concept. Lacking uniform criteria for classification, terms and particular methods categorized as ADR vary. This thesis will examine ADR methods available in Australia as defined by ACDC. But variations to the ACDC definition will also be taken into account.

1) Negotiation

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43 As at December 1990, only two cases relating the Conciliation Act 1929 had been reported. See Worden v Levito 7 (1974) SASR 20 and Baroutas v Limberis & Sons Pty Ltd & Ryan & Phillis 8 (1974) SASR 136. In Worden v Levito, a judgment made by a Special Magistrate in a Local Court under the Conciliation Act 1929 was set aside. One of the reasons for this was that formal and express consent was not given to the judgment by the appellant.

44 The importance of courts can be seen not only in their decisions on the matters asked by the disputing parties to decide, but also in their mere existence, which reassures those who have legal rights and discourages those who do not.

45 Ultimate settlement means a final solution which can literally be reached within a given legal system. It does not necessarily mean that a settlement will be voluntarily accepted by the disputants concerned. In this sense, it does not always mean that a dispute has been "ultimately" resolved between the disputants.

46 Dr. Alder, Director of the Program on ADR for the Supreme Court of Hawaii described 9 identifiable techniques of ADR: negotiation, conciliation, voluntary mediation, mandatory mediation, formal fact finding, arbitration, mandatory arbitration, summary jury trials, and rent-a-judge. By contrast, J. David, Manager, Education and Research, ACDC, Sydney, identified 8 methods of ADR, including negotiation, mediation, independent expert appraisal, case presentation, conciliation, hybrid arbitration, arbitration and private judge. See "Another Way", supra note 10, at 145.
Negotiation, according to ACDC, is a process where disputants "are the decision makers and settlement is one which both parties agree, without the aid of a third party".\(^\text{47}\) In the process, disputing parties "may create the rules by which they can organize their relationship with one another".\(^\text{48}\)

Thus negotiation, as a means of dispute resolution, has two basic features. First, it is a discussion participated in and conducted by the disputing parties themselves. This feature distinguishes negotiation from other methods of dispute resolution, all of which involve various forms of third party settlement. Secondly, the result of a successful negotiation must be accepted by all disputants concerned, although the result of a negotiation could be an agreement of settlement, an agreement on resorting to other means of dispute resolution, or an agreement on disagreed points, which will be the basis for further negotiation or, simply, be recognized as a failure. The voluntary acceptance of the result is not a unique feature of negotiation. Mediation, conciliation and independent expert appraisal also share this feature.

Although negotiation is generally regarded as the best way of resolving disputes,\(^\text{49}\) its application is subject to certain preconditions. Willingness to cooperate and reasonableness in compromise are two such preconditions. The willingness of the disputants to settle their differences through negotiation is crucial and is the very first step in the search for a satisfactory solution.\(^\text{50}\) However, in practice, the importance of willingness to negotiate has often been either ignored or rejected for strategic reasons.\(^\text{51}\) Reasonableness of disputants to compromise is

\(^\text{47}\) Information Brochure, ACDC: A New Option for Resolving Commercial Disputes, at 6.

\(^\text{48}\) Ibid.

\(^\text{49}\) It is the best because the parties to a dispute have total control over cost, time, issues to be discussed and place of negotiation. In theory, under the cooperation of disputing parties, it should yield a solution which would best suit the interests of the disputants.

\(^\text{50}\) Otherwise, if one party is unwilling to negotiate, he may regard the other party's proposal for negotiation merely as a sign of weakness and press his claims in an arrogant and uncooperative manner. This may even force a party with real weakness to be determined to "fight" merely for the sake of "face", or of hassles which the other party has to go through before "winning" his claims. Similarly, if any party refuses to negotiate, there is no way that negotiation will work.

\(^\text{51}\) Negotiation taking place after the commencement of legal proceedings is an example. In such case, the disputing parties started court proceedings, either because this has become a custom or standard practice in legal professionals, or because courts are perceived as a means providing advantages to the reinforcement of disputants' position in the following compulsory negotiation. Strategically or psychologically, proposing negotiation may be regarded as a confession of one's weakness; and in addition, negotiation without accompanying legal proceedings would
crucial as soon as the process of negotiation has commenced. Participants to a negotiation must be prepared to make concessions from their original claims if their intention is to end the dispute.52

(2) Mediation

Mediation, like all means of ADR except negotiation, is a process of third party dispute resolution. As defined by ACDC, it "is a process directed to enabling the parties to resolve their dispute by agreement. But his [the mediator's] endeavours will be to encourage an expeditious settlement forged by the parties themselves".53 The role of mediators in mediation as defined by ACDC is purely to respond to, or to simulate at most, the demands of the disputants. Thus, the mediators never make "recommendations as to what would be an appropriate settlement".54

Several features of mediation as defined by ACDC can be identified. First, in contrast to negotiation, mediation involves a neutral third party, accepted voluntarily by disputants. Secondly, in contrast to other means of third party settlement, the neutral party in the mediation process as defined by ACDC never gives his personal view of what is right or wrong in relation to the matters in dispute, or makes any suggestion regarding the substance of the settlement. Thirdly, in contrast to conciliation,55 mediators assist disputing parties by actually sitting in conference, and arranging an appropriate forum and agenda which he thinks suitable to encourage a settlement "forged" by the disputants.

Compared with other concepts of mediation offered by legal practitioners in Australia, the ACDC definition is perhaps the narrowest one in term of the mediator's role. For example, Davis argues that a mediator "has no power to impose an outcome on the disputing parties. Normally, it is beyond his proper function even to recommend or press for any particular outcome, and only exceptionally does a mediator do so".56 Here, mediators are allowed to recommend an appropriate

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52 In other words, it requires the parties to focus "on the real interests at stake and seeks to eliminate the urge to "win" a dispute, and to avoid position-taking, game-playing and personalizing a dispute". G.Pears, Beyond Dispute: ADR in Australia (Sydney, Corporate Impacts Publications Pty Ltd, 1989) 96.

53 Information Brochure, supra note 46, at 7.

54 Ibid.

55 ACDC's definition of conciliation will be examined later.

56 J.Davis, "Understanding the Available Techniques" paper presented at a conference "Cut Litigation Costs and Save Time Through ADR" held in Sydney on 22 July 1988, at 36.
settlement in "exceptional" cases. Sometimes, mediation appears to have even wider implications.57

Mediation offered by the ACDC is, necessarily, a voluntary process. The disputants have power to choose the mediator, as well as the time and place for mediation. The mediation session can be commenced either pursuant to mediation clauses incorporated in contracts,58 or to agreements between disputing parties after disputes have arisen. The degree of flexibility in choosing mediators and determining procedures is dependent upon the disputing parties. However, once these matters are agreed, the parties are bound by the terms of their agreement.

(3) Independent Expert Appraisal

As its name suggests, independent expert appraisal is a process where the disputants agree to seek an advisory opinion as to "how the dispute should be resolved" from a third party neutral, who is an expert with regard to the matter in disagreement.59 The basic features of this technique are, first, the opinion given by the expert is merely advisory; and secondly, the expert may, at the request by the disputants, perform some of the functions of a mediator or conciliator.60

This technique is suitable for disputes involving complicated technical matters or a continuous professional relationship. The idea in most cases is to demonstrate to both disputants, who are willing to settle their differences by following the established professional ethics or custom, what is acceptable practice for the parties in the given circumstances.

(4) Case Presentation

Another name for "case presentation" is "mini-trial", which is a process of third party settlement with "unneutral" persons as third parties.61 It is a procedure whereby senior executives from each of the disputing parties with authority to settle hear the case put by each party and after the submission of cases sit together for the

57 For example, Pickering simply states that mediation "is a process in which a third party neutral assists and facilitates two or more disputants to reach a mutually acceptable resolution to their problem". M.Pickering, "Current Developments in Commercial ADR" paper for the Centre for Commercial Law and Applied Legal Research, (1988) at 1. Along the same line, Pears defines mediation as a process in which a third party neutral plays an active part; but sometimes mediation can be conducted with minimal intervention from the mediators. Pears, supra note 51, at 101.

58 ACDC provides standard mediation clause for contracts.

59 Information Brochure, supra note 46, at 6.

60 Ibid.

61 The third parties here are not "neutral" because of their connection with the disputants.
purpose of reaching a settlement". Three features of the mini-trial can be identified. First, the third parties involved are not neutral by reason of their connection with the disputants. But they may have fresh ideas and objective attitudes, which have been lost by the original negotiators. Secondly, it is a forum which may provide a graceful excuse for the disputing parties to reconsider their positions so that they can retreat from the deadlock without worrying about losing face. In this forum, both disputing parties (more precisely, new negotiators from both disputing parties) have an opportunity to hear conflicting information and evidence from the original negotiators. Thirdly, it is a continued negotiation between the same disputing parties but with different negotiators. The differences between the process of "mini-trial" and ordinary continuation of negotiation is that in the capacity of "third parties" the new negotiators are not bound by the positions taken by the original negotiators. Apart from these three features, legal-minded lawyers may see the "mini-trial" as a "truncated form" of court proceedings, which brings "all the potential drama of the courtroom into the corporate boardroom".

(5) Conciliation

Conciliation is perhaps the most difficult ADR technique to define, because the distinction between conciliation and mediation, which is insisted on by some people, is artificial. In general, mediation and conciliation are treated as synonyms. However, the distinction between them has to be drawn when conciliation is designated as a separate ADR method.

The meaning of conciliation given by ACDC appears to distinguish conciliation from mediation in two respects. First, a conciliator transmits offers for settlement. Despite the fact that the meaning of "transmit" is not clear, the

62 Information Brochure, supra note 46, at 7.

63 Davis, supra note 55, at 54.

64 For example, in Goldberg, Green & Sander, eds, Dispute Resolution (Boston, Little, Brown and Company, 1985), conciliation is not mentioned, and mediation discussed in the book includes practices which can be regarded as conciliation by the ACDC definition.

65 The ACDC definition reads as follows:

an impartial third party acts to bring the principals together for the purpose of dispute settlement. In the course of this activity offers for settlement may be made and accepted. A conciliator may continue to "transmit" offers for settlement from one party to the other, even though the parties in dispute are declining offers of dispute processing.

Information Brochure, supra note 46, at 6.
function of transmitting offers is unique. Secondly, a conciliator provides or arranges the facilities for settlement. His function is to bring the disputing parties together. Thus, the conciliator may not necessarily sit with the disputants while they negotiate. In this sense, conciliators perform "a sub-set of the functions of the mediator".

In the context of mediation and conciliation as defined by ACDC, a vague, and perhaps unnecessary, line has been drawn between the two terms. There is no rational basis (or practical necessity) for restricting the role of conciliators, who are merely "providers" of facilities but not providers of any advisory or explanatory ideas or opinions. It is hard to image that disputants only need a special person to arrange a meeting room for their negotiation, as if the right to do so is reserved by that person; or that they are unable to arrange a negotiation process themselves even if they are willing to negotiate. Negotiating in the place and time arranged by conciliators seems, in the view of ACDC, to be what conciliation is. As noted by Davis, this function of conciliators can be performed by mediators.

(6) Hybrid Arbitration

Although provided by ACDC as one of its services, hybrid arbitration is not formally defined by the Centre. "Med-arb" (a term created by combining "mediation" and "arbitration") in a simply way means a process "where mediation if unsuccessful is followed by arbitration". As its name suggests, the process is a mixture of mediation (or conciliation) and arbitration. "During the first stage of the process", the third party neutral acts "as mediator between the parties". At the second stage,

66 However, one may ask, if the parties to a dispute sit together, why are offers needed to be transmitted by conciliators? In another words, if a conciliator is transmitting offers between the disputants, does this mean, having regard to the fact that disputants are supposed to be in a process of conciliation, that they are not having a conference?

67 Information Brochure, supra note 46, at 6.

68 Davis, supra note 55, at 44.

69 Information Brochure, supra note 46, at 6.

70 Davis argues that "a conciliator would not provide any advice at all to the parties, and would not even act as an 'explainer' of the legal, commercial or technical issues involved in the dispute". supra note 55, at 44.

71 Ibid.


73 Davis, supra note 55, at 45.
he acts as an arbitrator. Accordingly, he receives either written or oral submissions and makes an award on the basis of information obtained during the process of mediation.74 Presumably, when acting as an arbitrator, the third party involved is bound by the law of arbitration. Again, as clearly suggested by its name, a combination of mediation and arbitration provides an opportunity to the disputants to resolve their differences through a natural continuation from a less formal forum to a more formal forum. The uniform Commercial Arbitration Acts implicitly incorporate the "med-arb" process into the Acts,75 and the Arbitration (Civil Actions) Act 1983 (NSW) expressly adopts the "med-arb" process.76 This technique seems to suit the disputes which do not show a prospect of an easy compromise.

(7) Arbitration

Arbitration is certainly the oldest technique of ADR which has been applied to dispute resolution in Australia for many years.77 It is a familiar concept to Australian lawyers and the business community and has been applied extensively to settle commercial and civil disputes, e.g. disputes involving building and construction. Both the federal and State governments have passed legislation to deal with the problems of commercial arbitration.78

Briefly arbitration refers to a process where the disputants "consent to the intervention of a third party whose judgment they must agree to accept

74 Ibid.

75 Under the Acts, an arbitrator or umpire has power to order disputants to take appropriate steps to reach a settlement, except if the disputing parties express an opposite intention in writing. "Appropriate steps" are deemed to include mediation. For example, Commercial Arbitration Act (NSW), s.27.

76 Under this Act, arbitrators are required to mediate, or encourage the disputing parties to negotiate a settlement, before rendering an award. Arbitration (Civil Actions) Act 1983, s.9.

77 e.g. the Australian Conciliation and Arbitration Commission.

78 The federal Parliament has passed the Arbitration (Foreign Awards and Agreements) Act 1974, which makes the New York Convention effective within Australia; and the Foreign States Immunities Act 1985, which concerns the problems of sovereign immunity of a foreign State in an arbitration proceeding carried on within Australia. State governments, pursuant to the agreement made by the Standing Committee of the Commonwealth and State Attorney-General, have adopted the uniform Commercial Arbitration Act by local legislation. In particular, NSW adopted this Act by the Commercial Arbitration Act 1984; Victoria by the Commercial Arbitration Act 1984; North Territory by the Commercial Arbitration Act 1985; WA by the Commercial Arbitration Act 1985; SA by the Commercial Arbitration Act 1986; Tasmania by the Commercial Arbitration Act 1986; ACT by the Commercial Arbitration Ordinance 1986, and recently Queensland by the Commercial Arbitration Act 1990.
beforehand". Arbitration is an adjudicative and adversary process by nature, although not the same as court proceedings. But it is similar to court proceedings with its rules being uniformly regulated by Arbitration Acts in all State and Territories except Queensland. Formality in proceedings and the binding force of the award are features of arbitration.

Generally speaking, two forms of arbitration have been used for resolving civil or commercial disputes in Australia. One is arbitration by agreement (or consensual arbitration). The other is court-annexed arbitration. Consensual arbitration is based on an arbitration agreement made by the disputing parties either before or after a dispute has arisen. The important feature of this type of arbitration is that the power of the arbitrator to hear the dispute is given by the disputing parties. Otherwise, the arbitrator is not entitled to hear the case. By contrast, court-annexed arbitration, which has already been referred to, is conducted after a legal proceeding has been commenced in the courts. Under this process, the case is assigned to arbitrators by courts unless the disputants disagree in writing. Thus, the power of the arbitrators derives from the power of the courts. For this reason, court-annexed arbitration may not fall within the scope of ADR, although it is an alternative to formal court proceedings.

The uniform Commercial Arbitration Acts recognize consensual arbitration. Unlike the Commonwealth Conciliation and Arbitration Act 1904, the uniform Commercial Arbitration Acts give priority to the parties' autonomy, which is essential in a non-judicial process of dispute resolution. Accordingly, the parties may determine, by agreement in writing, on the number of arbitrators, the appointment of the umpire, the procedural requirements, and the form and effect of the award. Since the parties have autonomy in deciding any of these arrangements, the possibility of reaching an acceptable settlement may be increased.

The powers of the court to control arbitration are limited but still exist. They are of two kinds. First, during the arbitration, the court may appoint a new arbitrator or umpire if such an appointment is necessary. Secondly, after an arbitral award is made, the court may engage in judicial review. Although the jurisdiction to set aside or remit an award on the ground of error of law, and the power to give an opinion on an award stated in the form of a special case, have been removed by the Acts, the court is still empowered to set aside an arbitral award on

79 Information Brochure, supra note 46, at 7.

80 The court may exercise this power when a vacancy appears either because of the removal of the arbitrator or umpire by the court or because of the occurrence of unexpected technical difficulties in interpreting arbitration agreement. For example, see the Commercial Arbitration Act 1984 (Vic) ss. 10 & 11.
the grounds of misconduct and improper procurement. Consequently, the court may remit an award to an arbitrator for reconsideration on the grounds recognized by the Acts. In this sense, the court is still able to influence the process of arbitration.

International commercial arbitration has been given increasing attention in Australia. Two reasons may be given for this. The first is the need to strengthen the expanding trade relationships with Japan, China and other South-East Asia countries, which do not share the same legal tradition with Australia. In the course of these international trade contacts, foreign companies may become involved in commercial disputes in Australia, and Australian firms may as well be involved in similar disputes in foreign countries. But more often than not the disputing parties are reluctant to submit themselves to foreign legal systems with which they are not familiar. For this reason, arbitration is naturally considered as one of the substitutes for litigation in foreign courts. The second is the desire to establish Australia as a centre for international trade arbitration in the Asian Pacific Region. This consideration has led to the establishment of ACICA in Melbourne and ACDC in Sydney.

(8) Private Judge

Again, ACDC has not formally defined the process of private judging. Generally, the term is a synonym with rent-a-judge, a misleading term that refers to a process in which a retired judge (or any person with adequate legal qualification) is appointed by disputing parties as the third party neutral. It is a voluntary process. The parties may appoint a "judge" by agreement. The decision of the third party could either be binding or non-binding, depending upon the agreement between the disputants. The process may be regarded as a process which

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81 At the end of an arbitration proceeding, the parties concerned may appeal against the award on any question of law arising out of the award, provided that the appealing party has obtained consent from the other party or has been granted a leave of the Supreme Court. The court may set aside or remit an award on grounds recognized in the uniform Commercial Arbitration Acts. These grounds are: arbitrator's or umpire's misconduct, such as corruption, fraud, partiality, and bias; breach of agreed procedure; natural justice; bad face of an award; request by the arbitrator for correcting a mistake; and new evidence. For detailed discussion on these grounds, see J. Sharkey & J. Dorter, Commercial Arbitration (Sydney, Law Book Company, 1986) 266-90.

82 Rent-a-judge is certainly misleading. First, no active judge of a court of law can be rented under the law of any country; thus "rent-a-judge" in fact means "rent-a-retired-judge". Secondly, "rent-a-judge" is a process of ADR. There is no law in Australia against disputants appointing any person as third party ("judge" in this process) to resolve their dispute. Therefore, "rent-a-judge" could also be "rent-a-person-as-judge".
uses "adjudication outside the formal court structure." But this may not always be the case. When the disputing parties decide to have a non-binding decision, the decision so made is no more than an advisory opinion from an expert, who has considerable legal knowledge about the matters in dispute. This process has almost no distinctive feature except it is implied that the judge so "rented" must be a legal professional. It is also impractical to insist that the judge so appointed must follow formal court proceedings, because if the parties can choose the judge, they can also change the procedural rules. Nevertheless, the use of this process must be based on the competence of the third party with regard to the matter of law concerned.

6.1.3.2. Institutionalized ADR Services in Australia

Without limiting the freedom of individuals to use ADR, special institutions have been established in Australia to facilitate dispute resolution at both national and international levels. As far as commercial disputes are concerned, three institutions - the Institute of Arbitrators Australia (IAA), ACICA and ACDC - should be mentioned.

(1) The Institute of Arbitrators Australia

The Institute, established in 1977 in Melbourne, initially aimed at providing arbitration services for the building and construction industry. Although the majority of listed arbitrators are architects, building consultants and engineers, there are some legal professionals and people from other professions. Today, the Institute is seeking to extend its services to the wider business community and to play an active role in both national and international commercial dispute resolution. As at December 1990, the Institute has Chapters in New South Wales, Victoria, Western Australia, Queensland, South Australia, and the Northern Territory.

(2) Australian Centre for International Commercial Arbitration

ACICA is an independent body, despite its initial funding from the Victorian Government and its close association with IAA. Established in Melbourne in 1985, the Centre aimed at providing arbitration services to parties involving international commercial disputes. Since its operation in 1985, the Centre has extended its services to mediation and conciliation, with its main interest, however, still focusing on international arbitration.

83 David, supra note 71, at 12.

84 David, ibid; and Davis, supra note 55, at 50.

85 ACICA was established as a de facto branch of IAA, and operates in Australian States through local branches of IAA.
Generally, ACICA adopts the Rules of the London Court of International Arbitration in its arbitration proceedings. But it also allows disputants to choose other governing rules for arbitration, such as the UNICITRAL Rules or the uniform Commercial Arbitration Acts in Australia. Since 1985, the Centre has improved its international image and extended its activities in international commercial arbitration. The efforts of the Centre has undoubtedly helped Australia to move toward its goal of becoming a centre for international commercial arbitration, although there will be a long way to go before that target is reached.

(3) Australian Commercial Dispute Centre

ACDC was set up in Sydney in 1986 as a non-profit company with initial funding from the New South Wales Government. It aims at providing ADR methods to parties involving commercial disputes within and outside Australia, with its main activities concentrating on national commercial disputes. At present, the Centre has facilities in every Australian capital city. Judged by its activities in advocating and providing ADR services, the Centre's role in commercial dispute resolution seems to have been widely accepted.

The Centre provides a variety of ADR techniques for dispute resolution, and also conducts seminars on ADR designed for business community and legal professionals. Its activities in the national forum of dispute resolution, in contrast to IAA's role in building and construction arbitration, extend to various sectors of the economy. In addition, ACDC appears to have played a role in international commercial dispute resolution as well. Between May and August 1989, three international commercial disputes involving parties from the United States, London, and New Zealand were reportedly resolved through ACDC.

(4) Roles of the Institutions in Comparison

86 It was reported, for example, that in 1988 the President of ACICA, Mr. Fina was appointed a member of the Court of Appointment of the Hong Kong International Arbitration Centre and also elected a Vice-president of the International Federation of Commercial Arbitration Institutions. In the same year, the Centre was asked to nominate Australian arbitrators for commercial disputes involving parties from New Zealand, Hawaii, Hong Kong, Rumania, France, United Kingdom, Singapore, Thailand and America. (1988) 7:3 The Arbitrators 132-3.

87 It was reported that ADR methods were successfully used in cases involving mining, contracts, multi-party court case, construction and liquidation matters. (1989) 2:3 Resolution of Commercial Disputes 3, and (1989) 2:4 Resolution of Commercial Disputes 3.

88 Because of the requirements for confidentiality, the Centre cannot publish all cases resolved through its services. Summary of some cases was, however, reported in (1989) 2:3 Resolution of Commercial Disputes 1, and (1989) 2:4 Resolution of Commercial Disputes 2-3.
The three existing institutions emphasize different aspects of ADR. IAA concentrates on, but is not limited to, disputes involving buildings and construction in Australia. ACICA specialises in international arbitration. ACDC mainly engages in resolving commercial disputes through ADR. Although mediation has been included in ACICA's services, this service has not been exploited as much as arbitration provided by the same Centre. Similarly, the arbitration service provided by ACDC has not been used by the business community as much as mediation provided by it. This seems to suggest the existence of a natural boundary between the main role of the two Centres, although both are trying to extend into other's territory.

There is no need to limit the functions of any institution to a specified field. Convenience to disputants, after all, is the initial reasons to introduce ADR. Foreign investors may resort to any of these institutions for appropriate assistance, which is suggested by the special services provided by each Institution.

6.2. Settlement of Foreign Investment Disputes in China

6.2.1. An Overview

Settlement of foreign investment disputes in modern China has a shorter history than its counterpart in Australia, simply because the PRC had not had real foreign investment until 1978. The law and practice of resolving foreign investment disputes were developed mainly after 1979, although China has applied arbitration to the settlement of foreign trade disputes since 1956 and of maritime disputes since 1959. The laws and regulations so developed do not specify how to resolve disputes, but merely provide guidelines or guarantees of legal protection to foreign investors.

Chinese laws and practices on settling foreign investment disputes have two distinctive features. First, they emphasize the use of non-judicial methods of dispute resolution, some of which have been applied in settling various disputes in China since ancient times. The incorporation of these non-judicial means of dispute resolution into legislation has made the use of these techniques almost a compulsory procedure although the legislation does not spell out or even indicate how to carry

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89 For example, Art.14 of Joint Venture Law, CCH, China Laws for Foreign Business para 6-500, states that a dispute should first be negotiated by disputing parties, if negotiation is unsuccessful then the dispute can be submitted for arbitration.

90 For example, Art.26 of Cooperative Joint Venture Law, CCH, China Laws for Foreign Business para.6-100, states that if unsuccessful in resolving disputes through negotiation, mediation and arbitration, the disputing parties may take legal action in Chinese courts.
them out. This practice suggests a Chinese cultural preference as to the best means of dispute settlement.\textsuperscript{91} Secondly, specific provisions in legislation stressing a right to litigation and the availability of legal remedy seek to reassure foreign investors, whose confidence in the Chinese judicial system may be weak in view of China's lack of a formal legal system of any kind in the three decades preceding 1978. This practice also demonstrates China's efforts to establish a legal system and to improve its image as a country with adequate law and order.

The incorporation of non-judicial methods of dispute resolution into a formal dispute resolution system in China is not a unique practice in the world today.\textsuperscript{92} But it is certainly a confirmation (with modifications) of traditional Chinese methods of dispute settlement, which are based on a "social ethic oriented towards mediation and compromise, toward recognizing the extent to which another person's emotions and dignity are involved in his claim, rather than toward the abstract question of the justice of his claim".\textsuperscript{93} While many Chinese and foreign writers have discussed the use of mediation by the Chinese in both pre-PRC and present-day China,\textsuperscript{94} some have also noted that the continuity of mediation is only in the form of mediation (or in the terminology used in mediation) but not in its substance.\textsuperscript{95} This thesis will not look into the arguments whether there is continuity of the mediation tradition, but will look at mediation as a means of dispute settlement in commercial disputes involving foreign investment.

For the purposes of comparison, this section first examines judicial means of commercial dispute resolution in China. This will be followed by an examination of non-judicial means of dispute resolution. The term "ADR" will not be used in the Chinese context, because Chinese have never regarded non-judicial methods of

\textsuperscript{91} This cultural aspect of mediation was noted by J.Cohen, "Chinese Mediation on the Eve of Modernization" (1966) 54 Cali.L.R. 1201. He quoted an old Chinese proverb: "it is better to die of starvation than to become a thief; it is better to be vexed to death than to bring a lawsuit", to show such cultural preference.

\textsuperscript{92} e.g. Australia has family counselling services and court-annexed arbitration.

\textsuperscript{93} A.Tay, Law in China: Imperial, Republican, Communist (Sydney, Centre for Asian Studies of Sydney University, 1986) 4.

\textsuperscript{94} Many writings have recognized this fact. Among them, e.g. are Cohen, supra note 90, at 1201, and S.Lubman, "Mao and Mediation: Politics and Dispute Resolution in Communist China" (1967) 55 Cali.L.R. 1284.

\textsuperscript{95} For example, an article written in Chinese lists three opinions about the history of the present Chinese mediation system, but none of these three recognizes any continuation between mediation in Chinese history and mediation in the PRC. Y.Lin, "A Review on the Studies of the People's Mediation System of New China" (1988) 1 Studies in Law (in Chinese but with English Table of Contents) 91.
dispute resolution as an alternative to court proceedings. Rather they see the courts as alternatives to mediation or negotiation. Finally, the settlement of foreign investment disputes will be given special attention.

6.2.2. Judicial Dispute Resolution in China
6.2.2.1. Jurisdiction of the Courts Over Commercial Disputes

The jurisdiction of the courts is determined by the Organic Law of the People's Courts and Civil Procedure Law (Provisional). The criterion for determining the original jurisdiction of courts at each level is whether the significance (elements and impact) of a case has exceeded the geographical jurisdiction of the court concerned. Accordingly, the National Supreme Court can hear cases which have a significant impact on the national interest (or attract nationwide publicity). A Provincial Higher Court has power to deal with cases which have a significant influence only within the Province. Similarly, an intermediate court or an inferior court may deal with cases which have a significant influence within their territorial jurisdiction. The exception to those jurisdictional criteria is that any case involving foreign elements must be commenced at an intermediate court or above. Thus, an inferior court is in fact unable to handle any case involving foreign investment. The appellate jurisdiction of each court is determined by its status in the hierarchy of court system. In general, a court can always hear appeal from decisions of a lower court, which has original jurisdiction over the case concerned. On this basis, an appeal involving foreign investment can only be heard at a Provincial Higher Court or the National Supreme Court.

96 Statutes and Regulations of PRC (University of East Asia Press and Institute of Chinese Law (Publishers) Ltd) no.820308.

97 This deals with the division of jurisdiction between courts at different levels. However, jurisdiction of Chinese courts can also be dealt with in another approach, e.g. dividing into "general jurisdiction", "specific jurisdiction" and "exclusive jurisdiction". See Z.H.Zheng, "On the Adjudicatory Jurisdiction of Chinese Courts Over Foreign Investment Disputes" in Moser ed, Foreign Trade, Investment, and the Law in the People's Republic of China (2nd edn, HK, Oxford University Press, 1987) 532, 533-5.

98 The National Supreme Court may also handle any other matters determined by the Court, Organic Law of People's Court, Art.32, and Civil Procedure Law, Art.19.

99 Civil Procedure Law, Art.18.

100 Civil Procedure Law, Art.17.

101 Ibid.
The National Supreme Court has power to interpret laws and regulations. This power, unlike in Australia, is reserved to the National Supreme Court only. The interpretation so given by the National Supreme Court binds all courts in China. Although case law is not recognized in Chinese law, decisions of the National Supreme Court on some matters relating to foreign investment have received the effect of case law. 102

6.2.2.2. Courts and Foreign Commercial Disputes

Specific statistics of the caseloads involving foreign parties are not available. Summaries of some cases, however, have been given by various sources, mostly unofficial, in either English or Chinese. On the basis of this very limited information, a tentative analysis on some aspects of Chinese judicial practice in relation to commercial disputes involving foreign parties can be made. This analysis will concentrate on two main issues: first, whether foreign disputants can seek legal protection in Chinese courts, and secondly, inadequacies in some aspects of Chinese law in dealing with cases involving foreign parties.

Certainly, foreigners can sue and be sued in Chinese courts. 103 The rights of foreign investors to seek legal remedies are confirmed in the Joint Venture Regulations, 104 the Cooperative Joint Enterprise Law, 105 the Foreign Economic Contract Law, 106 and various laws and regulations concerning foreign exchange

102 For example, the National Supreme Court issued the Circular Regarding Several Issues Relating to the Application of Foreign Economic Contract Law in 1987. (1987) 4 Gazette of the National Supreme Court of PRC (Zhong Hua Ren Min Gong He Guo Zui Gao Fa Juan Gong Bao, in Chinese) The Circular extended the Foreign Economic Contract Law to various matters which are not defined in the Law. Many other circulars, notes and memorandum issued by the National Supreme Court can be found in Gazette of the National Supreme Court of PRC.

103 Article 44 of the Civil Procedure Law states that any person capable of exercising his legal rights in relation to litigation can act as a party in a civil lawsuit. This Article, in conjunction with Arts.185 & 186 of the Civil Procedure Law, gives foreign nationals equal rights as Chinese nationals in civil litigation. Thus, foreign investor or company can sue or be sued in Chinese courts according to law.

104 CCH, China Laws for Foreign Business, para.6-550, Art.111.


106 CCH, China Laws for Foreign Business para.5-550, Art.38. This Law governs contracts between Chinese enterprises (excluding individuals) and foreign companies or individuals, excluding contracts on international transport. See the Law, Art.2. For a brief introduction to the Foreign Economic Contract Law, see "Foreign Investment: Foreign Economic Contract Law" (1986) 27 Harv.Int'l L.J. 275; and J.S.F.Chan, Foreign Economic Contract Law: A Breakthrough" (April 1985) East Asian Exec.Rep. 9.
control, labour management and taxation. In the context of Chinese law, the provisions on settling disputes through courts, as pointed out earlier, point to China's efforts towards assuring foreign investors that legal protection does exist in China. Indeed, Chinese courts have increasingly become a helpful forum for resolving disputes involving foreign companies and individuals. In recent years, cases involving maritime disputes, contracts of sale, trademark or patent protection, cooperative production (counter-trade), joint ventures and other matters, though not voluminous in quantity, have been reported.

In most cases Chinese courts are believed to have delivered their judgments according to the relevant law and regulations. For example, a Hong Kong company sued a Chinese company for breach of an oral agreement reached in 1985 to buy copper rods and other building materials. The case was heard in the Shanghai Intermediate Court and a judgment in favour of the plaintiff was rendered in July 1989. In another case, a Hong Kong company sued the Electrical Station Construction Planning Office of a local government in a SEZ over a disputed payment arising from a contract. The case was dealt with in the Municipal Intermediate Court in accordance with law, in spite of the fact that the other party


110 X Teahouse, Hong Kong v Workers' Cultural Palace, Y County (1988) 2:9 CLP 31; and Case 11(4), Zhang, supra note 105, at 379.


was a government body. However, the performance of the Maritime Courts, though applauded in most cases, has been criticised in others. This limited information at least suggests that most Chinese courts are capable of performing their duties in accordance with law, and are willing to consider international practices in case of "gaps" in the law. But in some cases, such as the "Gema Phosphate" case, the

113 The contract transferred interests in a joint venture from the Hong Kong company to the Electrical Station Construction Planning Office (Office). The Hong Kong company disagreed with the Office on the exchange rate adopted by the Office and brought the case to the Court. The contract was regarded as illegal, because the joint venture agreement prohibits such transaction except by express agreement of both contracting parties, which was absent in the transaction between the H.K. company and the Office. Because the contract was void, neither the H.K. company's claim, nor the Office's right to the interests in the joint venture under the contract was upheld by the Court. Consequently, the H.K. company demanded termination of the contract and the Office agreed to mediate. The dispute was then settled through mediation on the basis of the Court's view of the contract. Hong Kong XXX Ltd v SEZ ESC (1988) 2:1 CLP 22.


115 For example, in M/MB Ellpe Case, Gebuschmarker Limited Partnership Company, a foreign company, sued Shanghai Municipal Foreign Trade Corporation for recovery of a debt attached to the vessel, M/MB Ellpe, bought by the Chinese Corporation from a Banama company. The Chinese Corporation was notified of the debt attached to the vessel when it was considering to buy the vessel, but it did not take due caution in proceeding with the deal. The Shanghai Municipal Intermediate Court found the Chinese Corporation liable for the debt. On this basis the parties agreed to proceed with mediation under Art.45 of the Civil Procedure Law. The case was eventually settled through mediation. Gebuschmarker Limited Partnership Company v Shanghai Municipal Foreign Trade Corporation (M/MB Ellpe Case) (1987) 1:3 CLP 15. In a maritime fraud case, a Japanese company, which issued bills of landing when the cargos had not been loaded, was ordered to pay damages to a Chinese company. Ningde District Economic and Technological Cooperation Corporation v Ri-ou Transportation Corporation (1989) 3:1 CLP 33. Both are handled fairly according to law or international customs.

116 A typical example is "Gema Phosphate" case (1989) 3:7 CLP 32. In this case, the master of Gema Phosphate refused to issue a clean bill of landing with regard to the cargo of manioc slices sent by a Chinese corporation. The parties could not agree on the state of the cargo, and the ship was then refused a clearance for sailing by the harbour authority. The shipowners took the matter to Guangzhou Maritime Court, which, however, refused to support the right of the ship's master to issue a cliaused bill of landing. The Court ordered the cargo to be discharged for inspection and subsequently arrested the ship because the owners refused to pay a guarantee required by the Court. A judgment was handed down after 85 days, and implied that the 30% mold on the cargo which was the cause of the dispute was the result of improper care by the shipowners. The compensation actually received by the shipowners for loss of income was US $24,164.42, compared with US $676,000 claimed by the shipowners. This judgment was described as "scandalous" by foreign observers. (1989) 3:7 CLP 34.
court seems to divert from law, if the report is correct. However, the case was not appealed to the responsible Provincial Higher Court, and thus we lost an opportunity to test the judgment of the Guangzhou Maritime Court and the attitude of the Provincial Higher Court to such case.

Inadequacies of Chinese law in dealing with foreign-related disputes can be seen in two respects. First, the lack of adequate rules of law results in inconsistencies in court practice. Sometimes, the courts gave judgment according

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For example, in *X Teahouse, Hong Kong v Workers' Cultural Palace, Y County* (1988) 2:9 CLP 31, Y County Court dealt with a contracts dispute between a Hong Kong company and a Chinese cultural organization. The contract was signed on 10 March 1982, and was approved on 22 March 1982. But on 7 June 1982, the central Government issued a policy prohibiting organizations, government authorities, schools and government institutions from engaging in commercial activities. Consequently, the contract signed between the H.K. company and the Chinese organization was retroactively terminated by the County Government. The H.K. company challenged the County Government's decision in the County Court. The Court upheld the policy and determined the contract was void. The contract was thus terminated without compensation to the H.K. company. This case was compared with Luohu Customs House case, by some foreign observers in (1988) 2:9 CLP 32. It was noted that in the latter case, the foreign party was compensated after the contract was terminated by the central Government on the ground of policy consideration. The difference between the two cases, which was not noted in the comparison, is that the former was retroactively terminated under a document which may generally apply to all contracts falling under the documents, and the latter was terminated under a special instruction from the central Government. In addition, it is not clear from the report what the Policy says about compensation to contracts signed before the introduction of the policy. The confusion in courts' practice in dealing with contract cases is, however, rooted in the Foreign Economic Contract Law which does not expressly deal with the effect of changes in policy or State plan on executed contracts. See P.M. Torbert, "Contract Law: the People's Republic of China" in Moser ed, *Foreign Trade, Investment, and the Law in the People's Republic of China* (2nd edn, HK, Oxford University Press, 1987) 321, 333.
to common international practice, which may be inconsistent with Chinese legal principles.\textsuperscript{118} Secondly, the courts sometimes did not strictly implement the law.\textsuperscript{119}

6.2.2.3. Court-conducted Mediation

A basic feature of court proceedings in China is that the courts have legal responsibilities to assist disputants to resolve their disputes through negotiation or mediation.\textsuperscript{120} The courts have followed such a practice in many cases by either mediating disputes before trial\textsuperscript{121} or allowing the disputants to proceed with mediation during trial.\textsuperscript{122} This practice is based on a belief that a settlement reached by the disputing parties is the best of all resolutions. After an agreement for settlement has been reached by the disputants, the courts may either certify in the court records as the evidence of the agreement, or issue a certified mediation

\textsuperscript{118} For example, in \textit{China Ocean Shipping Trally Co. v First Ocean Carriage Services Co. Ltd.} and \textit{Huang Fugen v First Ocean Carriage Services Co. Ltd.} \textit{3:10 CLP} (1989) 26, the Court ordered the defendant to pay compensation to the deceased’s father and mother for "emotional distress". This reward has no basis in Chinese law which has not formally acknowledged rights to claim general damages and emotional damages. The question to be noted is that the case had foreign elements. It is not clear how far Chinese courts are prepared to go beyond Chinese legal tradition in adjusting the differences between Chinese law and international practice in dealing with foreign-related cases.

\textsuperscript{119} For example, in \textit{X Teahouse, Hong Kong v Workers’ Cultural Palace, Y County} \textit{(1988) 2:9 CLP} 31, if the English translation of the name of the Court was correct, the Court appears to have exceeded its jurisdiction under the Civil Procedure Law which allows only an intermediate court or above to deal with foreign-related cases. A County county can never be an intermediate court under the present judicial system in China. Thus, the decision itself should be void under the Civil Procedure Law.

\textsuperscript{120} Under the Civil Procedure Law, the courts are required to mediate disputes before adjudicating; and disputants may also request mediation during any stage of court proceedings. Arts.97-102.

\textsuperscript{121} For example, in \textit{Hong Kong XXX Ltd v SEZ ESC} (1988) 2:1 CLP 22, the Court asked the disputing parties to mediate after the primary investigation. In \textit{China Ocean Shipping Trally Co v First Ocean Carriage Services Co Ltd and Huang Fugen v First Ocean Carriage Services Co Ltd} \textit{(1989) 3:10 CLP} 26, the Court conducted mediation before delivering its judgment.

\textsuperscript{122} For example, in \textit{Hong Kong XXX Ltd v SEZ ESC} (1988) 2:1 CLP 22, the dispute was settled through mediation.
document made pursuant to the agreement between the parties concerned. In both cases, the mediation agreement is enforceable at law.

Chinese courts have conducted mediation in dealing with domestic and international commercial disputes. The court's power to mediate is the same in both cases. Thus, in a case involving two Chinese disputants, a Chinese court investigated the facts and decided to mediate. Accordingly, the dispute was settled through mediation on the basis of the responsibilities of each party determined by the court. In another case between a foreign company and a Chinese corporation, the Shanghai Municipal Intermediate Court heard the claim made by the foreign company on a debt attached to a vessel purchased by the Chinese corporation. During the court hearings, an agreement satisfying 50% of the foreign party's claim was reached by the disputing parties. The foreign party accepted the settlement with reluctance. But the Court set aside the agreement on the grounds that the defendant's liability was not clearly defined and the plaintiff's consent was not completely voluntary. Further hearings were subsequently conducted. Having regard to the court findings, the defendant requested that mediation be conducted. The parties concerned then reached another agreement for settlement, which satisfied almost the full amount claimed by the foreign company. These examples suggest that mediation in courts is an effective and practical means of dispute resolution in China. This process allows disputants considerable flexibility in seeking a mutually acceptable resolution. Meanwhile it provides convenience of a logical progress from the means of mediation to the means of judicial resolution when the disputants cannot reach an agreement through mediation. However, the power of the courts to control the results so reached could be a negative factor, militating against the autonomy of the disputing parties.

6.2.3. Non-judicial Dispute Resolution in China

123 Civil Procedure Law, Art.101.

124 Civil Procedure Law, Art.166. See Yang Yuanzhang, Xie Guanshen & Xie Kailin's Case (1987) 1:9 CLP 35. In this case, a mediation agreement was reached in the Weidong District Court, Henan Province. When one party refused to perform the agreement, the Court acted under Arts.166, 173 and 175 of the Civil Procedure Law and sold the party's property impounded for the purposes of executing the agreement.

125 Civil Procedure Law, Arts.185 & 186.

126 Re: the Assembly of Five Model C620-1 Lathes (1987) 1:2 CLP 27.

6.2.3.1. Methods of Non-judicial Dispute Resolution

China has not identified as many techniques of non-judicial dispute resolution as Australia. Broadly, it adopts three categories of non-judicial dispute resolution techniques: negotiation, mediation and arbitration. The terms used for techniques in China have a wider application than they do in Australia. In particular, negotiation may cover "case presentation"; mediation may include "conciliation" and "independent expert appraisal"; and arbitration certainly contain "hybrid arbitration". But the notion of "private judging" is unknown in China. The discussion of non-judicial dispute resolution in China will follow these three categories. In addition, mediation will be discussed in a broader context (not limited to commercial disputes), because of the close connection between mediation for commercial disputes and that for ordinary civil disputes.

(1) Negotiation

The term "negotiation" is synonymous with "consultation" in China when referring to dispute resolution.129 Their Chinese equivalents are tanpan and xieshang.130 The meanings of tanpan and xieshang are not clear-cut in Chinese. Usually tanpan refers to a more formal process of discussion, such as negotiation between governments. But xieshang, as meaning cooperation and discussion, seems more appropriate when referring to negotiation or consultation between business partners, such as a consultation between a Chinese and a foreign party to a joint venture. This is why the word xieshang has been adopted in many foreign economic laws, Sino-foreign treaties, and Sino-foreign contracts. The English word "consultation" has been used in many translations of Chinese laws and documents. But for convenience of comparison with Australian practice, the term "negotiation" will usually be used in this subsection.

Negotiation is officially a means of dispute resolution in China.131 It is official, because it is required in law that disputing parties should negotiate their

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128 In the sense that negotiation can be continued to a higher procedures level, but not following the exact procedures as defined in Australia.

129 e.g. these terms are used interchangeably in E.Lee, Commercial Disputes Settlement in China (London, Lloyd's of London Press Ltd, 1985) 9-11.

130 The English word "negotiation" can be translated as either tanpan or xieshang, but the word "consultation" is normally translated as xieshang.

131 For example, Article 48 of the Economic Contract Law 1983 states that "if disputes arise over economic contracts, the parties concerned should try to solve them in time through consultation." CCH, China Laws for Foreign Business para.5-500. Article 26 of the Cooperative Joint Enterprise Law states that "if disputes arise between Chinese and foreign partners over the implementation of cooperative enterprise contracts, the matters should be resolved through consultation or
differences before proceeding with other means of dispute resolution. Two features of negotiation can thus be identified. First, it is an officially proposed means of dispute settlement. Secondly, although it is desirably as the first form of dispute settlement to be adopted, it is not compulsory under law.132

Negotiation has been commonly used to settle commercial and family disputes. For example, it is adopted in the Joint Venture Law as a process of dispute resolution.133 In relation to family disputes, the parties to a marriage dissolution are encouraged to negotiate an arrangement for maintenance by themselves. The court will give a judgment in this regard only if negotiation is unsuccessful.134

(2) Mediation

(i) Chinese Term for Mediation

The terms "mediation" and "conciliation" refer to the same process of dispute resolution in China. Their equivalent term in Chinese is tiaojie, which describes a process of dispute resolution in which an agreement for settlement between disputing parties is reached through a third party's assistance. In this section, the English words "mediation" and "conciliation" are used interchangeably, to refer to the process described by the Chinese word Tiaojie.

(ii) History of Mediation in China

It is said that in the "Spring and Autumn Period",135 this method was used by Confucius in resolving family disputes, when he held the position of "Sikou" in Nu State.136 Since then this process has been used continuously throughout Chinese mediation..." CCH, China Laws for Foreign Business para.6-100. Similar provision is also found in Art.14 of the Joint Venture Law.

132 Chinese courts cannot reject a case merely on the ground that no negotiation has been held.

133 Article 14 of this law specifies negotiation or consultation as a necessary step before resorting to conciliation and arbitration. Similar provisions are adopted by Article 14 of the Regulation on Labour Management (CCH, China Laws for Foreign Business para.6-520) and Article 109 of the Joint Venture Regulations.

134 The same principle also applies to the division of family property. Marriage Law of PRC, Arts.30, 33 & 31. Under the Marriage Law, the whole process of marriage dissolution is a combination of court proceeding and negotiation between the parties concerned. This process of negotiation allows disputing parties considerable autonomy.

135 This is a period in Chinese history between 770 B.C.-476 B.C.

136 (1) "Sikou" was a governmental post at that particular time in charge of judicial work; (2) Nu State existed in the "Spring and Autumn Period".
history, although it was once known by different names. Generally, three forms of mediation were adopted in ancient China. These were xiang zhi mediation (administrative mediation), zongzu mediation (clan mediation), and mingjian mediation.


138 For examples, it was called xiehe (harmony and reconciliation), jujian (intermediation), or tiaoting (intervention). See F.Shi, "The Origin of the System of People’s Mediation" (1987) 3 Law of China (in Chinese, with English Table of Contents) 44, 44-5. It should be pointed out that these Chinese words may be translated into different English terms.

139 “Xiang zhi” are two words. "Xiang" is the name of a basic administrative level in the traditional Chinese State system and "zhi" means administration or management. The physical size of a xiang varied in different periods of history. For example, in the Han Dynasty (206 BC-220), under xiang there were ting, li and kui. In the Tang Dynasty (618-907), under xiang there was li. In the Ming Dynasty (1368-1644), xiang was abolished, and li which consisted of 110 families replaced xiang as a basic administrative level. In the Qing Dynasty (1644-1911), xiang was not adopted. Today, it is usually established in rural areas, and is smaller than a district or county but larger than a village. Xiang zhi generally referred to a process of dispute resolution carried out by local officials at different basic administrative levels. The local official was also regarded as a village headman, who was in charge of local administrative affairs such as social order, tax collection, settlement of neighbourhood disputes, minor criminal offences and small civil claims. According to its functions, xiang zhi can be translated as administrative mediation. An important characteristic of this model of mediation was that the person in charge was an administrator exercising a certain executive power. Unlike the magistrate of a county, the local official of a xiang was not regarded as part of the judicial system in ancient China. Shi, id., at 45 and Cohen, supra note 90, at 1219.

140 "Zongzu" means clan. Zongzu mediation was a clan mediation in nature. Clan, which was based on an autarkical, small-scaled, and peasant economy, played an important role in traditional Chinese society. For the existence of close economic connections, members of a clan usually resided in the same residence and maintained their identity. Conflicts between members of a clan were usually dealt with by a clan elder or respectable senior through various methods such as mediation. This custom was always explicitly or implicitly recognized by various Chinese governments in history. Given the established order in a clan and power of a clan elder, some processes of mediation were in fact compulsory, or often accompanied by financial and physical punishments. Of course, disputes were also voluntarily submitted to clan elders by members of the clan. Shi, supra note 134, at 46, and Cohen, supra note 90, at 1217-9.
mediation (neighbourhood mediation). All these three forms of mediation were recognized under the law of the Nationalist Government which ruled China until 1949.

Three features of mediation in traditional China can be identified. First, Chinese governments in history constantly encouraged, explicitly or implicitly, the use of mediation as a substitute for litigation. Secondly, some processes of mediation were compulsory. Lastly, a third party might render service on his own initiative, which was often regarded as praiseworthy because most mediators were volunteers who acted for the "good of the disputants". This last feature has been inherited by the present models of mediation in China.

(iii) Forms of Mediation in the PRC

141 "Mingjian" means "among the people" or folk. It may be translated as "people's mediation". Since "people's mediation" has become a special term which describes a process of mediation in the present-day China, to avoid confusion, this term is translated as neighbourhood mediation in this context. Unlike administrative mediation and clan mediation, neighbourhood mediation was conducted by a neutral third party, who might be a local person or from other communities. Either the parties to a dispute may turn to a third party for assistance, or a third party may offer his assistance to the disputants on his own initiative. An important feature of this mediation process is that the third party was expected to be neutral and impartial. He had neither administrative powers nor clan authority. In traditional Chinese society, this type of mediation was extensively used by people in the areas where the clan as a social unit was undermined or had disintegrated. Shi, supra note 134, at 44-5; and Hang, supra note 133, at 38-9.

142 See the Law for Implementation of District Autonomy, and the Law for Implementation of Xiang Autonomy promulgated in 1930. Mediation committees were set up at both xiang and district levels, whilst clan mediation and neighbourhood mediation continued to function. Shi, supra note 134, at 45.

143 The status of mediators, such as local government officials or clan elders, might have resulted in direct pressure on the disputing parties. In addition, customs and moral norms socially accepted by the then Chinese society, in particular principles of behaviour and norms of morality established in a clan, might have imposed implicit pressure on disputants. These elements affected decisions for dispute settlement reached during mediation.
Although Chinese scholars engaged in the study of mediation have different opinions about the history of mediation in PRC, they would agree that today mediation exists in China in four specific forms. People's mediation mainly refers to mediation services provided by the people's mediation committees (PMCs). Administrative mediation, which was a common form of dispute resolution before the 1980s, has become less popular. The ongoing Chinese economic reform which has brought changes to the social structure of Chinese society is the main reason for the reduced role of administrative mediation today. Court-annexed mediation, which has been reviewed in the previous section, will not be examined here. Institutional mediation, which was created in the 1950s following the establishment of the Foreign Trade Arbitration Commission (FTAC) in 1954 and the Maritime Arbitration Commission (MAC) in 1958, has become a necessary step before commencing an arbitration proceeding. It was estimated that more than half of the cases submitted to FTAC (now FETAC) and MAC were resolved through mediation.

The establishment of the Arbitration Commission within the State Administration of Industry and Commerce (SAIC) has given rise to another model of

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144 There are three opinions. The predominant opinion considers that people's mediation, which sometimes refers to mediation by people's mediation committee (PMCs) and sometimes refers to all mediation processes in China, started in 1927 when some local revolutionary governments were established. The argument for this is that only after 1927 were some organizations of people's mediation set up by the governments. The second opinion argues that people's mediation was created in 1922 when the Peasant Association of Chi-Shan-Yue was established, because within that organization, a department of arbitration was set up. The third school disagrees with both. It insists that people's mediation was formed after the establishment of the PRC, because the Provisional General Rules Concerning the Organization of the People's Mediation Committees, which were promulgated in 1954, represented the formation of "people's mediation". Y. Lin, "A Review on the Studies of the People's Mediation System of New China" (1988) 1 Studies in Law (in Chinese, with English Table of Contents) 92.

145 People's Mediation Committees is an autonomous mass organization established under Provisional General Rules to facilitate dispute resolution in China. It is usually set up as a sub-organ of a residents' committee in the urban areas or a villagers' committee in rural areas. Its members are elected by people in the neighbourhood or the village. In 1986 there were about 950,000 PMCs and 6,000,000 mediators of PMCs in China. In the same year, more than 7,370,000 disputes, it was claimed, were resolved by PMCs. See J. Ren, the Vice-president of the Chinese National Supreme Court, paper presented at the Fourth International Conference of Judge of Appeal Court in Kuala Lumpur, "Mediation, Arbitration and Litigation in PRC" (1987) 2 Gazette of the Supreme Court of the PRC (in Chinese) 23.

146 Ibid.

147 Ibid. FTAC was renamed Foreign Economic and Trade Arbitration Commission (FETAC) in 1980.
mediation in China.\textsuperscript{148} The arbitration commission may provide a separate mediation service or a mediation session before proceeding to arbitration.\textsuperscript{149} Since AIC is a governmental body in charge of administrative aspects of industry and commerce, and the arbitration commission of AIC is a special body providing arbitration and mediation, the mediation service provided by the Arbitration Commission can be treated either as administrative mediation or institutional mediation.

(iv) Mediation by the People's Mediation Committees

The PMCs, established in 1954 according to the Provisional General Rules of the PMCs, are principal bodies of people's mediation.\textsuperscript{150} They are regarded as autonomous bodies organized and administered by masses themselves, who elect members of the PMC serving the local community.\textsuperscript{151} The autonomous status of a PMC is confirmed in the Civil Procedure Law and the Provisional General Rules. The basic function of PMCs is to avoid potential disputes and to resolve existing disputes by encouraging the parties to reach an agreement for settlement.

People's mediation is a process in which mediators from a PMC assist disputing parties to reach an agreement for settlement "by investigating truth, identifying right or wrong, and suggesting a solution". The consent of the parties concerned is the basis of PMCs' power over a given dispute. Generally, the disputing parties ask for the assistance of mediators, but if necessary, a PMC may also initiate the process on its own initiative. In either case, the disputants' consent is required by law.

(v) Administrative Mediation

Administrative mediation is another form of mediation available in China. It refers to a process of mediation in which a governmental body acts as a third party for the purposes of assisting the disputing parties to reach an agreement for

\textsuperscript{148} For a general discussion of the role of AIC in commercial dispute resolution, see J.A.Spanogle & T.M.Baransi, "Chinese Commercial Dispute Resolution Methods: the State Commercial and Industrial Administrative Bureau" (1987) 35 AmeJ.Comp.L. 761. Note: "the State Commercial and Industrial Administrative Bureau" and "the Administration of Industry and Commerce" are different English translations for the Chinese Government Authority- \textit{Guo Jia Gong Shus Guan Li Ju}.

\textsuperscript{149} Arbitration Rules of PRC Concerning Economic Contracts, Art.25, CCH, China Laws for Foreign Business para.10-620.

\textsuperscript{150} The Chinese Constitution, Art.111.

\textsuperscript{151} Some of them are retired senior citizens and the others usually do the work during their spare time. Each Committee consists of three to eleven members.
settlement. This process is also understood as governmental mediation.\textsuperscript{152} Administrative mediation can be carried out by different governmental bodies, including a local government in rural areas, administrators of a State-owned working unit and enterprise, and some special governmental authorities for mediation and arbitration. Like people’s mediation, administrative mediation is a voluntary process, although the mediators’ superior status may add pressure on the parties.\textsuperscript{153}

Administrative mediation is also carried out by special authorities such as AIC,\textsuperscript{154} and the local Labour Bureau of the Special Economic Zones.\textsuperscript{155} The process of mediation conducted by the special administrative authorities is similar to that carried out by other governmental bodies. A common characteristic of administrative mediation is that a superior-subordinate relationship exists between the mediators and the disputing parties.

Administrative mediation which is used in foreign investment disputes is slightly different from that used in domestic disputes. The principal law regulating this type of mediation is the Foreign Economic Contract Law.\textsuperscript{156} The administrative body involved is the assigned authority for foreign trade, which may be CCPIT or any relevant government department, because most Chinese-foreign trade is carried out under governmental control. Due to the position of the mediators, this type of mediation seems to be more advisory than conciliatory to the Chinese parties. The influence of the administration on the Chinese parties involved in the dispute is subtle and sensitive. Accordingly, if a foreign party to a dispute is confident of its position, this type of mediation may be a helpful way to reach its goal.


\textsuperscript{153} For example, if a manager or director of a working unit mediate a dispute which involves personnel of that working unit, the mediator’s status may be taken into account when the disputants consider a settlement. However, a mediator can neither force the disputants to consider his recommendation for settlement, nor has he power to make an award regarding the matters in dispute.

\textsuperscript{154} It is especially set up for resolving contract disputes, and can deal with disputes between parties from different working units or enterprises. The AIC is established at various administrative levels.

\textsuperscript{155} It can mediate industrial disputes arising from joint or foreign ventures. These industrial disputes have attracted attention in the SEZs. Under law, when an industrial dispute arises, the parties concerned are normally required to negotiate the dispute. If negotiation fails, the parties may resort to the Labour Bureau of local government for mediation. Provisional Measures Regarding Wages in the Enterprises in the SEZs of Guangdong Province, Art.18, \textit{Statutes and Regulations of PRC} (University of East Asia Press and Institute of Chinese Law (Publishers) Ltd) no.811224.

\textsuperscript{156} Art.48.
(vi) Institutional Mediation

Last but not least is institutional mediation. In this process, an arbitral body or institution acts as mediator to assist the disputants to reach agreement. For example, the Arbitration Committee on Economic Contract, established within various levels of AIC, is a governmental body which provides mediation services. Between 1984 and 1986, 58,052 cases, which were 88% of the cases submitted to the Arbitration Committees throughout the country, were mediated.

Institutional mediation can also be conducted by arbitral institutions. In the early stages of the development of Chinese foreign investment laws, only the Chinese arbitral institution was specified in law. But in recent legislation, access to mediation is provided without specifying that the institution must be Chinese. Thus the parties to a foreign commercial dispute may resort to any institution for mediation, although the Chinese party will probably prefer FETAC in most cases. Institutional mediation can also be used in conjunction with an arbitration proceeding. In this situation it is the primary step of an arbitration proceedings conducted by the same institution. About half of the cases submitted to FETAC and MAC each year are resolved in this process of mediation.

(3) Arbitration

Arbitration is a popular method of settling commercial disputes in China. While the Arbitration Rules Concerning the Economic Contracts of PRC, promulgated in 1983, is the basic law governing commercial arbitration, many other regulations, such as the Economic Contract Law and the Rules of PRC Concerning

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158 This Committee is required by law to conduct a process of conciliation before commencing an arbitration proceeding. Article 25 of the Arbitration Rules of PRC for Economic Contract states that "when handling cases, an arbitral body should conduct mediation first."

159 Ren, supra note 141, at 23.

160 e.g. Joint Venture Law, Art.14.

161 e.g. Foreign Economic Contract Law, Art.37.

162 Ren, supra note 141, at 23.

163 It must be pointed out that in later 1970s the Chinese showed considerable reluctance to utilize international arbitration, in particular, foreign arbitral institutes. They would rather resolve the differences between them and foreign parties through mediation than leave the matters in the hands of a foreign arbitral institute. See G.B.Hinman, "China, Modernization, and Sino-United States Trade: Will China Submit to Arbitration?" (1980) 10 Cali.W.Int'l LJ. 53, 72-5.
Property Insurance, contain provisions on arbitration. But as far as foreign arbitration is concerned, the basic legal framework consists of the Provisional Rules of Procedure of the Foreign Economic Trade Arbitration Commission of CCPIT, the Provisional Rules of Procedure of the Maritime Arbitration Commission of CCPIT, the Foreign Economic Contract Law, the Law of Civil Procedure, and other relevant provisions found in many laws and regulations on foreign investment. In addition, in 1986 China acceded to the 1958 New York Convention On Recognition and Enforcement of Foreign Arbitration Awards,164 which thereby became part of the legal framework for arbitration in China.165 Under this framework, a dispute can be submitted to either a Chinese or a foreign arbitral institute.166

Generally speaking, there are two types of arbitration in China: administrative arbitration and institutional arbitration. Administrative arbitration is used for settling disputes on economic contracts.167 Since the arbitral bodies are the Arbitration Committee on Economic Contract, established within the national AIC and its subordinate Administrations168 or other assigned authorities for contract

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164 (1987) Gazette of the State Council of the PRC (Zhong Hua Ren Min Gong He Guo Zui Gao Fa Juan Gong Bao, in Chinese) 234. Thereby, China has obligations to enforce foreign arbitral awards made in the member countries to the Convention. McDermott observed that "the Chinese seem willing to enforce foreign awards only in the very rare cases where the parties have both agreed to arbitrate outside the country and have actually participated in foreign arbitration". He also noted that there "have been numerous statements by various Chinese public officials from a variety of organizations assuring the international trade community that China will abide by any arbitral award. There have also been indications that Chinese courts will enforce arbitral awards, if necessary". J.McDermott, "A Survey of Methods for the Enforcement of Foreign Judgments and Foreign Arbitral Awards in the Asia-Pacific Region" (1989) 12:1 Loy.L.A.Int'l & Comp.LJ. 114, 137.

165 In the Chinese legal system, international conventions or treaties approved by the NPC or its Standing Committee are regarded as part of the domestic law. In the case of conflict between a domestic law and an international treaty, the international treaty prevails over the national law, provided that no reservation in relation to the conflicted provision has been made by China. Article 142 of the Civil Code (General Principles) confirms this practice.

166 e.g. Art.14 of the Joint Venture Law states that a dispute can be submitted to a Chinese arbitral institute or any arbitral institute agreed upon by the parties to the dispute. For discussion of the change in China's position regarding the use of foreign arbitral institutes, see M.C.Doty, "An Evaluation of the People's Republic of China's Participation in International Commercial Arbitration: Pragmatic Prospectus" (1982) 12 Cali.W.Int'l L.J. 128, 136-9.

167 For discussion of domestic arbitration in China, see Lee, supra note 128, at 30-8.

administration, proceedings instituted by these bodies may be regarded as administrative arbitration.

Administrative arbitration is quasi-judicial in nature. An agreement on arbitration between the parties is not necessary for commencing this process of arbitration before the Arbitration Committee. As in court proceedings, a party may submit an application for arbitration to the Committee, and the Committee will then notify the other party of the action if the Committee decides to accept the case. But if the other party has submitted the case to a court of law, the Committee does not have power to proceed with the case. During the arbitration proceedings, the Committee may conduct an investigation into the case and may also grant injunctions or other necessary measures. The jurisdiction of the Committee at different levels depends on the amount in dispute. If a party is not satisfied with the arbitral award, it may appeal to a court of law within a specified time limit. Otherwise, the award is regarded as equivalent to a court judgment. Although the Committee is required to conduct mediation during the proceeding, it cannot force the parties to reach an agreement. These are the principal features of administrative arbitration in China. Between 1984-86, 7,972 cases were arbitrated by the Arbitration Committees.

Institutional arbitration is the basic form used in international commercial arbitration. Through its new foreign economic laws, China has indicated a

169 Id. Arts.19 & 20. See also Lee, supra note 128, at 22-3.
170 The rule reflects general relationship between arbitration and courts when economic contract disputes are concerned. Economic Contrast Arbitration Regulation, Art.12. Statutes and Regulations of PRC (University of East Asia Press and Institute of Chinese Law (Publishers Ltd) no.830822. In the absence of a written agreement, the jurisdiction of courts prevails over the jurisdiction of arbitration authorities even if one disputant has applied to an arbitration authority for arbitration before the other party commences a court proceeding. See Official Replay concerning Whether the Courts Should Accept a Case Where One Party to a Economic Dispute Applied to an Arbitration Tribunal for Arbitration, Where the Arbitration Tribunal Has Already Registered the Case and Where the Other Party Commences Proceedings in the Courts (1987) 1:7 CLP 22.
172 Cases involving less than 500,000 RMB Yuan can be dealt with by the Arbitration Committee at a county or city level. Disputes concerning more than 500,000 Yuan will be handled by the Committee at a regional, provincial or national level, depending on the circumstance. Id, Art.10.
173 Ibid.
174 Id. Arts.25 & 26.
175 Ren, supra note 141, at 25.
willingness to comply with both Chinese and foreign institutional arbitration. Under these laws, arbitration rules of a foreign arbitration institution can be applied if the dispute is submitted to that institution.\textsuperscript{177} It seems that China prefers to leave the problems of the substantive law to be decided by the arbitration rules of each particular institution. For example, if an arbitration is held in China, Chinese law will be applied because the Arbitration Rules of FETAC do not provide for any possibility of using foreign law in its proceedings.\textsuperscript{178} At present FETAC has adopted three principles in its arbitration proceeding as guidelines for consideration when dealing with any cases. These are independence and initiative, equity and mutual benefits, and the taking into account of international practice.\textsuperscript{179} Following these guidelines, FETAC has adopted a flexible position whenever a conflict arises between laws of the parties' home countries concerning the same practice. Practices recognized by a relevant foreign legal system will also be given due consideration. Thus, the position and arguments of a foreign party, which are mostly based on the knowledge of its own legal system, may be appreciated and considered. Similarly, a Chinese party also expects its legal rights recognized under Chinese law to be accepted when a dispute is referred to a foreign arbitration institution. In the latter case, the three principles advocated by FETAC may be used as a defence by the Chinese party to avoid possible disadvantages to it arising from a foreign forum.

At present, two Chinese international arbitration institutions have been set up. FETAC is responsible for dealing with commercial disputes.\textsuperscript{180} MAC, as its name indicates, is set up principally for dealing with disputes involving remuneration for salvage services rendered by vessels to each other, disputes arising from collision

\textsuperscript{176} For example, Joint Venture Regulations, Art.110; and Foreign Economic Contract Law, Art.37.


between sea-going vessels and disputes concerning cargo shipping. By the end of 1986, there were 65 arbitrators in FETAC and 67 in MAC; and 102 cases had been dealt with by FETAC and 30 by MAC.

The basic principles adopted in the two laws are similar. Indeed, Articles 4-15 of the two laws are almost identical, except for adjustments made for the special purposes of the two different arbitration procedures. Under these laws, a case can be referred to arbitration by one or both parties only if an arbitration agreement has been reached between the parties, either before or after the dispute arose. The parties may appoint arbitrators from the members of the Commission, or authorize the Commission to do so. After the appointment of arbitrators, the arbitrators will select an umpire from the members of the Commission. If an umpire is not selected within the time limit, the chairman of the Commission will appoint one. At the beginning of the proceedings, the plaintiff is required to pay a certain percentage (0.5% in the case of FETAC and 1% in the case of MAC) of the amount claimed as a deposit, which may be regarded as the good faith of the plaintiff to initiate the proceeding, and may be used to cover costs if the plaintiff loses. The Commission may take certain security measures against the property in dispute upon the request of the parties. The parties have the right of representation, and may appoint either a Chinese or foreign lawyer as their representative or attorney. Usually, the hearing is conducted in open sessions unless the parties object. During the proceedings, the defendant may file a counter-claim, and the arbitrators may give a default award. The arbitral award is regarded as final, and no appeal to courts or other authorities is allowed. Like arbitration in Australia, the parties can reach an agreement on settlement, pending the process of arbitration, and may then withdraw the case from the proceedings.

6.2.3.2. Settling Investment Disputes Through Non-judicial Means

"The Chinese goal in dispute resolution is to preserve the business relationship through an emphasis on harmony in the settlement process". Thus, negotiation, or consultation, sometimes called friendly negotiation, or friendly consultation, is

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181 Its arbitration rules were made in 1959. For a brief review, see Lockett, id, at 256-7.

182 Ren, supra note 141, at 26.

183 As to matters relating to the appointment of arbitrators, see Lee, supra note 128, at 24-5.

regarded as an effective approach to dispute settlement. Direct contact between the parties concerned is a good way to remove misunderstandings and maintain business relationships. This has been proved in Chinese practice for resolving foreign trade disputes. For example, in 1975 China and the United States settled a dispute concerning a cancellation of two orders of grain by a Chinese buyer. Through negotiation the parties agreed to cancel the original contracts and the Chinese party paid the difference between the contract price and the much lower market price at the time of cancellation.\textsuperscript{185} Another example is an investment dispute between China and Japanese Nippon Steel Corporation on the construction of a steel work complex at Baoshan, China. After negotiation, the parties agreed that the payments would be deferred for five years and China would pay interest for the deferred payments at 7.25% per annum.\textsuperscript{186} A common feature of these two examples is that the parties involved in the dispute are pursuing a long-term business relationship. Maintaining this relationship is their main concern, which is why negotiation can be an effective method of dispute resolution under such circumstances.

New forms of mediation, such as joint mediation,\textsuperscript{187} have also been developed in Chinese practice. Joint mediation is a process in which mediators, who are chosen by disputing parties separately, transmit information and offers from one party to the other for the purposes of assisting the parties to reach an agreement. It was first used in settling Sino-US trade disputes.\textsuperscript{188} In this process, the parties seek


\textsuperscript{186} Id, at 263. For a detailed study on this case, see D.Sneider, "The Baoshan Debacle: A Study of Sino-Japanese Contract Dispute Settlement" \textit{(1985) 18 N.Y.U.J.Int'l Law.Fol.} 514.


assistance from their own national arbitration institutions. The mediator chosen by one party contacts the mediator chosen by the other party with a view to the settlement of the dispute. The mediators contact each other by letter, telex, telephone communication, or face to face meeting. At the end of mediation, a recommendation made by the mediators will be presented to the respective parties for consideration. In the whole process, the third parties act as both conciliators and advocates. The feature of this process is that the disputants do not have to meet face to face for a settlement of the dispute. Another feature is the role of the mediators. They are chosen separately by the parties concerned, but are not the attorneys of the parties. Their duty is to encourage the settlement of the dispute rather than to defend legally the position of the parties. Thirdly, the cooperation of the mediators is essential in this process, because there is no umpire in the process. Joint mediation has been accepted in some Sino-foreign trade agreements, such as the agreements between the Chinese and Italian arbitration institutions and between China and France.

Arbitration is the oldest method of non-judicial dispute resolution official upheld by the PRC for settling international commercial disputes. It is still a popular technique for settling commercial disputes involving foreigners, in particular in disputes over the international sale of goods. For example, a dispute on quality of goods sent by a Chinese seller in Tianjin on C & F terms to a buyer in Vancouver was submitted to the FETAC of CCPIT. The claimant, a foreign insurance company which had compensated the buyer for his loss from rusted nails, claimed a right of subrogation against the Chinese seller and the carrier (unknown nationality). The case was heard by the Commission and the claim of the foreign insurer was rejected on the ground of lack of evidence to establish the seller's or carrier's liability. Another example of the case submitted by a foreign applicant is a dispute involving the sale of gloves between a foreign buyer and a Chinese seller. The disputants

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189 In China these institutions are FETAC and MAC, and in the United States, they are the National Council for U.S.-China Trade (NCUSCT) and the American Arbitration Association (AAA).

190 Agreement Between CCPIT and Italian Association for Arbitration, May 1981.


192 The English translation of the Award can be found in (1988) 2:4 CLP 37. See also Wuhan Jute Bag Arbitration Case, where a foreign buyer claimed damages against a Chinese seller in relation to two contracts of sale. The claim was rejected by the Commission on the ground that the buyer had not opened letters of credit according to the terms of the contracts and therefore had no right to claim damages against non-performance of the contract by the Chinese seller. (1989) 3:4 CLP 32.
disagreed with the terms of the contract and the quality of the goods. Although the dispute was caused by the vague terms describing the quality of the gloves, the Commission found the Chinese seller was liable to pay 12% of the agreed price of the goods for damages suffered by the buyer.193 "One of the unique characteristics of Chinese international economic and trade arbitration is the integration between conciliation and arbitration."194 For example, a dispute between a Chinese seller and a foreign buyer was submitted to FETAC in February 1984. The Chinese seller failed to deliver the third shipment on time specified in a contract and the buyer sought damages. FETAC attempted to mediate the dispute but the Chinese party refused to accept FETAC's recommendation. FETAC then proceeded to arbitration and granted an award in favour of the foreign buyer in March 1984.195 Sometimes, cases have been submitted to the Commission by the Chinese party pursuant to arbitration clauses in contracts. Liuzhou Municipal Fan Factory v A Hong Kong Electronic Company is an example.196 In this case, the Commission decided that the Hong Kong company had not provided qualified products described in the contract, and directed the Hong Kong company to compensate the loss suffered by the buyer. Although most decisions of the Commission in the above-mentioned examples are against foreign parties, this may not be the case in every dispute handled by the Commission or other arbitration institutions in China.197 A reputation of impartiality, no matter true or not, will certainly discourage foreign investors from resorting to the Chinese arbitral institution for assistance.

6.3. Settlement of Investment Disputes Through Litigation

6.3.1. Some International Law Issues Concerning Judicial Settlement

Foreign investment disputes could arise between Australian investors and the Chinese Government, between Australian and Chinese companies, and between Chinese companies and the Australian Government. These disputes can be resolved through non-judicial means, such as negotiation, mediation and arbitration; and may

193 The Award in Chinese was reported in a conference on Sino-US trade and investment law held in Beijing in 1986.


195 Nafziger, supra note 185, at 159.

196 (1989) 3:7 CLP 34.

197 There is no official case reporting system in China. Based on information available, most awards delivered by the Chinese arbitral institutions are in favour of Chinese disputants, although this does not necessarily reflect the true practice of the Chinese arbitration institutions.
also be settled in some circumstances through litigation. As have been seen, Australian nationals and companies can seek legal remedies in the Chinese courts, and Chinese nationals and companies can also take legal action in the Australian courts. Legal proceedings in these courts are governed by the law of each country. But some international issues may arise in such proceedings. For example, when a case involves Australian or Chinese Government or their property, foreign state immunity must be considered; and when a judgment of an Australian court must be executed in China or a judgment of a Chinese court must be executed in Australia, the law relating to the recognition of foreign judgments will be a relevant. Nevertheless, these matters, which will be examined below, are also subject to the laws and policies of Australia and China.

6.3.2. State Immunity and Litigation
6.3.2.1. Australian Position on State Immunity

Australia adopted the restrictive doctrine of state immunity in the Foreign State Immunities Act 1985 (FSIA) (Cth), which brought Australia to the same general stand in relation to state immunity as the United States, the United Kingdom, Canada, and several other countries. In general, the FSIA is influenced by both Sovereign Immunities Act (SIA) of the United Kingdom and the Foreign Sovereign Immunities Act (FSIA) of the United States. For example, s.35, which treats the property of a separate entity in the same way as the property of a state, bears the marks of the SIA of the United Kingdom; and s.22, which extends s.17(3) to a separate entity of a foreign state is rather closer to FSIA of the United States than to SIA of the United Kingdom.198 Under the FSIA, Australian courts do not have jurisdiction over foreign states, except as provided by or under the Act.199 The exceptions are submission by foreign states, commercial transactions of foreign states, contracts of employment concerning Australia, personal injury and damage to property, real estate, copyrights, patents, trade marks, foreign state as a member of a body corporate, supervisory jurisdiction of courts with respect to arbitration which is entered voluntarily by a foreign state, and actions in rem in relation to ships and cargos.200 Obviously, the restrictive doctrine of state immunity, which was adopted

199 FSIA, s.9.
200 FSIA, ss.10-8.
as early as 1857 in Belgian courts,²⁰¹ contradicts the absolute sovereignty doctrine held by China.

Some features of the FSIA, that may raise potential conflicts with the present position of China, are reviewed below. First, the Australian Act defines a separate entity as a foreign natural person or foreign corporation that is an agency or instrumentality of a foreign state but is not a department or organ of the state.²⁰² The Act apparently intends to restrict the immunity of a separate entity of a foreign state as a counter action against the claim of immunity on State-owned enterprises engaging commercial activities.²⁰³ But the provisions on separate entities may not suit the case of China, which, as will be seen, may not claim immunity with respect to its separate entities at all. A dispute may arise with regard to what is a property of a State-owned enterprise which is a legal person under Chinese law and what is a property of a department of the Chinese Government which is not treated as a separated entity under the FSIA. Although the commercial activities of both entities are subject to the FSIA, the status of the entities may result in differences in the enforcement of a judgment against the Chinese Government.

Secondly, commercial transactions are described as commercial, trading, business, professional or industrial or like transactions into which the foreign state has entered or a like activity. In particular, commercial transactions include contracts for the supply of goods or services; agreements for a loan or other transactions for or in respect of the provision of finance, or guarantees or indemnities in respect of financial obligation.²⁰⁴ These transactions certainly cover most commercial activities a government may be involved in. But the nature of the land-use leases made between the Chinese Government and foreign investors is arguable under this Act.²⁰⁵

²⁰¹ Peele, supra note 182, at 547.
²⁰² FSIA, s.3(1).
²⁰³ The intention of the Act was illustrated by Senator Walsh's second reading speech on the FSIA in Senate on 8 Oct.1985. He pointed out that separate entities of a foreign State "are given, in most respect, the same immunity as the State. In practice, this means that entities with exclusively commercial functions, the majority of those involved in dealings with Australia, will lack immunity". Hansard vol.s.110, (20 Aug.-11 Oct.1985) 796. See also the Australian Law Reform Commission (ALRC), Report no.24, Foreign State Immunity (Canberra, AGPS, 1984) paras.72, 73 & 89.
²⁰⁴ FSIA, s.11.
²⁰⁵ The Chinese Government may probably argue that a land-use lease is not for commercial purposes, but a measure for accommodating foreign investors. Often the land-use right is not transferred independently as a commodity, but initially assigned
6.3.2.2. Present Position of China on State Immunity

Since 1949 the PRC has apparently adhered to the absolute immunity doctrine. However, state immunity in relation to commercial and trade activities had not been a real issue in Chinese law until 1978 when China adopted an open-door policy.

The early studies of international law theory in China, which was deeply influenced by the Soviet Union, did not explain what was China's understanding of absolute immunity. For example, while China was believed to uphold the "absolute" doctrine of sovereign immunity, at least one Chinese article criticised both the theory of absolute sovereignty, and the doctrine of restrictive sovereignty allegedly held by Western countries. This article then expressed its antagonism to the bourgeois as a right (or assurance) attached to the investment projects. Its existence is attributable to the peculiarity of the Chinese system of land ownership.

206 It must be pointed out that Chinese legal writings in the 1950s and 1960s did not expressly indicate Chinese views of sovereign immunity. In fact, the term "sovereign immunity" was rarely used. Nor was Chinese view of sovereign immunity expressly discussed. Even in articles dealing with issues of sovereign immunity, e.g. Keng-sheng Chou, "Trends in the Thought of Modern English and American International Law" in J.Cohen & H. Chiu eds, People's China and International Law (Princeton, Princeton University Press, 1974) 891-3, "sovereign immunity" was broadly described but not discussed, at least not in a scholastic way. It is possible that, in that period of time, Chinese legal scholars treated "sovereign immunity" as an inherent part of sovereignty. For example, an article reviewing Western views of sovereign immunity states that sovereign immunity "is an old question in international law. Under the traditional theory of international law, the recognition of this principle of State judicial immunity, based upon State sovereignty, independence, equality, dignity, friendly relations and other reasons, is generally beyond question". (see, Cohen, at 891.) As we will see, some Chinese writers used terms "absolute sovereignty" and "restricted sovereignty" where they in fact dealt with issues of "sovereign immunity". Having regard to the usage of these terms in China, "sovereignty" in this subsection where Chinese translation or Chinese views are concerned refers to "sovereign immunity".

207 The article argued that "the advocates of the theory of absolute sovereignty consider that in accordance with its sovereignty a State may, without being subject to any restriction, do anything it wishes to other States. That is to say, a State may impair the sovereignty of another state in order to exercise its own sovereignty. Obviously, this suits the policy of unrestrained aggression and expansion of imperialism". Yang Hsin & Ch'en Chien, "Expose and Criticise the Imperialists' Fallacy concerning the Question of State Sovereignty" collected in Cohen, supra note 190, at 111-2.

208 The article presented the following arguments:

The advocates of the theory of denial of sovereignty or the theory of restrictive sovereignty mainly proclaim that States should abandon or restrict sovereignty for the sake of "the general interests of mankind" or "consolidating into legal order". They declare that sovereignty is relative, divisible, and subject to restriction and abandonment, and that as a matter of
theories of sovereignty, "mutual respect for sovereignty". However, the article was not able to distinguish the essential differences between the principles of "mutual respect for sovereignty" and the doctrine of restrictive sovereign immunity. The arguments for "mutual respect for sovereignty" might stand if the arguments were made for clarifying what was deemed to be an acceptable relationship between sovereign states, but do not when being used to debate the substance of "sovereignty". In fact, the article failed to address whether sovereignty is divisible or subject to restriction and abandonment. Thus, the assumed antagonism to the restrictive sovereignty doctrine does not address the issues of restrictive immunity. Nor does it draw a line between restrictive and absolute immunity, as the article attempted to.

The vagueness of China's official position toward state immunity has not changed much since 1978, but a trend to break away from the conventional and controversial doctrine of absolute immunity has been seen in Chinese practice. The Huguang (Bukuang) Railway Bonds Case was perhaps the first major legal challenge to China's doctrine of absolute sovereign immunity since China opened its door to foreign investors. The case involved claims by a number of American citizens against the Chinese Government in relation to bonds issued by the Chinese Qing

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fact no state has complete sovereignty. The purpose of this theory is to prove that colonial rule and imperialist's infringement on and restriction and elimination of other States' sovereignty are all lawful.

Yang Hsin, id, at 112.

Ibid.

The article argued that "mutual respect for sovereignty absolutely does not mean that a State (regardless of how strong and large it is) may do whatever it wishes to other States on the pretext of exercising its sovereignty. Respect for sovereignty must be mutual: the principle that other States respect our sovereignty and we respect the sovereignty of other States. The exercise of sovereignty should be based upon the promise of not impairing the sovereignty of other States". Id, at 112.

Mutual respect does not conflict with the notion of voluntarily abandonment of some traditional sovereign rights by States on a reciprocal basis. Mutual respect for sovereignty also warrants the notion of respecting the independent legislative power of other countries to restrict state immunity provided that restrictions so made are mutual.

If the article dealt with the divisibility of sovereignty, it would probably have addressed directly the issue of sovereign immunity.

The vagueness of China's position can be seen in the fact that although China has not officially given up absolute sovereign immunity doctrine it has accepted restriction on its sovereign immunity in some bilateral treaties, e.g. the Australia-China Investment Protection and Promotion Treaty, Art.VII.
Imperial Government in 1911. After a lengthy court battle, in which the Chinese Government never formally appeared, the claims were denied by the court.\textsuperscript{214} It was settled on the bases of legal technicalities under the domestic law of the United States. The settlement of this case reveals China's present position with regard to state immunity, which has moved away from "absolute" doctrine of state immunity to a less "absolute" or rigid position on sovereign immunity. Although China has not denounced the doctrine of absolute sovereign immunity,\textsuperscript{215} it has not really adhered

\textsuperscript{214} The case involved several American citizens who held Huguang Railway Bonds, issued by the Qing Imperial Government of China in 1911, and sold by banks in France, Germany, England, and the United States. The Chinese Kuomingdao (Nationalist) Government stopped paying interest on the bonds in 1938; and the Chinese Communist Government, which refused to acknowledge any external debt owed by the previous Governments, defaulted the principals of the bonds at their maturity in 1951. In 1979, the then bondholders sued the Government of the PRC for money owed to the defaulted interest and principals of the bonds in the United States District Court of Alabama Eastern District. The Court served a notice to the Chinese Government, which refused to respond to the Court on the ground of state immunity. The Court entered judgments by default against the PRC on 21 October 1981 and 21 September 1982 in an amount of US $41,313,038.00, which was further increased on 27 November 1982 to cover the claim of Jeff Saile, an unnamed member of the certified class. China protested the judgment through An Aide Memoire of the Ministry of Foreign Affairs on 2 February 1983, after receiving the default judgments. Subsequently, several meeting were held between the Chinese and US Governments. As a result, the Chinese Government agreed to appoint a US counsel to seek relief from the default judgments in the Court of Alabama Eastern District, without conceding the Court's jurisdiction under the FSIA of the United States. The US State Department submitted a "Statement of Interest" to the Court in support of China's motion. After reviewing the motion brought forward by the counsel for China and the Statement from the State Department, the Court set aside the default judgments. The plaintiffs appealed against the Court decision setting aside the default judgments without success. See Jackson v the PRC 550 F.Supp. 869 (ND Ala, 1982), vacated and dismissed, 596 F.Supp. 381, affirmed, 794 F.2d 1490 (11th Cir. 1986) rehearing denied, 801 F.2d 404 (11th, Cir.1986).

\textsuperscript{215} China's adherence to the absolute sovereign immunity was reiterated in the Aide Memoire sent by the Chinese Government to the US Government in 1983. Paragraph 3 of the Memoire is as follows:

Sovereign immunity is an important principle of international law. It is based on the principles of sovereign equality of all states as confirmed by the Charter of the United Nations. As a sovereign state, China incontestably enjoys judicial immunity. It is in utter violation of the principle of international law of sovereign equality of all states and the UN Charter that a district court of the United States should exercise jurisdiction over a suit against a sovereign state as a defendant, make a judgment by default and even threaten to execute the judgment. The Chinese Government firmly rejects this practice of imposing the United States domestic law on China to the detriment of China's sovereignty and national dignity. Should the U.S. side, in defiance of international law, execute the abovementioned judgment and attach China's property in the United States, the Chinese Government reserves the right to take measures accordingly.

to absolute immunity doctrine either. Had it followed the absolute sovereign immunity rigidly, it would not have appointed a US counsel to seek relief from the default judgment in the US Court under the procedural rules of the US courts. Secondly, counsel on behalf of the Chinese Government sought relief from the default judgments on the ground of Fed.R.Civ.P. 60(b), which does not, however, provide state immunity as a basis for setting aside judgments. Counsel in fact argued for the Chinese Government under the domestic rules of the United States and his arguments were accepted on China's merits under the law of the United States. The lawyer for the Chinese Government succeeded in defending China's position on the ground of the domestic law of the United States, rather than on the basis of absolute state immunity. Thus although the Chinese Government did not submit itself physically to the jurisdiction of US courts, its legal representative, who was authorized to act on China's behalf, submitted himself to the jurisdiction of the Court. Indeed, the Court dealt with the defenses for China raised by the counsel as if the Chinese Government had been present in the court proceedings. Seeking relief in the Court by the counsel was a vague, indirect, de facto abandonment (or at least a compromise) of the absolute sovereign immunity doctrine by the Chinese Government. Thirdly, the defences presented by counsel for China seem to have omitted absolute sovereign immunity as a ground for seeking relief from the default judgments. The omission appears to suggest that the Chinese Government was prepared to resolve the controversy through a realistic approach, although the approach is not totally consistent with the doctrine theoretically upheld by China. This could be the case of either "the end justifies the means" or "the end is more important than the means". These facts reveal that the Chinese Government has

216 Under the FSIA of the United States, foreign state may appoint counsel to appear in the courts for the purposes of asserting immunity. Similar provisions are also found in the FSIA of Australia.

217 This rule gives six reasons under which a court may relieve a party from a final judgment, order or proceeding. The Court set aside the default judgments under the Rule 60(b)(4). Jackson v the PRC, reprinted in (1984) 23 ILM 402, 408.

218 For example, the judgment goes like this "it was not until August 10, 1983, that the China entered a special appearance and sought to have the default judgments set aside and the case dismissed. Jackson v the PRC (1984) 23 ILM 402, 404.

219 The copy of the motion filed by the counsel for China is not available. But the absolute sovereign immunity is not discussed in the judgment setting aside the default judgments, although a number of other arguments supporting China's motion are examined by the Court. Thus it can be assumed that the absolute sovereign immunity was omitted in the motion. The omission might not be an express consent from the Chinese Government, but was an acquiescence in the power of the counsel who was authorized to act for the interest of the Chinese Government. Another possibility is the counsel raised it as a defence but the Court ignored it.
relaxed its adherence to the doctrine of absolute sovereign immunity in practice though not in theory.220

The trend to break away from the absolute sovereign immunity doctrine is also occasionally shown in the studies of state immunity, which, however, have yielded only a small volume of academic writing. In an article written by the late Prof. Chen of Beijing University, the author, while insisting on absolute immunity in the Huguang Railway Bonds Case, raised several defences for the Chinese Government under the restrictive doctrine of state immunity. These included the definition of commercial activities, international practice of serving court documents, immunity of government bonds, "bad debts", the governing law for the Huguang Railway Bonds disputes under conflict of law rules, and time limitation under the law of Alabama.221 Some of these defences apparently were adopted by the counsel for China and were examined by the Court. The only defence, which is missing from Prof. Chen's arguments, is the issue of retroactivity of the FSIA, that is, however, mentioned in the US State Department's Statement.222 The arguments in the article by Prof. Chen are unlikely to be mere coincidence. In a country like China, legal scholars may affect the policy of the Government,223 or they may be affected by the policy of the Government.224 One way or another, the position shown in the article is likely to indicate to some extent the trend in China.

In addition, the tendency to relax the absolute sovereign immunity doctrine can be seen in another article. Although it still insists on absolute sovereign immunity, the article notes that "the Chinese Government has never entered into any economic contracts, which contain economic rights as well as obligations, with foreign investors. Foreign investment is accepted in China through the contracts between entities which are qualified as legal persons and foreign investors".225 The

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220 This was also noted in the Statement of Interest submitted to the Court by the US State Department. The documents states that the PRC "despite its adherence to the absolute principles of immunity has appeared in this proceeding and put forth a number of legal and factual defenses". (1983) 22 ILM 1096.


223 Because the Government often cannot produce its own distinctive and independent theories of international law.

224 Because the legal scholars are expected to serve the needs of the Government.

225 J.L.Duan, "A Brief Review of the Scope of Investment Disputes and International Arbitration" Faculty of Graduate Studies, Chinese University of Politics.
fact noted by the article reflects the present practice of China in dealing with issues of state immunity. This position of the Chinese Government on sovereign immunity is also seen in statements made by Mr. Ni, the Chinese member of the International Law Commission. On numerous occasions, Mr. Ni has insisted on absolute sovereign immunity doctrine, but he has also accepted that state-owned enterprises do not have sovereign immunity. In separating the Government, which still has absolute sovereign immunity, from independent legal entities, the Chinese Government hopes to limit its liability in case a dispute is brought to a

226 This practice is also seen in the Australia-China Investment Protection Treaty, where China waives immunity over the investment of its "nationals" in Australia. See Chapter 7 for details.

227 For example, in 1982 he stated that although "the increasing participation of States in commercial and economic activities was leading towards a limitation of State immunity", "a rule of international law could not be drafted on the basis of a single trend". (See Yearbook of the International Law Commission 1982 vol.1, at 66.) In 1983, he argued that the "affirmation that there appeared to be an emerging trend in favour of limitations on State immunity was even more difficult to accept in view of the scarcity of available evidence". (See Yearbook of the International Law Commission 1983 vol.1, at 70.) In 1984, he stated that "State immunity was still firmly established on the basis of the sovereign equality of States as a general rule of international law, and that would continue to be the position so long as States remained sovereign and equal". (See Yearbook of the International Law Commission 1984 vol.1, at 122.)

228 He stated that where "State-owned corporations or State enterprises with independent legal personalities had been set up by States that carried on business in other countries, such corporations or enterprises would have little difficulty in complying with the tax laws and regulations of the host States. State enterprises of his own country instituted proceedings and appeared as defendants in the courts of foreign countries". See Yearbook of the International Law Commission 1984 vol.1, at 124.

229 Legal entity, as defined in the Civil Code, is an organization which is competent in exercising civil rights and in performing civil acts. Such organization independently enjoys civil rights and assume civil duties under law. Civil Code of the PRC (General Principles) Art.36, Statutes and Regulations of PRC (University of East Asia Press and Institute of Chinese Law (Publishers) Ltd) no.860412.1. Under the Civil Code, a legal entity can be either a state-owned enterprise or a private enterprise. In the context of foreign investment, a legal entity refers to any organization, body and enterprise which has power to sign economic contracts with foreign investors under Chinese law, regardless of whether it is directly controlled by a Department of the Government.
foreign court. Under the present practice, a foreign party is expected to sue its contracting partner rather than the Government. Moreover, the Chinese Government expects foreign courts not to execute judgments against the property of the Chinese Government or against legal entities other than the one involved in the lawsuit. This is a result of the adoption of a realistic policy toward the restrictive doctrine accepted by several major trading partners of China, and is also an indication of China's de facto retreat from the absolute sovereign immunity doctrine.

The Chinese framework for foreign investment and trade suggests a possibility of Chinese legal entities, which include organs and organizations of the governments, being sued or suing in foreign courts. The Joint Venture Law, Cooperative Joint Enterprise Law, and Foreign Economic Contract Law all allow disputants to submit their disputes to foreign arbitrators. China should surely have realized that arbitration held within foreign countries might be subject to the supervisory power of foreign courts in some cases. Accordingly, the provisions on international arbitration in Chinese law can be an indication of China's willingness to be subject to the supervisory power of foreign courts, although a submission to foreign arbitration does not necessarily mean a submission to foreign adjudication.

In sum, the Chinese Government still upholds the absolute sovereign immunity doctrine, but seems to have limited its application. This can be seen in the Australia-China Investment Protection Treaty, entered into force on 11 July 1988. The Treaty has a limitation on immunity clause. Under this clause, the Australian and Chinese Governments agree that the issues of immunity involving investment of "nationals" of the two countries will be dealt with according to the law of the country where the litigation takes place. This suggests that the Chinese Government will not claim immunity over the investment of Chinese "nationals" in Australia. Thus direct conflict with sovereign immunity doctrine can be avoided by suing relevant legal entities of China rather than the Government. The Chinese Government may not

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230 Such consideration can be seen in the article by Prof. Chen, where he argued that if the Chinese Government can be sued in the US courts, it could then face endless lawsuits in the US courts because there are hundreds of thousands trades between China and the United States. Chen, supra note 205, at 449. Similar argument was also made by Mr. Ni, who observed that law should be phrased to the effect that would not "incline foreign plaintiffs to sue the State rather than a State enterprise, in order to force the State either to agree to an out-of-court settlement or to defend the suit in the foreign court, which might involve undesired waiver of its immunity". Yearbook of the International Law Commission 1984 vol.1, at 124.

231 This is also noted by Peele who regards this as an implicit waiver of sovereign immunity. See T.Peele, "The Law of Foreign Sovereign Immunity in Relation to Trade With and Investment in China" in Moser ed, Foreign Trade, Investment, and the Law in the People's Republic of China (2nd edn, HK, Oxford University Press, 1987) 346, 551-2.
claim absolute immunity over activities of a State-owned enterprise because of practical difficulties and considerations, such as the economic interests of China. The settlement of the Huguang Railway Bonds controversy suggests a new and practical approach to resolving disagreement between the absolute sovereign immunity doctrine held by the Chinese Government and the restrictive sovereign immunity doctrine held by several countries, including Australia. To prevent potential conflicts, foreign businessmen should avoid signing contracts with the Chinese government unless absolutely necessary or the Government waives immunity; or alternatively, they should sue the Chinese government in the Chinese courts.¹²³

6.3.2.3. Positions of Australia and China in Relation to Sovereign Immunity and Potential Disputes

Actions in rem under the FSIA may be a potential source of conflict between Australia and China if the Act is to be construed broadly. The conflict arises from s.18(2) which allows a legal action to be taken against a ship concerning a claim against another ship of the same state in an action in rem. This rule, in conjunction with s.32,²³³ may subjugate all commercial ships and cargos belonging to China to the jurisdiction of the Australian courts. This is just what the Chinese Government is trying to avoid by applying the concept of legal entity to international trades. The application of the provisions on actions in rem is very much dependent on the interpretation of the concept of state property under the Act. At present, there are no commercial ships in China, which are directly under the control of the Government. Rather, shipping companies act as independent legal persons under

²³² The Civil Code and Civil Procedure Law do not apply to the relationship between government as political entity and persons. But under the Civil Code, if a governmental body acts as legal entity, it is liable for its activities. Difficulties in suing the Government arise when the cause of action is not regulated in the Civil Code, such as torts, or contracts signed by government administration which is not a legal person (e.g. land-use lease). It is not clear if the disputing parties to such disputes can still sue the Government in the courts. The basis for disputants' rights to sue can be found in Art.41 of the Chinese Constitution, which allows Chinese citizens to criticise and make changes against any state organ or functionary for violation of law or dereliction of duty. This right seems not to be fully enforceable for lack of appropriate law. However, as far as commercial activities are concerned, the foreign parties can always sue the Chinese government, which acts as a legal entity, in Chinese courts. At least, two cases involving local governments have been reported. One involved a Hong Kong company and a local government in SEZs, see Hong Kong XXX Ltd v SEZ ESC (1988) 2:1 CLP 22; the other involved a Chinese party and the Municipal Government of Yinchuan, see T.X.Zhu, the President of the National Supreme Court, "Annual Working Report of the National Supreme Court" (1987) 2 Gazette of the National Supreme Court of the PRC (in Chinese) 3, 11.

²³³ It allows a judgment to be executed against ships and cargos of the same State.
Chinese law. Thus, when actions *in rem* arise, Australian courts should, and probably would in light of English court practice, only treat a ship as the property of a separate entity, although the Act may be interpreted broadly to include properties of other State enterprises in such situation. If so, the Act will not lead to direct conflict between Australia and China.

Another possible cause of confusion, which may not be easily resolved in the context of the present legal framework for state immunity in Australia and China, is the land-use right in China. The FSIA does not exclude the jurisdiction of Australian courts by the mere reason that the commercial activity is performed in China, although it does not extend to a proceeding which involves a state having interest in, or possessing or using immovable property outside Australia. Accordingly, if the land-use lease between a Chinese local government and an Australian investor is regarded as a commercial transaction, the Australian courts will probably have jurisdiction over any disputes arising therefrom. But if it is regarded as a proceeding involving ownership, possession and use of property, the lease will not be subject to the FSIA. The determination of the nature of the lease may involve issues of conflict of laws. Under Australian law, a land-use right is a proprietary right. But under Chinese law, a land-use right is not expressly recognized as a proprietary right, because Chinese law neither treats land as kind of real estate nor allows a land-use right to be transferred indefinitely. It is a very restricted right to use land for a limited period of time. Whether this right is a "proprietary right" is open to debate, even under Chinese law. Two conflicting situations may arise in the application of the Act. If the a land-use right is regarded as an interest of the State in, or the possession or use by the State of, immovable property in Australia; or an obligation of the State that arises out of its interest in, or its possession or use of, property of that kind.

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234 For example, see *Czarnikow v Rolimpex* [1979] AC 351 and *I Congreso* [1983] AC 244.

235 FSIA, s.14(1) states that a "foreign State is not immune in a proceeding in so far as the proceeding concerns:

(a) an interest of the State in, or the possession or use by the State of, immovable property in Australia; or
(b) an obligation of the State that arises out of its interest in, or its possession or use of, property of that kind.

236 The lease concerning the initial land-use right must be made between a local Chinese government and a foreign investor (natural or legal person).

237 FSIA, s.11(3) states generally that a commercial transaction refers to "a commercial, trading, business, professional or industrial or like transaction into which the foreign State has entered or a like activity in which the State has engaged". The section further specifies that "a contract for the supply of goods or services; an agreement for a loan or some other transaction for or in respect of the provision of finance; and a guarantee or indemnity in respect of a financial obligation" are regarded as commercial transactions, excluding "a contract of employment or a bill of exchange".
as a proprietary right under either Chinese law (although the Chinese law itself does not provide a clear answer in this respect) or Australian law, an action involving land-use right in China could not be heard in an Australian court. However, if land-use right is not regarded as a proprietary right (i.e. if it is treated as a commercial transaction), the Chinese Government could not claim sovereign immunity under the Act. In the second situation, if the Chinese Government does not act through a separate legal person\textsuperscript{238} it would have to face the issues of sovereign immunity. If the Chinese Government chooses to claim absolute sovereign immunity, conflicts will arise from the application of the Act.

In conclusion, the differences between the absolute sovereign immunity and restrictive sovereign immunity doctrines are evident, but not irreconcilable. While maintaining their sovereignties (legislative and judicial), Australia and China should be able to reach a compromise as to their immunities, such as in the Huguang Railway Bonds Case between the Chinese and US Governments, to avoid and to resolve their differences, if they hope to increase the trade contacts. The best China could do under its present legal and economic systems is to renounce state immunity over commercial activities and specified transactions under the FSIA, carried out by State-owned legal entities. This is justified under the Chinese Civil Code and Civil Procedure Law. Meanwhile, the effective means for Australia to avoid direct conflicts with China is to accept the differences between the Chinese Government and State-owned enterprises or organizations which are legal persons under Chinese law. In fact, common law courts have accepted the independent status of State agencies engaging in commercial activities.\textsuperscript{239} In 1979, the House of Lords in England recognized that Centrala Handlu Zagranicznego Rolimpex, a Polish State

\textsuperscript{238} In China, all lands are owned by the State. A legal entity can only obtain land-use right initially from the government, although its rights can be transferred later. In addition, land-use right is often assigned by the government administration which does not satisfy the tests for a legal person under Chinese law. To avoid such legal technicalities, the Chinese Government may establish special land management corporations as legal persons under Chinese law, which should obtain initial land-use right from the governments, then lease the right to others. Thus, China can argue that any dispute arising from land-use lease is between two legal entities, but not between the Government and person. But the rarity of lawsuits against the Chinese Government in relation to land-use right does not create a need, at least presently in the view of the Chinese Government, to take these measures.

\textsuperscript{239} Prof. Crawford points out that "common law courts have been strict in their adherence to the principles of the corporate separateness of state agencies for these and related purpose". J. Crawford, "Foreign State Immunity" in Attorney-General's Dept. ed, Asian Pacific Regional Trade Law Seminar: Papers and Summary of Discussion (Canberra, AGPS, 1985) 563.
enterprise is a separate legal entity in Polish law. Thus, Rolimpex, like any private-owned enterprise in the same situation, is exempt from performing its contractual obligation under the force majeure rule 18(a) of the Rules of the Refined Sugar Association. Similarly, in 1983 the House of Lords allowed an appeal by the Republic of Cuba with respect to the application of State immunity doctrine.

The majority of the House regarded the independent State organizations as legal entities. Lord Wilberforce’s comments perhaps suggest the general position of common law courts in relation to corporate separateness of State agencies. He observed that the sale of cargo in Vietnam by the ship master is a commercial transaction which "was not that the Cuban State, but of an independent State organization. The status of these organizations is familiar in our courts, and it has never been held that the relevant State is in law answerable for their actions".

Although there may be pragmatic difficulties for the Australian courts to determine whether a State enterprise is a Chinese legal entity, in the light of common law

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240 Czarnikow v Rolimpex [1979] AC 351. The case is an appeal by an English sugar importer from the decision of the Court of Appeal ([1987] QB 176), which confirmed the award of a penal of the Refined Sugar Association in London.

241 Lord Viscount Dilhorne observed that

The respondents are an organization of the State. Under Polish law they have a legal personality. Though subject to direction by the appropriate minister who can tell them "what to do and how to do it", as a State enterprise they make their own decisions about their commercial activities... They are managed on the basis of economic accountability and are expected to make a profit. The arbitration in my opinion rightly found as a fact that the respondents were not so closely connected with the Government of Poland as to be precluded from relying on the ban imposed by the decree as government intervention.


242 I Congreso [1983] AC 244. The dispute involved a claim by a Chilean company for compensation against Cuban Government. In September 1973 after the Chilean revolution, two Cuban cargo vessels owned by Mambisa, a Cuban State enterprise, left Chile for their safety because Cuban Government decided to discontinue commercial and diplomatic relation with Chile. The Playa Larga which had discharged part of her cargo returned to Cuba and The Marble Islands discharged her cargo in Vietnam, a sale which is consistent with the terms of the bills of landing and approved under Cuban law. The Chilean company brought an action in 1975 in rem against Mambisa which was the owner of a vessel (The Congreso) that was delivered in Sunderland. The Cuban Government claimed sovereign immunity. The Court of Appeal dismissed the appeal by the Cuban Government to set aside the writs and subsequent proceedings in three legal actions brought by the Chilean company. But the House of Lords reversed the decision of the Court of Appeal.


244 The FSIA does not set forth criteria for determining a separate entity of a foreign state. But, the ALRC commented in 1984 that "agency of a foreign State" comprises
court's practice, the legal status of Chinese enterprises under Chinese law would probably be recognized in Australian courts.

6.3.3. Issues of Judicial Assistance

Australia and China do not have a judicial assistance agreement between them. Issues of judicial assistance between the two countries are basically regulated by the domestic law of each country. In China, rules governing service of foreign process and recognition of foreign judgments are described in the Civil Procedure Law. In Australia, rules regarding service of judicial documents within a foreign jurisdiction are found in the court rules of each State and Territory and (in the case of State entities) in the Australian FSIA; and the rules concerning enforcement of foreign judgments are found in Acts of each State and Territory in relation to reciprocal enforcement of foreign judgments, and the common law. The issues of judicial assistance will be examined below.

Australia and China have adopted broadly comparable rules regarding service of foreign process, although following different approaches. The Chinese law specifies six methods of serving judicial documents in a foreign jurisdiction, but

all agencies of the foreign State which are not departments or organs of the State because the degree of government control is insufficiently close. There will be no formal requirement that the agency show that it is exercising 'sovereignty', although it should clearly be relevant that the entity is exercising what are on any view governmental functions (eg immigration control). It is not intended that 'agency' be interpreted as requiring a precise relationship of principal and agent in the technical common law sense. Rather it is expected that a court would consider whether the entity is exercising governmental functions on behalf of the foreign State.

ALRC, supra note 203, para.72. The ALRC suggests that the exercise of governmental functions is the criterion to determine whether an entity is an agency of a foreign State. Because of the Chinese Government's extensive involvement in economic activities, Australian courts may sometimes have difficulties in determining whether a Chinese State-owned enterprise is exercising governmental functions. Disagreement may arise if the Chinese Government intends to claim immunity for one of its separate entities.

245 Arts.196-198 & 202-205.


247 These are through diplomatic channel, direct delivery to a Chinese citizen overseas through the Chinese diplomatic representatives, mailing if allowed by the law of the foreign country, judicial assistance under agreement, through counsel of the foreign parties, and public notices (6 months limit). Civil Procedure Law, Art.196.
Australian laws take a broader approach,\textsuperscript{248} which sets up general rules for service of foreign process. Moreover, both countries require that the documents must be translated into the appropriate language and be served with both the original copy and the translation.

The rules governing the recognition of foreign judgments are also similar in the two countries. For example, the Chinese courts will recognize foreign judgments by virtue of a judicial assistance agreement. If there is no agreement, the Chinese courts will make decisions on a case by case basis. The considerations to be taken into account are whether the judgment is consistent with China's treaty obligations; whether it is consistent with the principle of reciprocity; whether it is consistent with Chinese law; and whether it is consistent with the public interests of China.\textsuperscript{249} These principles are complementary to each other. Even where there is a judicial assistance agreement which does not specify particular matters subject to assistance, a Chinese court may refuse to enforce the judgment on the ground of contravention of Chinese law or of the public interest.\textsuperscript{250} For example, a foreign judgment against a Chinese enterprise in relation to a payment in foreign exchange may not be enforceable in a Chinese court because of the existence of foreign exchange control in China. Moreover, a judgment against the property of the Chinese Government or of a State-owned enterprise may not be enforceable in China on the ground of the public interest which, however, has not been clearly defined in Chinese law. In Australia, similar rules may be found in the Acts of each State and Territory on enforcement of foreign judgments. For instance, in New South Wales, a foreign judgment which is obtained in a proclaimed country can be enforced in the courts if the foreign court delivering the judgment has appropriate jurisdiction over the defendant (by reason of nationality, residence or voluntary submission) and the judgment is final, was not obtained by fraud or duress, is consistent with natural justice, is not of a penal nature, is not for a revenue debt and is consistent with

\textsuperscript{248} The court rules of each State usually do not specify the means of service, e.g. Victorian Court Rules states that the documents can be served in any necessary manner. The FSIA specifies several methods of service, such as by agreement, through diplomatic channel, and served to an authorized person. s.24. The methods in the FSIA are not meant to be exhaustive, because the Act concerns only service to foreign governments.

\textsuperscript{249} Civil Procedure Law, Art.204.

\textsuperscript{250} In particular, these include judgments violating China's sovereignty and security, matters exceeding the Chinese court's jurisdiction, judgments inconsistent with China's national or social interests and judgment (or any documents) which do not have attached official copies of the translations in Chinese. See Zheng, supra note 96, at 543.
The requirement that a foreign judgment should be derived from a proclaimed country is equivalent to the Chinese requirements for a treaty obligation or reciprocity. The specific rules may be comparable with the Chinese rules on the requirement for the consistency of a judgment with Chinese law and public interest. However, since China is not a proclaimed country, the statutes on the enforcement of foreign judgment in most States, except in South Australia, cannot apply to a Chinese judgment. Accordingly, the judgment of Chinese courts may not be given effect in a local judgment, although it may be enforceable under the common law, which generally provides four defences: want of jurisdiction, fraud, denial of natural justice, and contravention of public policy. Despite the differences in the classification of tests for the recognition of foreign judgment, these four defences in Australia may be broadly comparable with the two Chinese rules, legality of the foreign judgment under the domestic law of the enforcing country and consistency of the judgment with the public interest of the enforcing nation.

6.4. Settlement of Disputes Involving Investment from Taiwan

Despite the fact that Australia does not have diplomatic relations with Taiwan, the value of Australia-Taiwan trade exceeded the total of Australia-PRC trade in 1988-89. During this period of time, Australian exports to Taiwan reached $1.57 billion and imports from Taiwan were $1.92 billion. This is contrasted with exports ($1.2 billion) to and imports ($1 billion) from the PRC at the same time. Given the prospects for economic growth in Taiwan, Taiwan trade and investment in Australia may have a considerable impact on the Australian economy in coming years.

The settlement of disputes involving Taiwanese investment in Australia has some relevance to this thesis. From an Australian perspective, Taiwan raises a


252 South Australia has adopted a liberal attitude towards the enforcement of foreign judgment. Under its Foreign Judgment Act 1971, judgments of Chinese courts may be subject to the Act on several grounds, such as international comity or equality determined by the discretion of the courts. See Pryles, supra note 229, at 457.


255 It was reported that gross domestic growth of Taiwan may reach $350 billion in 10 years. Aus.Fin.Rev. 4 April 1990.
unique international law question. Bound by its treaty obligations to the PRC, the Australian Government cannot establish official ties with Taiwan Government. But impelled by the economic importance of Taiwan trade and investment, the Australian Government must provide adequate protection to Taiwanese investors who would not commit themselves without being provided with a legal guarantee of their rights in Australia. From the Taiwanese perspective, the investors need protection against not only infringement of their rights by Australian companies, but also possible claims by the PRC Government against their property in Australia. From the PRC perspective, Taiwan is an inseparable part of China, and therefore any direct dealing between the Australian Government and the Taiwan Government is contrary to the principles of the Australian-Chinese Friendship Treaty signed in 1972. The treatment of Taiwan business in Australia is thus a major concern of China. The issue is presently a political one, but it will have an added economic flavour soon or later when the PRC has to compete with Taiwan in Australian markets.

In the context of Australian foreign investment law, the Taiwan issue is twofold: how to treat a Taiwanese investor equally under Australian law given that his Government is not recognized by Australia, and how to protect his property in Australia from possible PRC’s claims given that the Chinese Government insists on its jurisdiction over Taiwan. In addition, the lack of official status in Australia makes a foreign investment in Australia particularly vulnerable in case of any legal proceeding. For these reasons, the federal Parliament passed the Foreign Corporations (Application of Laws) Act in 1989. The Act does not expressly mention Taiwan, but gives all protections needed by a Taiwanese company or investor who carries on business in Australia.

The protection provided to a Taiwanese company under the Act can be seen in two respects. First, a Taiwanese company can be treated as a foreign corporation in Australia.256 Thus all provisions relating to foreign investment under the FATA, TPA, ITAA and other relevant Acts are equally applicable to the Taiwanese company. In another words, a Taiwanese company cannot be discriminated against in Australia, in particular when it is involved in legal proceedings, merely because it

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256 This is achieved in three steps under the Act. First, s.3 defines a "foreign corporation" as a body or person incorporated in a place outside Australia", and Taiwan is a place outside Australia. Secondly, s.7(2) states that "whether a body or person has been validly incorporated in a place outside Australia is to be determined by reference to the law applied by the people in that place", and thus the status of a Taiwanese company should be determined by Taiwanese law. Thirdly, s.9(1) states that the application of this Act is not "affected by the recognition or non-recognition" of a foreign State or of a place by Australia, and Taiwan can be treated either as a State or place for this purpose. The first and second provisions can be applied to any foreign corporation, but the third one has particular interest to a Taiwanese company.
would generally otherwise lack official status in this country. Secondly, a Taiwanese company and its activities or assets are not subject to any form of claim or control by the PRC. Section 8 of the Act expressly indicates the intention of the Australian Government to reject any act or claim by the Chinese Government in relation to Taiwanese investment in Australia, but specifies neither Taiwan nor the PRC in its text.257 Under this section, if the Chinese Government bases any claim of a Taiwanese company on its jurisdiction over Taiwan, the claim can be recognized by an Australian court only when the claim is valid under Taiwanese law. Thus it is practically impossible for the Chinese Government to enforce a claim based on its law, such as expropriation measures, against any Taiwanese property in Australia. The application of section 8 also extends to the enforcement of judgments against a Taiwanese company or its property in Australia. The application of the Act in the case of Taiwan will attract criticism from the PRC based more likely on economic reasons than political reasons, because the PRC will certainly treat Taiwan as a strong competitor in, or threat to, its trade with Australia.

6.5. Conclusion

Both judicial and non-judicial means of dispute resolution are available in Australia and China. Although it has been accepted that non-judicial means of dispute resolution are a better way to resolve foreign investment and trade disputes than formal court proceedings, judicial means of dispute resolution are a necessary part of dispute resolution system in the two countries. While non-judicial methods of dispute resolution often provide advantages of saving time, reducing costs and maintaining good business relationships between the disputants, judicial means of dispute resolution may protect legal interests of the parties involved and provide legal remedies once non-judicial methods are unsuccessful. The importance of domestic courts in settling international commercial disputes is also seen in the requirement adopted in many international agreements that local remedies must be exhausted before resorting to international forum of dispute resolution, such as the International Court of Justice. Because of the importance of the courts of law in dispute

257 Section 8 states that

Where an act of a foreign State, or an entity of a foreign State:
(a) purports to affect a foreign corporation or its assets or dealings; and
(b) the act is based on, or derived from, the assertion of sovereignty or other authority over the place in which the foreign corporation was incorporated;
the act is not to be recognized, or in any given effect to, under Australian law unless it is recognized, and would be given effect to, under the law applied by the people in the place in which the foreign corporation was incorporated.
resolution, Chinese courts have considerably improved their role in international commercial dispute resolution in China.

Protection of Taiwanese investment in Australian against potential Chinese claims is not a present issue between Australia and China. The Chinese Government so far has not indicated any intention of claiming sovereignty over Taiwanese properties outside Taiwan. Such demand is simply impractical. None of China's trading partners in Western countries will give assistance to the enforcement of this demand. An attempt by the Chinese Government to make and to enforce any claim over Taiwanese property in Australia or any other industrialized countries will be detrimental to the already low-keyed trade relationships between China and these countries. The result will be destructive to China's goal of modernization. This explains why China has not and will not in immediately future raise question of sovereignty over Taiwanese investment in Australia, or any other industrialized countries. The legislative protection given to Taiwanese investment in Australia is mainly a concession to the Taiwanese Government which endeavours to achieve a kind of legal recognition from the Australian Government, and partly a fool-proof device to prevent any potential claims by the PRC in the future.
Chapter 7 The Australia-China Investment Protection Treaty

7.1. An Overview

Direct foreign investment has greatly increased in volume since the Second World War, not only between developed countries, but also between the developed and the developing countries. Promotion and protection of foreign investment have thus become a major concern of both capital-exporting and capital-importing countries. Common interests require them to seek mutually acceptable solutions for settling investment-related issues, which, if not dealt with properly, may damage relations between the countries involved and hinder the flow of international investment. Three commonly accepted approaches to the resolution of investment-related issues are multinational treaties, bilateral treaties and national legislation. These approaches will be reviewed in turn.

Attempts to reach uniform international conventions on the promotion and protection of foreign investment have been made by GATT, OECD and UN, as well as by some regional economic organizations, such as the EEC. Given the complexity of the issues and the conflicting interests involved, GATT so far has not reached any agreement on the issues. OECD, limited by the representation of the interests of its members, has not produced any proposals acceptable to most

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2 In the Uruguay Round, launched at the GATT Ministerial Meeting in Punta del Este in 1986, services, intellectual property and trade related investment measures were first time in GATT history listed in its agenda. As at December 1990, China was still not a member to the GATT. Some legal issues relating to China's participation in the GATT are discussed in R.E.Herzstein, "China and the GATT: Legal and Policy Issues Raised by China's Participation in the General Agreement on Tariffs and Trade" (1986) 18 L. & Pol.Int'l Bus. 371.

3 The OECD countries adopted a Declaration on International Investment and Multinational Enterprises in June 1976. The Declaration is intended to promote cooperation among Member countries in the area of international investment and to encourage the operations of multinational enterprises in the Organization.

4 The UN has engaged in many activities aiming at the promotion of international investment. For example, UNCTC has carried out a Transnational Technical Program, see S.Asante & R.Brown, "The Negotiation With Transnationals: the Technical Assistance Programme of UNCTC" (1988) 16 Int.Bus.Lawy. 425; and a UN Code of Conduct on Transnational Corporations is currently undergoing study. A discussion on this Code is found in UNCTC, supra note 1, at 229.

5 The Single Market Programme of EEC creates favourable climate for investment, although investment is only one of the areas where the EEC countries have taken substantial measures of cooperations, mainly by deregulation.
developing countries. In terms of multilateral treaties, the Washington Convention, initiated by IBRD, is so far the most successful international convention on the protection of foreign investment. Under this Convention, the International Centre for Settlement of Investment Disputes (ICSID) was created for the purposes of resolving disputes between States and private parties of other member States. Initiated also by the World Bank, the Multilateral Investment Guarantee Agency (MIGA) was established in 1985. The Agency provides not only guarantees against non-commercial risks in its member countries to foreign investors, but also provides advisory services to its members for the purposes of encouraging equity or other direct investment flows to developing countries. In 1989, 52 countries had become the members of MIGA. Given their important roles in settling disputes arising from investment activities between the developed and developing countries, ICSID and MIGA will be examined further.

The main function of ICSID (Centre) is to provide a forum for the peaceful settlement of investment disputes between a contracting State and nationals of other contracting States. This type of disputes has been a cause of many political, diplomatic and - in earlier times, at least - even military conflicts between capital-exporting and capital-importing countries. The Centre provides arbitration and conciliation services to member States, which have decided to submit either a given

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8 As at 30 June 1989, the Convention had been signed by 15 capital-exporting countries and 58 capital-importing countries. Of them 52 countries had ratified the Convention. The World Bank, id, at 103-4.
9 Investment-related disputes between governments of developing countries and private investors of developed countries sometimes resulted in military invention by the governments of the investors. For example, the 'Jecker' claim between a Swiss-French banking corporation and Mexico ended by an armed intervention by the French Government in Mexico in 1861-2. Some Latin American countries reacted to such intervention by proposing the 'Drago Doctrine', which purported to prohibit the use of force for collecting the public debt of Latin American countries, and later the 'Calvo Doctrine', which aimed at restricting the rights of foreign private investors to seek diplomatic protection from their home governments and providing local system as the forum for dispute resolution. See, I.Shihata, "Towards a Greater Depoliticization of Investment Disputes: The Role of ICSID and MIGA" (1986) 1:1 Foreign Investment Law Journal 1, 1-2; and M.Z.Yao, "Legal Protection of International Investment" in the Chinese Society of International Law, ed, Selected Articles From Chinese Yearbook of International Law (Beijing, China Translation & Publishing Corporation, 1983) 147, 169-72.
dispute or a particular class of disputes to the jurisdiction of the Centre.\textsuperscript{10} The flexibility of the Centre can also be seen in its arbitration rules, which become applicable only when no objection has been raised from the disputants. However, once the contracting parties decide to resort to the ICSID machinery, the jurisdiction of the Centre over the given dispute is seen to be exclusive of any other remedy.\textsuperscript{11} At the end of 1989, 98 States had signed the Convention, and 91 had ratified it.\textsuperscript{12} Australia is among the 7 countries which have signed but not yet ratified the Convention. At December 1990, China had not signed the Convention.

The Convention\textsuperscript{13} establishing Multilateral Investment Guarantee Agency was opened for signature by the World Bank in 1985. The Convention has become operative since it has been ratified by 5 capital-exporting and 15 capital-exporting countries whose subscriptions exceed 1/3 of MIGA's authorized capital. The Agency started to provide guarantees in 1989 and had received 15 definite applications for guarantee at end of June 1989, covering investment in 11 countries.\textsuperscript{14} Under the Convention, the Agency obtains rights of subrogation against a host country which is a party to the Convention, once the agency has paid an insured who has suffered damages from the specified non-commercial risks. The contracting States are bound by the Convention to settle the claims with the Agency through either consultation or international arbitration. Thus the Convention seeks to replace the existing investment guarantee programs provided unilaterally by some capital-exporting States to their nationals.\textsuperscript{15}

The unilateral investment guarantee program, as an approach to settlement of investment disputes, is an attempt by the governments of capital-exporting countries to promote their foreign trade and protect the interests of their nationals. The program was first provided by the United States Government, and was followed by

\textsuperscript{10} Under the Convention, the mere ratification of the Convention does not constitute an obligation to use the Centre.

\textsuperscript{11} For detailed study of the operation of ICSID, see Shihata, supra note 9, at 3-12.

\textsuperscript{12} ICSID, 1989 Annual Report, at 14.

\textsuperscript{13} See (1985) 24 ILM 1605.

\textsuperscript{14} The Agency requires an applicant first to file a preliminary application and then a definite application for guarantee. As at June 1989, the Agency had received 69 preliminary applications for guarantees against noncommercial risks in 24 member countries and 21 preliminary applications concerning investment in 15 non-member countries. The World Bank, supra note 7, at 103.

\textsuperscript{15} For details on MIGA, see Shihata, supra note 9, at 13-24.
several developed countries, such as the Federal Republic of Germany and Japan.\textsuperscript{16} The program, varying in different countries,\textsuperscript{17} operates in most countries on the basis of a two-tier system. First, capital-exporting countries sign bilateral investment guarantee agreements with other countries, which recognize the rights of subrogation of the designated authorities of the contracting countries in respect of claims against each other.\textsuperscript{18} Secondly, a designated authority or agency of a contracting country provides insurance against political risks to its nationals who have invested in the other contracting country. Once a claim has arisen, the designated agency compensates the insured according to the terms of the insurance contract, and then is subrogated in respect of the claim against the other contracting government.\textsuperscript{19} This is still the way investment guarantee programs operate in most countries.\textsuperscript{20}

The Australian Overseas Investment Insurance Scheme, introduced initially by the Export Payment Insurance Corporation Act 1965 (Cth), represented a different model of unilateral investment guarantee program. The US program aimed at protecting the interests of Americans investing in foreign States.\textsuperscript{21} But the Australian scheme emphasizes "export trade and other foreign transactions."\textsuperscript{22} In addition, the operational system of the Australian Scheme is not subject to bilateral investment guarantee agreements such as those entered into by the United States. Under the Export Payment Insurance Corporation Act 1965 (Cth), the Export Payment Insurance Corporation, which was set up in 1956, provided insurance

\textsuperscript{16} Yao, supra note 9, at 154-63.

\textsuperscript{17} The program operating in the United States before the 1960s covered both non-commercial and commercial risks, but the commercial risks were subject to a number of conditions. By contrast, the Schemes, adopted by Australia, Federal Republic of Germany and Japan, were available to non-commercial risks only. G.Philips, "Insurance of Overseas Investment - The Australian Scheme" in J.Starke, ed. The Protection and Encouragement of Private Foreign Investment (Sydney, Butterworths, 1966) 119, 122.

\textsuperscript{18} For example, the United States-Canada Investment Guarantee Agreement, see UNCTC, supra note 1, at 5.

\textsuperscript{19} Yao, supra note 9, at 156.


\textsuperscript{21} Yao, supra note 9, at 155-60.

\textsuperscript{22} Phillips, supra note 17, at 120.
against non-commercial risks to Australian businesses engaged in export of Australian goods or involving overseas investment transactions. Although the Export Payment Insurance Corporation Act was repealed in 1974, the scheme continued to operate under the Export Finance and Insurance Corporation Act 1974 (Cth). In 1985, the Export Finance and Insurance Corporation was replaced by the Australian Trade Commission, created under the Australian Trade Commission Act 1985 (Cth). The Commission provides overseas trade insurance and reinsurance services, overseas investment insurance services, and financial services to Australian businesses. Under the 1985 Act, insurance is available for all kinds of risks, commercial and noncommercial, at the discretion of the Commission. The so-called Overseas Investment Insurance Scheme has thus been gradually replaced by a more general insurance scheme, which is available for activities relating to both foreign investment and foreign trade. The distinction between the Australian scheme and the programs in other countries, such as the United States and Japan, is that the Australian Government has not formally incorporated the machinery of diplomatic protection and the rights of subrogation into its investment guarantee scheme, although it would be able to use the diplomatic channel to press its claims after compensation had been made to the insured. The reason for the purely unilateral approach taken by Australia could be that Australians have not invested heavily in some of the politically risky areas, such as Africa, Latin America, and Vietnam. There is thus little need to confront the possible difficulties of negotiating bilateral agreements with these countries. In addition, even if investments have been made in risky areas, such as Eastern Europe and China, there exist treaties of economic cooperation which may provide limited assistance in case diplomatic protection is needed.

The bilateral investment protection treaty, as a type of treaty specifically dealing with matters of investment, was again developed after the Second World War in the practice of the United States, which between 1946 and 1956 signed some 16

23 For details, see Phillips, id, at 119-136.

24 There are economic cooperation treaties between Australia and a number of Eastern European countries, e.g. the Australian-Bulgarian Trade Agreement, Aus.T.S. 1974 no.32, the Australia-East German Trade Agreement, Aus.T.S. 1974 no.7 and the Australia-Hungary Trade Agreement, Aus.T.S. 1974 no.25. There is also the investment protection treaty between Australia and China, which covers issues of expropriation and nationalization.

Friendship, Commerce and Navigation (FCN) treaties with its trading partners. However, the practice of using bilateral treaties to protect investment is not a new phenomenon. The FCN treaties were developed on the basis of the conventional treaty of amity, commerce and navigation, which was adopted several hundred years ago for the purposes of promoting trade relations, protecting shipping, and safeguarding nationals and their interests according to mutually acceptable principles. The treaty of amity, commerce, and navigation, and similar instruments such as the treaty of commerce, were commonly used by European countries. The earliest British commercial treaty was made in 1217 with Norway, and the first British commercial treaty which was applicable to Australian colonies was the Treaty of Commerce with Denmark signed in 1661. But FCN treaties were the first type of treaty that directly (although in broad terms) addressed the issues of foreign investment, such as the legal rights of foreign corporations, the protection of investments, state immunity and dispute settlement. The FCN treaty was accepted by several capital-exporting countries, such as the Federal Republic of Germany, the United Kingdom, Japan and Switzerland, in the 1960s, but is no longer being negotiated today. Instead it has been replaced by the investment promotion and protection treaty, an expression first used in the bilateral treaties signed by Federal Republic of Germany in the 1960s. Most treaties within the present bilateral treaty network for the protection of foreign investment are titled bilateral investment promotion and protection treaties, although they may be based on various models, such as the models used by Federal Republic of Germany, Netherlands and the United States, or the models proposed by the Asian-African Legal Consultative Committee (AALCC).

27 Walker, id, at 58.
28 E.Nwogugu, The Legal Problems of Foreign Investment in Developing Countries (Manchester University Press, 1965) 121.
29 Dept. of Foreign Affairs, Aus.T.S. (1971) no.1, at 34.
30 Nwogugu, supra note 28, at 121.
31 UNCTC, supra note 1, at 4.
32 Yao, supra note 9, at 165.
The Australia-China Investment Protection Treaty was signed in Beijing on 11 July 1988 and entered into force on the same day.³³ This is the first such treaty signed between Australia and China, although a trade agreement was signed between them in 1973.³⁴ The Treaty consists of 17 Articles, covering major issues of investment protection, such as the treatment of investment, the convertibility of investment-related funds, limitations on state immunity, expropriation and dispute settlement. This is the first bilateral investment promotion and protection treaty signed by Australia, although there is an Australia-Turkey Agreement on Trade, Economic and Technical Cooperation³⁵ which deals with issues of foreign investment to a limited extent. By contrast, there are more than 18 investment promotion and protection treaties between the Chinese Government and foreign countries.³⁶ The Australia-China Investment Protection Treaty stands as part of the present international bilateral treaty network for investment protection, which consists of over 260 bilateral treaties today.³⁷

The Australia-China Investment Protection Treaty was a result of the rapidly expanding economic contacts between Australia and China (up to 4 June 1989). As a bilateral treaty between a developed and a developing country, the Treaty is inevitably affected by both the treaty models preferred by developed countries, such as the United States, and the models recommended by the AALCC, which represent developing countries' views of international law. The features and potential conflicts between Australia and China in the context of the Treaty will be examined in the following sections.


³⁶ As at mid-1987, China had signed bilateral investment promotion and protection treaties with Austria, Belgium-Luxembourg, Denmark, France, Federal Republic of Germany, Finland, Italy, Kuwait, Netherlands, Norway, Romania, Singapore, Sri Lanka, Sweden, Switzerland, Thailand, and the United Kingdom. See UNCTC, supra note 1, at 131-2.

³⁷ As at mid-1987, there were over 265 bilateral investment promotion and protection treaties throughout the world. UNCTC, id, at 7.
7.2. Treaty Definition of Nationals

The definition of "national" is an important issue in the Treaty, where the term "national" appears more frequently than "company", in particular in some crucial provisions such as the provisions on immunity. Under the Treaty, "national" includes both a natural person, who is either a citizen of or a permanent resident in Australia or China, and a company incorporated under the law of Australia and China. The status of a natural person (citizen or permanent resident) is determined in accordance with the domestic law of Australia or China, as the case may be. So are the legal requirements for establishing a company, which in the context of the Treaty refers to any "corporation, association, partnership, trust or other legally recognized entity that is duly organized" under the laws of Australia and China.

The concept of "company" also extends to any such bodies established under the law of a third country but controlled either by a company or by a citizen (or permanent resident) of Australia or China. The extension of "national" to companies bears the marks of the Dutch Model Agreement on Encouragement and Reciprocal Protection of Investment revised in 1987.

Although the status of a natural person and the establishment of a legal entity are subject to the domestic law of Australia or China, the Treaty has not avoided the possibility that the two countries may have overlapping jurisdiction over the same natural person or company under certain circumstances. For example, the Nationality Law of the PRC neither recognizes dual nationality, nor distinguishes between citizenship and the status of permanent resident. If a Chinese citizen who has a permanent resident status in Australia invests in China, the problem could arise as to whether the investment falls within the scope of the Treaty, and in the case of expropriation whether the person should be treated as a Chinese or an Australian. If he is seen as a Chinese, he will not be eligible for the protection under the Treaty. Similar problems could arise when a company is established under the law of a third country but controlled by a Chinese citizen who is also an Australian permanent resident. The Treaty itself does not directly address these issues.

38 Treaty, Art.VII.
39 Treaty, Art.II(d).
40 Id, Art.II.
41 Ibid.
42 The text of the Model Agreement can be found in UNCTC, supra note 1, at 175.
43 Statutes and Regulations of PRC (University of East Asia Press and Institute of Chinese Law (Publishers) Ltd) no.800910.2.
Three ways of resolving these conflicts may be suggested. First, the person concerned may have to consider whether to give up his Chinese citizenship or submit himself to the jurisdiction of the Chinese Government. Under the present legal framework for foreign investment, a foreign national enjoys more privileges and preferential treatment than a Chinese national. Thus, if the Chinese Government refuses to extend these privileges to Chinese overseas who have Chinese passports, these Chinese will have to renounce their Chinese citizenship in order to be eligible for the privileges. None of these options is likely to result in any increase of foreign investment in China, but, rationally, encouraging Chinese overseas to maintain their Chinese citizenship would be likely to bring potential or additional benefits to China.

Another possibility is that the Chinese Government may amend its immigration law, clarifying the status of a Chinese citizen who is also a permanent resident of a foreign country. But it is unlikely that the Chinese Government would make this change, unless investment involving Chinese nationals overseas becomes such a significant factor in China's economic development that it is effectively impelled to do so.

Thirdly, Australia and China could negotiate a new provision dealing with the status of such permanent residents. Thus, either the citizenship prevails over the status of permanent resident, or the status of permanent resident prevails over citizenship. The argument supporting the dominance of citizenship is that nationality has been a traditional ground for diplomatic protection in international law. As the Permanent Court of International Justice in the Panevezys-Saldutiskis Railway Case said "in the absence of a special agreement, it is the bond of nationality between the State and individuals which alone confers upon the State right of diplomatic protection".44 In addition, consideration for sovereignty could also support the predominance of citizenship.45 By contrast, the case supporting the dominance of permanent resident status, from the Chinese point of view, is that the decision so made will force Chinese overseas who prefer to retain their Chinese citizenship to give up Chinese passports for the sake of Treaty benefits. Such provisions will not have the effect of attracting more foreign investment. Instead, China will lose relevant benefits associated with the tie of nationality between the Government and Chinese overseas.46

44 PCIJ Series A/B no.76, at 16.
46 The benefits to the Chinese Government are jurisdiction over such Chinese overseas, and economic contributions from Chinese overseas whose patriotic feeling may be strengthened by their Chinese citizenship.
7.3. Treatment of Investment Under the Treaty

7.3.1. The Principles of Treatment Adopted in the Treaty

The Treaty adopts three basic principles in dealing with issues of the treatment of investment. These are "most-favoured-nation treatment", "fair and equitable treatment" and "non-discrimination". Under the Treaty, Australian and Chinese Governments have obligations to "ensure fair and equitable treatment" to the investments of each other's nationals; to apply non-discriminatory measures to the management, maintenance, use, enjoyment or disposal of investments by each other's nationals; and to treat the issues of compensation, transfer of investment-related funds and of other relevant activities of each other's nationals "on a basis no less favourable than that accorded to investment and activities associated with investments of nationals of any third country".47 But the "most-favoured-nation" provision is subject to any exceptions made in special bilateral or multilateral regional arrangements for economic cooperations or in a double tax treaty with a third country.48 The Treaty does not define "fair and equitable treatment", "non-discrimination" and "most-favoured-nation treatment".49 However, their meaning can be derived from common usage as accepted in general international practice.

7.3.2. Meaning of "Fair and Equitable Treatment"

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47 Treaty, Arts.III, VIII & X.

48 Treaty, Art.III(c) states that a contracting party is not obliged to extend its preferential treatment agreed in "any customs union, economic union, free trade area or regional economic integration agreement to which the contracting party belongs" to the investment of the nationals of the other contracting party. This provision seeks to draw a line between the benefits given to investment under ordinary investment promotion and protection treaty and benefits available to investment made under special economic and trade agreements, which may be regional. Such regional economic and trade cooperations can sometimes be made between two countries, such as the Australia-New Zealand Close Economic Relation Agreement which in fact establishes a free-trade zone between the two countries, and can also be made among a group of countries, such as EEC community. The distinction between ordinary treaty benefits and restrictive treaty benefits is, probably, the substance of the treaty but not the type of the treaty (bilateral treaty v multilateral treaty). If a treaty covers a wide range of economic, trade and investment issues, it will probably fall within the exceptions under Art.III(c).

49 For general discussions of these principles, see K.Hyder, Equality of Treatment and Trade Discrimination in International Law (Hague, Martinus Nijhoff, 1968); H.M.Catudal, "The Most-Favoured-Nation Clause and the Court" (1941) 35 Ame.J.Int'l L. 41; G.Schwarzenberger, "The Most-Favoured-Nation Standard in British State Practice" (1945) 22 B.Y.B.Int'l L. 96; Seyid Muhammad, The Legal Framework of World Trade (London, Stevens & Sons Ltd, 1958).
"Fair and equitable treatment" is a common expression in bilateral and multilateral treaties. The term does not have a precise and fixed meaning, at least not in the way that "most-favoured-nation treatment" does. The term is subjective and relative. The relativity can be seen in the concept of "equitableness" which must be decided in a comparative context. "Equitableness" requires a subject to be brought in for comparison.

In the context of a bilateral treaty, the question is whether "fair and equitable treatment" should be judged against international law or national law. Fairness and equitableness under the national law may not be fair and equitable under international law. Since an investment promotion and protection treaty is an international treaty, "fairness" and "equitableness" in relations to treatment of foreign investment must be decided by international law. Accordingly, the term "fair and equitable treatment" in a bilateral treaty imposes an obligation on the contracting parties to implement the measures of treatment in accordance with international standards.

But such an "international standard" is again rather a subjective, relative and controversial criterion than a certain and unambiguous test. States sometimes disagree upon the substance of the international standard in a given case. Unlike the notion of "most-favoured-nation treatment", which is a requirement imposed on the manner of the performance, the principle of "fair and equitable treatment" emphasizes the obligation of the contracting parties to evaluate their performance by the substantive criteria of "fairness" and "equitableness".

7.3.3. Meaning of Non-Discrimination

"Non-discrimination" in bilateral treaties is associated with the notions of "fair and equitable treatment", "national treatment" and "most-favoured-nation treatment". "Discrimination" requires a ground of comparison. Thus, discrimination against investors of a contracting country exists when they are not treated equally to investors from a third country or nationals of the recipient country. In fact, "non-

50 The objective standard of the "most-favoured-nation treatment" is to extend the most favoured treatment, which is available to a third country, to the nationals of a contracting country to which the host country promised to give the "most-favoured-nation treatment".


52 Under this principle, the obligation of a contracting State is to make the benefits given to a third country under the conditions similar to those governing the treaty, from which its obligation arises, available to its treaty partner, regardless of the substance of the benefits.
"discrimination" can be regarded as the negative criterion, by contrast with the positive principles of "fair and equitable treatment", "national treatment" and "most-favoured-nation treatment"; and it imposes an obligation on a contracting country not to adopt any measure which is discriminatory against the investors of the other contracting country.

Sub-committee I of the International Committee on Legal Aspects of a NIEO suggested that the non-discrimination principle means that equal cases should be treated equally and unequal cases unequally. It argued that whether cases are equal or not should be determined in view of the objectives of rules or policies concerned. In the context of the New International Economic Order, this means that whether discrimination exists should be judged against the principles and purpose of the NIEO, treating developing countries favourably in proportion to their level of development. But in the context of a bilateral treaty, this could mean that equality or inequality of cases should be determined by the objectives of the treaty involved and of the relevant policies of the country which is obliged to apply the non-discrimination principle. The Committee's view reflects one aspect of non-discrimination principle. Another feature of non-discrimination is that its meaning may vary (i.e. the degree of discrimination may vary) in comparison with the treatment of nationals of the host country, or of nationals of the most-favoured-countries (when the contracting States grant "most-favoured-nation treatment" to each other), and with international standards which have not been met by the host country. Thus, a measure may be regarded as discriminatory in the context of national treatment, but may be non-discriminatory in the context of "most-favoured-nation-treatment". Broadly, the idea of "non-discrimination" requires a contracting country to treat the nationals of the other contracting country in the same way as its nationals or nationals of a third country (in case of "most-favoured-nation treatment"). When the practice of the host country is consistent with international standards, "non-discrimination" does not cause problems between the contracting countries, regardless of the substance of the treatment. But when treatment does not meet international standards, mere equality between the nationals of the other contracting country and nationals of the host country, or between the nationals of the

53 Schwarzenberger observed that most-favoured-nation treatment "requires the absence of discrimination as compared with third states. It does not imply either national or reciprocal treatment of the beneficiary". See Schwarzenberger, supra note 49, at 96.

other contracting country and nationals of any third country, would be insufficient to protect the interests of the investors belonging to the other contracting country.

"Non-discrimination" requires the equal treatment of foreign investors in a recipient country. Its application must be supported by "fair and equitable treatment". The two principles are separate but yet related. A measure satisfying the requirement of "non-discrimination" does not always meet the standards of "fair and equitable treatment". Thus "equal treatment" in the notion of "fair and equitable treatment" implies the ideas of "non-discrimination", in particular in the substance of a given measure.

7.3.4. Meaning of Most-Favoured-Nation Treatment

The notion of "most-favoured-nation treatment" means that whenever one contracting party agrees on more favourable terms with a third State, the other contracting party (to the first treaty) will benefit from the new, more favourable terms. This principle is often subject to the restriction, in particular in bilateral treaties, that the rights and obligations arising from the second treaty must be comparable with those derived from the first treaty. Since reciprocity and mutual benefits are the basis of a bilateral treaty, no State is willing to extend treaty benefits associated with a specified mutual commitment unconditionally to a third party which has not made the same commitment, except when a State unilaterally decides to provide a benefit, e.g. abolishing import duties on a specified product, to all nations. Thus, "most-favoured-nation treatment" involves treating alike the contracting countries which have made the same arrangements with the host country.

Compared with notions of "non-discrimination" and "fair and equitable treatment", "most-favoured-nation treatment" is more certain and less ambiguous. As long as a host State treats its treaty partners according to the most favourable terms applicable to them, its treaty obligation is deemed to have been fulfilled, regardless of whether the terms so provided are up to international standards in other

55 Assuming, for example, that there are only two paper-mill joint ventures in China, one from Canada and the other Australia. The Chinese Government treats both equally, but also badly in comparison with international standards. This certainly contradicts the notion of "fair and equitable treatment", but does not literally contradict the notion of "non-discrimination" or even the "most-favoured-nation treatment". Obviously, "non-discrimination" in the national setting has been achieved but in the international perspective has not.

56 UNCTC, supra note 1, at 48.
respects. In addition, some restriction on the application of "most-favoured-nation treatment" has been commonly accepted in international practice, greatly reducing potential disputes in the implementation of the "most-favoured-nation" clause. Given the fact that most-favoured-nation treatment may mean that treating a State "on a footing not inferior to that of the most favoured third State", this principle probably allows foreign investors to receive the most favourable terms which could be available to them in a particular country.

7.3.5. Issues Relating to the Application of the Principles

The three principles of treatment of foreign investment are designed to be supplementary to each other. In general, the fulfilment of one or two principles by a contracting State is not good enough. For example, in the case of the transparency of law and policies, a State cannot be regarded as having fulfilled its treaty obligation by treating all foreign investors equally but yet without transparency of its law and policies. A policy which is internal and thus inaccessible to foreign investors (though equally inaccessible to all of them) can be regarded as "non-discriminatory" and as satisfying the principle of "most-favoured-nation treatment", but may still conflict with the Treaty obligation to guarantee the transparency of their laws and policies.

But sometimes, fulfilment of the three principles together at the same time could be a difficult task. For example, in the case of war or armed conflict, the obligation of the contracting parties is to give "most-favoured-nation treatment" and not to discriminate against the nationals of other countries who have suffered losses from the specified events. Performance by contracting countries cannot be judged against a narrow explanation of "fair and equitable treatment" that does not take the ability of the host country to pay into account, when the host country and investing country cannot reach an agreement on the meaning of "fair and equitable treatment" in this case. Thus the Treaty in fact exempts the parties from the absolute obligation.

57 Schwarzenberger commented that the most-favoured-nation treatment "does not demand compliance with any definite and formal rules of conduct". supra note 49, at 96.

58 For example, Australia-China Investment Protection Treaty restricts the "most-favoured-nation" clause from being applied to the benefits under customs union, economic cooperations, free trade or regional economic cooperations, and double tax treaties. Art.III(c).

59 Schwarzenberger, supra note 49, at 96.

60 Treaty, Art.VI.

61 Treaty, Art.IX.
to compensate by stipulating that a contracting party extends to the nationals of the other contracting country treatment "no less favourable than that accorded to nationals of any third country, should it adopt any measures relating to such losses".62 This provision has two meanings. First, the Treaty implies that the contracting parties do not have an unconditional obligation to make compensation in such cases. The principle of "most-favoured-nation treatment" is applicable only when the contracting countries take "any measures relating to such losses". Secondly, "any measure" does not literally mean measures of compensation; it could well refer to measures of non-compensation. Such decision does not conflict with the principles of "most-favoured-nation treatment" and "non-discrimination", although nor does it often stand together with the principle of "fair and equitable treatment". But after all, the Treaty allows the contracting countries either not to take any measure or to take "any measure". "Fair and equitable treatment" in this particular provision is evaluated by taking the country's ability to pay, and thus could become an issue between the countries concerned.

The supplementary character of these principles can be seen however, in the fact that the specification of one principle in most provisions does not exclude the application of other principles in the same provisions. For example, Article VIII of the Treaty requires the contracting parties not to discriminate in the case of expropriation and nationalization. But "non-discrimination" here also suggests the "most-favoured-nation treatment" and may imply "fair and equitable treatment". In fact, the provision states that expropriation or nationalization of investment is allowed with "reasonable compensation" only on the grounds of public interest. In addition, it should be carried out in a non-discriminatory manner, and decided in accordance with the law of the host State. This requirement imposes an obligation on the host State to apply the law fairly and equally. So does "reasonable compensation". Clearly, the principles of "non-discrimination" must be supported by the other principles.

7.4. The Governments' Responsibilities Under the Treaty
7.4.1. Encouragement of Investment

Article II of the Treaty requires the Australian and Chinese Governments to encourage and promote mutual investments between them. This responsibility is subject to the law and policies of the two countries. This means that either of them has the right to decide what type of investment it prefers, and to what extent it allows foreign investment to operate in a given case. The responsibility cannot be

62 Ibid.
regarded as unfulfilled by the mere fact that a country restricts, or refuses to approve, a particular investment project, as long as the decisions so made are consistent with the prevailing law and policies of the contracting parties, which are fair, equitable and non-discriminatory.

The responsibility under Article II does not extend to the case of "treaty shopping". Thus, if a company incorporated under the law of either Australia or China is controlled by a national of a third country, which has no substantial business activities in the country of incorporation, the recipient country may refuse to admit the investment of such companies. In another words, the parties do not have to treat such companies in accordance with the principles of treatment mentioned in the Treaty. The criteria for identifying such companies is twofold: whether a company is controlled by a non-Australian or a non-Chinese national, and whether it has substantial business in Australia or China. A company controlled by a national of a third country may be ineligible for the treaty benefits only when it does not carry on substantial business in the contracting countries. The criterion so adopted bears more the marks of Australian law than Chinese law, because foreign-controlled companies are an Australian concept, which does not have practical significance in Chinese law. The practical implication of this provision is that a solely foreign-owned enterprise or joint venture controlled by foreign investors incorporated under Chinese law may be excluded from the treaty benefits when investing in Australia, if the enterprise does not have substantial business in China. Similarly, a foreign-controlled Australian company which does not carry on substantial business in Australia cannot be protected by the Treaty when investing in China. It is too soon to evaluate the actual impact of such exclusion on the investment in each country by the investors who are thus ineligible.

7.4.2. Responsibility to Facilitate Entry and Sojourn of Personnel

Article IV of the Treaty imposes a "soft" obligation on a contracting country to permit the nationals or employees of the companies of the other contracting country to enter and remain in its territory for investment-related activities. This

63 For example, in the FATA and ITAA, some definitions of companies controlled by foreign interests are provided. Foreign-controlled companies are sometimes treated differently from Australian-controlled companies under Australian law.

64 Chinese law does not really distinguish between foreign-controlled enterprises and the joint ventures with majority share controlled by Chinese interests. Differences between these enterprises in taxation are insignificant. In addition, there is no maximum limit on foreign investment in joint ventures. Nor is there any sign that the Chinese Government wants to distinguish joint ventures controlled by foreign interests from those controlled by Chinese interests.
obligation is "soft", because the permission so rendered is subject to national immigration law and policies, which appear to be well beyond the reach of the Treaty. A contracting country, of course, has a treaty obligation to adopt laws and policies which are applicable to the nationals (and their employees) of the other contracting country in a fair, equitable, and non-discriminatory manner. But the "fairness and equitableness" of immigration law and policies would not involve any privilege or special treatment being given to the other contracting country for the purposes of investment. The Treaty does not create any substantial obligation for Australia or China to give special treatment in relation to immigration matters, except a promise not to treat the nationals and personnel employed by the nationals of the other contracting country in a manner inconsistent with the law and policies of the host country, whatever that law and these policies are.

But the same Article also imposes a strict obligation on a contracting party to allow the nationals of the other contracting party to employ any person of their choice. 65 Although this sub-clause is subject to the previous sub-clause, which does not grant a right of automatic entry and sojourn (not even "sympathetic consideration" as agreed in some of the treaties signed by Federal Republic of Germany) to the nationals of the other contracting country, it imposes a strict obligation that a contracting country cannot refuse the employment of personnel working for the nationals of the other contracting country on the basis of "nationality" (citizenship). This provision is more significant in China than in Australia, because Chinese governments (both central and local) have special regulations and policies regarding the employment of Chinese nationals by foreign-

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65 Treaty, Art.IV2.
related enterprises. Under the Treaty, the Chinese Government has an obligation not to restrict the employment of Chinese nationals by Australian nationals (including companies) on any ground which is associated directly or indirectly with its jurisdiction over the employees by reason of their citizenship.

7.4.3. Transparency of Law and Policies

Article VI of the Treaty requires a contracting country to guarantee the "transparency" of its law and policies affecting the investment of the other contracting country. As a matter of fact, "the transparency of laws" is more or less a metaphor. The obligation in relation to the transparency of law and policies consists of three requirements: access to the law and policies, a promise to provide a copy of such laws and policies on request, and readiness of one country to give an explanation to the other with regard to its laws and policies. Nothing is specifically said about substantial "transparency", which means, presumably, that Australian and Chinese Governments should have the responsibility to make their laws and policies certain, clear and unambiguous. Apparently, the Governments were not prepared to commit themselves to the real transparency of law and policies, which could be a restraint on the flexibility on the Government's legislative or discretionary power in relation to control of foreign investment. Maintaining the maximum flexibility could thus be, inter alia, a reason for not assuming responsibilities to make their law and

66 There is little coordination between the national legislation or policies and local regulations in relation to labour management. For example, the State Council issued in 1988 an Opinion on the right of foreign-related enterprises to employ Chinese nationals, allowing foreign-related enterprises to employ Chinese nationals through "open recruitment". (Implementation of the Right of Autonomy of Foreign Investment Enterprises in Their Use of Personnel, CCH, China Laws for Foreign Business para.12-606). This document seems to suggest that no restriction on the procedure and candidates for the employment should exist. But in fact, some local governments, such as the Beijing Municipal Government, require certain foreign-related enterprises to recruit their employees through the foreign service units designated by the local government. (e.g. Provisional Measures for the Administration of the Registration of Employment of Foreign Enterprise Representative Offices Stationed in Beijing, CCH, China Laws for Foreign Business para.12-586). Similarly, in Shanghai, foreign enterprises are not allowed to recruit persons who resigned their positions in a State-owned enterprise or working unit without approval by the enterprise or the unit, or university students who have not finished their studies. The foreign enterprises must apply to the Municipal Labour Management Bureau when recruiting from other provinces. See Y.Z.Chen, "Legal Issues Relating to Recruitment of Foreign-Related Enterprises" (1989) 1:1 Law Science (Fa Xue, in Chinese) 45. These facts suggest that some sort of restriction does exist in China. The basis for such restriction is, of course, the jurisdiction of the Chinese governments and various State-owned enterprises over Chinese citizens who work for the State-owned enterprises. For general discussion on Chinese labour law, see H.Zheng, China's Civil and Commercial Law (Singapore, Butterworths, 1988) 366.
policies "transparent". In addition, a transparent law and policy is more vulnerable to criticism based on the accepted principles of treatment of foreign investment than a general or vague law or policy. This probably explains why no country is willing to commit itself fully to the responsibility of providing the real transparency of law and policies. In any event the complexity of foreign investment law and policies means that to seek complete transparency of law and policies in relation to foreign investment may be a practically fruitless task. As far as the transparency of law and policies is concerned, neither Australian nor Chinese Government has been free from criticism.  

7.4.4. State Responsibility and Nationalization
7.4.4.1. Provisions on Expropriation and Nationalization

Article VIII of the Treaty deals with issues of expropriation, nationalization and other similar measures (indirect expropriation). Under this Article the contracting parties promise not to take measures of expropriation or nationalization and similar actions against each other's investment unless they are required for the public interest, carried out in a non-discriminatory manner in accordance with the law of the host country and accompanied with reasonable compensation. The differences

67 The degree of transparency expected or seen as possible or desirable depends upon the views of observers and, more often than not, some measures of investment law and policy would become unsuitable before the time allows the law and policy to evolve into a relatively high stage of transparency.

68 For example, the Australian Government was criticised for the uncertainty of its policies in dealing with some foreign investment projects. See "Japanese Want Clear Investment Guidelines" SMH 15 March 1989; and "Wesley Vale Stand Off Sends Mixed Message to Investors" Aus.Fin.Rev. 16 March 1989. The Chinese Government has been criticised many times on its use of internal rules and vagueness of its regulations and policies. A.Tay, "Introducing China's Business Laws and Practices" CCH, China Laws for Foreign Business, paras.2-260 & 2-265.

69 Treaty, Art.VIII.
between expropriation and nationalization or indirect expropriation, are not significant in this Treaty, because the same rules apply to both.

(1) Public Interest As Basis of Nationalization

The lawfulness of nationalization, expropriation or similar actions is, according to common international practice, subject to the requirement that the action must be in the public interest, non-discriminatory, consistent with the law of the expropriating country and subject to reasonable compensation. "Public interest" is a commonly accepted ground for expropriation and nationalization by a State. But "public interest" is a notion with uncertain content, because so many factors affect the meaning of "public interest", which vary not only from State to State, but also in different periods of time within each State. Thus, it is noted that "there is no agreed definition of 'public purpose' in international law nor is there a standard definition common to all national legal systems". Indeed, some international lawyers have sought to exclude causes associated with the socialist countries, such as the Soviet Union, from the recognized meanings of "public interest". But they were unsuccessful in restricting the use of "public interest" by the socialist countries as

70 For example, G.White defines "nationalization" as a measure "which sets in motion a legal process whereby private rights and interests in property are compulsorily transferred to the State or to some organ created by the State, with a view to the future exploitation of those rights and interests by and for the benefits of the State". According to , a technical difference between nationalization and expropriation lies "in the duration of the process of transfer which they respectively authorise". Thus, an expropriation law may provide "the basis for indirect transfer of property of a certain type at any time in the future during the continuance of the law". In contrast, a nationalization law usually provides for transfer to the State or to a State-controlled body to be carried out upon the enactment of the law, and does not contemplate future transfers to be carried out after an indefinite period of time. Different from both, an indirect expropriation can be carried out in varying ways, such as the imposition of confiscatory taxes. G.White, Nationalization of Foreign Property (London, Stevens & Sons Ltd, 1961) 41-50. Nwogugu adds that indirect expropriation can be achieved through "nibbling the foreign property owner to death" by "side-stepping an outright and explicit taking". Thus, the result of indirect expropriation is "a gradual deprivation of the constitutive rights of property". Nwogugu, supra note 28, at 23.

71 Practically, a sovereign State cannot stop another sovereign State from expropriating and nationalizing the property of its nationals situated in the territory of the other State, although it may criticise the illegality of the expropriation and nationalization measures. In this case, the expropriated State can refuse to recognize the effect of the expropriation and nationalization, and take whatever peaceful counter-measure available, such as diplomatic interventions, taking the expropriating country to International Court of Justice, or economic retaliation.

72 UNCTC, supra note 1, at 77. "Public purpose" is a synonym of "public interest".

73 For example, White, supra note 70, at 5-11.
grounds for expropriation and nationalization, as post-war experiences showed. Having regard to these facts, international courts seem to accept a variety of grounds of "public interest", and to have given governments "a very wide margin of appreciation of what comes within the concept, in the light of general governmental policy".74 This view seems to imply "that the contents of the concept may change with successive Governments and, a fortiori, that it may differ according to the internal order of the countries concerned".75 Thus, a realistic approach to the meaning of "public interest", although not necessarily an undisputable one, is to acknowledge "that under international law it is a matter for the national system concerned to determine what is in the public interest".76

(2) Non-Discrimination In the Process Of Nationalization

"Non-discrimination", as mentioned earlier, imposes an obligation on a State which takes measures of expropriation and nationalization to treat all foreign nationals equally or to treat the same type of investment equally. Equality here appears to refer to equality in law, but not equality of the outcome resulting from the application of the law. Thus, the issue whether factual inequality, or relative disadvantages to a particular foreign investor in different contexts, such as a comparison with the nationals of the expropriating country or a comparison with the nationals of a given third country, is of discriminatory nature is open to debate. But fairness or natural justice seems to impose a moral obligation on a contracting party not to deliberately subjugate the other to factual inequality.

(3) Consistency With Law As A Restraint Upon Nationalization

"Consistency with the law of the expropriating State" seems to be a procedural requirement, probably based on the idea of procedural fairness. But the procedural requirement does not provide substantial protection for foreign investors. Any measure of expropriation and nationalization is likely to be carried out in accordance with the legal procedures of the expropriating country, but may nevertheless not be

74 UNCTC, supra note 1, at 77.
75 Ibid.
76 Ibid.
accepted by other countries,\textsuperscript{77} by virtue of the unacceptable ground of "public interest" or of discrimination. In addition, the law itself in some countries does not guarantee procedural fairness at all. Thus, ideally, this requirement should be extended to the proposition that "public interest" and "non-discrimination" must be upheld in the national law of the expropriating country. Since a contracting State has a general obligation to treat the nationals of the other contracting country fairly and equitably, it has a general obligation to adjust its domestic law for the purposes of fulfilling its treaty obligations. Therefore, the expropriating country has a direct obligation to ensure its measures of expropriation and nationalization (the contents of the measures: "public interest" and "non-discrimination") are consistent with its national law, and has an extended obligation to treat the nationals of its treaty partners fairly and equally.

(4) Reasonable Compensation In Nationalization

"Reasonable compensation" is a crucial aspect of the legality of expropriation and nationalization. As a matter of definition, it has been argued that the taking of aliens' property without compensation is confiscation, not expropriation and nationalization.\textsuperscript{78} This treats compensation as an inherent part of the concepts of expropriation and nationalization. In general, compensation includes three elements: promptness, adequateness, and effectiveness.

Prompt compensation "was understood as referring to the time at which payment should be made, not to the time at which the amount of compensation

\textsuperscript{77} Consistency with domestic law is discussed in the \textit{United State v Italy (Case concerning Eletronica Sicula S.p.A. (ELSI) ICJ Reports 1989)}. In this case, the United States alleged that the Italian Government violated the FCN Treaty between US and Italy. One of the alleged violations involved Para.2 of Art.III which states that a contracting party shall within its territory permit, "in conformity with the applicable laws and regulations", the nationals and corporations of the other contracting party to carry on business. With regard to the expression "in conformity with domestic laws and regulations", the Court observed that this "surely means no more than that Italian corporations and associations controlled by United States nationals must conform to the local applicable laws and regulations; moreover, they must do so even if they believe a law or regulation to be in breach of the FCN Treaty, and, indeed, even if it were in breach of the FCN Treaty". The Court seems to imply that such requirement is on procedures rather than on substance. Thus, it continued that compliance "with municipal law and compliance with the provisions of a treaty are different questions. What is a breach of treaty may be lawful in municipal law and what is unlawful in the municipal law may be wholly innocent of violation of a treaty provision". See \textit{US v Italy ICJ Reports 1989}, at 65. Consistency with law is also a restraint for nationalization and expropriation in the US-Italy Treaty, but the Court did not deal with this particular issue.

\textsuperscript{78} Nwogugu, supra note 28. at 22.
should be assessed".79 The Treaty does not describe the requirements for prompt compensation in great detail. Article VIII2 simply states that the compensation "shall be paid without undue delay". The fulfilment of this requirement may depend upon the economic, political and diplomatic factors affecting the expropriating country and the relationship between the expropriating and expropriated countries. Thus, an excuse of economic hardship may not be regarded as undue delay, although tension in diplomatic relation between the countries concerned may be a factor to be taken into account.

Adequate compensation "is a vague term capable of varying interpretation when it has to be expressed in terms of money".80 Many factors, such as the market value of the expropriated property and the calculation of interest between the date of taking of the property and the date of payment of compensation, will affect the adequateness of compensation. The Treaty provides specific rules for calculating the market value of an expropriated property. First, the market value is defined as the "market value of the investment immediately before the measures [e.g. of expropriation] became public knowledge".81 Literally, this could mean the market value of a particular property on the day before an expropriation measure is officially announced. But sometimes this should extend to a situation where an expropriation measure has been introduced into the Parliament and been reported by newspapers as likely to become law, but has not been officially confirmed. In this case the market value of the possible target for expropriation may have decreased before the news was officially confirmed. Secondly, in the case where market value is not assessable, the value of the expropriated property should be determined "in accordance with generally recognized principles of valuation and equitable principles taking into account the capital investment, depreciation, capital already repatriated, replacement value and other relevant factors".82 This rule requires the expropriating country to assess the value fairly and equitably on the basis of the specified factors and according to commonly accepted methods of evaluation in international practice. Thirdly, the Treaty also requires the expropriating country to pay "interest at a reasonable rate from the date the measures were taken to the date of payment".83 But the provision leaves the meaning of "reasonable rate" undefined. Problems with

79 White, supra note 70, at 12.
80 Id. at 13.
81 Treaty, Art.VIII2.
82 Ibid.
83 Ibid.
the "reasonableness" of an interest rate include whether the rate on a particular date should be used or whether an average rate between a specified period of time should be considered; whether an artificial rate should be used, such as the rate adopted by the Bank of China or the Australian Reserve Bank, or which commercial rate should be considered. The problem perhaps should be resolved by considering the nature of an interest payment, which in the view of Latham CJ is a compensation for delay in payment on the acquisition.84 If so, it is only fair that an interest payment (the compensation) should be decided by taking into account actual loss.85 Thereby, a fair interest payment should be calculated from the day the payment on the expropriated property was due to the day the payment is made, according to the rate of the bank where the owner of the expropriated property is likely to deposit the payment during the period the interest was due. Nevertheless, the reasonableness of a rate is sometimes judged by its acceptability to the party which receives the compensation. In this case, it does not matter which method is taken as long as the parties concerned agree. "Reasonableness" needs to be proved only when disagreement arises between the parties.

Effective compensation "implies that the compensation, when paid, must be not only adequate in amount, but also of real economic value to the alien recipient".86 This is a requirement on the means and in particular the currency of payment. The Treaty specifies rules for ensuring effective compensation. Under the rules, the expropriating country has an obligation to convert the amount of compensation into an internationally acceptable currency,87 which must be computed on the daily average exchange rates over a six month period immediately prior to the "taking of the measure". The term "taking of the measure", which determines the date for calculating the six month period, may be ambiguous. It is unclear whether this refers to the announcement of the measure or the implementation of the measure. The difference between them could be significant in some cases.

84 Marine Board of Launceston v Minister for the Navy (1945) 70 CLR 518, at 526.
86 White, supra note 70, at 15.
87 Article VIII2 of the Treaty states that the compensation "shall be freely convertible and shall be freely transferable between the territories of the contracting parties". This does not, however, appear to impose an obligation on the contracting parties to provide a "required currency", but an obligation to provide a convertible and transferable currency. This distinction is crucial when the value of the compensation can be affected by the differences caused by the incomparable exchange rates between various currencies.
7.4.4.2. Treaty Obligations and the Historical Perspective of the PRC in Relation to Nationalization

The past practice of the Chinese Government in dealing with issues of nationalization and expropriation cannot determine its present practice, which is now subject to the treaties signed by China. But past experience may provide reference to the possible actions China may take in relation to the issues which are not defined or dealt with in the Treaty. In particular, it may indicate China's understanding of reasonable compensation, which is the most likely cause of dispute between Australia and China in the case of nationalization or expropriation. For these reasons, the history of the PRC in dealing with issues of expropriation and nationalization will be reviewed below.

The Chinese Government has never formally set forth its position on expropriation and nationalization. Nor has it publicly published any official statistics as to the total value of expropriated foreign property and how measures of expropriation were carried out since 1949. Information from both Chinese and foreign unofficial sources suggests that foreign property was taken in two ways: direct confiscation and indirect expropriation. Direct confiscations were carried out mainly against firms from the United States and United Kingdom, which had confronted China in the Korean War, or which took measures against Chinese overseas properties claimed by the PRC. Indirect expropriation took place when the Chinese Government "deliberately" imposed various "restrictions, regulations, and taxes et cetera" on foreign businesses, which were consequently forced into debt and had to surrender their properties to the Chinese Government. No compensation was paid for confiscated property. But it is not clear how the indirect expropriation was carried out, and whether there was any compensation for the indirectly

88 For example, the properties of Standard Oil, Texaco, Sino-American Oil Company, Shanghai Electricity, Shanghai Telephone, China Electricity Companies, Shell (Asia) Company, Shanghai Dockyards and the Muller Shipyard were confiscated or requisitioned by the Chinese Government in the 1950s. S.Liu & Q.Wu, China's Socialist Economy: An Outline History 1949-1984 (Beijing, Beijing Review, 1986) 58.

89 See the statement of the British Minister of State, Foreign Office, made in the House of Lords on 20 October 1954, reprinted in J.Cohen & H.Chiu, eds, People's China and International Law (Princeton, Princeton University Press, 1974) 703. The Chinese source also noted that some foreign business, such as Yizhong Tobacco Company, China Soap Company and Astor House Hotel in Tianjin were voluntarily transferred to the Chinese Government, but does not explain why these "bourgeois" owners of the properties, but not the others, were "voluntarily" to do so. Liu, id, at 58.
expropriated properties,\textsuperscript{90} despite the fact that Chinese information implies that some sort of compensation was paid to foreign owners of the expropriated property.\textsuperscript{91}

Since neither the Chinese Government nor scholars have addressed the "thorny legal questions implicit in claims arising out of the PRC's acts against foreign interests in China",\textsuperscript{92} there is no convincing evidence that the Chinese Government would have taken these harsh measures against foreign property had the relationships between China and most Western countries not been as tense as they were. Rather there is evidence to suggest that the Chinese Government would have treated foreign property more leniently, in the way it treated the ordinary Chinese owners of

\textsuperscript{90} It appeared that indirect expropriation took the form of liquidation of foreign companies, see Cohen, id. at 703 & 717, and of "voluntary" transfer of foreign property, see Liu, ibid. No direct evidence of "compensation" is available in either case.

\textsuperscript{91} Liu and Wu state that "the Chinese Government did not confiscate all the property without any compensation". (See supra note 88, at 58.) This statement is not supported by any statistics or further information in the book. It is equally unclear what is the meaning of "voluntarily transfer". It could mean either that the foreign owners donated their properties to the Chinese Government or that the owners had no choice, like most private owners of property in China, but to join the transformation program which purported to transfer private ownership to collective or State ownership in return for some kind of compensation. Confusion further arises from some official statement of the Chinese Government. For example, in the Order of the Government Administrative Council to requisition the properties of the British-owned Shell Company of China, the Chinese Government stated that it, \textit{inter alia}, would "requisition by purchase all its [the Shell Company of China] existing stocks of petroleum". See Cohen, supra note 89, at 689. It is unclear whether the Order was executed literally. If it was, petroleum stocks of the Shell Company of China would have been compensated for, even to a limited extent. But if the "stock" referred to the stocks overseas, the order was certainly not enforceable.

\textsuperscript{92} Cohen, supra note 89, at 718.
businesses, had Western countries had better relations with China. Undoubtedly, the Korean War, the freezing of the Chinese overseas properties by foreign governments, and the economic embargo against the PRC were attributable to China's decisions to confiscate foreign property. Such decisions affected the relations between the PRC and the countries concerned, but the decisions themselves were also a result of already very bad relations with these countries. Given that some foreign governments had frozen properties claimed by the PRC and cut off diplomatic ties with the PRC, the Chinese Government did not lose anything by taking those unfriendly measures. These facts suggest that the Chinese Government will probably not repeat its past practice, having regard to its desire to maintain the extensive economic connections between China and many Western countries. The interdependence between the Chinese economy and the world economy strongly suggests that the Chinese Government cannot afford to take measures which may seriously damage its goal of economic reform.

In terms of the Australia-China Investment Protection Treaty, there is no probability that the Chinese Government will lightly take measures of expropriation and nationalization without due compensation. This can be supported by several arguments. First, in the past the PRC has rarely been criticised for dishonouring treaty obligations voluntarily accepted. Secondly, there is no legal technicality which may discharge the Chinese Government from performing its treaty obligations. Under the Civil Code (General Principles) of the PRC, the provisions of an international treaties entered into by China prevail over the provisions of the national

93 The Chinese Government took two methods to deal with the private ownership of business in urban areas. The properties which belonged to the so-called Four Big Families (Jian, Sun, Kong and Chen families, all occupied high governmental positions, including the past President of the ROC, Jian Keishi himself) and the previous Government were confiscated. But the businesses owned by ordinary Chinese were encouraged or forced to transfer to the collective or State ownership of property through some transitional programs in which some amount of compensation were paid. See Liu, supra note 88, at 21-2, 83-6, & 137-45.

94 This proposition is supported by several facts. First, while the new Chinese Government was determined to abolish all "imperialist privileges" in China, it had decided to "allow the remnant imperialist economic forces to continue to exist for a certain period of time under government supervision or control". Secondly, the Chinese Government divided the remaining foreign firms into three main categories. Those foreign firms which were deemed to have infringed on China's sovereignty or to be important to the national welfare and people's livelihood were requisitioned. Those less important were put under close control by the Government. Ordinary enterprises, "which did not stand in the way of China's progress, were left intact". Thirdly, formal confiscations were carried out after the Korean War took place and the US Government froze the property claimed by the PRC. See Art.3 of the Common Program of the Chinese People's Political Consultative Conference, collected in Liu, supra note 88, at 487, and discussion in Liu, at 57-8.
law in the case of discrepancy unless a reservation in relation to the matters in discrepancy has been made.\textsuperscript{95} There is no reservation in the Australia-China Investment Protection Treaty, and therefore the Chinese Government must follow the rules in the Treaty as they are. Thirdly, having regard to the existing economic ties (trade and Chinese investment in Australia), the Chinese Government cannot expropriate or nationalize Australian property in China without providing acceptable compensation, risking its overseas property in and outside Australia to be subject to claims arising from such nationalization and expropriation. Fourthly, Chinese foreign investment laws (Joint Venture Law and Solely Foreign Owned Enterprises Law) have provided legal guarantees against the nationalization of foreign enterprises, including the payment of compensation if nationalization is necessary.\textsuperscript{96} Lastly, there is special provision for dispute settlement in the Treaty. Australian nationals or the Government can always take the matters to Chinese courts or an international arbitration tribunal pursuant to its provisions. Therefore, the issues which are more likely to cause disagreements between Australia and China are not whether there is any compensation, but whether the compensation is reasonable.

The "reasonableness" of compensation has not been discussed in detail by the Chinese Government, nor by the Chinese judiciary. Thus, the likely position of the Chinese Government on the issues of reasonable compensation can only be examined in the light of general provisions in law and some scholarly writing which, like most scholarly studies in China, often serves the practical needs of the Government. This tendency was evident in the 1950s,\textsuperscript{97} when the Chinese Government directly or indirectly confiscated all foreign properties in China. The level of consistency between scholarly writings and the official position shown in the practice of the PRC

\textsuperscript{95} Civil Code, Art.142.

\textsuperscript{96} The Solely Foreign Owned Enterprises Law has a provision providing such guarantee, CCH, China Laws for Foreign Business para.13-506, Art.5; and Joint Venture Law was amended in March 1990 to add such guarantee.

\textsuperscript{97} For example, an article on nationalization divided the international views of compensation into three opinions: full compensation, partial compensation and no compensation. The article commented that the first opinion was the bourgeois theory which was based on the "sanctity and inviolability of private property"; that the second opinion was a compromise which took into account the ability of the expropriating country to pay; and that the third opinion was an exercise of state sovereignty, in a situation where requiring "the nationalizing State to make compensation to owners of foreign nationality may frustrate the exercise of the sovereign rights of a State to carry out economic and social reform, because it may be impossible or difficult for such State to assume an obligation to make compensation". Then the author of the article stated that "(w)e believe that the third theory is correct". H.Li, "Nationalization and International Law" in Cohen, supra note 89, at 718-29. See also Chou & Others, "The Legal Basis for the Nationalization of the Suez Canal Company" also in Cohen, at 730-2.
in the 1950s suggests that the present Chinese position on compensation may be reflected in some scholarly writing.98

No doubt the Chinese Government will pay compensation pursuant to the Treaty in the case of nationalization, but as has been seen, the meaning of "reasonable compensation" is uncertain. The main difficulties are that neither the definition of "reasonableness" nor the criteria for judging the "reasonableness" are universally agreed by the international community. Several questions thus arise: whether so-called "partial compensation" can be regarded as reasonable and whether an amount of compensation reached according to a method of calculation based on "full compensation" is more reasonable than an amount derived from another computing method based on "full compensation". In addition, given the uncertainty in the meaning of "full" and "partial" compensation, it may be questioned whether an amount based on "partial compensation" is necessarily less reasonable than an amount based on "full compensation". These questions inspire divergent answers for lack of a uniform approach to the issues of reasonable compensation.

The Chinese Government appears to have been affected by various views of reasonable compensation in its practice. In the 1950s, it directly or indirectly confiscated foreign property in China without due compensation (if any at all). But today it has addressed the issues of compensation in several ways. For example, in the Australia-China Investment Protection Treaty, the Chinese Government agrees to give "reasonable compensation"; in the Solely Foreign-Owned Enterprise Law, it promises to give "appropriate" compensation;99 and in the Regulations on Joint Exploitation of Offshore Petroleum Resources, it reserves a right to purchase compulsorily, or to requisition, part or all of the petroleum owned by foreign participants of the ventures in the cases of war or emergency.100 The terms which describe the compensation obviously vary to some extent and can only provide a general illustration of China's understanding of reasonable compensation.

In this regard, one scholar suggests a clearer position than these official views. Yao, in his book International Investment Law, observes that "partial

98 e.g. M.Z.Yao, International Investment Law (Guo Ji Tou Zi Fa, 2nd edn, Wu Han, Wu Han University Press, 1987, in Chinese) 384.

99 Solely Foreign-Owned Enterprise Law, Art.5, CCH, China Laws for Foreign Business para.13-506. The Chinese words xiangying may broadly refer to the "appropriateness" of the compensation to the property value, or the "appropriateness" to the expropriating measures. Therefore, appropriate compensation may not always mean the "appropriateness" in terms of the market value of the expropriated property.

compensation" is a "relatively practical and reasonable" theory for compensation.\textsuperscript{101} He argues that the "partial compensation" theory satisfies the demands of the new international economic and legal order,\textsuperscript{102} which represents the demands of developing countries and some developed countries to change the economic and trade relationships between countries. Compared with the scholarly writings in the 1950s, Yao's view suggests that China's position may have moved from "no compensation" to "partial compensation". Yao's view corresponds broadly to the unexplained official views of the PRC as reflected in its treaties and laws: the PRC seems reluctant (in particular in domestic laws) to take the same stand with the Western countries with regard to issues of reasonable compensation. Both general provisions in laws and scholarly views suggest a possible Chinese official position on reasonable compensation, which seems not to be at the same standard as the views held by Australia.\textsuperscript{103} However, the change of attitudes of both the Government and scholars between the 1950s and 1980s may suggest a move toward the Western position on the issues of reasonable compensation - a view which may be expected to prevail, at least, while economic relationships between China and foreign countries continue to improve and expand.

7.4.5. Responsibility in Relation to Foreign Exchange Control

Article X of the Treaty requires a contracting country to permit free transfer of investment-related funds and to provide convertible currencies to the investment-related funds and the earnings of the nationals of the other contracting country derived from investment-related activities. These provisions raise no difficulty for the Australian Government, which has in fact suspended most substantial controlling measures on foreign exchange. The Treaty obligation is thus no more than a confirmation of the guarantee on the convertibility of investment already provided unilaterally by the Australia Government. But to the Chinese Government the application of the Treaty may result in conflicts with its exchange control measures. For example, it is doubtful whether the Chinese Government can really guarantee the earnings of the Australian nationals received in Chinese currency to be freely

\textsuperscript{101} Yao, supra note 98, at 384.

\textsuperscript{102} Id, at 386.

\textsuperscript{103} Australian view of nationalization, which bears the marks of a federal system (in term of expropriating power), is basically consistent with the views of the United States and the United Kingdom. For details, see R.Lumb, "Alien Property in Australia" in O'Connell ed, International Law in Australia (Sydney, Law Book Company, 1965) 500; and A.Farran, "Australia's Resources Policies and International Law" in K.Ryan ed, International Law in Australia (Sydney, Law Book Company, 1984) 305.
converted into recognized foreign currencies. Uncertainty clearly arises from the Chinese Government's ability to perform this obligation.

In fact the language of the provisions on foreign exchange control seems rather vague. On one hand, Article XI requires the contracting parties to allow free transfer of investment-related funds, but emphasizes that the transfer is subject to the law and policies of the contracting parties. Doubt arises from the vagueness of the provision, which may mean either that the "free transfer" is an illusory "right" because it is subject to the restriction in law, or that it is a right which must be recognized by law. If the right of "free transfer" is subject to domestic law, the guarantee to provide foreign exchange to the restricted "free transfer" will not provide any significant protection to an Australian investor. By contrast, the Australian Government may well argue that the "free transfer" is an unrestricted right which must be confirmed in Chinese law under the principle of "fair and equitable treatment". If this view prevails, Australian nationals will be entitled to unrestricted access to foreign exchange. This would conflict with Chinese foreign exchange control regulations, which provide foreign investors with limited access to the conversion of foreign exchange, in particular their earnings derived from sales on the Chinese domestic market. The truth is that the Chinese Government simply does not have enough foreign exchange savings to meet the demands which may arise from all the investment promotion and protection treaties signed by it. The impracticability of such interpretation defies the rationale of the provisions concerning the State's responsibilities in relation to exchange control.

Therefore, provisions on foreign exchange control are likely to be interpreted as a flexible and minimum-protection type of provision. The provisions, while imposing at least a soft treaty obligation on the Chinese Government, seem to allow legal technicalities to conditionally relieve the Chinese Government from any practical difficulties it may have in providing the amount of foreign exchange required. The applicability of such arrangement lies in a broad interpretation of the relationship between national law and the right to "free transfer" under the Treaty. Minimum protection to the investors is aimed at in the Treaty. The

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104 Treaty obligation to allow "free transfer" of foreign exchange is not strict. It is conditional and flexible, subject to the "freedom of transfer" allowed under domestic laws of Australia and China. Thus, it is a "soft treaty obligation".

105 The phrase "subject to national law" technically allows the Chinese Government to restrict or impose conditions on "free transfer" of foreign exchange by passing appropriate law. This means that the treaty obligation to allow free transfer of foreign exchange is required to be performed when relevant national law does not suggest contrary intention. However, this is different from an obligation to make a law to protect free transfer of exchange.
confusing and vague language of the provisions is no doubt a result of compromise between the contracting parties. That compromise itself suggests that more compromises will be needed in the implementation of these provisions.

7.4.6. Government Responsibility and Government Contracts

7.4.6.1. The Treaty Obligation in Relation to Government Contracts

Article XI of the Treaty states that a contracting party shall, "subject to its law, adhere to any written undertaking given by a competent authority to nationals of the other contracting party with regard to an investment in accordance with its law and the provisions of this Agreement". This is an obligation to perform contracts signed by the Governments or their agencies concerning investments which have been admitted into Australia and China in accordance with their national laws and the provisions of the Treaty. The obligation consists of four basic elements. First, the contracts must be written undertakings, and thus oral or implied undertakings are excluded. Secondly, the contracts must be signed by a competent authority, whose authority to deal with the substance of the contract is determined by national law. This recognizes the unenforceability of a written undertaking under national law, when the government agency which signed the contract lacked authority to do so. Thirdly, the contracts must concern investments, which are legally accepted by the country whose government agencies signed the contracts, and which fall within the ambit of the Australia-China Investment Protection Treaty. Thus a contract for a loan provided by an organization which is not a corporation under the law of Australia and China is excluded from the application of this provision. Fourthly, perhaps the most controversial element is that the effect of a government contract is subject to the law of the country whose Government has signed the contract. This restriction may practically render unenforceable some government contracts in either Australia, where the power of the executive arm of the Government is limited generally by the federal Constitution or the common law, and by relevant statutes; and in China, where the law governing contracts entered into by governments agencies in their administrative capacity is very uncertain. The relationship between the treaty obligation with regard to government contracts and national laws in Australia and China will be examined below.

7.4.6.2. Government Contracts and Australian Law

In the context of Australian law, it must be noted that the "competent authority" mentioned in the Treaty usually refers to a Department or agency of the federal Government. But the application of the Treaty may extend to a State
Government in some cases. Thus government contracts in Australia refer to both contracts signed by the federal Government and those made by a State Government.

In terms of contracts between the Australian federal Government and Chinese nationals or companies, apart from the general law governing the validity of contracts, there are several factors affecting the validity of such contracts under Australia law. First, the undertakings assumed by the agencies of the Government must be clear and specific. A vaguely worded written undertaking may not be enforceable in the Australian courts.106 Secondly, the federal Government or its agencies cannot "fetter the exercise of a statutory power where parliament has prescribed how that power is to be exercised".107 Thus, when Chinese companies and nationals make contracts with Australian governments agencies, they must ascertain that the obligations so assumed by the government agencies are not restrictions on the exercise of the Government's executive power.108 Thirdly, the term "competent authority" in the Treaty under Australian law means a government agency which has been authorized to enter into the contracts. The authorization could be statutory or executive. When the Government enters into a contract under a statute, "the requirements imposed by that statute must be observed if the contract is to be valid and enforceable".109 The capacity of the Government is thus "confined strictly to the limits of the authority".110 When the Government enters into a

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106 Rederiaktiebolaget Amphitrite v the King [1921] 3 KB 500, and the discussion in D. Flint, Foreign Investment Law In Australia (Sydney, Law Book Company, 1985) 460-2. See also South Australia v Commonwealth (1962) 108 CLR 130. In this case the Railways Standardization Agreement of 1949 between the Commonwealth and South Australia was discussed. The majority of the High Court held that the Commonwealth did not breach its legal obligation under the Agreement because either the Agreement did not specify such an obligation or rose only a political obligation.

107 Flint, id. at 462. See also Ansett Transport Industries (Operations) Pty Ltd v Commonwealth (1977) 17 ALR 513, where Mason J. pointed out that "the public interest requires that neither the Government nor a public authority can by a contract disable itself or its officer from performing a statutory duty or from exercising a discretionary power conferred by or under a statute by binding itself or its officer not to perform the duty or to exercise the discretion in a particular way in the future", at 530.


110 Id. at 482.
contract in its executive capacity.\footnote{Richardson argues that "the Crown has a power independent of statute to make contracts incidental to carrying out the ordinary and well-recognized functions of governments". J.Richardson, "The Executive Power of the Crown" in L.Zines ed, Commentaries on the Australian Constitution (Sydney, Butterworths, 1977) 50, 72-3.} the "capacity of the executive government or a statutory authority is restricted by the limited purposes for which the Commonwealth was established".\footnote{Id. at 74. See also Davis v Commonwealth (1988) 82 ALR 633. In this case, Brennan J. comments that the executive power "extends to the advancement of the nation whereby its strength is fostered".} Thus, under Australian law, the competence of a governmental Department or agency to enter into a contract must be examined against the Constitution and statutes,\footnote{Flint argues that "the power of the Australian Government to enter into contracts is limited not only by statute but also by the powers given to the Australian Government by the Constitution". supra note 106. at 475.} and occasionally the implied power derived from the nationhood of Australia.\footnote{Richardson, supra note 111, at 76. For a detailed discussion on Crown contract, see Renfree, supra note 109, at 469-84.} This means that the validity of a given contract can only be determined on case by case basis. Unless specified otherwise by law, these basic factors must be noted by Chinese companies and nationals when entering into contracts with Australian government agencies, including agencies of Australian State governments.

7.4.6.3. Government Contracts and Chinese Law

The responsibility of the Government under government contracts is an unsettled issue in Chinese law. In general, there are two kinds of government contracts: one signed by government agencies which are legal persons under Chinese law,\footnote{There are several legal requirements for being a legal person. First, a legal person must have its own capital or assets which meet the minimum amount required by the State. Secondly, a legal person must have its organization, a charter of organization and a place of business. Thirdly, a legal person must be able to assume civil liabilities, suing or being sued in the courts of law. Lastly, the status of a legal person is not automatically conferred, and an entity can only obtain the status through application to the government administration. Civil Code (General Principles), Art.41, CCH, China Laws for Foreign Business para.19-150.} the other entered into by government agencies which are not separate legal
The distinction between the two types of government agencies leads to different legal consequences under the present Chinese legal system. In particular, Chinese law recognizes only the contracts signed between legal persons, between individual business households or commune members and legal persons, and between Chinese legal persons or economic organizations and foreign enterprises, economic organization or individuals. Thus, government contracts entered into by government agencies which are not legal persons are not enforceable in the Chinese courts, at least as Chinese law stands today. Uncertainty arises from the inconsistency between the wording of the Treaty, which subjects the validity of government contracts to the rules of domestic law, and the perceived purposes of the Treaty which is to provide a protection for investors, in particular in China, who take investment risks on the basis of written undertakings from the Governments.

Examples of the former are the contracts signed by various central or local government-owned import and export corporations, which act in their own capacities although they attach, sometimes closely, to the governments. Examples of the latter are the written undertakings made by local foreign investment administrative commissions, such as the Development Zone Administrative Commission in Dalian, Guangzhou and Tianjin, to provide infrastructure and other necessary services for an investment project; or the contracts on land use rights. There are no uniform rules applying to the transfer of land use rights in China. The legal status of the government agencies which transfer land use rights to the users of land on behalf of the governments is uncertain. Some local governments, such as Shenzhen and Shanghai, have land administrative bureaus to manage the matters. Others give the power to transfer land use rights to the Development Zone Administrative Commissions. But none of the local legislation dealing with the transfer of land use rights has defined the legal status of the government agencies in charge. Broadly, these agencies cannot be legal persons under the present Chinese law unless specified as such by law. But the legislation alone cannot reflect the true picture of Chinese practice. More often than not, some local governments create agencies to exercise statutory power without following formal legal procedures which establish a link between the newly created agencies and the existing statutory powers. Thus, it is no surprise when some legal writings suggest that in some cities the land use rights are transferred through specific urban real estate agencies designated by local governments, although there is no local legislation to support the existence of such agencies. See Q.Zhang, "The Basic Principles for Legislating on Urban Land Market" (1989) 3 Law of China (Zhong Guo Fa Xue, in Chinese) 75. Accordingly, it is possible that contracts on land use rights in some areas of China are entered into by the government agencies which are legal persons under Chinese law.

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Economic Contract Law, Art.2, CCH, China Laws for Foreign Business para.5-500.

Id, Art.54.

Id, Art 2.

When a Chinese government agency is not a legal person, it cannot be treated as an economic organization either, which under Chinese law usually refer to non-profit entities such as university or social club.
The application of the Treaty in the context of Chinese law will be further examined below.

The obligation of the Chinese Government to perform its written undertakings is subject to Chinese law. When such undertakings are contrary to the general principles of the Economic Contract Law, the Foreign Economic Contract Law, and Civil Code, they are not enforceable. But when the undertaking is neither confirmed nor prohibited, the obligations arising from such undertakings are disputable. This is the case with government contracts (or written undertakings) entered into by a government agency which is not a legal person.

Chinese law does not address the issues arising from "contracts" or written undertakings signed by government agencies in their executive capacity. It seems that written undertakings, agreements or promises made by government agencies which are non-legal persons are not seen as "contracts", and are therefore not protected under the contract laws. The non-protection of this kind of contractual relationship in law may be due to one of the two reasons. Either the lawmakers did not think such contractual relationships existed, or they deliberately excluded these because of the difficulties in explaining the contradiction between basic principles of civil law and the legal implications of such relationships. Both reasons are associated with the same fundamental proposition in Chinese civil law, namely only natural persons and legal persons can enjoy civil rights and assume civil liabilities on an equal basis. This proposition is confirmed by Article 2 of Civil Code, which states that the Chinese Civil Code adjusts only the property and personal relationships between natural persons, between legal persons, or between natural and legal persons, who are equal subjects under law. Although some Chinese scholars recognize that in some circumstances the State may act as a subject in civil

121 For discussion of the Economic Contract Law, see H.Zheng, supra note 66, at 45-7 & 49-52.


123 Some may argue that the relationships are not contractual, but administrative by nature, because a government agency is higher than the other party to the written undertaking by virtue of its administrative status. This is true when a party to the undertaking is not a legal person under Chinese law, but is not correct when both parties are legal persons. However, the effect of a contract entered into by an executive in its executive capacity is an unsettled issue in Chinese law, although it seems fair in terms of natural justice to require the executive to take some responsibility in this case.
law,\textsuperscript{124} no one has suggested that a contractual relationship may be entered into by a government agency which is not a legal person. Instead, most would argue that because the activities of the Government in administering the economy and the relationships between the State and enterprises are economic relationships or administrative relationships of a superior-and-subordinate nature, which are unequal, the activities are subject to the economic law or administrative law, rather than contract law.\textsuperscript{125} These provisions of the law and writings of the scholars appear to suggest that the Government in its administrative capacity may enter into some economic (or civil) relationships, but that the relationships are not contractual. This gives rise to the possibility that the written undertaking by the Chinese government under the Treaty may be enforceable under the so-called economic law or administrative law, if the law is proved to be relevant.

There is no code of economic law in China. In fact, like many unsettled issues in Chinese law, economic law is a vague concept. No satisfactory distinction has ever been drawn between civil law and economic law in China.\textsuperscript{126} The abovementioned "unequal relationship" between the Government and enterprises is one of the distinctions which have been proposed, although it too is unsatisfactory. The overlapping of the civil law and economic law can be seen in the very existence of the Economic Contract Law and the Foreign Economic Contract Law, which are the only laws dealing with contractual relationships or their like within the category of economic law. Both are regarded as economic law, but both deal with contractual relationships which are also generally included under the Civil Code. The economic law does not provide any sanction to the enforcement of written undertakings made by the Chinese Government under the Treaty, although it does not deny the possibility of enforcement either.

Chinese administrative law does not provide any assistance in deciding on the validity of government contracts entered by the government as such rather than a separate legal person. So far, the only piece of administrative legislation, which deals

\textsuperscript{124} R.Tong & Others, Basics of Civil Law (\textit{Ming Fa Ji Chu} Beijing, Law Publishing House, 1983, in Chinese) 31. The authors give the issuing of public bonds by the State and inheriting of unclaimed property by the State as examples.

\textsuperscript{125} S.Li & Others, Practical Handbook of Law (Annotated) (\textit{Shi Yong Fa Lu Shou Ce} Beijing, China's Economics Publishing House, 1986, in Chinese) 128.

\textsuperscript{126} Lubman observes that it "remains to be seen exactly how distinctions between the civil law and the economic law will be made in legislation. The attention being paid to it signifies a recognition that China must now address the issue of defining legal aspects of the uneasy economic relationships- and the shifting accommodations required- between the individual and the socialist State". S.B.Lubman, "Emerging Functions of Formal Legal Institutions in China's Modernization" (1983) 3 China L.Rep. 195, 231.
with the government's responsibility in the event of its violation of civil rights of citizens, legal persons or organizations, is the Administrative Litigation Law.127 But this law neither expressly contemplates breach of governmental contracts, or of a written undertaking by a government agency, as a cause of action, nor does it specifically exclude it.128 Moreover, the Law seems to be difficult to apply to contractual relationships even by analogy.129 In spite of these difficulties, the provision of the Administrative Litigation Law which allows Chinese citizens, legal persons or organizations to challenge any administrative act that can be sued against under law and regulations may indirectly provide a ground of action. Since there is no law or regulation in China dealing with government contracts, a possible way to argue the applicability of the Administrative Litigation Law is to point out that the breach of a written undertaking by an administrative authority is a litigable cause under the Treaty, which should be regarded as a source of law in China.

Literally, the Treaty allows the breach of written undertakings by governments to be sued upon in the Chinese courts. Article XI imposes an obligation on a contracting country to perform its written undertakings. Article XII(2) allows nationals of a contracting party to bring a legal action against the other contracting party in the competent judicial or administrative bodies of the other contracting State. These two Articles may support a legal action by an Australian national against the breach of a written undertaking by an agency of the Chinese

127 The English text can be found in (1989) 3:5 CLP 37-57.
128 Administrative Litigation Law, Art. 2.
129 Art. 2 of the Law states the general principles, which allow citizens, legal persons or other organizations to bring legal action against the administrative authorities and their personnel who infringe upon legal rights of citizens, legal persons or other organizations. Articles 11 & 12 specify allowed and disallowed causes of action. In particular, administrative sanctions such as imposition of fine and revocation of licenses; administrative orders restricting personal freedom and freezing property; infringement upon the autonomy of State-owned enterprises by the administration; the decisions of the administration to reject the application for business license or to refuse the request of citizens, legal persons or organizations for protection of their freedom or property; the decisions of the administration not to provide pensions to disable persons or families of deceased; the decisions of the administration to demand certain performance from citizens, legal persons or organizations; the infringement by the administration upon the personal freedom or property rights; and any administrative cases which are allowed to be heard by the courts of law. On the other hand, administrative acts involving national defense or diplomatic matters, administrative regulations or decisions which are universally applicable, the decisions of the administrative authorities in relation to the punishment, appointment or dismissal of their personnel and any matters to which the administrative authorities have power to make final decisions according to law, cannot be pursued under Administrative Litigation Law. In the light of these specified matters, a breach of contracts or written undertakings can hardly fit into any of these.
Government. Nevertheless, no case arising from the Treaty has been dealt with in the Chinese courts since the Treaty entered into force in 1988. (The Administrative Litigation Law was passed in 1989.) It is hard to predict how the Chinese courts would react to a complaint against the breach of a written undertaking by the administration brought by a foreign national.

As have been seen, neither the Civil Code and contract laws, nor the Administrative Litigation Law, deals with disputes arising from the written undertakings made by administrative authorities.130 However, the enforcement of Article XI of the Treaty may be supported by several other arguments. First, although the Chinese Constitution does not address the effect of international treaties entered into by China on the system of domestic law, international treaties are a recognized source of law in the Chinese legal system.131 These treaties have the same effect as the domestic law. Secondly, as we have seen, although Chinese law does not directly allow the breach of a written undertaking by an administrative authority to be sued upon in the courts of law, it does not prohibit it either. Thus, it is at least arguable whether the restriction "subject to the law of the contracting party" in the Treaty may deprive an Australian national of rights to bring a legal action against the responsible Chinese administrative authority for a breach of written undertaking. Thirdly, the purpose of this Article is to provide protection for the rights of Australian or Chinese investors against the abuse of administrative power by the two Governments. Although the Treaty cannot fetter the exercise of the executive powers by the two Governments, it does impose legal and moral obligations on them. Thus, it is reasonable to expect the Governments to interpret this law in a way consistent with the purposes of the Treaty. These considerations together lead to a conclusion in favour of the enforceability of the provision with respect to written undertakings made by the Governments. Given the uncertainty of Chinese law in this regard, Chinese courts may be able to accept cases involving the breach of written undertakings by the Chinese government. This is of course dependent upon other relevant factors, such as political and economic considerations which may be taken into account by courts, in each particular case. The political

130 But Civil Code imposes general civil liabilities on administrative authorities and their personnel who violate the legal rights of Chinese citizens, legal persons or organizations in the exercise of their executive functions. See Civil Code, Art.121. Thus, it can be argued that the breach of a written undertaking by the administration is the violation of the legal rights of Australian nationals or companies which have the same rights as Chinese citizens and legal persons. See Civil Code, Art.142.

131 For example, Unit of Jurisprudence, Law Dept. of Beijing University, ed. The Basic Principles of Jurisprudence (Fa Xue Ji Chu Li Lun 5th edn, Beijing, Beijing University Press, 1988, in Chinese) 364-5.
consideration seems crucial in deciding court's position in a particular case, given that Chinese judicial system has not been really separated from the Executive and immune from the influence of the Communist Party.

However, a dispute arising from a written undertaking does not have to go to the courts for a settlement. Negotiation, consultation and arbitration, as provided under the Treaty,\textsuperscript{132} may provide an easier solution and avoid legal difficulties. Having regard to the eagerness of the Chinese Government to attract more foreign investment, Australian nationals and companies may reasonably expect their disputes with the Chinese Government to be settled without the need to resort to the formal judicial system of China.

7.5. Limited Sovereign Immunity Under the Treaty

Article VII of the Treaty states that:

Any question arising in relation to an investment or activity associated with an investment of a national of either Contracting Party concerning immunity from the jurisdiction of the courts in any proceeding, the procedure for service of initiating process or immunity from execution shall be resolved in accordance with the law of the Contracting Party which has admitted the investment.\textsuperscript{133}

This provision limits the immunity of Australian and Chinese nationals (including companies) that may otherwise claim sovereign immunity on their investment-related activities. The effect of the provision is to confirm the restrictive immunity doctrine held by Australia, and to reveal \textit{de facto} acceptance by the Chinese Government of the restrictive immunity doctrine, at least in the present case. Under the provision, the Australian and Chinese Governments expressly waive their state immunity over investment-related activities, which are included in the commercial activities under the FSIA of Australia. Thus, no Australian or Chinese citizen (this literally includes the head of the State) or company (referring to any corporation recognized under the national laws of Australia and China) is entitled to immunity whatever as long as the litigation relates to their commercial activities fall within the Treaty.

Uncertainty arises from the application of this provision under Chinese law, which does not have a special law on state immunity. Provisions concerning immunity in this case can be found, however, in the Civil Procedure Law. Article 187 states that when foreign courts restrict the civil litigating rights of Chinese citizens or companies, the Chinese courts will impose the same restrictions on the

\textsuperscript{132} Treaty, Art.XII.

\textsuperscript{133} Treaty, Art.VII.
rights of the nationals and companies of that country on the basis of reciprocity. Article 188 states that civil litigation involving foreigners, foreign organizations or international organizations which have immunity will be dealt with in accordance with the international treaties to which China is a party. These two provisions set forth the guidelines for the Chinese courts to handle cases involving state immunity. But on the ground of "reciprocity", the Chinese courts will have little opportunity to restrict the immunity, if there is any, of the very few existing Australian government-owned companies, such as the Commonwealth Bank, Qantas and Telecom.134 Thus, the restrictive immunity of Australian companies in China is less significant than the restrictive immunity of Chinese companies in Australia.

7.6. Settlement of Disputes Under the Treaty

7.6.1. Types of Disputes Under the Treaty

Three kinds of disputes - disputes between Australian and Chinese nationals, disputes between a national and the other contracting Government and disputes between the two Governments - are specified in the Treaty. Disputes in the first category arise between individuals of the two countries, as in contractual or labour disputes. The second kind of dispute arises from various investment-related activities involving a private party and an administrative authority, as in disputes arising from written undertakings, nationalization or executive actions. The third arises from the interpretation and implementation of the Treaty, which are often results of disagreement between a private party and a contracting Government.135 The general approach to a settlement of the dispute in these cases is first to negotiate or consult. This feature is evident in the proposed process for disputes between private and State parties, or between States. Then if unsuccessful, disputants can resort to local legal remedies or agreed arbitration proceedings. The incorporation of negotiation and consultation in the Treaty makes these means compulsory or obligatory for resolving disputes between individuals or individuals and a State under

134 Principle of reciprocity means that when Australian courts treat Chinese State enterprises as separate entities, Chinese courts will not regard agencies of the Australian Government as the Government itself. Thus, issue of immunity does not arise from cases involving enterprises owned by the Australian Government unless the Australian Government claims sovereign immunity.

135 For example, when a private party challenges the measures of exchange control or the transparency of law, it often does not have effective means to bring the administrative authorities to a negotiation or sufficient ground for a legal action. But it can request its home State to enquire into the matters concerned through the mechanism available to the Government under the Treaty.
National administrative tribunals or courts of law are additional forums for disputes involving two private parties or a private party and a State, but are not available for disputes between the two Governments. According to different approaches to dispute settlement, disputes between private parties and disputes involving a State will be discussed separately.

7.6.2. Settlement of Disputes Involving Private Parties

Disputes falling within this category are those between an Australian national or company and a Chinese national or company, and those between an employee of an Australian or Chinese national (or company) and a private party that does not have the same nationality as the employer of the disputant. The extension of this provision to personnel employed by nationals of Australia or China is probably for the purpose of protecting nationals of a third country working for Australian or Chinese companies. But the language of the provision literally extends to Chinese employed by Australian companies in China and Australian working for Chinese companies in Australia. The treatment of the disputes between nationals of the two countries and between employees of Australian or Chinese nationals and the nationals of the two countries, as will be seen, differs to some extent.

Article V imposes three obligations on the contracting parties. These are full access to local remedies, free choice of means of dispute resolution, and recognition and enforcement of resulting judgments or awards. Under the Treaty, the contracting parties have different obligations towards the disputes between Australian nationals and Chinese nationals, or disputes involving only one contracting party, such as the disputes between nationals of the same country or involving a national of third country.

Full access to local legal remedies, including remedies before judicial and administrative bodies, must be available with respect to all disputes falling within this category. Thus, the Australian and Chinese Governments promise to provide access to the local judicial system to disputes between their nationals, with one party being employed by a national of the other contracting country. As a result, some disputes between nationals of the same country, which could be within the exclusive jurisdiction of a contracting country, may fall under the protection of the Treaty. The handling of such disputes may sometimes be subject to the supervision of the

136 The requirement to negotiate is deemed to have been fulfilled when any party has expressed such intention in writing for 3 months in the case of disputes between private party and State, or 60 days in the case of disputes between the two Governments.

other contracting party. The enforcement of judgments resulting from such disputes becomes a matter of treaty obligation.

By contrast, the contracting parties assume an obligation to permit their nationals to choose freely the means of dispute resolution, including international arbitration, only when their disputes involve nationals of both contracting countries. Accordingly, the Chinese Government does not have an obligation to permit disputes between two Chinese disputants (with one of them working for an Australian company), or between a national of third country and a Chinese party, to be referred to international arbitration. The exclusion of disputes between Chinese nationals from the provision seems understandable by virtue of the common jurisdiction over both disputants, but the exclusion of the disputes between a national of third party and a national of Australia or China appears to be puzzling. Non-intervention by Governments, as the provisions suggest, is not a privilege given to the disputants, who in fact is not subject to such intervention in Australia even without treaty protection. As a matter of fact, free choice of dispute resolution techniques is a natural right of the disputants. The Chinese Government does not lose anything, not even its symbolic sovereignty, as in the case involving two Chinese disputants, by allowing a Chinese party to a dispute involving a national of third party to choose freely the means of dispute settlement.

There is also an obligation to recognize and enforce judgments or awards in relation to disputes between private parties. The judgments or awards concerned may either be given by national judicial or administrative bodies, or by foreign courts or international arbitral tribunals. In the case of domestic judgments or awards, enforcement is subject to national law. In the case of foreign judgments or awards, enforcement is subject to national law and international treaties signed by Australia or China. The obligation to provide for the recognition and enforcement of judgments or awards in relation to disputes between private parties seems more flexible than the obligation to provide access to local legal remedies and to allow free choice of the means of dispute resolution.

7.6.3. Arbitration Proceedings for Resolving Private-State or State-State Disputes

The agreed arbitral procedures under the two provisions share similarities. There are five main features of the proceedings. First, the arbitral tribunal consists of three persons, with two appointed by the disputing parties respectively and the third (the Chairman of the tribunal) by agreement of the two separately chosen

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arbitrators or by a designated international authority. Secondly, in both proceedings the arbitral tribunal should encourage the disputants to settle their disputes amicably. This means that the arbitral tribunal may resort to mediation, conciliation or other means to assist the disputing parties to settle the disputes. Thirdly, the case is decided by majority vote. Fourthly, the award of the tribunal is final and enforceable in the territory of each contracting party according to the domestic law of the contracting country. Lastly, the costs of the arbitration proceedings are shared by the parties.

Differences between the two proceedings can be seen in several respects. First, in disputes between States, the country which initiates arbitration proceeding must in the notice instituting the proceeding set forth in summary form the grounds of its claim, the nature of the relief sought and the name of the arbitrator appointed by it. This is not necessary in the arbitration proceeding involving a private party and a State. Secondly, in an arbitration proceeding involving the two Governments, the tribunal which has been formed in accordance with the relevant provisions of the Treaty has power to render a default judgment. But a tribunal set up for settling disputes between a private party and a Government is not granted with such power. Thirdly, although neither Australia and China is a party to ICSID, they have agreed to use the arbitration rules of the 1965 Convention on the Settlement of Investment Disputes Between States and Nationals of Other States in the proceeding involving a private party, unless the disputants choose other rules by a written agreement. But in a proceeding involving the two Governments, the procedural rules are to be decided by the disputing parties or the arbitrators.

The positions and status of disputants in respective proceedings result in that the two arbitration proceedings have common as well as distinguishing features. In a dispute between a private party and a State, the disputants are not equal. On one hand, the private party should be given due protection; on the other, the protection so given must be restricted within a limit which does not contravene the sovereignty of the State. For these reasons, any disputing party to a private-state dispute may seek assistance, after the failure of negotiation, from local judicial or administrative bodies, or from an arbitral tribunal pursuant to agreement. Neither the use of local

139 If the disputing parties cannot agree upon the Chairman of the tribunal after 60 days of commencing an arbitration proceeding, the President of the IBRD should be asked to appoint the Chairman on behalf of the disputants involving a private-government dispute, and the President of the International Court of Justice should be consulted for the appointment of the Chairman in disputes involving the two Governments.

140 In particular, the parties pay their own arbitrators (the one appointed by them separately), and share the costs of the Chairman and associated expenses.
legal remedies nor resorting to arbitration proceedings is compulsory. Access to the local legal system is a guarantee of the legal rights of private investors, and the acceptance of the jurisdiction of an arbitral tribunal by a State must be voluntary, for the State has sovereign immunity (although it could be restricted) which can only be waived by the State itself. This is why no compulsory proceedings has been agreed in the process of dispute settlement involving a private party and a State. For the same reason, in a dispute between two equal Governments, arbitration is implied to be an compulsory procedure. The two Governments have in the Treaty waived their immunity from compulsory arbitration on an equal and mutual basis. Such concession is made between disputants of the same legal status.

In addition, the mere fact the both processes are arbitration proceedings also warrant some similarities. For example, the principle of fairness as reflected in the appointment of arbitrators is adopted in both proceedings. Under these proceedings, two arbitrators are appointed by the disputants respectively and the third is

\[141\] The Treaty does not expressly say so. But under Art.XII, a disputing party may after the failure of negotiation notify the other State of its wish to submit the dispute to an arbitral tribunal. The other party is required to respond in the manner prescribed in the Treaty. Otherwise, the initiating party, according to the agreed rules (Annex B of the Treaty) may proceed with arbitration, regardless of whether the other party accepts or not. Immunity to the proceeding has been waived by the State by its signing of the Treaty. Although the Treaty does not expressly address the situation where one party refuses to respond to the other’s request for arbitration, it sets up a mechanism which can in fact be followed without the other’s cooperation. In particular, one party should notify the other of its intention to resort to arbitration in accordance with the agreed procedures. After 60 days from the notification, the initiating party may ask the President of the ICJ to appoint the Chairman of the tribunal, even if the other party has not appointed an arbitrator within the prescribed time limit. The tribunal so formed may decide the place and time of arbitration, and may give default judgment by majority vote. The judgment so rendered is final and binding on the parties who signed the Treaty. For these reasons, the other party must respond within the agreed limitation of time in order to avoid a default judgment against it.
appointed in a neutral manner, either by the agreement of the previously chosen arbitrators or by the recommendation of a neutral authority.  

7.7. Application of the Treaty and National Law

Bilateral investment promotion and protection treaties base their existence on the principles of mutual benefit and common interest of the contracting parties in relation to investment-related activities. Foreign investment is today an important form of economic contact between countries. Individual borrowers have as much need to borrow money to finance their business operations as have individual lenders to invest their money for the highest return possible. So are the needs of a recipient country to keep a balance between attracting a high inflow of foreign investment and protecting the national economy, and the needs of a capital-exporting country to provide practical and effective protection to its nationals investing overseas. To pursue the best economic result through investment-related activities is thus the common interest of the host and investing countries. These common interests are intended to be protected by bilateral investment promotion and protection treaties.

In the case of the Australian-Chinese Agreement, the treaty is necessary in order to establishing some basic legal principles to guide cooperation between two countries with distinctive legal traditions. As have been seen, contrasts exist in many respects between Australian and Chinese laws, often resulting in different legal and practical consequences. For example, Australian law allows foreign investment to operate through public companies, private companies, partnerships or trusts; but Chinese law admits foreign investment only through solely foreign owned companies, Sino-foreign equity joint ventures and Sino-foreign contractual joint ventures. These legal entities recognized under the law of the two countries overlap to a degree. A partnership in Australia is subject to a special set of tax laws, but in China it may be

142 The arbitrators appointed by the disputing parties can be a national of the disputing country. The arbitrators so appointed have an implied obligation, probably subtle in most cases, to their nominators, although their duties are to settle the disputes in accordance with their knowledge of common professional usages, international law and customs and natural justice. The third neutral person is designated to prevent possible conflicts between the arbitrators of the disputants. Different or conflicting views may be held by the arbitrators, but they are not the merely extension of the disputes between the disputing parties. In a sense the arbitral tribunal may be the continuation of the disputes at a higher level where the disputants have better legal and professional judgment on, as well as more realistic attitude to, the matters concerned. For general discussion of appointment of arbitrators, see P.O’Keefe, Arbitration in International Trade (Sydney, Prosper Law Publications, 1975) 135-142; and J.Phillips, Arbitration: Law Practice and Precedents (Cambridge, ICSA Publishing, 1988) 21-2.

143 For example, see Preamble to the Treaty.
subject to a law applicable to any of the recognized forms of investment as the case may be. Similarly, conflicting legal principles are also found in the areas of nationalization, state immunity and executive discretionary power. A bilateral treaty, such as the Australia-China Investment Protection Treaty, provides assistance in the resolution of these current and potential legal difficulties by establishing a common ground which clearly sets forth the principles (legal or moral) relating to the protection of investment and associated activities.

The purposes of the Australia-China Investment Protection Treaty are, as indicated in the Preamble to the Treaty, to promote economic cooperations and capital flow between Australia and China, and to provide protection of international acceptable standards to investment between the two countries. The Treaty, like many other international treaties, can only pursue these purposes to the limits of the commitment the two Governments are prepared to make and of the laws which, sometimes, may not be directly changed by the executive branch of government. As have been seen, restrictions on the application of the Treaty, through phrases such as "subject to national law" are found in several of its provisions. These results in different effects being given to the Treaty under the laws of Australia and China. The Treaty is to be implemented with these agreed variations.

The restriction "subject to national law and policies" recognizes the different practices of the contracting parties with regard to the same matters. This feature is evident in the area of exchange control, where Article X of the Treaty requires a contracting party to permit free transfer of investment-related funds in accordance with its law and policies. The application of the provision results in different consequences in Australia and China, because the Chinese Government has adopted complicated exchange control measures, whereas the Australian Government has greatly relaxed its control measures. The wording of the Treaty, however, allows the Chinese Government to maintain its control measures subject to the provision that the funds can be "transferred freely and without undue delay".

In fact, the freedom to transfer funds is not absolute under the Treaty. Rather it can be argued to be a freedom within the limits of national law and policies. Thus, it is not clear to what extent restrictions on free transfer of the funds is allowed under the Treaty. On one hand, the Treaty purports to provide protection to the investors' rights to transfer their investment-related funds. On the other, their rights to do so are subject to national laws and policies, which are however restrained by the agreed principles of "fair and equitable treatment", "non-discrimination" and "most-favoured-nation treatment". None of these principles directly supports an

144 For example, para.4 of the "preamble", Arts.III, IV1, V, VIII1, X & XI.
unconditional right to transfer investment-related funds between Australia and China.

Nevertheless, the Chinese Government may not interpret the provisions in such a negative manner. For the purpose of attracting more foreign investment, it is likely to relax its control measures to the extent which meets the minimum needs of foreign investors. In practice, the implementation of the Treaty will require the active cooperation of the contracting parties on the basis of economic interdependence, rather than on the ground of strict legal obligations.

This flexibility, compromising language and soft rules are features of bilateral treaties, in particular, between countries with different legal traditions. In a bilateral treaty, no State can impose its own legal system, principles derived from its own legal tradition and measures in favour of its interest on the other State. But a State may make concessions unilaterally in either express or implicit terms to other State in order to receive economic or political benefits in return. This is the basis of the Australia-China Investment Protection Treaty, where the two Governments have agreed to undertake specified obligations under the condition "subject to their national laws". Given the differences in their legal systems, provisions containing this formula rarely set out specified rules for treaty implementation. The parallel structure allows the contracting countries to maintain their distinctive legal systems, while adjusting their laws and policies for the purposes of implementing the Treaty.

145 Only in the provisions on expropriation and nationalization, and dispute settlement, the rules are relatively certain and specific. Even in these provisions, however, the phrase "in accordance with national law" is still adopted in some places where differences in the Australian and Chinese laws can be found. The Treaty, Arts.VIII & XII.
Conclusion

An issue arises repeatedly in this thesis is the exercise of executive power in Australia and China. The executive power in China is wider than the executive power in Australia in several respects. First, the Executive in China has subordinate legislative power which can be exercised without direct authorization from the legislature. Secondly, the exercise of executive discretions in China is not subject to any effective means of control, e.g. to close judicial supervision. Thirdly, the Chinese Executive Government extensively involves itself in commercial and business activities, through either the State plan or direct involvement in commercial transactions. These features of executive power have resulted in very different approaches to the regulation and administration of foreign investment in China compared with those adopted in Australia. Today, foreign investment law and policy in Australia are based on the direct or indirect sanction of statutes and the limited discretionary power of the Executive; while in China they are based on Acts, subordinate regulations and broad executive power. Because of the existence of subordinate legislative power in China, the boundary between regulations which are enforceable in courts of law and policy which is not enforceable is often unclear in China. The Executive has a discretion in choosing to make regulations or policy. The situation is further confused by overlapping in the use of terms in China. For example, a banfa or guiding could be a policy or a rule of law, depending on what effect is given by the Executive who made it. This requires that the status of a particular rule or measure must be determined according to circumstances.

Another issue which affects the approach to the regulation and administration of foreign investment in Australia and China is the State system of each country. The division of power between the federal and State governments in Australia restricts to some extent the federal power to regulate foreign investment. Mining and newspaper sectors are examples. This requires active cooperation between federal and State governments. An example of such cooperation is the joint statement by the federal Minister for Resource, the Acting Minister for Mines for South Australia and Queensland Minister for Resource Industries on the granting of petroleum and gas exploration permits to several companies in June 1990.1 The Chinese Government is not subject to any such limitation and thus may regulate or deal with any issues of foreign investment in any way it considers appropriate. This

1 The Ministers announced that in Western Australia Nocen International Ltd had been granted a permit over Area W89-13, and Petrofina Exploration Australia S.A. and the Shell Company of Australia Ltd had been granted a permit over Area W89-14; and in Queensland Comalco Aluminium Ltd had been granted a permit over Area Q89-1. News Release for the Minister for Resources on 20 June 1990. DPIE 90/129J.
difference between the Australian and Chinese foreign investment and law and policy should be noted by foreign investors in both countries, and in particular by Chinese investors in Australia.

Exchange control can be used as a means of encouraging or discouraging foreign investment in a particular sector of the economy, and of conserving foreign exchange for a country. Australia adopted exchange control measures mainly as a method of encouraging or discouraging the flow of foreign investment in a particular industry before 1983. It was a result of the Government's direct or indirect involvement in the market, in particular, the financial market. Thus, following the Government's substantial deregulation in many industries in the 1980s, foreign exchange control measures which give the Government power to monitor closely the movement of foreign investment in many sectors of the economy have been suspended, although not formally abolished. Unlike Australia, China has adopted foreign exchange measures mainly for the purposes of conserving foreign exchange. The shortage of foreign exchange has been a problem in developing the Chinese economy since 1949. Before 1978 when China adopted the open-door policy, the Chinese Government had exercised strict control over the then limited amount of foreign trade. Foreign exchange was carefully balanced by the Government's direct control of imports and exports. After 1978, direct involvement of the central Government in all foreign trade or investment activities become impossible. Exchange control measures were adopted to monitor and restrict the use of foreign exchange in a way which results in a shortage of foreign exchange in China. This means that as long as Chinese currency is not regarded as one of the "hard currencies", foreign exchange control measures in China will continue, although particular measures may be relaxed depending on the success of China's modernization program.

Exchange control measures in China are designed to encourage long-term foreign investment and projects which can generate foreign currency income. In this sense, China and Australia share similarities in the use of exchange control measures, i.e. encouraging or discouraging foreign investment in a particular industry or type of business. As a result of foreign exchange control in China, foreign-related enterprises which export all or most of their products do not feel the restraints of the control measures. But enterprises which target the Chinese domestic market may have difficulties in converting their profits into foreign currencies. The Australia-China Foreign Investment Protection and Promotion Treaty provides in principle for free conversion of foreign currency in the two countries. But the access to foreign currency is subject to the national law and policy, which may in fact restrict such access. The implementation of the Treaty in practice is still to be seen.
Taxation is a means of encouraging foreign investment in Australia and China. Australia imposes the same taxes on local and foreign investment and encourages foreign investors by giving them national treatment in taxation. The Chinese Government imposes different taxes on foreign investment and on local enterprises and encourages foreign investment by making many tax concessions available. The differentials between the taxes on foreign investors and local enterprises in China are not discriminatory, because foreign investors are given many privileges which are not available to Chinese enterprises. The differences in the taxation of foreign investment and of local enterprises in China are inevitable in the present Chinese economic system which mixes the State planned economy and a market economy. This situation will continue as long as China maintains an open-door policy without at the same time making fundamental changes to its economic system. Such changes could involve either (like most East European countries) moving towards a market economy or, (in Deng Xiaoping's terms) succeeding in China's socialist modernization, which is envisaged as a combination of Chinese socialist ideology and Western technology.

The settlement of foreign investment or trade disputes between Australia and China is assisted by the Investment Protection and Promotion Treaty between the two countries. Today, non-judicial means of dispute resolution have been widely accepted in Australia and China, in particular, in the area of commercial dispute resolution. Negotiation, mediation and arbitration are familiar to businessmen in both countries. There is no doubt that any dispute arising from two-way investment between Australia and China will be dealt with in the light of these methods, which have the advantage of maintaining an amicable business relationship between the parties concerned. The Australia-China Investment Protection and Promotion Treaty confirms the use of these methods. Judicial remedies are also available to foreign investors in Australia and China. Although Chinese courts are relatively new to foreign investors, their importance in resolving foreign trade and investment disputes has increased. But their performance and efficiency in dealing with foreign investment and trade disputes remain to be seen. Access to judicial justice has been guaranteed by Chinese law, in particular in the case of Australians investing in China, by the Australia-China Investment Protection and Promotion Treaty.

Trade and mutual investment between Australia and China improved gradually in 1990. In this year, two-way trade between them recovered to about $2,425 million and two-way investment between them reached about $750 million, with Australian investment in China being $350 million and Chinese investment in
Australia being $400 million. Australian investment operates through about 80 joint ventures in China and Chinese investment in Australia involves mainly joint ventures at the Channar iron ore mine and in the Portland Aluminium Smelter.

In September 1990, the Fourth Meeting of the Australia-China Joint Ministerial Economic Commission was held in Beijing. The two countries undertook to develop further trade and investment relationships between them. In this Meeting, China in principle give assurances that it would continue to import Australian wool and would increase these imports as the recovery of its domestic economy gained momentum. The two countries also agreed to increase cooperation in a number of areas, including transport and communications where Australia has competitive advantages, infrastructure construction both in China and third countries, cooperation in the production of automotive components, continuing the projects under the Concessional Finance Facility which were in the pipeline prior to 13 July 1989, and cooperation in exchanging information and technology in the energy area. This Meeting establishes outlines for economic cooperation between Australia and China in 1991. Although the increase in the trade and investment between Australia and China is very much dependent upon the domestic economy of each country, the Meeting suggests a relatively positive prospect for Australian and Chinese economic relations. An understanding that growth in mutual trade and investment would be beneficial for both countries seems also to have been reached. This is certainly a step toward the normalization of their trade relations, which were substantially affected by the events in June 1989 in China.

As we have seen, the legal systems, and in particular the foreign investment laws and policies, differ substantially in the two countries. This thesis has identified many of the important issues in the exercise of legislative and executive power over foreign investment in the two countries. Such a comparison, it is hoped, will provide assistance to academics and practitioners in the two countries, and in other countries as well, in their efforts to understand Australian and Chinese foreign investment law and policy.

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2 News Release of the Minister for Trade Negotiation on 4 September 1990, Beijing.
3 Ibid.
Appendix: Selected Addresses of Authorities for Foreign Investment Control in China

Administrative Board of the Zhuhai Social Economic Zone, Administrative Building of People's Municipal Government, Xiangzhou District, Zhuhai, Telephone: 24811

Anhui Foreign Economic Relations and Trade Department, 135 Hongxing Rd, Hefei, Telephone: 76794

Beijing Municipal Committee of Foreign Economic Relations and Trade, 2 Zhengyi St, Beijing, Telephone: 5007201

Chongqing Committee of Foreign Economic Relations and Trade, 35 Linjian St, Chongqing, Telephone: 42766

Dalian Foreign Economic Relation and Trade Committee, 1 Stalin Square, Dalian, Telephone: 31480, 32643

Department of Foreign Economic Relations and Trade of Guangxi Zhuang Autonomous Region, Qixing Rd, Nanning, Telephone: 25581

Department of Foreign Economic Relations and Trade, 55 Heping Rd, Dongli District, Harbin, Telephone: 53627

Economic Technological Development Corporation, Dalin Economic and Technological Development Region, Jin County, Dalian City, Telephone: 34041

Foreign Economic and Trade Committee of the Municipal People's Government of Beihai, Donggong St, Municipal Government Building, Beihai, Telephone: 3381

Foreign Economic and Trade Department of Ningxia Hui Autonomous Region, 64 W Nanhuan Rd, Yinchuan, Telephone: 23731

Foreign Economic Committee of Hainan Administrative Region, Haifu Rd, Haikou, Telephone: 24907

Foreign Economic Relations and Trade Administrative Committee of Wuhan, 344 Jiefangdadao, Wuhan, Telephone: 56761

Foreign Economic Relations and Trade Committee of Jilin Province, 56 Stalin St, Changchun, Telephone: 24193

Foreign Economic Relations and Trade Department of Xinjiang Uygur Autonomous Region, 10 Yuanjie Rd, Urumqi City, Telephone: 24747

Foreign Economic Relations and Trade Department of Yunnan Province, 113 Huashan Rd (S), Kunming, Telephone: 28175

Fujian Provincial Commission of Foreign Economic Relations and Trade, 24 East Ave, Fuzhou, Telephone: 53616

Fuzhou Municipal Commission of Foreign Economic Relations and Trade, 24 Wushan Rd, Fuzhou, Telephone: 55223

Gansu Provincial Bureau for Foreign Trade and Economic Relations, 28 Dingxi Rd, Lanzhou, Telephone: 25321

Guangdong Provincial Commission of External Economic Relations, 305 Dongfang-Zhong Rd, Guangzhou, Telephone: 32444

Guangzhou City Committee for Foreign Economic Relations and Trade, Guangzhou Municipal Government, Telephone: 330360
Guangzhou Economic and Technological Development Region Control Commission, 2159 Dongfang Guesthouse, Guangzhou, Telephone: 669900-1159

Guizhou Provincial Bureau for Foreign Trade and Economic Relations, 13 Beijing Rd, Guiyang City, Telephone: 23792

Hebei Provincial Bureau for Foreign Economic Relations and Trade, 58 Beimalu Rd, Shijiazhuang, Telephone: 27869

Hunan Foreign Economic Relations and Trade Committee, 69 Wenhau Rd, Zhengzhou, Telephone: 32773

Hunan Provincial Bureau of Foreign Economic Relations and Trade, Wuyi Dong Lu, Changsha, Telephone: 26215

Jiangxi Provincial Department of Foreign Economic Relations and Trade, Foreign Trade Building, Zhangqian Rd, Nanchang, Telephone: 65983

Lianyungang Foreign Economic and Trade Commission, Jiefangshonglu, Lianyungang City, Telephone: 2854

Liaoning Provincial Foreign Economic Relations and Trade Committee, 1, Block 4, Beilin, Huanggu District, Shenyang, Telephone: 692067

Nantong Foreign Economic and Trade Committee, 41 Qingniandong Rd, Nantong, Telephone: 2336

Ningbo Foreign Economic Relations and Trade Commission, 182 Jiefang Rd South, Ningbo, Telephone: 62298

Office for Economic and Technical Development of the City of Qinhuangdao, 30 Wenhua Bei Lu, Qinhuangdao, Telephone: 4886

Qingdao Foreign Economic Relations and Trade Commission, 17 Hubei Rd, Qingdao, Telephone: 86701-363

Qinghai Provincial Foreign Economic Relations and Trade Department, 102 Shulin Xian, Xining, Telephone: 76806

Shaanxi Provincial Committee of Economic Relations and Trade, Xincheng (New City), Xi'an, Telephone: 27608

Shandong Provincial Commission of Foreign Economic Relations and Trade, 1 Shengfuqianjie, Jinan, Telephone: 23951, EXT 2155

Shanghai Foreign Economic and Trade Committee, 33 Zhongshan Yi Rd East, Shanghai, Telephone: 232200

Shantou Special Economic Zone Administrative Committee, The Longhu Processing Area, Eastern Suburb of Shantou City, Guangdong Province, Telephone: 34773

Shanxi Provincial Bureau of Foreign Economic Relations and Trade, 6 Xinxian St, Taiyuan, Telephone: 25721

Shenzhen Municipal Committee of Social and Economic Development, Municipal Government Building, Shennan Zhong Road, Shenzhen, Telephone: 38795

Sichuan Foreign Trade Commission, Chenghau St, Chengdu, Telephone: 32372
The Jiangsu Provincial Committee of Foreign Economic Relations and Trade, 50 Zhonghua St, Nanjing, Telephone: 23678

Tianjin Economic and Technological Development Region Control Commission, 221 Jiafangbei Rd, Tianjin, Telephone: 398540

Tianjin Foreign Economic Relations and Trade Committee, 55 Chongqing Rd, Heping District, Tianjin, Telephone: 314828 and 396143

Wenzhou Municipal Foreign Economic Trade Commission, 45 Fuxue Lane, Wenzhou, Telephone: 6262 & 7689

Xiamen Municipal Economic Relations and Trade Committee, Huli Industrial Zone Office Building, Xiamen SEZ, Fujian, Telephone: 41902

Yantai City Commission of Foreign Economic Relations and Trade, 16 Yuhuangding Rd, West Yantai, Telephone: 24451 Ext 556

Zhanjian Foreign Economic and Trade Committee, 67 Yuejinlu, Chikan District, Zhangjing, Telephone: 45239

Zhejiang Provincial Department for Foreign Economic Relations and Trade, 24 Changshen Rd, Hangzhou, Telephone: 22701


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