Joint ventures in China: overview

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domestic company joint ventures (jvs)

1. Are JVs expressly regulated?

Under the General Provisions of Civil Law (Civil Law), JVs are specifically divided into the following three categories:

- Corporate JVs.
- Partnership JVs.
- Contractual JVs.

Each is regulated under relevant laws including the:

- Company Law.
- Partnership Enterprise Law.
- Contract Law.
- General Provisions of Civil Law.
- Sino-Foreign Equity Joint Ventures Law.
- Sino-Foreign Co-operative Joint Ventures Law.
- Anti-Monopoly Law.
- Administrative Provisions on Registration of Partnership with Foreign Capital.
- Administrative Measures on the Establishment of Partnership Enterprises in China by Foreign Enterprises or Individuals.

2. Which types of JV are allowed?

The legal regime of the People's Republic of China (PRC), allows both contractual JVs and corporate JVs. In addition, partnership JVs are also permitted.

Contractual

Contractual JVs are established under a contract that stipulates that each participant operates the business independently from each other, and respectively assumes civil liabilities, rather than joint and several liabilities.

Corporate

A corporate JV can be established by enterprises or by an enterprise and an institution. A corporate JV is a newly-established economic entity that must independently assume liability and is subject to the Company Law. Under the Company Law, a JV can be a company with limited liability or a joint-stock limited company.

Others

A partnership JV can be established by enterprises or by an enterprise and an institution. Partnership JVs are subject to the Partnership Enterprise Law and operated according to a partnership agreement.

3. What are the principal corporate/company laws governing corporate JVs?

A corporate JV, whether it is a limited liability company or a joint-stock limited company, is subject to the Company Law. A corporate JV with foreign elements must also comply with Sino-Foreign Equity Joint Ventures Law, Sino-Foreign Co-operative Joint Ventures Law and their respective implementation rules.

Formation and registration

4. What are the typical founding documents for a corporate JV?

A joint venture contract and the company's articles of association are typically the most critical for a corporate JV, however it is possible to limit this to just the articles of association. To formally establish the corporate vehicle, several supporting and administrative documents are required. These include:

- Incorporation certificates/ID copies of the founders.
- Appointment letters for the directors, supervisors and general manager.
- Certificate of premises.
- Government forms.

5. Is the use of foreign language in a JV's founding documents (both corporate and contractual) restricted?

The founding documents are typically reviewed by the competent authorities in China during registration or anti-monopoly approval processes, and the competent authorities will only accept founding documents in Chinese. If these documents are executed only in a foreign language, the competent authorities normally request these documents to be translated into Chinese by a certified translation company with affixation of the company seal or by personal signature of the legal representative. In practice, competent authorities often accept bilingual founding documents as a way around this.

6. Are public officers (for example, public notaries) involved in a JV's formation procedure?

Domestic JVs in China do not require public officers to be involved in the formation procedure.
7. Are JVs registered with any local registries? Are public sector bodies’ authorisations required for a JV’s establishment?

Local registries
A corporate JV or a partnership JV must be registered with the local branch of the State Administration for Commerce and Industry.

Public sector bodies
If the business scope (being the proposed business activities) of a corporate JV or a partnership JV contains any item which is subject to the other authorities’ approval or licences then such approvals must typically be obtained from the relevant regulatory authorities before the registration.

The establishment of a JV (corporate JV, partnership JV or contractual JV) is also subject to Anti-Monopoly Law in certain circumstances. Unless prior approval is obtained, the Anti-Monopoly Law prohibits the formation of JVs that would have the effect of restricting or eliminating competition. The formation of a JV can be interpreted as a formation of concentration by contract. Therefore, a JV is potentially subject to prior approval by the Anti-Monopoly Bureau of the Ministry of Commerce when the revenue of the JV participants exceeds a certain threshold.

These approvals or filings are compulsory and cannot be bypassed through self-assessment by the JV parties themselves.

8. What other formal requirements must be complied with to validly constitute a JV?

The authorities have significant discretion to seek additional information on a case-by-case basis. Subject to these requests, there are no other formal requirements that must be complied with to validly constitute a joint venture other than those described in Question 7.

Permitted markets

9. Can the JV structure be used in every industry sector? Are there any restrictions to be considered and carefully assessed before investing in a JV?

A domestic JV is subject to local or state regulatory approval, depending on its proposed business sectors. Historically, certain industries have been exclusively run by state-owned enterprises and are not open to private enterprises. These include:

- Major infrastructure, including telecommunications, ports, roads and airports.
- High-speed railways.
- National grid systems.
- Defence industries.

However, the government now allows private parties to invest in some but not all of these sectors.

Purpose

10. Can a JV be established with any purpose?

For a contractual JV under the Contract Law, the purpose must be legitimate and not be harmful to China’s national interests and social interests.

Both corporate and partnership JVs must:

- Comply with all laws and administrative rules and regulations.
- Observe social morals and business ethics.
- Conduct business in good faith.
- Subject themselves to the supervision of the government and the public.
- Fulfill the JV’s social responsibilities.

The business scope of a JV is also subject to the regulations of the State Administration for Commerce and Industry (through its local branches).

Share capital and participation

11. What possible forms of participation are there in a JV’s share capital? How can a JV member contribute and are there statutory limits on the possibility to make contributions in kind?

For a corporate JV, share capital can be contributed in cash or contributions in kind, including:

- Tangible assets.
- Intellectual property.
- Land use rights (being the Chinese form of leasehold (rather than land ownership)).

For a partnership JV, the general partner can make the contribution in:

- Cash.
- Tangible assets.
- Intellectual property.
- Land use rights.
- Provision of labour.
- Other contribution (however, contribution by way of provision of labour by a limited partner is not permitted).

Since the participants operate the JV’s business independently under a contractual JV, there is no share capital issue for a contractual JV.

12. Can a corporate JV’s share capital be denominated in a foreign currency?

The Administrative Rules for Registration of Companies (Registration Rules) provide that a domestic JV can only use the Chinese currency (Renminbi) as the currency for its share capital.

Duration and limits on membership

13. Are there statutory limits on a JV’s duration?

Under the Company Law, there are no statutory limits on the duration of a company in China. However, since the expiry of the term of a JV company is a key event for the termination of a JV, the Registration Rules provide that the term of a company is a statutory item for registering a new company and must be included in the articles of association.
14. Are there statutory limits on the number of members participating in a JV?

Under the Company Law, the minimum number of members of a JV in the form of a limited liability company is two and the maximum number of members is 50. For a joint-stock limited company, the Company Law sets out a requirement that, to establish a joint-stock limited company, the number of promoters/initiators or initial members of a joint-stock limited company must be between two and 200, more than half of whom must be ordinarily domiciled in China.

The Partnership Enterprise Law provides that the participants of a limited partnership must be between two and 50 and at least one participant must be the general partner.

There are no statutory limits as to the number of members participating in a contractual JV. However, from a practical standpoint, a large number may be unwieldy to manage.

Public sector bodies

15. Can a public sector body enter into a JV agreement? Subject to what conditions? In particular, do public private partnerships (PPP) laws and regulations apply?

Practically, it is possible for a public sector body to enter into a JV agreement with a private sector body. The PPP model is playing an increasingly significant role in various sectors in China, especially in the public infrastructure sector. However, currently there are still no unified and specific PPP laws and regulations in place in China. Laws and regulations applying to PPP projects exist in different relevant areas of laws. The main rules governing PPPs are scattered throughout various administrative regulations and local policies.

It is notable that, in a partnership JV, any of the following cannot be a general partner bearing unlimited liability of the partnership:
- A wholly state-owned company.
- A state-owned enterprise.
- A listed company.
- A public welfare institution.
- A public organisation.

Non-competition and anti-trust clauses

16. Are there statutory constraints on the use of non-competition or anti-trust clauses in a JV agreement?

Since the Anti-Monopoly Law came into force on 1 August 2008, non-competition clauses in a JV/shareholders’ agreement are treated cautiously by the Anti-Monopoly Enforcement Agency.

According to the Anti-Monopoly Law, the Anti-Monopoly Law Enforcement Agency must be notified in advance where the "concentration" of market players reaches the prescribed threshold. Until obtaining the approval, they cannot proceed with the proposed co-operation. The Anti-Monopoly Law Enforcement Agency will weigh up the anti-competitive effect with any pro-competitive effect of concentration. According to Article 28 of the Anti-Monopoly Law, "if the operators concerned can prove either that the favourable impact of the concentration on competition obviously exceeds the adverse impact, or that the concentration is in harmony with the public interest", the Anti-Monopoly Law Enforcement Agency under the State Council may decide not to prohibit the concentration.

In some circumstances, the Agency can decide to impose restrictive conditions, such as the removal of the non-competition clause, in order to reduce the adverse impact of the proposed structure on competition.

De facto company/partnership

17. Must the contractual JV satisfy any conditions to avoid failing within the definition of de facto company/partnership?

A JV may be deemed as a partnership JV even if the JV has not been registered with the authorities but has the features of a partnership, according to Article 50 of the Opinions of the Supreme People’s Court on Several Issues Concerning the Implementation of the Civil Law.

Limiting member liability

18. Can a JV agreement provide that a JV member can participate without incurring any risk, loss or reward?

For a corporate JV, such a clause may cause the whole agreement to be void. According to the Explanatory Note on Certain Issues on Trial of the Disputes of JV Contract by the Supreme Court of the PRC (only applicable to the corporate JV/members), there are two circumstances that will make the contract/agreement void:
- If one of the JV members invests in the business and participates in the operation but only shares the profits without bearing any risk/loss, the clause will be invalid and the member must return the extra benefits obtained under the clause to the JV.
- Where one of the JV members invests in the JV but never participates in the operation and never bears the risks/losses. This will violate a key legal principle under PRC laws and the JV arrangement may be deemed as an illegal lending activity that will cause the whole contract to be void. If there are individual participants/members, the principle of free will is likely to be adopted by the court, as set out in the Contract Law.

A partnership JV can reach any agreement in relation to risk and loss sharing between its members.

Anti-trust

19. Do any anti-trust rules, guidelines or policies apply to a JV agreement?

The Anti-Monopoly Law, including, but not limited to, abuse of dominant position and regulation of mergers and acquisitions activities, is applicable to a JV agreement. The Anti-Monopoly Law Enforcement Agency must be notified in advance and clearance sought where the "concentration" of market players reaches the prescribed threshold. Until obtaining the approval, they cannot proceed with the proposed acquisition by entering into a JV agreement.

Governance and limits on directors

20. Can the parties to a JV freely regulate the JV or are they subject to certain restrictions?

Under the Company Law, the shareholders’ meeting is the governing authority of a company/domestic JV. Shareholders’
voting rights depend on the proportion of their respective equity interests. The board is responsible to its shareholders.

A partnership JV and contractual JV can have flexible arrangements in relation to the governance in their respective partnership/contractual agreements.

21. Are there limits or restrictions on the eligibility of an individual as a member of the board of directors/statutory auditor?

Generally under the Company Law, the following individuals are not eligible to be appointed as a member of the board of directors, board of supervisors or senior management:

- Those with no (or limited) civil capacity.
- Those sentenced for a crime due to an offence of corruption, bribery, encroachment of property, misappropriation of property or undermining the socialist market within the last five years.
- Those who served as the legal representative, director or manager, and were personally responsible for the bankruptcy/liquidation of a company or enterprise due to mismanagement within the last three years.
- Those who served as the legal representative of a company or enterprise whose business licence was revoked due to its violation of law, and who were personally responsible for the revocation, and the revocation occurred less than three years ago.
- Those in default of a personal debt of a significant amount.

However, directors, supervisors and senior managers in certain sectors (for example, a securities company or listed public companies) are regulated by different laws or regulations in relation to their appointment eligibility. There are no limits or restrictions on the nationality and the ordinary place of residence of the individual as a member of the board or as statutory auditors.

Termination

22. What legal regime applies to a JV’s termination? Can a JV be terminated for just cause on request of one party?

Under the Company Law, a JV can be terminated:

- On the expiry of the term of the JV, or as set out in the articles of association.
- As per the approval of the shareholders.
- Due to merger or division of the JV.
- Where the business licence of the JV is revoked by law or the JV is ordered to terminate or be cancelled.
- Where the JV is dissolved by the court in accordance with the Company Law.

In some special circumstances, such as the JV experiencing serious difficulties in its business, shareholders (more than 10% of voting rights) can apply for a termination of the JV by the court.

For a partnership JV, it may be terminated when:

- The term of the partnership expires and the participants decide not to extend the term.
- A cause of termination specified in the partnership agreement occurs.
- All the partners decide to dissolve the partnership.

- The number of partners does not meet the statutory requirements for 30 days.
- The objective of the partnership specified in the partnership agreement has been achieved or becomes impossible to achieve.
- The business licence is revoked, or is ordered to be closed down or is dissolved according to laws and regulations.
- Other reasons provided by laws or regulations occur.

A contractual JV can be terminated under the Contract Law, namely through mutual agreement or under statutory conditions for the unilateral termination, or one or more of the termination conditions provided in the JV contract is satisfied.

In addition, if the parties to the JV cannot agree with each other in resolving a dispute, they may be able to terminate the JV through arbitration or court proceedings.

23. Is the termination of a JV agreement subject to any public sector body’s approval?

For a corporate JV or a partnership JV, the de-registration process will be undertaken with the local State Administration for Commerce and Industry and in accordance with the relevant administrative procedures.

Choice of law and jurisdiction

24. Are there constraints on the choice of the law and the jurisdiction applicable to a JV?

All JVs established in the PRC are subject to PRC law. The jurisdiction for disputes can vary depending on the parties to the JV. The principle is that a dispute without any foreign-related element is submitted to the jurisdiction of a domestic court or arbitration institution.

JVS WITH FOREIGN MEMBERS

Validity and authorisation

25. What are the rules relating to validity and authorisation of JVs with foreign parties?

Subject to restrictions under the foreign investment policy and other relevant laws it is possible to have foreign parties in a JV in the PRC. There is no requirement on the minimum or maximum number of Chinese parties and it is possible for two foreign investors to form a JV in China and that the JV is then categorised as a wholly-owned foreign enterprise.

Effect of foreign membership

26. Are any of the rules relating to domestic company JVs (see Question 1 to 24) different for JVs with members incorporated under, or governed by, the laws of a foreign country?

Laws and regulations

Sino-foreign JVs are subject to the PRC Law on Sino-foreign Equity Joint Ventures (SFEJV) or the PRC Law on Sino-foreign Contractual Joint Ventures (SFCJV).
Public sector and restrictions

The establishment of a JV with foreign members is subject to the filing of the Ministry of Commerce (MOFCOM) or its local counterparts. JVs which are subject to special administrative measures for admission will need to seek other clearance. For JVs with foreign parties, certain documents provided by the foreign parties must be notarised by the notary public at the country of the foreign parties and authenticated by the Chinese Embassy or Consulate based in that country.

JVs with foreign members are subject to restrictions and prohibitions in a number of sectors under the Foreign Investment Industries Guidance Catalogue (Catalogue) and Negative List for Admission of Foreign Investments (Negative List) jointly issued by the National Development and Reform Commission and MOFCOM from time to time. The most recent versions of the Catalogue and Negative List were issued on 28 June 2017 and became effective from 28 July 2017. Therefore, it is important to confirm whether the sectors to be invested in are subject to any restriction or prohibition.

The State has relaxed its foreign investment controls in recent years. It is expected that JVs with foreign members will be subject to fewer restrictions and will be treated as domestic company JVs in the administration by the authorities.

Foreign currency

JVs with foreign members can refer to a foreign currency or RMB as the denominated currency for capital contribution.

Termination

As the governing authority of a JV with foreign members is the board of directors or joint management committee (for SFCJV only), it can be terminated under the termination provisions of the articles of association or by the approval of the board of directors. Also, under the SFEJV Law and SFCJV Law, a SFEJV or SFCJV must be dissolved in any of the following situations:

- Expiration of the JV term.
- Where a serious loss occurred and the JV is unable to continue its operation.
- Failure of either party to fulfill its obligations defined by the contract or the articles of association, due to which the JV is unable to continue its operation.
- The enterprise cannot continue to operate due to serious losses due to a force majeure event.
- Other reasons as defined by the JV contract and the articles of association.

Under the SFEJV Law, if an SFEJV is unable to obtain the desired objectives of the operation and does not have a prospect for future development at the same time, it must also be dissolved. The SFCJV Law provides another situation under which the SFCJV must be dissolved (where the SFCJV is ordered to close down in accordance with the law due to a violation of laws and/or statutory regulations).

The termination of an ordinary SFEJV or SFCJV is subject to the filing with the authority that originally filed the establishment of the JV. In addition, the JV must be de-registered with the local branch of the State Administration for Commerce and Industry. SFEJVs and SFCJVs that are subject to special administrative measures for admission may need to seek additional clearance during termination processes.

Economic or financial incentives

27. Are there economic or financial incentives for foreign direct investments in a JV?

At a national level, China adopts a flat rate for enterprise income at a rate of 25%. This was introduced by the Enterprise Income Tax Law in 2007, which abolished the differentiated treatment between domestic enterprises and foreign-invested enterprises. Local governments and the sub-economic or development zones may also have the power to incentivise foreign-invested companies. Therefore, it is important to also examine local regulations and conditions before making any investment in a particular location.

Minimum investments/contributions

28. Are there mandatory minimum equity investments or contributions in kind thresholds for a foreign JV member?

According to the Law on Sino-Foreign Equity Joint Ventures or the Law on Sino-Foreign Contractual Joint Ventures, the foreign member of a JV must contribute at least 25% of equity capital. Contributions below this will result in the entity not being classed as a Sino-Foreign Joint Venture from a tax perspective.

THE REGULATORY AUTHORITIES

Ministry of Commerce (MOFCOM)

Main activities. Regulating foreign trade, export and import, foreign direct investments and market competition.

W www.mofcom.gov.cn

State Administration for Commerce and Industry (SAIC)

Main activities. Corporate registration and licensing.

W www.saic.gov.cn
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Professional qualifications. Commercial; mergers and acquisitions; private equity; foreign direct investment.
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- Worked on numerous high-profile transactions involving non-Chinese parties investing in China’s automotive, aviation, consumer goods, real estate and retail sectors.
- Helped many Chinese and other parties around the world on transactions that involved Chinese investors entering sectors such as agribusiness, aviation, consumer goods, real estate, resources and retail.
- Regularly help non-Chinese parties with their Chinese investment strategies.
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Professional qualifications. Mergers and acquisitions; joint ventures; new business establishment; corporate and strategic advice; corporate governance; employment law.
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- Regularly advise foreign investors on structuring and implementing investments in China and provide ongoing advice to joint ventures and wholly foreign-owned enterprises.
- Provide regular assistance to corporate clients including multinational corporations with interests across industries in China, such as energy and resources, residential and property, aviation, education, healthcare, medical devices, food and beverage, manufacturing, retail and consumer products.