David Faure and Anthony Pang

The power and limit of the private contract in Ming-Qing China and today

Abstract

This paper argues that the responsibility system of the 1980s in China was based on the revival of the contractual tradition that had been current over much of China in the Ming and the Qing dynasties (14th to 19th centuries). The strength of the Chinese contract rested on its flexibility. However, because it implied minimum state regulation, it served poorly as a negotiable instrument. The same strengths and weaknesses are detectable in the use of contracts in China today.

We would like in this paper to comment in general terms on the tradition of written contracts in China. We take as our starting point the common knowledge that China had enjoyed a strong contractual tradition in the Ming and the Qing and that had been built upon by legislative changes in the Republic. During the first few decades of the People's Republic, the contractual tradition had been compromised because of the overbearing involvement of the state in the economy, but it had been revived since 1979 and had been rapidly developed through practice and further legislation.

The contractual tradition

The popular handbook *The Complete Book of Ten Thousand Treasures* (*Wanbao quanshu*) published in the Qing dynasty was meant to provide the essentials of business.[1] In it one would find chapters on geography, geomancy, fortune-telling, observations on security in travel, etc., all very important subjects for the successful conduct of business. Not surprisingly, a section on written contracts is also included. A similar section on contracts is included in the popular late Qing do-it-yourself manual, *No Seeking Help in Ten Thousand Matters* (*Wanshi buqiu ren*).[2] The presence of a chapter on contracts in these popular texts suggests that in the Ming and the Qing dynasties, written contracts were widely used. For all we know, they might have been widely used as well in the Song, but given that the Song-controlled portions of China were much more limited than the Ming, it was in the Ming that the written contract would have spread to many parts of China. It might not be unreasonable to argue that the spread of the written contract was one of the consequences of the very successful development of trade and handicraft industry in the Ming.

By far, most contracts in the Ming, Qing and even the Republic, would have been of a purely private nature. By this we mean they were concluded between private individuals without the involvement of the state. However, because most of these written contracts were made in the process of land transaction, and, besides several other stipulations, Ming and Qing law would have required the registration of the transfer upon the payment of a fee at the yamen, we know that by law there could have been few private written contracts. Nevertheless, the payment of any fee being a matter to be avoided, one should not be surprised to learn that few transactions would have been registered and that most transfer of property was a matter conducted privately between the contracting parties and the state played only a minimal, if even a formal, role. An indication of this formal role of the state is the legalistic language in which the contract was written. It is well known that members of the immediate family were given the right of pre-emption in land sale, and hence the land deed carried a line to

[1] *Zengbu wanbao quanshu*, 1758, j. 6.

[2] The copy I have is *Wanshi buqiu ren*, 1949, Xiamen.

indicate that members of the immediate family had been offered the property in question before it was sold to a party outside the family. This concern for legality reflected very closely the stipulations of the penal code. The provision for members of the family to preempt the sale of a plot of land, for instance, served as evidence that the property in question had not been sold by stealth, an act punishable in the code. Similarly, the contract might specify that land had not been transferred in settlement of debt, for the settlement of debt by transfer of land was also banned by the code. What better reason, therefore, was there for the sale of land than the need of money to pay one's tax or to bury one's parents? The frequent reference to these reasons for the sale of land could have no bearing on the tax rate or the cost of burial in imperial China. They were written into the contract because it was convenient for vendors and purchasers to produce a legally acceptable cover if the need arose.

One might litigate on the occasion of breach of contract, but the maintenance of contracts in the Ming, the Qing or the Republic was relegated most of the time to personal trust. The governance of that was not temporal law but the laws of the deity. In this respect, the contract signed for purely secular activities might slide easily into the religious realm: the predecessor of the contract would have been the pledge that was made before the gods, and its enforcement was never very far from the religious realm. One must not, however, be naive about the enforcement of religious observations. The realm of religion was closely bound up with local society, where participation in religious celebration was often a matter that varied with village or lineage membership. Contractual obligations that were set up in the form of lineage or village ritual participation, therefore, carried a strong social as well as a religious element. A typical example of this ritual-legal concept in action would have been participation in the lineage trust, where property was held in the name of ancestor and the rules of inheritance gave rise to the principles of equity. The property might not be sold (even though in practice it often was) but the management rights would have been divided into as many shares as the ancestor in whose name it was held had sons even though quite often all male offspring would have been given a share of the proceeds. Entry into such a contract might have been set up by document. That document would have been a genealogy, which proved to the satisfaction of all parties that they had descended from the ancestor. The contract would have come into effect not through a process of signing one's signature, but by all contractual parties agreeing to the genealogy itself. If all male descendants had an equal share by acknowledged descent, the right to the share would have been invoked by acceptance of membership.

The strength of the written private contract rested on its flexibility, but so did its weakness. There was no subject that could not be covered by a contract. Contracts were written for the purchase of land and people, for marriage and divorce, for inheritance arrangements, or for loans of money. However, while contracts were drawn up for business partnership, there were few contracts in the nature of what one might think of today as commercial papers. The impression we have of Ming and Qing contracts is that contracts were drawn up as evidence of the assignment of individual rights, but few individuals could have signed on behalf of an institution. No written contract was needed for employment, and merchants depended on their account books rather than the written contract in their business transactions. Although much business was conducted on credit, with some exceptions that we shall look at in the next section, there was a dire absence in the Ming and Qing of an infrastructure that might facilitate the exertion of credit at a distance. Credit, in other words, was personal: the agent working on his own capital and taking his own risks.

In this situation, merchants aimed for mutual protection. In the Maritime Customs decennial report on Wuzhou, 1892–1901, we have perhaps one of the best descriptions of the functioning of merchant associations for this purpose:

'Mercantile associations are established for mutual trade protection. . .. Should a merchant send cargo (e.g.) to Nanning by native carriage, he cannot, generally, effect any form of insurance, nor have any reasonable security that the cargo will reach its destination, it is the easiest thing possible for the boatmen to appropriate the merchandise, and say that it was lost by shipwreck upon the rapids. Accordingly, a merchant, in cases of possible malpractice, applies to the association for assistance; the association forthwith dispatches detectives, at the expense of the association, to gather evidence, and should a case be proven, it is passed on to the magistrate's court for adjudication. Associations furthermore undertake to collect debts. A merchant invariably endeavours to settle a case by means of his association, rather than by means of his guild court, as he thus avoids giving trouble to other merchants' (CIGC.DR, 1892-1901: 336-37, Wuchow).

Many of these merchants, it should be noted, might be resident in Wuzhou but would not have been Wuzhou natives. A guild regulation that incorporated the threat of 'ostracism of the defaulting purchaser' quoted in the same report brings home the dependence on collective action for the enforcement of personal credit.

One of the best descriptions we know of the sudden change to this environment is recorded by an officer in the Maritime Customs in 1891 when the telegraph and the steamer had transformed the nature of foreign trade:

'In old times business was done in Shanghai by men having command of large capital, who brought heavy consignments here and stored them till there was a chance of sale, or they bought goods and sent them home to find a market. Now a very large and increasing amount of foreign produce is bought on commission, orders being conveyed abroad by telegrams and the total price and rate of exchange being settled before the order is dispatched. Similarly, the silk trade is largely done now on orders from Europe, and purchases from the Chinese merchant are not completed until the finance of the transaction is definitely arranged and the laying-down cost calculated to a fraction of a penny. The daily or hourly fluctuations of exchange may have made this necessary, but the system entails consequences anything but desirable. It facilitates the carrying on of trade with small or almost no capital: it promotes a sharpness in business and a keenness in competition which tend to make getting business a more important consideration than how it is got; and it renders it necessary, too, for us Customs people to be far more watchful of frauds than in days when Chinese trade was confined to men of more means and making larger profits, to whom there was not the same temptation to take advantage of us as when business is done on a fine margin not exceeding 2½ per cent' (CIGC.DR, 1881-1891: 323, Shanghai).

What the passage does not make clear is that the admission of small traders was quite crucial in the expansion of the market. At some stage in the evolution of business from tradition to modernity, the credit of banks, of paper instruments and their financiers, would seem to take over. Credit institutions do not ever replace personal credit, but they differentiate the market place. The written contract takes on a different character in different sectors of the market.

The involvement of the state in the use of contracts

Until the legal reforms of the Qing government in the 1910s, the state was only minimally involved in the creation and execution of written contracts. Parties to a contract sought whatever legal protection they could, within the terms of the penal code, and while the penal code went quite far in offering protection for landed property, it was a weak instrument for the creation of credit. In particular, it left quite open the two areas on which modern business survives, that is, the pooling of capital and the circulation of bills.

Questions concerning the pooling of capital relate to the institutions of partnership and the business company, and included in them is the concept of the corporation (or the legal person). As our research stands, we know more about the mechanics of Ming and Qing partnership than we do about the operation of the company laws in late Qing or Republican China. Into the late Qing, although we cannot really be certain of an earlier origin, some partnerships increasingly took on the character of share-holding companies, so much so that in a recent book, two Chinese historians have described equity held by contract in the Zigong mines as 'contractual stock' (Peng and Chen, 1994). This is a useful concept for thinking about the Zigong mines or Ming and Qing partnerships in general. Partners in the Zigong mines hold transferable contracts on the contribution of capital and the distribution of gains. However, as the two writers, Peng Jiusong and Chen Ran, point out, there was no open market in which these contracts traded. Instead of open market dealing, partnerships were privately established. In the small communities out of which the Zigong financiers operated, one might imagine that partners essentially had to work together. The obvious question that arises from this description, therefore, is why the purchaser of a share would automatically be accepted as a co-worker. In answer, one might argue, and the argument seems to be implicit in Peng and Chen, that the partnership was essentially a matter of the pooling of capital, the financiers being sleeping partners and the active partners contributors of labour. Interest was paid to the financiers as a matter of course, purely and solely on the basis of the amount of capital owned. Practically, their documentation, which on this score comes primarily from the Republican period, shows that it was not custom alone that maintained the privilege of the share-holder, but its recognition by the local law court.

The example of Zigong demonstrates, therefore, the fallacy that business companies must necessarily be created by law. Nevertheless, it also shows that what counts for customary practice might well have embodied an element of the enforcement of contractual obligations by authorities that were outside the contractual parties. It is conceivable, and demonstrated to a limited extent in the case of Zigong, that custom might exert quite effective regulations within a regional context for particular lines of business. If this is true, what impact might one detect in the enactment of a company law by the state?

It is easy to exaggerate the immediate impact of the company law in the early twentieth century. However, what one would notice is, whatever the impact of the law, the increasing use of the word 'company' and its Chinese equivalent, *kongsi*, in the business environment.[3] Changes were coming about in Chinese businesses in the Republican period, but they were changes that had been brought about by managerial style, industrial development, accounting procedures, taxation, or banking, just to name some of the most obvious sources of change, rather than the law as it applied to company registration. As long as most Chinese businesses remained family firms, the idea of founding a company or holding a meeting for a board of directors was quite extraneous to the operation of the firm. Registration under the company law was attractive only when the firm might have wanted to expand its capital resources beyond the immediate context of the family, or, as long as it had no reason to object to presenting some of its books publicly at regular intervals, when it wanted to protect the principal share-holders through the provision of limited liability that was made possible by the company laws. Between the companies that might have wanted to register with the Republican government and the mines of Zigong is a difference in scale. The companies that registered included land development companies, insurance companies, spinning mills, the Shanghai stock exchanges, that is, many of the most highly

[3] The best discussion we know of the change in terminology in relation to business is Pui-tak Lee (1995: 7-41).

capitalized corporations in the Republic. Yet, one might say they did not ever go the entire extent made possible by the law. The financial markets in Shanghai dealt in government bonds and commodities rather than company shares. Chinese companies were never very transparent in the ways in which they operated, and it must have been risky to invest in company shares unless one had good grounds to put faith in personal trust.

The law as it applied to bills took a very different turn. Bills of all sorts multiplied in the Republic as it had never done in any other era in Chinese history, and yet, the economist Ma Yinchu, who understood the circulation of Chinese bills more than most people, was highly critical of the under-developed market for them.

In the introductory chapter of his *Zhonghua yinhang lun* (*A Treatise on Banking in China*), Ma Yinchu noted the importance of paper instruments in the creation of credit (Ma, 1929).Banks dealt in paper instruments: if paper instruments were poorly developed, banks would be poorly developed, so went Ma's argument. But why were paper instruments poorly developed in China? Ma gave two reasons. Firstly, there was no law governing the issuing of bills. Secondly, China had no bill brokers or discount houses.

To come to these conclusions, Ma had in mind the processes by which bills were created and circulated. His favourite examples had to do with bills of exchange in the normal course of long-distance trade. Issued by a bank for the settlement of payment, the bill of exchange might be sold by a supplier of goods as a negotiable instrument. Some such bills had been in existence from the Song dynasty, as is well-known, and in the Ming and the Qing, the use of promissory notes drawn on native banks was a common means of remittance. However, this is where the twentieth century was different from the nineteenth: no nineteenth-century Chinese writer worried about documentation for goods in storage, but Ma argued that the bill of exchange that was advanced in settlement in payment for goods might be sold to the bank only with adequate documentation on shipment or warehousing. Such documentation was quite inadequate in the China of the 1920s, and Ma offered this as one reason for the slow development of the bill of exchange. Citing the example of the Shanghai-Nanjing Railway, he argued that it took the clout of the Bank of China to ensure that the railway authorities would acknowledge its own deposit receipts. Elsewhere in the book Ma gave another example of a similar extension of bank credit. The banks set up modern warehouses in Wuhu, the centre of the rice trade in China, so that documentation might be given for goods deposited. When in Ma Yinchu's opinion, a thriving business in bills was a prerequisite to the growth of a national banking business, he was thinking of banks being engaged in a combination of mortgaging and remittance.

There was, of course, already a ready market for bills in the 1920s. Chinese banks dealt in bonds issued by the government, the native banks and the foreign banks were engaged in drafts, and many banks issued currency notes. Ma Yinchu's proposal for a law on bills was, therefore, also a proposal for the imposition of control on bills that became negotiable instruments. Ma understood more clearly than most writers on the subject that paper notes that circulated privately were not currency for the simple reason that a contract drawn up between two parties (the issuer and original purchaser of the bill) would not necessarily impose any liability between the issuer and a third party (subsequent purchaser of the bill). In the absence of a law on the circulation of bills, bills of exchange that were drawn on native banks would have been regulated by the rules that the banks had set up among themselves. Opinions on the native banks would vary. It would seem that they provided a major service to economic development in several parts of China, especially in those areas such as the lower Yangzi and the Pearl River Delta in the 1910s and 1920s that saw considerable prosperity as a result of booming exports, and yet banking failures during economic downturn were quite common even though it is still quite hard to assess what impact these failures might have had on

the economy as a whole, or in the cities such as Shanghai or Guangzhou in which the native banks were located. Implicit in Ma's argument, therefore, is not so much the need for a law on bills, but for tighter control of banking operations, which was indeed implemented on Western-style Chinese banks, but which did not seem to have touched native Chinese banks.

However, in advocating a law on bills, Ma seemed also to have had in mind the need to facilitate the use of cheques among business corporations. In an essay written in 1922, he noted that one of the major differences between Chinese and western companies in the settlement of credit was that Chinese companies tended to rely on their account books while westerners used bills (Ma, 1925). Ma did not elaborate on the use of accounts, for he was more interested in advocating the popularization of bills, but the extension of trade credit among Chinese firms is well-known, even though studies into Chinese accounts have not yet thrown a great deal of light on the size of inter-firm trade credit. Theoretically, accounts were settled before the major festivals. In reality, credit might be carried in the books for substantial periods of time, and one might suspect that companies that were cash-rich could have served as pseudo-banks. Deposits made with private companies that came under no banking regulation would not have been given any protection, nor would credit extended from such companies enter into the banks. For such reasons, Ma would have justifiably regarded the use of accounts rather than cheques as a tradition that impinged upon the development of banking in Republican China.

Once we consider commercial papers, therefore, private contracts take on a very different character and the reason for this difference can be outlined. To think in terms of the contract, one thinks of the micro situation of voluntary agreement certified through writing and maintained, if necessary, by the courts. To think in terms of commercial papers, one thinks of the macro situation of the creation of credit and the implications of credit created working its way through the money economy. How credit might filter through the economy has much to do with the character of the market. It has to do with confidence in the credibility of the commercial papers, and that depends both on the propensity of the market to test credit instruments as well as the ability of the instruments to stand up to scrutiny. At that level, one needs not only legal protection, but also protection of the sort that shelters the market from state interference.

There is, therefore, a third aspect in the growth of government involvement in the Republican period that might have made a difference to the operation of contracts. That is the development of the legal structure. One would not want to under-estimate the scale of the Qing legal structure. That would have centred upon the magistrate, the appeal procedure that would stretch into the central government in Beijing, a substantial body of lawyers in the capital and in the provinces, many of whom would not have held official positions, and a body of legal literature including precedent cases and explication of the law. Yet, one would also have to note that the Qing legal structure did not recognize the position of the private lawyer, and that legal education as such was not an established tradition in either the training of the official or public discourse. To move beyond the Qing into the Republic, one might note in particular the impact of newspaper reports on court proceedings: the North China Daily News (and the North China Herald) giving detailed reports in English on civil suits, advances in the accounting profession, lawyers trained in the new legal tradition that had been adopted in the 1900s, and managers who were increasingly more accustomed to the language of the law. One does not wonder that in the international climate of Shanghai, with changes in the legal structure, changes might come about in business organization, but one has to ponder how in inland Sichuan, business structure might have changed. Juxingcheng Bank was registered with the government in 1915 as an unlimited partnership under the 1914 Company Law. Despite the change in terminology, it was really a family

business, where unlimited liability rested on the family and limited liability on other share-holders. It gave up this structure to register as a limited company in 1937 only when it was under pressure from the Sichuan provincial government to do so (*Juxingcheng yinhang*, 1987). The more curious case is Lu Zuofu of the Minsheng Company who in the 1920s came upon the idea of organizing a transport operation in terms of a centrally controlled company rather than a loose conglomeration of sub-contractors. The company not only expanded very quickly with the backing of Sichuan warlords but was also very adept at the management practices that were becoming popular in the 1930s. It maintained clear division of duties, it implemented unified accounting principles, and it compiled written regulations in many aspects of the company's operations. One would suppose that the management models for such an operation would not really have been the family firm but an institution that was rather accustomed to horizontal integration. The Maritime Customs would come close to mind (Ma, 1990).

All in all, the Republican period would have left the private contract very much in its traditional forms. But a modern sector would have been growing where the state increasingly played a role in the drawing up of contracts. That said, however, special reference should be made of the institution of the public assessor (*gongzheng*), whose office under the district court seems to have begun in the Republican period. As an officer of the court, the public assessor was under obligation to keep a full and clear record of all transactions. His purview, however, seemed confined to adjudication and certification. A witness had been common in traditional private contracts. The substitution of the public assessor for the witness would have been another step in the formalization of the contractual process.[4]

[4] For documents that the public assessor might have used, see Dong Hao (1937: 389-435).

Business contracts in the People's Republic

The impact of the revolution on the contractual tradition is a subject that will eventually have to be examined in the light of the broader question of the continuity of business practices from the 1930s to the 1950s. We would hazard the speculation that there was much greater continuity in business practice than one might prima facie suppose. Our impression is that current studies on post-1949 business practices have concentrated on employment practices, and there, no doubt, marked transformation had come about. From the mid-1950s, when business companies were taken over by the state, we would expect also a fundamental shift in accounting practices: where the accounts had been designed to reflect profit and loss, now they were essentially tax accounts. There must have been an impact on management style arising from this sort of change. Moreover, collectivization, no doubt, brought the family firm to an abrupt end. Nevertheless, placed in the longer view, the organization of quite a few businesses (e.g. Dalong Machine Works, Minsheng Shipping, the Rong brothers' textile mills) that survived from the 1920s into the 1950s were placed under a centralized management structure only in the 1930s. These structures did not conflict with the command structure imposed by the state until the Cultural Revolution. It probably was not until the Cultural Revolution generation that management was decidedly interrupted.

In agriculture, there would have been even greater continuity even though Richard M. Pfeffer, who examined the role of contracts in China from the 1950s up to 1963, found it very hard to make up his mind:

'The Chinese, to my mind, have not resolved the contradictions inherent in contracts within their system.... In agriculture in the 1960s they strengthened the administrative structure encompassing contracts by setting up the materials-exchange conference hierarchy'.

'While it is always imprudent to emphasize the high degree of actual control in such a complex, contradictory and inefficient system, I am inclined to minimize the importance of individual initiative at the production-unit level in most contracts in China. In practice such initiative appears to have been severely restricted by various organizational and ideological factors. If at a particular time it was not the central government, then it was the provincial or lower-level government, or, if not the government, then the Party, which performed the restraining function. There seems always to have been someone'.

'This is not, however, to accept the simple commandist view of contracts or of Chinese society. In the first place, commands, if they are to function with minimal efficiency over time and on a society-wide basis, must incorporate elements of agreement. For authority to be accepted over time, it must reflect to some degree the wishes and capacities of those over whom it is to be exercised' (Pfeffer, 1973: 63-64).

It almost rests on an act of faith that individual agreement mattered but this passage is a good reminder that contracts do not have to be what they seem. Only with hindsight have we been able to be optimistic about the contractual traditions of the early 1960s incorporating a strong voluntaristic element.

Private contracts were revived under the responsibility system from the end of 1978. However, even in the early 1980s, the applicability of private contracts was highly problematic, as the following case would illustrate:

'When state plans are changed and contracts are not executed, disputes follow. This sort of situation is quite common. The dispute over a manufacturing contract and loan between the Shanghai Glass Machine Tool Factory and the Chengdu No. 3 Brick and Tile Factory under litigation at Chengdu middle-level court is a typical example. The Chengdu No. 3 Brick and Tile Factory (party A) had been funded by the state to manufacture paper [coated?] mortar-boards. In October 1978, it signed an exclusive manufacturing contract with the Shanghai Glass Machine Tool Factory (party B) at a value of 1,960,000 yuan. In December 1979, A's operation was declared dispensable by the provincial authorities in a reordering of economic priorities (in effect the project was abandoned). When A notified B, B had already begun production. Moreover, A did not indicate that the contract was to cease immediately. When the work was completed, with A's agreement, the goods were delivered. When they arrived, A's bank account had already been cancelled. Including interest, A owed B the sum of 770,000 yuan, and was unable to pay. A dispute followed. In 1983, B sued through the Chengdu middle-level court. The court took the view that it was through a change of the state's policies that A was unable to pay, and that the relevant state department should be held liable. After much dispute. . .' (Zhen and Liu, 1985: 257).

The article continued to summarize various views on the question of liability, but the courts agreed that it rested with state administration in the province or at national level. In a different form from what Pfeffer might have expected, private the contract might be, but the hands of the state loomed large when the state still controlled a substantial portion of the economy. As Pfeffer also noted, one might say the same of the western economy; and to press this argument to its conclusion, the test of the independence of contracts rested, ultimately, on the ability of the court to hold the state to its liabilities.

Drastic changes in economic laws in the People's Republic since 1979 with the view to induce investment may be regarded as a 'legal revolution'. Many state corporations which in the early eighties were still themselves welfare states in microcosm have within the last fifteen years transformed themselves in whole or in part into public corporations whose shares (or shares in the form of American depository receipts or fund units) are traded on the stock exchanges in Hong Kong, New York, Canada, Singapore and Ireland.

Listing in foreign currencies requires compliance with the rules of foreign stock markets, their applicable companies and securities laws, and, above all, international standards in auditing and accounting treatment. Without fanfare, a body of economic laws has evolved in the People's Republic to make this transformation possible. The transformation has been so impressive that in opening up its market to the world, Vietnam has largely adopted the joint venture, companies and property laws of the People's Republic as its own.

Anyone who has had continuous dealings with China from the late 1970s and early 80s would find it impossible not to notice the change. Business corporations formed in those early years were in essence trading arms of the ministries under the State Council. Having no commercial record or experience, not to say an international commercial reputation, these corporations used to present their credentials by referring to their size (in terms of production capacity or numbers of workers under their control) or the departments or ministries that they represented. Their directors were invariably bureau chiefs or departmental heads under the immediate charge of the ministers. A plant in Nanjing, for instance, might easily employ up to 100,000 workers, but, because state plants would have had to take care of their employees' welfare, it would have owned and managed child-care centres, kindergartens, schools, research institutes, cinemas, shops, housing, etc. It would have been a township, and the head of the plant would have been mayor. Transformation into a business corporation in those early days did not alter the plant's state responsibilities or bureaucratic structure.

In those days, not only foreigners, but also Chinese people from Hong Kong, found it difficult to grasp the legal framework of those corporations. Their legal share-holders and registered capital were enigmas and their assets unascertainable and unverifiable. Their company structure resembled the traditional Chinese family for the chairman of the board or the general manager alone dictated all decisions. The joint venture law was yet in its embryonic stage. Outsiders learnt to trade with these corporations through trial and error. Many foreign merchants went home gleefully with an agreement for jointly building a hotel or upgrading a production line, planned or invested accordingly, only to discover some time later that the piece of writing termed 'agreement' in Chinese was merely a letter of intent. Only those documents termed 'contracts' were legally binding.

However, these business corporations began to learn through the intricacies of dealing with foreign companies. In the People's Republic, the corporation was formed through official sanction, its existence was a sanctity, and its registered capital (as distinct from its investment capital) was audited annually and required to be kept intact. It was difficult for the bureaucrat-turned-merchant to appreciate that there were two-dollar foreign shelf companies comprising one-man bands. Dealing with such shelf companies sometimes resulted in losses. Little wonder in those days that Chinese corporations traded or secured commercial deals often through Hong Kong and invariably through their clusters of trusted friends or traders introduced by them. In time, the corporations expanded abroad. But, as trade disputes with foreign firms, especially in the United States, might sometimes lead to the state being sued, the corporation often expanded in those days by entrusting its capital to trusted individuals who set up subsidiaries abroad in their own individual names as shareholders and who financed these operations through their personal accounts.

Meanwhile, in the Special Economic Zones, beginning with Shenzhen, new commercial laws had been created. The joint-venture ensured investment from foreign partners while the Chinese corporation maintained fifty-one percent of the shareholding, the right to appoint a majority of directors, and chairmanship of the board. Coupled with this arrangement was the almost irrevocable recognition of the legal representative of a corporation be it local or

foreign. This ensured the continuity of the original partnership and the partners' written (and oral) commitments. Changes in the shareholding of a foreign company did not necessarily entail the right of the new shareholders (or pledgees of such shares) to appoint another legal representative to replace an existing representative to the joint venture unless the Chinese side of the joint venture would agree. Some banks as pledgees learnt such truth the hard way when they found the bankrupt retained as their legal representative in joint ventures.

The joint venture law was eventually relaxed to permit more than fifty-one percent ownership by foreign partners, among whom were subsidiaries of Chinese companies registered abroad. In 1989, the cooperative venture law was formulated to permit division of assets between the Chinese side and its foreign partner proportionate to their respective shareholding at the end of the cooperative venture. The law was applicable to one-off enterprises such as building and reselling flats for profit.

Parallel with all this development was the growth of private enterprise. The responsibility system of 1979 was a reversal to the contractual tradition but it went beyond the early 1960s in that it was quite clear from 1979 that responsibility was to be given to the household. Extended to industry, the individual manager could be given a contract to manage a factory for profit in return for a fixed yield to the state. Individual entrepreneurs have thrived and with them has grown a massive network of private resources.

To cope with the rapid changes in economic law and the ensuing economic expansion, lawyers are gaining increasing importance in the People's Republic. In the early 1980s, cadre merchants themselves negotiated and drafted even complicated contracts. Lawyers in those days were often trained in the pre-Cultural Revolution era and could not keep abreast of the times. There were times in the early 1980s when they appeared only after the negotiation process and only because the foreign merchant had brought along a Hong Kong lawyer to the negotiation table. Later, as more legal work was required, one-issue lawyers appeared, for example, persons experienced in trade disputes now dealing exclusively with employment matters. Specimen joint venture contracts, purchase and sale contracts, were now supplied and used by the corporations. Since the mid-1980s, the pool of law graduates has been enlarged and with increasing dealings with their foreign counterparts, some have acquired international standard. In comparison with the needs of the market, however, the shortage of lawyers is still acute.

What China went through between 1979 and 1994 was no less than a repetition of the legal history of the late Qing and the Republic. And the essence of the change had to do with the nature of contracts and finance. While one does not expect private contracts to be less often resorted to, one has to expect the differentiation of the market. The structure for finance has come about so that the state is drawn in, through the making of laws and the maintenance of the judicial process, in the creation of a new infrastructure for business. When that structure has developed, it will not be kept apart from the realm of private contracts. That will spell major changes in the traditional sector.

Cross-roads

One thinks of the many junctions ahead of China's social and economic development when one thinks of the social milieu into which written contracts must now fit. Personal trust must still remain the essential building block for contractual arrangements, but the question that arises is whether the addition of legal entities into the formula might prove threatening to a patronage structure that has always been well entrenched in Chinese society. One might think of the move out of the environment of the family firm into some division of ownership and management, although one suspects that unless and until the law has demonstrated its viability and permanence, no share-holding structure will replace direct ownership. It

may well be true that many state enterprises are going economic concerns, but until some transparency is introduced into their management, no share-holder will know how the collapse of one through the default of some 'triangular debt' will bring down another. There is, as always, the open question of the privatization of state enterprises, and that is how state interests might be maintained when the enterprise is turned into a business company and a share structure is introduced. It may not even be far-fetched to remind ourselves that contracts are awarded from the state or from collectives on fixed terms. Land is not held free-hold anywhere in China, nor does a private individual or firm hold claims to a construction for more than a stipulated period of time. When ownership ultimately reverts to the collective or the state, does a contractual arrangement continue upon the payment of a fee or does the state take over management? One would have thought that eventually it must be spelled out where, on the one hand, lies the linkage between established state and local institutions that might represent the collective economy and, on the other, the holding of private property through instruments such as a share that can be passed along to one's descendants. One does not necessarily see a return to the principles of the lineage – the modern company will be strong competitor with that – but one must not assume that the road China chooses to follow is necessarily that which took the West to where it now is. As the poet put it, China might just choose the one less travelled by, and that could make a difference.

David Faure, *University of Oxford*
Anthony Pang, *Pang, Kung & Co., Hong Kong*