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# CHINA Legal Bulletin

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## Executive Summary

### **Foreign Exchange Regulations Amended**

As the economy matures, the Chinese government is responding with adjustments to some of the fundamentals of the Chinese economic system. One obvious example is the policy adjustment on the control of foreign exchange inflows and outflows, which is the subject of recent amended regulations. Among the major changes is the shift from a free intake and checked outflow to a more equalized process on both ends. Also, restrictions on foreign deposits by domestic entities have been lifted, and stricter controls have been introduced to ensure that money is properly accounted for and not representing any illegal interests.

*Pan Lidong and Deng Yong*

### **Recent Revisions to Rural Land Use Rights**

While all land in China remains property of the state, land use rights are once again gaining prominence as a tool for development. In an effort to promote the development of rural areas, the government has issued decisions which allow greater flexibility on the part of farmers and small communities to leverage their land for their own interests. In this article we provide the requisite background information to understanding this ever changing issue, and a peek into what we think the future might hold for those looking to invest in property in China.

*By Zachary Wortham, Phenix Zheng, and Cristina Di Luigi*

## NEWS FLASH

### **Wang Jing & Co. Joins Terralex**



Wang Jing & Co. Law firm has been asked and has agreed to join the Terralex legal network ([www.terrallex.org](http://www.terrallex.org)), a leading, worldwide network of independent law firms. Terralex boasts a global network of the top law firms from more than 200 countries, districts, and cities, with thousands of attorneys covering all practice areas of the legal profession. After respected firms Liu, Shen & Associates and Hylands Law Firm in Beijing, and All Bright Law Offices in Shanghai, Wang Jing & Co is the fourth member of Terralex in China, and the sole member in Guangzhou, the largest city in the South of China and the capital of the richest province in China, Guangdong. Membership will further aid Wang Jing & Co. in its goal of providing complete, international, multidisciplinary legal services to each of its clients whether in China or abroad. This relationship will also serve to upgrade the competitive strengths and level of service our firm is already providing in the Chinese legal services market.

EXECUTIVE EDITOR:  
WANG JING

SENIOR EDITOR:  
MAARTEN ROOS

EDITOR AND DESIGN:  
ZACHARY WORTHAM

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# Foreign Exchange Regulations Amended



## Foreign Exchange Regulations Amended

The amended Regulations on Foreign Exchange Administration (**New Regulations**), promulgated on August 5<sup>th</sup>, 2008 by the State Council, show a major shift in Chinese policy towards foreign exchange matters.

### 1. Redirecting foreign exchange capital from Outflow Management into Equilibrium Management

Since the early 1990s, the shortage of foreign currency led the Chinese government to adopt policies on foreign trade and foreign investment aimed at encouraging the inflow of foreign capital and severely restricting the outflow of foreign capital.

More recently, foreign exchange reserves have grown so rapidly that by the end of June 2008, Chinese foreign exchange reserves had reached USD 1.8 trillion, an increase of 35.73% over the previous year. Holding such a huge amount of foreign exchange reserves increases the financial risk of devaluation and encourages international speculation. Thus the New Regulations call for the Equilibrium Management of foreign capital, a shift away from policies restricting and supervising only the outflow of foreign capital, towards including normative restrictions and supervision policies for the inflow of foreign capital as well.

### 2. The foreign income of a domestic entity or individual may be transferred into the territory of the Peoples Republic of China or deposited overseas.

The former regulations included a compulsory administrative system for the settlement of foreign exchange income of domestic entities. This system stipulated that all foreign exchange income of domestic entities under normal trading and service transactions shall be transferred back to China and shall not be deposited abroad, which shall then be sold to the designated foreign exchange banks or upon approval, deposited in foreign exchange accounts with these banks for financing foreign exchange operations. The foreign exchange banks then sell the foreign exchange to the Peoples Bank of China, where it becomes part of the foreign exchange reserves.

The New Regulations cancel these compulsory provisions on domestic entities, allowing them to deposit the foreign exchange overseas, or to transfer the funds back to China where it can either be sold to a bank, or deposited directly in the entity's foreign exchange account. The aforesaid provisions thus allow entities and individuals greater freedom when dealing with foreign currencies.

### 3. Foreign income and expenditures under normal trading and service transactions shall be based on authenticity and lawfulness. Financial institutions dealing in the sale of foreign currencies or settlement business shall reasonably examine the authenticity of the transaction documents and the consistency between the foreign exchange income and expenditures.

The New Regulations greatly simplify the procedures for verifying foreign exchange transactions. Financial institutions conducting the sale of international currencies or settlement business must reasonably examine the authenticity of the transaction documents and the consistency between foreign exchange income and expenditures. Meanwhile, the State Administration for Foreign Exchange (SAFE) shall supervise and inspect these procedures, either through registration requirements, off-site data checks, or on-site inspections.

Taking the processing trading business as an example, recently a local SAFE has requested that companies which include processing trade in their business scope submit customs entry documents when the finished goods arrive at the processor (or purchaser), and when processing charges (usually in a foreign currency) are collected. In the past, companies could only collect foreign currencies based on the customs declaration form of the exported finished products. This stricter requirement for documentation indicates that the SAFE is adopting a hard line when it comes to potentially fraudulent activity.

### 4. Strengthening the monitoring of cross-border capital flows

The New Regulations further strengthen the monitoring of cross-border capital flows. Financial institutions shall handle foreign exchange business through foreign

## LEGAL UPDATE:

### Labor Contract Law Implementations

In recent months, local authorities have issued a number of regulations in regards to the Labor Contract Law:

- Companies located in Tianjin are now required to engage in annual collective wage bargaining with employee unions; where all information requested must be given 5 days before bargaining and the rate of wage increases in collective wage bargaining agreements must follow guidelines issued by local government. Failure to engage in collective wage bargaining could result in the local labor bureau becoming actively involved and/or the loss of preferential tax treatment.

- The Regulations of Promotion of Harmonious Labor Relations in the Shenzhen Special Economic Region recently issued provide for bargaining on labor compensation, working hours and labor discipline, and authorize collective bargaining on major matters. The term major matters however has not been defined. The Shenzhen regulations also indicate that such national unions as the All-China Federation of Trade Unions will be able to send professional negotiators into collective bargaining at the enterprise level.

- In Shandong province companies that want to lay off 40 or more workers have been told they must first apply for approval from their local human resources and social security authorities. The order is an interpretation of the national Labor Contract Law, which states that all companies that want to lay off more than 20 employees must first get approval from their labor unions and report their layoff scheme to the labor authorities.

- The Hubei provincial human resource and social security department stated that companies must report to local governments 30 days in advance if they want to lay off 50 or more employees, or 10 percent of their total workforce.

# Foreign Exchange Regulations Amended cont.



exchange accounts, and file with the SAFE any foreign exchange income and expenditures by its customers and any changes in the foreign exchange accounts of its customers. The SAFE is entitled to monitor all cross-border capital flows and shall strictly enforce the law.

## 5. Strengthening the punishment for illegal activities

The penalty for illegal inflow of capital, illegal exchange settlement, violation of the administration of exchange settlement funds flows, and illegally carrying foreign exchange when entering or exiting PRC territory is set at not less than 30% of the involved amount, and in cases of serious violation up to 100% of that amount. Anyone caught altering the use of foreign exchange or foreign exchange settlement funds

without authorization will be penalized at less than 30% of the total amount, or between 30% and 100% in case of serious violations.

By Pan Lidong & Deng Yong

# Recent Revisions to Rural Land Use Rights

## Recent Decisions on the Transfer of Land Use Rights

### Background

The protection of property rights has always been an enigmatic issue in China. Only in October 2007, did China's first Property Law become effective. This marked a historically important change in the way China perceives private property rights and regulates public and private property. In fact, equal protection is granted to public and private properties, contravening the long tradition in favor of public ownership over private ownership. Along these same lines and in an effort to help grow wealth in less affluent rural areas, on October 12<sup>th</sup>, 2008, the Central Committee of the Communist Party passed the *Decisions on Several Important Issues in Promotion of Rural Reform and Development* (the Decisions). Crucially, the Decisions give farmers the right to lease, assign, exchange, and carry out transactions related to their land use rights (in joint shareholding entities). This, it is hoped, will help balance urban and rural development and improve food safety and supply issues and could have the effect of modernizing rural finances.

The Decisions stress that the current rural infrastructure needs improvement and that during the reform process; the authorities should liberate and develop rural productivity by taking full advantage of the market system when allocating resources and coordinating the development of urban and rural areas. This approach attempts to consolidate farming production to make it more efficient, while at the same time providing farmers with a new

source of income from unused land to start new businesses.

In addition, the new policies are also expected to attract more investment in rural areas, a way to provide the necessary funding for the modernization of agriculture processes and urbanization. A comprehensive plan for industrial development, infrastructure development, the creation of public services, and a response to employment needs is expected in the near future.

### Existing Conditions for Marketable Land Use Rights

In order for China to achieve its aim of stimulating the rural economy through the use of marketable land use rights, China will need to be able to guarantee the existence, certainty, security and enforceability of property rights in the long-term. However at present, Chinese law does not allow for the full and unrestricted ownership of land. In fact, the Chinese Constitution states that land in urban areas is owned by the State and land in rural and suburban areas is owned either by the State or collectives, and no individual or organization may own land. In accordance with the constitutional dictate, Article 47 of the recently-adopted Property Law confirms that the State owns all urban lands, as well as some lands in rural areas. Concerning rural land, Article 58 of the Property Law defines collectively-owned property as that which belongs to collectives as foreseen by the law.

As no land can be owned outright, China has thus developed a system of non-ownership interest in land referred to as land use rights. This system is divided into three categories: the right

to the contracted management of the land, the right to the use of the land for construction purposes, and the right to the use of the land for housing purposes. The right to use the land implies in itself the right to possess, use the land, and the right to gain fruits from the land, however the right to dispose of or sell the land is prohibited. In addition, individuals are given land use rights for a limited period of time. For farmland this is 30 years, upon which there is an assumption of automatic renewal, except if otherwise determined by law.

### The Transfer of Land Use Rights

Under the current legal system, the transfer of land use rights related to collectively-owned land is prohibited except in the case of bankruptcy or merger. With such restrictions, it is impossible to maximize the financial interests related to land use rights over collectively-owned land. In the past, rural governments and collectives have sought to circumvent these restrictions through the illegal practice of transfer of collective construction rights. In early 2000 several local governments or legislative organizations even went so far as to issue detailed rules on the transfer of the use rights of collective construction land in their jurisdiction. In 2004, one provincial-level government put an end to this practice with the *Administration Measures on Transfer of the Use of Right on Collective Construction Land in Guangdong Province*, in an effort to protect local farmers from greedy businessman and power hungry government officials. With the release now of the Decisions, local governments are reviving this issue; the best example of this is Hebei Province's recent passing of the *Administration*

# Recent Revisions to Rural Land Use Rights cont.



*Measures on Transfer of the Use of Right on Collective Construction Land in Hebei Province.* These measures seem better destined for success now that the CPC is showing a clear and positive attitude towards reform.

## Anticipation on legal reform

Although the Decisions have only been released for a short while, it is possible to posit a few trends for the future of legal reform relating to rural land use rights. Firstly, previously issued local rules on transfer legitimized several ways in which the transfer of collective land could be completed including: sub-contracting, lease, release, exchange of land-use rights, or investment as contribution capital from share-holding entities. The Decisions have codified some of these, for example allowing the mortgaging of land use rights over collectively-owned land.

Secondly, we are of the opinion that future legislation will, indeed, equalize the rules on land use rights for collectively-owned land with those for state-owned land. The Decisions create the same transfer taxes and fees that apply to the transfer of state-owned land. Under the Law on the Administration of Real Estate, when land is used for commercial tourism, recreation and luxury housing purposes, an auction or public bidding must be adopted. And further, the official intended use of the land may never be changed, i.e. the land should be used as planned.

However, collectively-owned land and state-owned land are inherently different in their nature, and the Decisions thus can also be seen to create an important source of conflict. What to do about the controls associated with the transfer of the land, such as the condition that an affirmative is required by two thirds of the members of the villagers committee or over two thirds of the villagers

representatives This type of restriction exists to protect the interests of farmers, but were the transfer of land use rights to be liberalized on a broader scale, this type of restriction would be insufficient to deter manipulation of the villagers committee by a vocal or powerful minority, which may then abuse their power for their own gains.

Another example relates to the allocation of revenue from the transfer of land use rights. While this item is easy to control in case of state-owned land, for collectively-owned land a certain part of the revenue will usually be remitted to social security funds for the members of the collective organization. The allocation plan for any revenue must be approved by a majority, and executed, and supervised by the collective organization.

“ the new policies are also expected to attract more investment in rural areas, a way to provide the necessary funding for the modernization of agriculture processes and urbanization ”

It would be better if detailed rules were adopted to protect farmers; minority interests could be given a preemptive right to stop unreasonable agreements and the right to claim for compensation.

Allowing for the possibility of a buy out by the collective organization would also further protect minority interests.

## Conclusion

The CPC has shown its interest in commencing the huge task of reforming the legal system used for rural, collective land use rights. This is a delicate issue that will require finding a careful balance between the eventual goal of an open and universal land market, and the protection of Chinas farming industry and rural citizens rights.

By Zachary Wortham, Phenix Zheng, and Cristina Di Luigi

## WANG JING & Co. UPDATE

### Shanghai Office moves to Bank of China Tower in Pudong

On December 15th after more than 9 years in the China Merchants Tower, Wang Jing & Co. Shanghai Office will be moving to the prestigious Bank of China Tower, also in Pudong. With 30% more office space, this move will allow the Firm to continue to expand its Shanghai practice, especially in the core areas of maritime and commercial dispute resolution, and assisting foreign and foreign invested companies on general corporate, commercial, and IP issues.

If you would like to visit our Shanghai Office, please contact your usual representative or Senior Consultant Maarten Roos at [mjroos@wjnco.com](mailto:mjroos@wjnco.com).

### Evander Holyfield, World Boxing Champion visits Guangzhou Office



At the invitation of Client Service Manager Zachary Wortham, the former four time heavy weight boxing champion of the world, Mr. Evander Holyfield, came to the Guangzhou offices of Wang Jing & Co. Mr. Holyfield was seeking our advice on establishing a business in China as well as strategies for protecting his Intellectual Property in China. Mr. Holyfield then asked that we accompany him to attend the 104th Canton Fair, the largest trade fair in the world. Wang Jing & Co. was proud to have Mr. Holyfield in our offices and we look forward to a long and successful business cooperation.

#### GUANGZHOU

Tel. (+8620) 8760 0082  
Fax (+8620) 8778 4482  
[info@wjnco.com](mailto:info@wjnco.com)

#### SHANGHAI

Tel. (+8621) 5887 8000  
Fax (+8621) 5882 2460  
[shanghai@wjnco.com](mailto:shanghai@wjnco.com)

#### TIANJIN

Tel. (+86 22) 2532 3818  
Fax (+86 22) 2532 3820  
[tianjin@wjnco.com](mailto:tianjin@wjnco.com)

#### SHENZHEN

Tel. (+86 755) 8882 8008  
Fax (+86 755) 8284 6611  
[shenzhen@wjnco.com](mailto:shenzhen@wjnco.com)

#### QINGDAO

Tel. (+86 532) 8666 5858  
Fax (+86 532) 8666 5868  
[qingdao@wjnco.com](mailto:qingdao@wjnco.com)

#### XIAMEN

Tel. (+86 592) 268 1376  
Fax (+86 592) 268 1380  
[xiamen@wjnco.com](mailto:xiamen@wjnco.com)

#### FUZHOU

Tel. (+86 591) 8781 2260  
Fax (+86 591) 8781 2210  
[fuzhou@wjnco.com](mailto:fuzhou@wjnco.com)

#### HAIKOU

Tel. (+86 898) 6672 2583  
Fax (+86 898) 6672 0770  
[hainan@wjnco.com](mailto:hainan@wjnco.com)

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