

COOPERATIVE JOINT VENTURES

Legal status

Cooperative joint ventures, in which the Chinese and foreign parties cooperate on the basis of a joint venture contract, became common in the early 1980s. The Law of the People's Republic of China on Chinese-Foreign Cooperative Joint Ventures (the "Cooperative Joint Venture Law"), promulgated in 1988 and amended on October 31, 2000, essentially confirmed the established practice. "Contractual joint venture" is another term for cooperative joint venture.

Cooperative joint ventures take one of two different forms:

- a "pure" cooperative joint venture in which no legal entity separate from the contracting parties is established and the parties make their contributions to the project and bear the risk of profit and loss directly; and
- a "hybrid" cooperative joint venture in which a separate business entity is established and registered and the parties' liabilities are generally limited to their capital contributions to the entity.

Although the Cooperative Joint Venture Law does not explicitly distinguish between these two types of ventures, it provides that cooperative joint ventures that meet the relevant legal requirements may qualify as "legal persons" under Chinese law. The Cooperative Joint Venture Regulations make further distinctions concerning the treatment of cooperative joint ventures with legal person status and those without. A hybrid form cooperative joint venture would generally qualify as a legal person, while a pure form cooperative joint venture would not.

Establishment

The documentation required for the establishment of a cooperative joint venture and the procedures for obtaining approval of the project are very similar to those outlined above with respect to equity joint ventures.

In the case of a cooperative joint venture, the examination and approval authority (generally MOFCOM or its local counterpart). The contract and articles of association become effective upon issuance of an approval certificate.

Parties' contributions

One of the reasons many investors in the past have chosen to utilize a cooperative joint venture structure instead of an equity joint venture has been that the investors are able to make their contributions to the joint venture in forms other than those allowed for an equity joint venture.

The Chinese party to a cooperative joint venture might, for example, be made responsible for providing the required local labor, including the payment therefor. The Chinese party might also be responsible for providing the necessary factory or office facilities.

Relevant rules have become more restrictive in light of the issuance of the Cooperative Joint Venture Regulations. In some cases, it may not be permitted to count some of these forms of assistance as joint venture contributions, although practice in this regard varies considerably. Foreign investors should focus on how to categorize and structure the parties' contributions to a cooperative joint venture.

Unlike the case of an equity joint venture, a foreign party's investment in a cooperative joint venture may be repatriated

prior to the expiration of the term of the joint venture, if the joint venture contract provides that ownership of all of the fixed assets of the joint venture shall revert to the Chinese party upon expiration of the joint venture term. However, the methods by which early repatriation may be accomplished are limited, and careful planning is required before establishment of the cooperative joint venture.

Operation

Pure cooperative joint ventures will usually have a shorter term than equity joint ventures, while hybrid cooperative joint ventures may have longer terms similar to those of equity joint ventures. Cooperative joint ventures are favored for hotels and commercial complexes and in infrastructure projects where the parties intend that the joint venture assets will stay with the Chinese party at the end of the joint venture term. Cooperative joint ventures are also commonly used for projects where the Chinese partner lacks material assets to contribute to the joint venture. Cooperative joint ventures in manufacturing are generally discouraged. The operational activities of cooperative joint ventures are restricted in much the same way as those of equity joint ventures.

It is common for cooperative joint venture contracts, especially those of pure cooperative ventures, to provide for the reversion of all of the assets of the joint venture to the Chinese party upon termination of the venture. In other cases, the liquidation procedures follow those applicable to equity joint ventures.

Foreign exchange

Cooperative joint ventures are generally subject to the same foreign exchange rules as equity joint ventures.

Profits

A substantial advantage of cooperative joint ventures is that the parties may agree on the distribution of profits at a ratio different from that of the parties' capital contributions.

Financial administration

An accountant registered in the People's Republic of China must be engaged to audit and verify accounts. The parties may engage the accountant jointly or individually. A cooperative joint venture without legal person status must keep unified account books, and the parties must, in addition, keep their own separate account books.