

1989

A COMPARISON OF JOINT VENTURES IN THE PEOPLE'S REPUBLIC OF CHINA AND JAPAN

Richard E. Pelosi Jr.

Follow this and additional works at: [https://digitalcommons.nyls.edu/
journal_of_international_and_comparative_law](https://digitalcommons.nyls.edu/journal_of_international_and_comparative_law)



Part of the [Law Commons](#)

Recommended Citation

Pelosi, Richard E. Jr. (1989) "A COMPARISON OF JOINT VENTURES IN THE PEOPLE'S REPUBLIC OF CHINA AND JAPAN," *NYLS Journal of International and Comparative Law*: Vol. 10 : No. 1 , Article 9. Available at: https://digitalcommons.nyls.edu/journal_of_international_and_comparative_law/vol10/iss1/9

This Notes and Comments is brought to you for free and open access by DigitalCommons@NYLS. It has been accepted for inclusion in NYLS Journal of International and Comparative Law by an authorized editor of DigitalCommons@NYLS.

A COMPARISON OF JOINT VENTURES IN THE PEOPLE'S REPUBLIC OF CHINA AND JAPAN

I. INTRODUCTION

There are various methods by which a firm can enter the market of a foreign country. It can set up a subsidiary, open a branch office, contract with a distributing agent or enter into a joint venture with a company in the host nation.¹ Joint ventures have traditionally been an extremely popular form of doing business abroad, in that they allow market penetration and the sharing of costs and risks.²

This Note will examine and compare the joint venture laws of the People's Republic of China ("PRC") and Japan, to determine which nation is more amenable to the establishment of joint ventures within its respective borders. As the Chinese and Japanese economies gain increasing strength,³ it is imperative that the government and corporations of the United States become more cognizant of the way in which these two Pacific Rim powers view the joint venture as a mode of doing business.

II. JOINT VENTURES

A joint venture is a "legal entity in the nature of a partnership engaged in the joint prosecution of a particular transaction for mutual profit."⁴ Contrary to a partnership, however, a joint venture "does not entail a continuing relationship between the parties."⁵ Joint ventures have been likened to marriages; the union dissolves when the interests of the parties are no longer in concert.⁶

Joint ventures can be broken down further into equity (or statutory) and contractual joint ventures.⁷ Equity joint ventures are those

1. Asahina, *Establishing A Presence: A Comparative Analysis of Entry Vehicles-I*, EAST ASIAN EXECUTIVE REPORTS, June 1985, at 18-19.

2. McArthur, *Joint Ventures in Japan*, 20 U. BRIT. COLUM. L. REV. 471 (1986).

3. See generally Surrey, Fishburne & Chaudhri, *Joint Ventures in China: The First Water Stop*, 21 TEX. INT'L L.J. 221 (1986) [hereinafter Surrey]; E. HAHN, *DOING BUSINESS IN JAPAN* (1984).

4. BLACK'S LAW DICTIONARY 753 (5th ed. 1979).

5. *Id.*

6. Ballon, *Joint Ventures*, in BUSINESS IN JAPAN 134, 135 (P. Norbury & G. Bownes ed. 1974); King, *Joint Ventures*, in CURRENT LEGAL ASPECTS OF DOING BUSINESS IN THE FAR EAST 100-01 (R. Allison ed. 1972).

7. Surrey, *supra* note 3, at 222-23.

established under a code or set of laws⁸ and will be the focus of this Note. Contractual joint ventures are "contractual arrangement[s] between two or more parties whereby the parties undertake a business (frequently a construction project) or limited term coventure"⁹ Unlike an equity joint venture, the parties to a contractual joint venture do not set up a corporation but "prefer to govern their rights entirely by contract."¹⁰ Of the two types of joint ventures, equity joint ventures are more commonly used in the PRC¹¹ and Japan.¹²

III. JOINT VENTURES IN THE PRC

Traditionally, the Chinese approach to law was a strong opposition to formalized legislative codes; the Chinese preferred "the natural law concept rather than . . . legal positivism."¹³ The Chinese felt that if members of society had proper respect for each other, laws would be

8. *Id.* at 223.

9. *Id.* Additionally, contractual joint ventures, as opposed to equity joint ventures, do not involve the creation of limited liability companies. Goossen, *Joint Ventures Under the New Civil Code*, EAST ASIAN EXECUTIVE REPORTS, Mar. 1986, at 9.

10. Surrey, *supra* note 3, at 223. The Seventh National People's Congress, on April 13, 1988, passed a 28 article document governing contractual (or cooperative) joint ventures. The Law of Sino-Foreign Co-operative Ventures, April 13, 1988, *translated in CHINA LAWS FOR FOREIGN BUSINESS* ¶ 6-100 (CCH Australia Ltd. trans. 1988). As will be explained *infra*, Western investors have typically avoided this form of investment because of the ambiguity that surrounded the contractual joint venture's legal status. Bates & Jianping, *The New Cooperative Joint Venture Law*, EAST ASIAN EXECUTIVE REPORTS, May 1988, at 7. Contractual joint ventures are generally more flexible investments than equity joint ventures, and the Chinese are hoping that this law will make contractual joint ventures more attractive to the foreign investor. *Id.* Until the Ministry of Foreign Economic Relations and Trade ("MOFERT"), however, pursuant to the provisions of Article 27, promulgates a set of implementing regulations that will hopefully clarify the rather broad principles set forth, foreign investment in contractual joint ventures will probably not reach desired levels. *Id.*

11. Surrey, *supra* note 3, at 223.

12. Shapiro, *Legal Aspects of Doing Business With Japan 1985*, 249 PRACTICING L. INST. 49 (1985).

13. H. KIM, FUNDAMENTAL LEGAL CONCEPTS OF CHINA AND THE WEST - A COMPARATIVE STUDY 20 (1981). The natural law concept in China is manifested in the concepts of Heaven (*T'ien*), the Way (*Tao*), and Human Nature (*Hsing*), to name a few. *Id.* at 25. As such, law is rooted in the moral behavior of the people, a concept grounded in Confucianism. The chief purpose of the law is to instruct the people in conducting themselves in a manner that will bring about a "harmonious social order in accord with the natural order." *Id.* at 17. Traditional Chinese law was feudalistic rather than democratic, in that: customary law was favored over statutory law; the law's purpose was to create a harmonious society, not establish rights and duties; and the law "reflect[ed] [an] organic rather than a mechanistic society." *Id.* at 17-18. In short, traditional Chinese law was "more paternalistic than individualistic." *Id.* at 20.

unnecessary.¹⁴ From the Buddhist influence, the Chinese have come to believe that in a dispute, compromise is better than confrontation (in which one side must win and the other lose).¹⁵ However, these concepts only related to the way in which the Chinese dealt with each other—foreigners were a different matter entirely.¹⁶

The PRC realized, however, that it needed foreign investment to galvanize its economic development.¹⁷ Thus, in 1979, China shed its historical antipathy of dealing with foreigners,¹⁸ and enacted legislation authorizing the formation of equity joint ventures with foreign companies.¹⁹ This marked the first time in the history of Communist China that foreign corporations would be allowed to directly participate in profits and management.²⁰ The enactment of this law is even more amazing when it is examined in light of the regime governing the country of promulgation. According to classic Marxist-Leninist thought, the whole concept of a joint venture seems to be unilaterally opposed to "state ownership of the means of production."²¹ Nevertheless, the PRC's officials decided that allowing foreign joint ventures would quicken China's economic development by "attracting foreign capital

14. *Id.* at 19.

15. Carl, *Contemporary Law in the People's Republic of China*, 32 Sw. L.J. 1255, 1256-57 (1979). In settling disputes this way, both sides retained their dignity and the community was not further troubled by disruption. *Id.*

16. J. BRIERLY & R. DAVID, *MAJOR LEGAL SYSTEMS OF THE WORLD TODAY* 478-80 (2d ed. 1978).

17. Jaslow, *Practical Consideration in Drafting a Joint Venture Agreement with China*, 31 AM. J. COMP. L. 209 (1983). In 1986, Chinese economic planners stated that the PRC would need "\$5 to \$7 billion in foreign investment over the next five years in order to meet plans for rapid upgrading of domestic industry without borrowing large amounts on world capital markets." Spaulding, *Structuring a Joint Venture: The Foreign Exchange Factor*, EAST ASIAN EXECUTIVE REPORTS, May 1986, at 13. To achieve these levels of foreign investment, Chinese planners have resolved to upgrade their efforts to increase the attractiveness of the PRC to overseas investors. *Id.*

18. Jaslow, *supra* note 17, at 211. An example of foreign activity that has failed to endear foreigners to the Chinese was the British mass importation of opium into China in the early 19th century. This activity led to the Opium War in 1839. After the war's cessation, China was forced to submit to a number of unfair treaties drafted by the various Western nations, which were perceived as a great humiliation by the Chinese for many years. *Id.* at 211 n.12.

19. Law of the People's Republic of China on Chinese-Foreign Equity Joint Ventures, July 8, 1979 [hereinafter PRC JV Law], translated in LEGISLATIVE AFFAIRS COMM'N OF THE STANDING COMM. OF THE NAT'L PEOPLE'S CONGRESS OF THE PEOPLE'S REPUBLIC OF CHINA, *THE LAWS OF THE PEOPLE'S REPUBLIC OF CHINA, 1979-1982*, at 150 (1987) [hereinafter PRC LAWS].

20. Jaslow, *supra* note 17, at 209.

21. Surrey, *supra* note 3, at 224.

and expediting the transfer of foreign technology to China."²² The joint venture was

designed to enable China to embark on certain projects now, albeit at the cost of allowing foreign equity participation. Thus China preferred sharing profits with outsiders to either delaying the projects until it could finance their foreign exchange currency costs from domestic or international sources or diverting foreign exchange from other economic activities.²³

A. *The Joint Venture Law*

The Joint Venture Law is short, containing only fifteen articles. Article 2 is a key provision; it provides that the "Chinese Government shall protect . . . the investment of foreign joint venturers, the profits due them and their other lawful rights and interests in an equity joint venture, pursuant to the agreement, contract and articles of association approved by the Chinese Government."²⁴

The foreign investor must contribute at least 25% of the joint venture's "registered capital."²⁵ Additionally, the joint venture will be a limited liability company, with each investor liable only to the proportion of its investment of the registered capital.²⁶

The parties to the joint venture decide on the association's life span, "according to its particular line of business and circumstances."²⁷ The parties may extend the duration of the joint venture at its expiration, subject to the government's approval.²⁸

The Joint Venture Law was a dramatic change for the PRC; it marked the end of an era of "economic and political isolation from the

22. *Id.*

23. *Id.*

24. *Id.* art. 2. Thus, this article is a statement that the Chinese Government intends to protect the foreign investor from expropriation, alleviating the fear that capital infused into the PRC may be taken for no particular reason. Deng Xiaoping and his top ministers have repeatedly tried to assure foreign investors that "Chinese socialism is a sufficiently secure economic investment to permit substantial investment from the West." Rogers, *Deterrents to Joint Venturing in China: A Look at Shanghai Real Estate Projects*, EAST ASIAN EXECUTIVE REPORTS, July 1986, at 9, 16.

25. PRC JV Law, *supra* note 19, art. 4. This provision has been interpreted to allow a foreign investor to own 100% of a joint venture and "still enjoy the benefits of the Law." Surrey, *supra* note 3, at 225. This, however, is a virtually non-existent practice. *Id.*

26. PRC JV Law, *supra* note 19, art. 4.

27. PRC JV Law, *supra* note 19, art. 12. This is the only guidance given and, as such, is exceedingly vague.

28. *Id.*

rest of the world"²⁹ Its terseness, however, gave little reassurance to foreign investors, who felt far more comfortable with detailed investment codes.³⁰ As a result, the level of foreign investment fell short of PRC expectations.³¹

B. *The Joint Venture Regulations*

The paucity of foreign investment, combined with the PRC's routine practice of promulgating exhaustive regulations to implement "general legal pronouncements,"³² encouraged the State Council to issue the Joint Venture Regulations.³³ These regulations answer many of the questions that arose from the Joint Venture Law, in addition to "compensat[ing], in some measure, for the fact that China does not, to date, have a companies law which, in other countries, provides many of the details governing the establishment and operation of various business arrangements."³⁴ China's hope was that, in enacting these regulations, the world would see their "determination to adhere to a policy of opening to the outside world."³⁵

The Ministry of Foreign Economic Relations and Trade of the People's Republic of China ("MOFERT") must examine and approve of each joint venture.³⁶ Joint ventures are to be established to "pro-

29. Surrey, *supra* note 3, at 226.

30. *Id.* Foreign investors received no comfort from the JV Law's brevity or scarcity of detail "because of the numerous issues not dealt with in the law." *Id.*

31. *Id.*; see also Klingenberg & Pattison, *Joint Ventures in the People's Republic of China*, 19 VA. J. INT'L L. 807, 811 (1979). As of May 1988, however, more than 9700 joint ventures have been approved by the PRC. Gargan, *Making the Right Contacts in China*, N.Y. Times, May 30, 1988, at A33, col. 4.

32. Surrey, *supra* note 3, at 226.

33. Regulations for the Implementation of the Law of The People's Republic of China on Joint Ventures Using Chinese and Foreign Investment, *translated in* BEIJING REV., Oct. 10, 1983, at 10 [hereinafter PRC JV Regs.]. The Joint Venture Regulations consist of 118 articles in 16 chapters. The document is broken down as follows: (1) General Provisions; (2) Establishment and Registration; (3) Form of Organization and Registered Capital; (4) Ways of Contributing Investment; (5) Board of Directors and Management Office; (6) Acquisition of Technology; (7) Right to the Use of Site and Its Fee; (8) Planning, Purchasing and Selling; (9) Taxes; (10) Foreign Exchange Control; (11) Financial Affairs and Accounting; (12) Staff and Workers; (13) Trade Union; (14) Duration, Dissolution and Liquidation; (15) Settlement of Disputes; and (16) Supplementary Articles.

34. Surrey, *supra* note 3, at 226-27.

35. Dacheng, *Another Important Document on Joint Ventures*, BEIJING REV., Oct. 3, 1983, at 4.

36. PRC JV Regs., *supra* note 33, art. 8. MOFERT may, however, delegate approval authority to provincial or regional bodies, if it so desires. *Id.* In order to secure MOFERT's approval, the Chinese participant must submit the following: (1) an application; (2) a feasibility study prepared by both parties; (3) a joint venture agreement, con-

mote the development of China's economy and the raising of scientific and technological levels for the benefit of socialist modernization."³⁷ Certain industries are deemed to be "preferred industries" for joint ventures, such as energy development and the computer and electronics industries."³⁸

Three contractual documents are required to establish a joint venture.³⁹ The Joint Venture Agreement states the main points and principles governing the joint venture's establishment.⁴⁰ The Joint Venture Contract lays out the rights and obligations of the parties.⁴¹ Finally, the Articles of Association indicate the purpose, organizational principles, and method of management of the joint venture.⁴² The formation, validity, interpretation and execution of the Joint Venture Contract are governed by Chinese law.⁴³ This is one of the Joint Venture Regulation's least popular articles with foreign investors, because China's legal system is neither fully evolved nor is it devoid of substantial uncertainty in its enforcement.⁴⁴

1. Investment Contribution

The form of investment contribution to the joint venture may be either in cash or "in kind."⁴⁵ Typical examples of "in kind" capital contributions include industrial property and technology, specifically those types of articles or processes that the Chinese do not have and

tract and articles of association, signed by authorized representatives of the venture; (4) a list of the candidates for chairman, vice chairman and directors appointed by the parties; and (5) a document signifying the approval of the local authorities where the joint venture will be situated. *Id.* art. 9. Approval or disapproval of the joint venture will be decided within three months. *Id.* art. 10. The applicant must register with the local administrative bureau for the province within one month of receipt of the certificate of approval from MOFERT. *Id.* art. 11.

37. *Id.* art. 3.

38. *Id.* High technology industries are highly desirable for the PRC, because these fields will allow the Chinese to modernize their economy and compete with First and Second World nations in the business arena. Bates, *supra* note 10, at 7.

39. PRC JV Regs., *supra* note 33, art. 13.

40. *Id.*

41. *Id.*

42. *Id.*

43. *Id.* art. 15.

44. Surrey, *supra* note 3, at 229 n.24. This weakness has been recognized by both Chinese and Western business people. Much of this ambiguity stems from the fact that, until relatively recently, lawyers were almost non-existent in China. This scarcity was a result of the communist takeover. Today, there are approximately 20,000 lawyers in the PRC, but, when compared with the nation's one billion-plus population, the number appears to be minute. Spaulding, *supra* note 17, at 17.

45. PRC JV Regs., *supra* note 33, art. 25.

thus desire.⁴⁶ For "in kind" capital contributions, determination of the contribution's value may be arrived at by either an agreement amongst the parties or by a third party determination agreed to by the parties.⁴⁷ All "in kind" contributions must be vital to the joint venture's success, not readily available in China,⁴⁸ and approved by Chinese authorities.⁴⁹ Finally, after all contributions are in by both parties, a Chinese registered accountant will verify the value and issue a certificate of verification.⁵⁰ Upon receipt of the certificate of verification, the parties issue an investment certificate,⁵¹ which serves as the only source of evidence of their investment.⁵²

2. The Board of Directors/Managerial Positions

The Board of Directors is the venture's highest authority.⁵³ The Board must be composed of no less than three members, with the chairman being appointed by the Chinese participant and the vice-chairman by the foreign participant.⁵⁴ The Board is required to meet at least once a year.⁵⁵ Unanimous agreement of the Board is required for the following actions: (1) amendment of the Articles of Association; (2) termination and dissolution of the joint venture; (3) an increase or assignment of the registered capital of the joint venture; and (4) merger of the joint venture with any other economic entity.⁵⁶

A management office is required, consisting of a general manager and several deputy managers, for the daily running of the operation.⁵⁷ The managerial positions may be held by Chinese or non-Chinese citizens.⁵⁸ In order for the joint venture to open branch offices outside of China, MOFERT's approval is required.⁵⁹

46. Surrey, *supra* note 3, at 232.

47. PRC JV Regs., *supra* note 33, art. 25.

48. *Id.* art. 27.

49. *Id.* art. 30.

50. *Id.* art. 32.

51. *Id.*

52. Surrey, *supra* note 3, at 232. This is so because there is no provision in the Regulations for the issuance of stock. *Id.*

53. PRC JV Regs., *supra* note 33, art. 33.

54. *Id.* art. 34. The remainder of the Board of Directors is chosen by both parties. *Id.*

55. *Id.* art. 35. Additionally, Article 35 requires a quorum of two-thirds of the directors but, unlike the American practice, directors are permitted to give proxies for meetings, which may be used in the determination of a quorum's existence. Surrey, *supra* note 3, at 233.

56. PRC JV Regs., *supra* note 33, art. 36.

57. *Id.* art. 38.

58. *Id.* art. 40.

59. *Id.* art. 42.

3. Technology Transfer Requirements

Terms and conditions relating to the transfer of technology to the joint venture are critical because the acquisition of foreign technology was one of the major forces spurring the Chinese to open their borders and markets to the outside world.⁶⁰ The following are the technology transfer requirements for joint ventures. First, the technology transfer agreement must be approved by MOFERT. Second, the expenses for the technology's use must be fair and reasonable and "not higher than the standard international rate."⁶¹ Third, the term for a technology transfer agreement generally may not exceed ten years. Fourth, at the technology transfer agreement's expiration, the technology importing party shall have the right to use the technology forever. Fifth, the exchange of information on the technology's improvement shall be reciprocal. Sixth, the technology importing party can buy its raw material and equipment from any source it sees fit. Lastly, there may be "no irrational restrictive clauses prohibited by Chinese law . . ."⁶²

These technology transfer requirements have caused some apprehension amongst foreign investors, particularly United States investors who are used to "tight licensing arrangements."⁶³ Some advanced technology licensors categorically require licensees to purchase from approved suppliers, to submit to rigorous quality maintenance checks, geographical market restrictions, and "prohibitions on any tinkering with the technology."⁶⁴ Chinese inflexibility in this area has led to some cessation of negotiations in the past⁶⁵ and there is no reason to believe that it will change in the near future.⁶⁶

The fruit of the joint venture is its product and the sale of this product is vital to the enterprise's financial success.⁶⁷ The "Chinese Government encourages joint ventures to sell their products on the international market."⁶⁸ Joint ventures may sell products that "China

60. Surrey, *supra* note 3, at 233.

61. *Id.* at 234.

62. PRC JV Regs., *supra* note 33, art. 46.

63. Surrey, *supra* note 3, at 235. For example, the ten-year limitation on licensing agreements has caused some trepidation, as has the provision dealing with the Chinese party's right to use the technology forever at the end of the licensing period. *Id.*

64. *Id.*

65. *Id.*

66. *Id.* at 239. In the area of technology transfers, there is still not enough experience on the implementation of the Regulations. *Id.* at 235. The first technology licenses to reach the end of the ten-year maximum term will not expire until 1993; thus, some Western companies may be waiting to see how the Regulations and MOFERT's implementation/interpretation of the Regulations will affect foreign entities. *Id.* at 239.

67. *Id.* at 240.

68. PRC JV Regs., *supra* note 33, art. 60.

urgently needs or imports . . . on the Chinese market.”⁶⁹

4. Tax Implications

Joint ventures are taxed in accordance with Chinese law.⁷⁰ Additionally, the joint venture's staff members and workers must pay “individual income tax according to the Individual Income Tax Law of the People's Republic of China.”⁷¹ Machinery, parts, equipment and other materials used for the production of export goods are exempt from taxation and customs duties.⁷² Additionally, export goods that are approved by the Ministry of Finance are exempt from taxation.⁷³ The joint venture can also apply for a tax reduction or exemption “for a certain period of time for products that are sold on the domestic market when it has difficulty . . . pay[ing] such tax in its initial period of production.”⁷⁴

5. Labor Disputes

All joint venture labor matters will be handled in compliance with the Regulations of the People's Republic of China on Labour Management in Joint Ventures Using Chinese and Foreign Investment (“Labor Relations”).⁷⁵

69. *Id.* art. 61.

70. *Id.* art. 69.

71. *Id.* art. 70.

72. *Id.* art. 71.

73. *Id.* art. 72. China, in its desire to modernize and create a more favorable balance of trade, must create incentives for investors to come to China. One such incentive for the foreign investor is the chance of selling its product to an untapped market of about 1.2 billion consumers. The Chinese, although interested in putting higher quality consumer goods on the domestic market, are also interested in recruiting foreign talent that will produce goods to sell on the international market. The PRC hopes that the creation of a favorable tax environment, in addition to the promise of a large group of new consumers, will lure foreign investors to China. This is the primary rationale for the exemption of certain export goods from taxation. See generally Note, *People's Republic of China - 1983 Joint Venture Implementing Regulations - The Supplement of Detail, in an Attempt to Attract Foreign Investment*, 15 GA. J. INT'L & COMP. L. 389 (1985).

74. PRC JV Regs., *supra* note 33, art. 72.

75. Regulations of the People's Republic of China on Labour Management in Joint Ventures Using Chinese and Foreign Investment [hereinafter PRC Labor Regs.], translated in 1 LAWS AND REGULATIONS OF THE PEOPLE'S REPUBLIC OF CHINA 44 (1982). Not all of the regulations concerning labor can be found in the Labor Regulations; some of the regulations are contained in the Joint Venture Regulations. Article 94 of the Joint Venture Regulations states that the salaries of the joint venture's high ranking officials will be set by the Board of Directors. PRC JV Regs., *supra* note 33, art. 94. Article 95 gives the workers the right to set up a trade union. *Id.* art. 95. Article 98 gives the trade union representatives the right to attend board meetings as non-voting members to report

Article 2 of the Labor Regulations requires that there be a labor contract between the joint venture and the workers' trade union, covering such matters as dismissal, wages, and vacation time.⁷⁶ Article 8 of the Labor Regulations provides that workers and staff members in a joint venture shall be paid "120 to 150% of the real wages of the workers and staff members of state-owned enterprises of the same trade in the same locality."⁷⁷ The reason for this is that the PRC feels that the joint venture will not provide the housing, medical and educational benefits that the state enterprises furnish.⁷⁸ In a remarkable divergence from Marxist-Leninist philosophy, Article 4 of the Labor Regulations permits the joint venture to dismiss workers who fail to achieve certain standards.⁷⁹

6. The Duration of the Joint Venture

The parties to the joint venture have the right to decide the duration of the association, although the average length is from ten to thirty years.⁸⁰ This article is indicative of the Chinese view that the joint venture is not meant to last indefinitely; rather, it is intended to last long enough to allow the Chinese to gain some expertise so that they can in turn run the operation by themselves (and not have to share the management or profits with any foreigners).⁸¹ The following is a list of the ways in which the joint venture may be terminated, such as: (1) the term's expiration; (2) inability to continue the operation due to heavy losses or *force majeure* (e.g., war); (3) breach of contractual arrangement; and (4) the occurrence of some agreed upon event that would call for dissolution.⁸² With the exception of the expiration of the

worker opinions. *Id.* art. 98. Article 98 also instructs the Board of Directors to "heed the opinions of the trade unions and win its co-operation [sic]." *Id.*

76. PRC Labor Regs., *supra* note 75, art. 2.

77. *Id.* art. 8.

78. Surrey, *supra* note 3, at 246.

79. PRC Labor Regs., *supra* note 75, art. 4.

80. PRC JV Regs., *supra* note 33, art. 100. Article 100 was amended in 1986, however, to allow for certain joint ventures to be extended to 50 years, if the venture: (1) is a large investment that has a long construction period and a low profit, or (2) has advanced or high technology for the manufacture of sophisticated equipment that is provided by the foreign venturer, or (3) the products are internationally competitive. Horsley, *Promoting Foreign Investment: Notes on Recent Developments*, EAST ASIAN EXECUTIVE REPORTS, Mar. 1986, at 9. Although this amendment seems to indicate that the Chinese are gaining confidence in their dealings with foreigners, terms such as "advanced technology," still have not been dispositively defined by Chinese officials. *Id.*

81. Surrey, *supra* note 3, at 247. Foreigners tend to hope that the government will allow the association to extend for an "additional term." *Id.*

82. PRC JV Regs., *supra* note 33, art. 102.

joint venture's term, the approval authority must consent to the cessation of the venture.⁸³

7. Disputes Between the Parties

In accordance with traditional Chinese legal thought, Article 109 directs that disputes between the parties "shall, if possible, be settled through friendly consultation or mediation."⁸⁴ If the parties cannot settle their disputes in this manner, they should either arbitrate their grievances⁸⁵ or, if the parties have not stipulated for arbitration in a written agreement, take their case to the Chinese People's Court.⁸⁶

While the Joint Venture Implementation Regulations cleared up many of the ambiguities remaining from the Joint Venture Law, there are still areas that could cause problems for the foreign investor.⁸⁷

IV. ADVANTAGES AND DISADVANTAGES OF JOINT VENTURES IN THE PRC

Management of the joint venture is one of the first problem areas the foreign investor will encounter.⁸⁸ Control of the joint venture begins with the Board of Directors.⁸⁹ Unlike the Board of Directors of a normal corporation, however, a joint venture's Board is composed of two groups, each allied with the participant and country they represent.⁹⁰ Because of the Board's composition, it would be wise "not to overload the joint venture with too many unanimity requirements because this could lead to paralysis of the day-to-day operations of the enterprise."⁹¹

The advantages of the management structure in China, however, outweigh the disadvantages. Unlike other Communist nations, the

83. *Id.*

84. *Id.* art. 109.

85. *Id.* art. 110. Arbitration may be conducted in China before the Foreign Economic and Trade Arbitration Commission of the China Council for the Promotion of International Trade or through an arbitration agency in a third country. *Id.*

86. *Id.* art. 111. This course of action, however, runs contrary to established Chinese practices and will, in all probability, never be used in a business context. The Chinese feel that virtually all problems can be worked out through conciliation and mediation, ensuring that no party loses "face" and thereby preserving the business relationship. See generally Jaslow, *supra* note 17 (discussing a comparison of the Chinese view of dispute resolution with that of various Eastern European nations).

87. Surrey, *supra* note 3, at 248.

88. Jaslow, *supra* note 17, at 217.

89. PRC JV Regs., *supra* note 33, art. 33.

90. Jaslow, *supra* note 17, at 217.

91. *Id.* at 219 (citing Lorinczi & Dorian, *U.S.-Hungarian Joint Ventures: Prospects and Problems*, 10 L. & POL. INT. BUS. 1205, 1216 (1973)).

PRC allows the Western investor to own more than 49% of the joint venture.⁹² Additionally, even if the Chinese participant has contributed a majority of the investment, the foreign investor can gain equality of voting power if it is written into the contract that each side will have an equal number of members on the Board.⁹³

Another significant advantage for the foreign investor is that the general manager, responsible for the day-to-day running of the operation, does not have to be Chinese.⁹⁴ This allows the foreign party to exercise significant "de facto control," especially since it is the foreign participant who possesses the superior technical and managerial ability and experience.⁹⁵ This control is a "buffer against the local partner's" advantage of having the operation in its country.⁹⁶

There are several problems the foreign investor may encounter when entering into a joint venture in the PRC. One area that is frequently problematic for joint ventures in developing countries is the utilization of local labor.⁹⁷ Most of the difficulty arises from the fact that the laborer is usually unskilled in the joint venture's work, which is often a high technology area.⁹⁸ In addition to his lack of training, the Chinese worker is "the product of a system which, until very recently, put little or no premium on productivity or self-motivation."⁹⁹ Consequently, many joint venturers have found their staffs to be unwilling to change and below par in terms of training and motivation.¹⁰⁰ This is not always the case but, even in those situations where it is true initially, circumstances will generally improve after the Chinese are exposed to the new working methods of their foreign co-venturer and have time to familiarize themselves with their required tasks.¹⁰¹ Many foreign venturers describe their Chinese workers as "hardworking and creative" and often praise them for "their precision handwork in spe-

92. Jaslow, *supra* note 17, at 223-24. For example, in Yugoslavia, the Western participant is limited to 49% of the investment. *Id.* It is still possible, however, for a party holding 49% of a corporation's stock to have voting control, as long as there are at least three shareholders and neither has more than 50% of the shares. *Id.* at 218 n.51.

93. *Id.* at 218 n.52.

94. PRC JV Regs., *supra* note 33, art. 40.

95. Jaslow, *supra* note 17, at 220-21.

96. *Id.* at 222.

97. Surrey, *supra* note 3, at 249.

98. *Id.* This lack of technical expertise can hardly be blamed on the individual Chinese worker. Until recently, Chinese industry had not properly functioned or developed in the post-World War II era; accordingly, the skills of Chinese workers and managers had not been adequately nurtured. See Rogers, *supra* note 24, at 18.

99. Surrey, *supra* note 3, at 249.

100. *Id.*

101. *Id.*

cialized manufacturing processes."¹⁰² Because worker competence and ability is sometimes a problem, another area that demands the foreign participant's full attention is quality control.¹⁰³ Consumer goods are usually in great demand in state-planned economies, which are notorious for their lack of emphasis on quality control.¹⁰⁴ This will force the foreign joint venturer to apply greater scrutiny than is normally required to ensure that the goods produced "will be acceptable in the international marketplace."¹⁰⁵ In order to provide this greater level of scrutiny, the joint venture will have to employ additional quality control managers (usually foreign) and spend extra time on inspections.¹⁰⁶

A final major problem area for investors is gaining access to the Chinese consumer; in fact, the prospect of being able to tap that relatively uncharted market is one of the chief reasons foreigners want to start joint ventures in the PRC.¹⁰⁷ There is often a clashing of goals—the Chinese are eager to make products to sell in the international arena to create a favorable foreign exchange balance, whereas the foreign party is frequently searching for a new market for its goods.¹⁰⁸ This impasse is partially rectified in Article 61 of the Joint Venture Implementing Regulations, which allows for products manufactured by the joint venture to be sold on the Chinese market.¹⁰⁹ The article goes no further than saying, however, that the only goods allowed to be sold on the domestic market are those that "China urgently needs or imports."¹¹⁰ This rather nebulous guidance is often of little comfort to the prospective joint venturer, but, at the very least, it does open the door for negotiations.¹¹¹

102. Stavits & Gang, *A Survey of Shanghai Joint Ventures*, 15 CHINA BUS. REV. 46, 47 (1988); see also Surrey, *supra* note 3, at 249.

103. Surrey, *supra* note 3, at 249.

104. *Id.*

105. *Id.*

106. *Id.*

107. *Id.* at 226. The Chinese consumer has shown a great affinity for purchasing Western or modern goods. Although the salary of a Chinese worker is low compared to that of a worker in a more highly industrialized country, the number of potential customers is extremely attractive to the Western investor searching for new markets and new customers. *Id.*

108. *Id.* at 240. See generally Note, *supra* note 73.

109. PRC JV Regs., *supra* note 33, art. 61.

110. *Id.*

111. See generally Note, *supra* note 73 (discussing a series of Department of Commerce telegrams sent right after the adoption of the Joint Venture Regulations which support the assertion that foreigners covet access to the Chinese market and hope to gain greater access through negotiation).

V. JOINT VENTURES IN JAPAN

In *The Book of Five Rings* Miyamoto Musashi, known to the Japanese as *Kensei*, or "Sword Saint,"¹¹² wrote, "The principle of strategy is having one thing, to know ten thousand things."¹¹³ When a foreign party enters into a joint venture with a Japanese company, the foreign party is committing itself to more than one dealing; rather, it is entering into a complex, multi-faceted marriage-like relationship.¹¹⁴ In fact, the Japanese partner considers the joint venture to be a *kogaisha*, or "child company," ascribing to itself and the foreign party the respective roles of in-laws who "should take joy and pride in the offspring."¹¹⁵

Before examining the way to create a joint venture, it is first necessary to generally understand the Japanese concept of law. Japan, unlike the United States, is a code country.¹¹⁶ Since most of the law in Japan is promulgated in the form of statutory rules, "many businessmen consider themselves experts on corporate law and do not use lawyers in joint venture negotiations."¹¹⁷ The Japanese would rather "rely on . . . effective human rapport . . . [than] legal documentation."¹¹⁸ The Japanese prefer compromise to litigation and try to use their courts to

112. M. MUSASHI, *THE BOOK OF FIVE RINGS* 18 (V. Harris trans. 17th ed. 1974) (The cited language is a description of Musashi, written by Harris in a preliminary section, before the translated text began.).

113. *Id.* at 44. *The Book of Five Rings* is one of the classic martial arts texts. Written in 1645 in a cave, where Musashi spent the last two years of his life, *The Book of Five Rings* is the definitive text on *Kendo*, or the Way of the Sword. During his lifetime, Musashi, a *ronin* (masterless samurai), fought more than 60 duels, never losing one. *Id.* at 15. He is widely regarded by the Japanese as the greatest samurai in their history. The book is unique, in that it "deals with both the strategy of warfare and the methods of single combat in exactly the same way." *Id.* at 18. The book, however, is not a "thesis on strategy," but rather a "guide for men who want to learn strategy." *Id.* *The Book of Five Rings* is required reading for Japanese business executives, bureaucrats and martial artists, and is universal in its application. *Id.* at 22.

114. Ballon, *supra* note 6, at 135. In Japan, marriage is more the joining of two families rather than two individuals. This practice is still kept alive today (although not as prevalent as in the past) by "go-betweens," who are more concerned with the compatibility of the two families than the two individuals. *Id.* This is also true in business. While the Western partner usually looks at itself as the bridesmaid and is concerned only with its partner, the Japanese partner looks at the venture as a child who is getting married, ascribing the role of in-law to itself. *Id.* Thus, it appears that the Japanese partner looks at the venture in a broader fashion than does the Western partner. *Id.*

115. *Id.*

116. King, *supra* note 6, at 113.

117. *Id.* Even though the Japanese partner may feel comfortable without an attorney in negotiations in Japan, it is standard for an American partner in a joint venture to "check his proposed agreements with a Japanese corporate lawyer." *Id.*

118. Ballon, *supra* note 6, at 142.

facilitate this end.¹¹⁹

A. Japanese Companies

Traditionally, the joint venture has been the "primary vehicle for major foreign investments in Japan."¹²⁰ Before a foreign firm can set up a joint venture with a Japanese firm, it must first understand the Japanese system of companies.¹²¹ There are five different types of companies in Japan: (1) *Kabushiki Kaisha* ("KK"), a limited liability company that is the predominant form used by Japanese companies involved in international or large-scale business; (2) *Yugen Kaisha* ("YK"), a smaller limited liability company; (3) *Goshi Kaisha*, a company with unlimited and limited liability shareholders; (4) *Gomei Kaisha*, a company in which all shareholders have unlimited liability; and (5) *Sogo Kaisha*, a company that can only be incorporated for insurance business.¹²² Of the various types of companies, KK and YK are the forms most suited for joint ventures.¹²³ KK is the form most frequently employed, however, for reasons relating to "public image."¹²⁴ Thus, when a joint venture with a Japanese company is mentioned in this Note, the reference is to a KK.

B. Investment Goals

Before entering into a joint venture, the foreign party needs to decide what its goals are and then find a suitable Japanese partner. Factors to be considered are the reputation of the Japanese company (an especially critical element in Japan), its business philosophy, and its future plans.¹²⁵ One point that many Western investors fail to take into account is that the Japanese generally seek long-term investments,

119. *Id.* at 142-43. In fact, the United States has approximately 150 lawyers for every 100,000 people, whereas Japan has only eight. *Id.* at 142. Litigation is perceived as being inherently combative and, as such, goes against the natural Japanese tendency to avoid open conflict. *Id.* Additionally, litigation usually results in one side winning and the other losing; this too is seen as not being satisfactory, since the Japanese believe that all interests are capable of being satisfied to a certain degree in any dispute. *Id.*

120. Shapiro, *supra* note 12, at 47.

121. Asahina, *supra* note 1, at 20.

122. *Id.*

123. McArthur, *supra* note 2, at 477.

124. *Id.* A KK is almost always a large company, with a loyal work force. It is perceived by the Japanese business community as the premier form for doing business on a large scale; thus, a Western partner who enters into a joint venture with a different type of company would not be thought of as a company that understands the Japanese economy or marketplace. Asahina, *supra* note 1, at 20.

125. E. HAHN, *supra* note 3, at 63.

usually lasting ten to twenty years.¹²⁶ This is manifested in the way the partners view profits. Typically, the Japanese party wants long-term profits, and will expend significant time and energy in refining existing products and developing new ones.¹²⁷ These actions are imperative for the Japanese company's survival in the highly competitive business environment in Japan, where great emphasis is placed on continued long-term growth and solidified market share.¹²⁸ The foreign party, on the other hand, usually enters the joint venture with the idea of developing products that will ensure a large short-term profit.¹²⁹ To increase the chances of the joint venture's success, it is imperative that the parties have consonant goals.¹³⁰

C. Joint Venture Agreements

The 50/50 joint venture (a form where both parties are considered equal partners for purposes of profit-sharing and responsibility) is the form preferred by the Japanese government.¹³¹ Control over the partnership is exercised "through the joint venture and related agreements."¹³² Joint venture agreements are governed by the Japanese Civil Code.¹³³ The Joint Venture Agreement usually outlines and defines the

rights and obligations of the parties with respect to a number of basic matters: the parties' contributions; finance for the joint venture's operations; the parties' shareholdings; the number of directors each party can appoint; methods of termination and liquidation; as well as the parties' agreement on important operational matters.¹³⁴

Other areas in which agreements are needed are "technical assistance given to the joint venture, licensing of patents, transfer of personnel to

126. Tung, *Keys to Success in Joint Ventures in Japan*, EAST ASIAN EXECUTIVE REPORTS, Nov. 1984, at 12.

127. McArthur, *supra* note 2, at 475.

128. *Id.*

129. *Id.*

130. *Id.*

131. Ballon, *supra* note 6, at 138.

132. McArthur, *supra* note 2, at 479.

133. See generally MINPŌ (Civil Code). The Civil Code is one of the five basic codes of Japan, the others being the Civil Procedure, Penal, Criminal Procedure and Commercial Codes. *Form of Citation of Japanese Legal Materials*, 42 WASH. L. REV. 589, 597 (1967).

134. McArthur, *supra* note 2, at 479-80.

the joint venture, and management and distribution of the products."¹³⁵

The Japan Fair Trade Commission ("JFTC") reviews all international trade agreements in accordance with guidelines they devised and, if it finds anything in the agreement it feels is an unfair business practice, it "will suggest that the agreement be amended."¹³⁶

D. Board of Directors

Another necessary step in the formation of the joint venture is the composition of the Board of Directors. The Joint Venture Agreement and the Articles of Incorporation delineate the Board's make-up and degree of authority over the joint venture.¹³⁷ This is a potential problem area, for even if the Japanese party agrees to foreign control of the venture, the government will object if the degree of foreign control is greater than the proportion of its stock ownership.¹³⁸

Article 255 of the Commercial Code requires that the board have at least three members,¹³⁹ although the normal number is six or seven.¹⁴⁰ Although there is no requirement, the joint venture's president is usually the president of the Japanese parent company (at least initially).¹⁴¹ The remainder of the Board is a mix of Japanese and foreign directors.¹⁴²

E. Labor Recruitment

Another problem area for the foreign participant is labor recruitment. The Japanese lifetime employment system, with its extensive fringe benefits, makes it extremely difficult for the foreign investor to recruit quality managers, engineers, and workers.¹⁴³ Japan's best workers are usually unwilling to labor for foreigners or for a company that

135. *Id.* at 480.

136. Beem & Impert, *Establishing a Joint Venture*, EAST ASIAN EXECUTIVE REPORTS, Jan. 1986, at 17, 21 (citing Anti-Monopoly Act Guidelines for International Licensing Agreements issued by the Fair Trade Commission on May 24, 1968).

137. Ballon, *supra* note 6, at 146.

138. *Id.*

139. SHŌHŌ (Commercial Code) art. 255.

140. Ballon, *supra* note 6, at 146.

141. *Id.* There is virtually no difference between an American and a Japanese Board of Directors. One of the few differences is that in a KK the declaration of dividends is "subject to the approval of a general meeting of shareholders." Asahina, *Establishing A Presence: A Comparative Analysis Of Entry Vehicles-II*, EAST ASIAN EXECUTIVE REPORTS, Oct. 1985, at 9, 16.

142. Ballon, *supra* note 6, at 146-47.

143. McArthur, *supra* note 2, at 474.

has not proven itself capable of providing them with the lifetime security of the large Japanese companies.¹⁴⁴ This problem can be exacerbated, however, with the aid of the Japanese partner, who can "second" (or transfer) his own workers to the joint venture, thus giving the Western partner access to skilled and motivated workers.¹⁴⁵

Transferring workers in this manner is not without its drawbacks.¹⁴⁶ First, the Japanese workers will remain loyal to the Japanese partner, because they are eventually going to return to the parent company.¹⁴⁷ Second, when the workers do go back to the Japanese parent, they will bring all of the knowledge and know-how they learned while working on the joint venture with them.¹⁴⁸ Finally, seconded employees "increase the Japanese partner's de facto control over the business."¹⁴⁹

F. The Revised Foreign Exchange and Foreign Trade Law

The most significant statutory restriction foreign investors face in Japan is the Revised Foreign Exchange and Foreign Trade Law ("FECL"), passed in 1979.¹⁵⁰ The FECL is of great importance to parties contemplating a joint venture, as it controls fundamental issues such as the acquisition of shares in the joint venture¹⁵¹ and the transfer of technology and industrial property rights.¹⁵² The new, less stringent FECL was not passed to attract foreign investment; rather, it was promulgated in response to severe pressure from foreign nations, especially the United States.¹⁵³ Nevertheless, the FECL requirements are still strict. Two of the more important provisions for the foreign investor to be concerned with are Article 26, regulating direct domestic in-

144. *Id.*

145. *Id.*

146. *Id.* at 482.

147. *Id.*

148. *Id.*

149. *Id.*

150. Revised Foreign Exchange and Foreign Trade Control Law, Law No. 228, 1949, translated in EIBUN-HORAI-SHA (CODES, TRANSLATIONS INSTITUTE) LAW BULLETIN, No. 5010, AA 2 (1985).

151. *Id.* art. 26.

152. *Id.* art. 29.

153. McArthur, *supra* note 2, at 485. The United States was among the most vocal of the nations protesting against the almost insurmountable barriers the Japanese had erected to keep foreign products out of Japan. The United States not only protested to Japan directly, but also at the meetings of the General Agreement on Tariffs and Trade ("GATT"), a group of nations formed immediately prior to the end of World War II. GATT's purpose was to ensure that the postwar economic recovery was as swift and painless for the world community as possible. *Id.*

vestment,¹⁵⁴ and Article 29 regulating technology importation/transfer agreements.¹⁵⁵

1. Direct Domestic Investment

Examples of direct domestic investment under the FECL are: (1) acquisition of stock or shares of a company; (2) establishing a branch in Japan; and (3) lending money to a juridical person having its main office in Japan.¹⁵⁶ Article 26 of the FECL further provides that the foreign investor must notify the Ministry of Finance of direct domestic investment, and he or she cannot act on that investment until the statutory waiting period has expired.¹⁵⁷ Additionally, the Minister of Finance and the Minister of the industry involved have the power, under Article 27, to change, postpone or cancel the transaction if they determine that: (1) it might imperil Japan's national security or adversely affect public safety; (2) it might adversely and seriously affect Japanese businesses engaged in the same types of business; and (3) it might disrupt the smooth running of the Japanese economy.¹⁵⁸

2. Technology Transfer Agreements

Article 29 requires that both parties to the joint venture must file reports with the Ministry of Finance and the Ministry of the industry involved in the joint venture, when there is an agreement involving the transfer of technology or industrial property rights, or when technical assistance is to be rendered to the foreign co-venturer.¹⁵⁹ There is a statutory waiting period of thirty days that must expire before the license between the parties becomes effective.¹⁶⁰

G. Termination of Joint Ventures

The average life of a Japanese joint venture is normally between six to eight years.¹⁶¹ Most joint ventures have no set termination date and have the "usual provisions for termination on insolvency or breach."¹⁶² A recommended termination clause is one that provides an option for termination in the case of "irreconcilable differences" be-

154. FECL, *supra* note 150, art. 26.

155. *Id.* art. 29.

156. FECL, *supra* note 150, art. 26(2).

157. *Id.* art. 26(4). The normal waiting time is 30 days.

158. *Id.* art. 27.

159. *Id.* art. 29.

160. *Id.*

161. Shapiro, *supra* note 12, at 53.

162. *Id.* at 54.

tween the parties to the venture.¹⁶³ Two of the more common reasons for termination are: (1) the foreign party has learned how to operate in the Japanese market and no longer needs the Japanese party or wants to split profits; and (2) the Japanese party finds that the foreign partner can offer it nothing further and has thus outlived its usefulness.¹⁶⁴

The success rate of joint ventures in Japan is not very high.¹⁶⁵ Frequently this is due to a failure by the foreign (usually Western) party to adapt itself to "Japanese business practices, negotiating styles, and social customs."¹⁶⁶

VI. ADVANTAGES AND DISADVANTAGES OF JOINT VENTURES IN JAPAN

One of the major advantages of joint ventures in Japan is access to the "greatly maligned Japanese distribution system . . . [that] often inhibits foreign companies from selling their products competitively."¹⁶⁷ A foreign company that tries to market its products the way it does in its native land will often find that the Japanese consumer will not respond.¹⁶⁸ A "Japanese partner's contacts and experience in, and understanding of, the distribution system ensure that the joint venture's products reach the consumer in the same manner as those of the Japanese competition, thereby increasing the products' chances of success."¹⁶⁹ The Japanese partner's "goodwill . . . and knowledge of the market" are vital to the venture's success.¹⁷⁰

Without the aid of a Japanese partner, the foreign joint venturer may have great difficulty securing financing from local institutions.¹⁷¹ The Japanese party's "relationship with its bank and its credit standing can facilitate sufficient debt financing for the business."¹⁷²

163. *Id.*

164. McArthur, *supra* note 2, at 483.

165. *Id.* at 489. A 1981 MITI survey reported that "one out of every seven foreign companies 'retrench and eventually pull out of Japan.'" Tung, *supra* note 126, at 9 (quoting JAPAN EXTERNAL TRADE ORGANIZATION, FOREIGN COMPANIES IN JAPAN 8 (1982)).

166. Tung, *supra* note 126, at 9. Ralston Purina Company, the pet food manufacturer, has had a joint venture operating in Japan for 22 years and has found that, in addition to choosing the right partner and working together, three factors have been fundamental to their success: (1) strong continuity in management; (2) detailed discussions at all times on major strategic issues; and (3) senior management participation by both sides of the joint venture. Hatfield, *Reaching the Japanese Market: The Joint Venture Solution*, EAST ASIAN EXECUTIVE REPORTS, Oct. 1986, at 17.

167. McArthur, *supra* note 2, at 473.

168. *Id.*

169. *Id.*

170. *Id.*

171. *Id.* at 474.

172. *Id.*

Additionally, the Japanese partner undoubtedly has contacts in the government and administrative agencies whose consent is essential for conducting business.¹⁷³ As in the case of financing, a foreign company with no record in Japan may not be able to secure the necessary governmental licenses without the aid of a domestic partner.¹⁷⁴

Finally, a Japanese partner gives the foreign party "access to good Japanese management personnel and to a skilled labor force,"¹⁷⁵ who probably would not work for the foreign party otherwise.¹⁷⁶

A major disadvantage of undertaking a Japanese joint venture is that "[m]anagement control must be shared, and in most cases negative control (i.e., a mutual veto) is the most that can be obtained regardless of how formal share ownership is divided. . . ."¹⁷⁷

Another disadvantage is that usually there are fundamental philosophical differences between the parties with respect to business strategy and marketing strategy.¹⁷⁸ It is imperative when deciding which Japanese partner to ally with that the foreign investor fully understand the Japanese partner's goals and methods.¹⁷⁹

The final major disadvantage of joint ventures with Japanese companies is that the foreign party is providing technology to a potential competitor.¹⁸⁰ Promises made by the Japanese party not to use the technology or know-how "outside the parameters of the joint venture" are generally ineffective in preventing that partner from using the information after the venture has been terminated, since "[v]iolations are difficult to police, prove and prohibit."¹⁸¹ The best protection method is to "license the joint venture itself, not the other partner, and impose strict restrictions on the disclosure of confidential information."¹⁸² This can only be achieved if there is physical partitioning of the Japanese party's seconded employees from the persons who are receiving the actual technology.¹⁸³ Often, however, this is impossible, because the seconded employees may be needed for manufacturing activities.¹⁸⁴

173. *Id.*

174. *Id.*

175. Shapiro, *supra* note 12, at 47.

176. *See infra* notes 188-90.

177. Shapiro, *supra* note 12, at 48.

178. *Id.*

179. McArthur, *supra* note 2, at 474-75.

180. Shapiro, *supra* note 12, at 48-49.

181. McArthur, *supra* note 2, at 476.

182. *Id.*

183. *Id.*

184. *Id.*

VII. CONCLUSION

Joint ventures are a means by which both parties can make use of each other's strengths while minimizing their potential losses by sharing capital and risks.¹⁸⁵ Because the venture's success or failure hinges on the joint management of the operation, both sides must enter into the agreement in a spirit of cooperation and attempt to sublimate their parochial interests in favor of the common goal.¹⁸⁶ Differences in opinion can make the operation and management of the joint venture difficult, if not impossible.¹⁸⁷

The PRC has proven that it is excited about foreign investment.¹⁸⁸ At the present time, China is only starting to be regarded as a country in which a foreign party can "achieve a respectable rate of return" on its investment.¹⁸⁹ In fact, given China's post-World War II system of government, it is remarkable that the PRC is considered by foreign investors at all.¹⁹⁰ This reversal is a "great tribute to China's current leadership."¹⁹¹

Western countries have noted that, since the 1983 negotiations, plant constructions and the general business climate have improved in terms of speed and amicability.¹⁹² Additionally, although there are "many stories about bureaucratic nightmares," many foreign managers find the PRC bureaucracies "generally tolerable."¹⁹³

The result is that the PRC is an environment that welcomes foreign investment, albeit not without certain restrictions.¹⁹⁴ The Joint Venture Law and the Joint Venture Implementing Regulations are concerted efforts by the PRC to attract foreign investors to China, in order to aid China in achieving its goal of economic modernization by the turn of the century.¹⁹⁵

Japan, on the other hand, has had over 100 years experience with foreign joint ventures.¹⁹⁶ One of the major differences between joint ventures in Japan and the PRC is that the Japanese are not very willing to adapt their business practices and philosophy to those of the

185. E. HAHN, *supra* note 3, at 63.

186. *Id.*

187. *Id.*

188. Surrey, *supra* note 3, at 222.

189. *Id.* at 257.

190. *Id.*

191. *Id.*

192. Stavits & Gang, *supra* note 102, at 47.

193. *See id.* at 48.

194. *See generally* Surrey, *supra* note 3, at 232-33.

195. *Id.*

196. Ballon, *supra* note 6, at 134.

West.¹⁹⁷ European executives have long complained about joint ventures in Japan.¹⁹⁸ Three main problems in dealing with the Japanese are: (1) the Japanese parent company always desires an increase of the joint venture's market share, "almost regardless of company profitability;" (2) the Japanese work philosophy and employment practice; and (3) the complete divergence of the Japanese "salary structure with its unique fringe benefits and expense accounts" from the European/Western model.¹⁹⁹

Additionally, Japan's statutory scheme is not designed to attract foreign investment, but rather to subtly discourage it.²⁰⁰ The bureaucratic maze in Japan is a formidable one, almost incapable of successful negotiation without domestic aid.²⁰¹

This is not to say that a joint venture in Japan is doomed from its inception, however, the foreign investor should embark on this course fully aware of the relatively low survival rate of such operations.²⁰² To achieve success in a Japanese joint venture, a foreign party will have to adjust itself to Japanese business practices, be willing to meet the Japanese halfway, find a Japanese partner whose goals and objectives are compatible, gain the personal trust of the Japanese partner, and be able to offer the Japanese partner a unique product or service.²⁰³

Both Japan and the PRC have attractive and unattractive features in the way they have structured their respective joint venture laws. Compromise and accommodation are necessary for success in business relations with both nations. For the investor willing to attempt to surmount these obstacles, the potential rewards are limitless.

Richard E. Pelosi, Jr.

197. *Id.*; see also Surrey, *supra* note 3, at 224.

198. Ballon, *supra* note 6, at 134.

199. *Id.*

200. See generally McArthur, *supra* note 2, at 471; King, *supra* note 6, at 135.

201. McArthur, *supra* note 2, at 474.

202. See generally J. ABEGGLEN & G. STALK, *KAISHA, THE JAPANESE CORPORATION* (1985).

203. Tung, *supra* note 126, at 12.

