

Webcast: A Primer on Chinese Environmental Law: Key Trends, Issues and Risk-Management Approaches for Corporate Counsel

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ASSOCIATION OF CORPORATE COUNSEL

Moderator: (Bruce Clafter)

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Operator: Just a reminder, today's conference is being recorded. Go ahead, (Bruce).

(Bruce Clafter): Thank you very much, (Lance). This is (Bruce Clafter) speaking. I'm at Applied Materials in California, and I'd like to welcome you all to our primer this morning on Chinese environmental law. We're very fortunate to have two excellent speakers presenting this morning. I'll give you a quick biographical sketch, an introduction, in a moment.

Just a couple of reminders before we get into the program itself. First of all, there is a webcast evaluation button on the right side of your screen. We would very much appreciate it if you would take the time to fill that out after the webcast so that we can make adjustments for future programs.

Secondly, we're going to try and reserve as much time as we possibly can for questions during this presentation. You can send a question at any time by clicking into the question box on the right side of the screen at the bottom, and I will be reviewing the questions

during the conference, and I'll try and collate the ones that are similar in nature and pose those to (Tad) and (Hongjun) at the end. And then, there will be opportunities for you to jump in at the end, as well. So, at any time during the call, please send us your questions.

Our speakers this morning are both partners at the Business Law section of Holland & Knight. They generally reside both in Washington and in China, spend quite a bit of time there. (Tad) is a principal in the firm's China team, as is (Hongjun). They both spend the majority of their practice working with multinational corporations on various China matters with some emphasis on environmental law, and that's going to be the subject of today's primer. There are full biographical sketches, again also on the right side of your screen, if you want to click in there.

Tad and (Hongjun) work with a variety of companies and trade associations as well, tracking environmental and regulatory issues in China on a regular basis, and they're going to take us through the basics of China environmental law so that we're better equipped to practice there ourselves on behalf of our companies.

So, I'm going to turn it over to (Tad) now.

(Tad Ferris): Thanks, (Bruce). Thank you, everyone, for joining us today. I have with me Dr.

(Hongjun Zhang), who - folks who don't know him may be interested to note that he is, prior to joining our practice, legislative director at the National People's Congress in charge of law drafting and implementation of law nationwide, particularly with regard to environmental law and policy. And prior to that, enforcement in - Planning Officer in the state Environmental Protection Administration, the equivalent to our U.S. EPA.

With that, I'd like to just give folks a quick overview of where we're going to go today. Again, this is a whirlwind tour. We have about 45 minutes, plus some question and answer time, to address the full range of issues related to environmental law and implementation in China. What we'd like to do first, though, is give some folks - give the folks on the phone some grounding, talk about legislation and rulemaking in China. No matter what area of law you address in China, I think these issues will be relevant.

We particularly have some insights that we can provide folks from the (fact that) at least half of our practice now is focused on rulemaking, advocacy, those kind of issues in China. It will help in-house counsel with understanding where they might, for example, engage on proposed lawmaking, and will link well with the other parts of our session today. Then, we'll provide an overview of the environmental legal system in China just to give folks, again, some stronger grounding in this particular area, run through some key issues for corporate counsel. Of course, in the time we have available, we can't address every issue, but that's why we'll have a question and answer period and, of course, there will be ways to interact with us even after the session today.

Then, we'll look at some trends that are shaping the future of China's environmental law system and, if we have time, we were asked to, and we did provide in this, some key issues in China's safety and health law areas, which in and of themselves are enough for lengthy additional discussions, but wanted to give folks, since this is the EHS Committee, some understanding of that area of law in China, as well.

(Bruce Clafter): (Tad), we have a request for you to raise your voice a little bit. People are having trouble hearing.

(Tad Ferris): OK.

(Bruce Clafter): Thank you.

(Tad Ferris): There's also a slight echo on the phone. If folks have any issues, just let us know, and I will raise my voice. Again, also we'll have Dr. Zhang speaking, as well. And for folks who have the screen and see little blocks there, when they do get access to a PDF of this presentation, that - those little blocks are actually Chinese characters which, apparently, this webcast software can't accommodate. But, they will be in the, I assume, and (Bruce) can confirm, the PDF version of this that (ACCA) will be making available to the participants.

Again, starting with legislation and rulemaking, I'd like to give a run-over and then hand it over to Dr. Zhang who, as one of China's principal lawmakers, will have some input. First, we'll just give folks sort of a comparison, since many of us on the phone are approaching this issue from the U.S. perspective, and then trying to interpret from that standpoint. It's good to sort of look at some of these issues in comparison, China versus the U.S.

So, with that, I'll let Dr. (Zhang) cover this slide. (Hongjun)? And if you could speak up?

(Hongjun Zhang): Sure. By this slide, we want to give first overview why in China you say something very different (than the way) what you say here in the U.S. was the reason with the culture, government and other reasons. And people all know about the rule of law, and

the rule of (law) authority. We give you with Chinese character here in the first slide, basically try to - showing, you know, a background, which is a political figure, ((inaudible)), whatever, in the past can even change a language, a Chinese character. When you show in the PDF document, it will say that regarding who will resolve dispute here in a (space) ((inaudible)) the charge and the (car) play the most important role, and in China it's more like the Ministry authority. You know, people might have a big dispute. They often to go government authority for resolution.

And also, another interesting thing regarding the historical view - historical background regarding the Chinese law, you know, the U.S. law and the - (most of our) Western law basically originated from both civil law and the criminal law, you know, civil law and the criminal law, if not - you know, basically are the same weight in China is quite different historically. Law basically means criminal law. That have some practical implication to the environmental law and implementation. People will - you know, the relation of the environmental law is not something nice or good, but is something they say is OK. So, that people's - the view from people's general ((inaudible)) makes significant implication to the environmental law implementation in China.

(Tad Ferris): Thanks, (Hongjun). And just for folks to put a sharp focus on that slide seven, where you see a box where it says (Cow) and a box where it says (Half), the characters in China for (Cow) and (Half) are very similar. And that was an example from previously - previous dynasty in China where the emperor, merely by a mistake in his writing the character, changed the whole meaning of that word, meant to write (Cow) and, instead, meant (Half), and how the whole system was changed because of that mistake by the authority, and that whole tendency to emphasize authority figures.

For example, if you have a dispute in a village, you wouldn't necessarily go and say, "Well, what does the law say?" You may go and see the village elder, to put it at the very most local level. And also, on the criminal law point that (Hongjun) made, that is why, even today, there tends to be increasing focus on applying criminal law to environmental violations in China in order to really get the notice of the, particularly, Chinese-regulated community there.

Next slide, eight, we wanted to sort of give you a brief, back-of-the-envelope overview of law-drafting protocol. In China, laws are often written in general terms. This is something that is often daunting for in-house - daunting for in-house counsel. In the U.S., of course, we can often say also as in-house counsel that the laws can be overly complex but, at a minimum, they're typically more detailed than in China. The law-drafting process in China, often agencies assume a dominant role, not as in the U.S. a wide range of stakeholders. Still, even with recent transparency initiatives in China, public participation initiatives, it is the government that plays a dominant role.

The next three slides we're not going to go through in detail, but we wanted to provide those as follow-up. Really, we go over first the overview of China's modern statute-making process, then we look at the state council rulemaking process. the statute-making process is driven by the Congress, as it is here, and we wanted to highlight on figure one that there are two procedures that are primarily chosen for the preparation of drafts. One is via National People's Congress special committee. (Hongjun) was the legislative director in one of these committees. And the second would be via agencies, often similar to here in the U.S., where the agency would propose a new law and send it up for a congressional review.

We want to highlight these procedures to - and we'll talk about some of the main takeaways from this just so individuals on the phone know how laws are developed and where there might be opportunities for intervention engagement within this process. It is changing day to day. However, often these processes do provide opportunities for us as in-house counsel through our teams to actually engage in and comment on new laws.

Figure two is the state council rulemaking process. State council is the highest level executive agency in China. We'll go over the nature of that agency soon. But, just to give you that sense. And then, finally, figure three provides an overview of the state council agency rulemaking process. This is often where we, as companies in modern China, typically engage on rules. These are typically the rules that affect us day-to-day. For example, the state Environmental Protection Administration, this is their rulemaking process that they typically engage in.

And I wanted to go then to, more importantly, slide 12 because I think this gives us some sense of why we have processes in place. The way a particular rulemaking effort is (initiative) can be somewhat, let's say, without systematic process. Some of the influences on the rulemakings and observations include systematic thinking. You know, this is whereby a rulemaking is (an issue) just because the agency officials logically identify that something is missing from the legal system. For example, we don't have rules that cover injection of hazardous waste. We need those. That is one thing that we can't all of a sudden anticipate as in-house counsel.

However, some of the things that we can anticipate that exist in the Chinese rulemaking system right now are, for example, remarks on the margins of political or other high-level reports. What does this mean? Well, often, the very senior officials in the Chinese government receive report services from their staff. These are among the senior-most politicians all receive these reports. If they see something, for example, on - I'll give you an example - a recent example - the fact that waste from electronic and electrical equipment is creating legal dumping problems in the southeast of China, they make a comment. It could be just a few words in the margin of that report. "This is important. We must see to it."

That very comment, passed on through the bureaucracy in China by a senior-most official, can initiate a whole range of rulemakings. Now, that isn't exactly what we call a transparent process, but just to understand that that kind of thing can exist triggered by these reports, triggered by, for example, citizen group campaigns that put a big spotlight on certain issues in China are all influences when in this system at present.

There is also the issue of agency politics. We're very familiar with that in the U.S. In China it is very much alive and well. The whole reason that these agencies fight for power and existence, every five years they are - go through a reorganization during which some of them may be merged, some of them may be shut down. One of the ways that's important to remember that an agency in China shows that it has relevance in China's administrative system is to make rules. You will see that they are very capable, as we go through this slide show, of making rules. The challenge is implementation.

However, as multinational corporations, we often find it daunting where we have internal company standards that require that we comply with the host country rules, and those rules

number, let's say in the terms of new rules, over let's say 1,000 every month. And we'll talk about that in more detail soon. But, just to know that agency politics is fighting can also be a great driver for some of the new rulemaking initiatives, and to understand that system can also give us a little more predictability, for example, if we know that the Ministry of Information industry in China, for instance, is the last industry ministry in China, we know that that agency's going to be particularly adept at fighting for its continued existence.

International influence, also something we need to - we'll talk about a little further soon in terms of trends. This is often a driver, that whole sense if we need to catch up with what the - you know, the other countries are doing that we believe are influential. We'll talk about which of those countries are particularly influential as well later in this presentation.

And then, also very much like here, local innovation or rulemaking initiatives can be very influential at the top levels of government, at the Congress, et cetera, the state council. Often where they - these policymakers see local initiatives spreading out throughout the country, they may say, "Why not implement this local measure nationwide?" (Hongjun), do you have an example of where local measures in China resulted in national legislation?

(Hongjun Zhang): There are several - such ((inaudible)) policy in the past. One example is automobile, emission controls vendor. The vendor normally start in Beijing and Shanghai, and then was expanded to national level. Another example is it relate to technical vendors, air pollution, water pollution. In the past, one new higher level of requirement comes out in local level, quite often that higher requirement in local jurisdiction become national requirement nationwide, you know, later on. Some other examples regarding institutional reform regarding training, regarding, you know, how indicator be used if enforcement action

and such and such. The local innovation and the initiative has been becoming - become increasingly important in China.

(Tad Ferris): Thank you, (Hongjun).

Like to move now to - since we're time-limited, to provide an overview of China's environmental legal system. Again, we can go into great depth. The whole development of rulemaking legislative initiatives in China has been changing almost month to month in the past few years. Just a final thought on that. Ten years ago it would be inconceivable for companies to actually provide input into law drafting in China. It would be generally reviewed as an infringement on China's sovereign right to draft its own laws. In fact, that's often the response they gave. But, that issue has changed dramatically over the past few years, and the more we can encourage our companies, our colleague companies to engage in this kind of activity in China, the more familiar the Chinese authorities will become with this approach, and the more accepting it will be.

We're now moving to slide - for folks online, slide 14. Wanted to give a general, again using comparison, just to give folks a good baseline understanding of some of the personnel resources. And again, this is at the national environmental authority level. In China you have 200-plus officers at the National Environmental Authority, or 1,000 if you include the state Environmental Protection Administration affiliate or supporting organizations, and this is often a way that the national EPA addresses some of its staff shortfalls is it borrows the staff from other organizations, including the - for example, the Research Academy on Environmental Sciences, et cetera.

The challenge with this, just to put a sharp edge on it for in-house counsel, is that, often, those affiliate organizations may also have private sector roles, so it's important to understand in any initiative, for example if you're engaging with SEPA on a law-drafting initiative, a compliance plan, et cetera, to understand what, if any, affiliate or supporting organizations are involved so you can better determine whether there are any confidential business information issues. But, it's important to understand that, when folks talk about, you know, SEPA only has 200-plus staff, that that is really not a clear picture of what really happens. They do borrow and, in fact, they are now receiving more funds that we can talk about to further augment their staff and resources.

Budgets right now for the national environmental authorities, just to show, China's at around 10 million. Again, that's changing, but that is hardly enough to dent some of the daunting tasks they face in China. Regional offices of the national EPA in China under development. In fact, news stories over the past week, if you've been following them, have underscored that, indeed, they are establishing these offices throughout the country.

We'll move to the next slide. We wanted to touch upon enforcement, generally, because this is often an issue for us. Often, we are faced with what tend to be very different characterizations of China enforcement. There is indeed a lot of enforcement going on. Often it is not against our companies, at least in the news-making way, thankfully. But, enforcement actions are generally implemented based on written enforcement guidelines. Believe it or not, these guidelines do exist. We can lead folks to - actually we've prepared translations of these that have been published, just to understand that they are based particularly at the national level, where there are big - often big cases initiated on very detailed enforcement guidelines.

The authorities are very sensitive to deferential - differential treatment of foreign and domestic entities under the law. Often, we perceive that we are treated differentially and, indeed, the actual cases that, legally speaking, the laws now generally apply equally to foreign and domestic entities. They've been undergoing revision of these laws for some time since WTOX session too, for example, where something only addressed importation before, they added manufacturing so that, at least on the law, it looks like there is equal implementation.

However, in practice, we still find that there are instances of differential treatment, particularly where it appears that more sophisticated foreign installations are subject to actions for minor infractions, whereas there may be domestic entities, including the big state-owned enterprises, that may appear to be responsible for very significant violations of Chinese law, but not be held accountable for those violations. This is often still a daunting aspect of operating in China.

You'll find if, for example, you're involved in a merger or acquisition of a state-owned enterprise that, if you dig down deep into the due diligence, you'll find that they typically hold very few permits of the many, many permits, licenses, et cetera, that they're required to have in place, particularly in the environmental area. This is often because they have enjoyed a relative freedom from this, not necessarily intentionally, but politically is much more difficult in China for the government to enforce against the state-owned enterprises, and it is one of the reasons that, over the past few years, they have started to push for privatization of these entities and, among other things, have issued laws requiring that these entities establish Offices of General Counsel and other efforts aimed at increasing the sensitivity of these organizations to legal issues.

Next slide. Again, speaking on the enforcement issue, generally, penalties are chosen from a basket of options. They may choose one, they may choose a number of them, again going from the most simplistic all the way up to the nuclear option, depending on the relevant law involved, what infractions are involved under what laws, the severity of the development. Often, you'll see in Chinese laws they typically refer to things, is it, you know, very serious crime, and you're, like, "What is that?"

But, often that - and we'll talk about that rulemaking tendency. That leaves additional flexibility to the authorities involved. It'll also depend on the nature of the entity and, again, that's where some of these differential treatment issues come in, and other factors.

Looking at the typical array of enforcement tools that they can use, go from the warning letter, which is a simple admonition, often in writing, a warning letter accompanied with a compliance plan and, often, that compliance plan is something that can be negotiated. In other words, "You shall do the following by this time in order to come into compliance."

An enforcement order specifying the date for re-inspection and compliance verification, in other words there's no compliance plan, but you have to figure out how to come into compliance by date certain.

A blacklist or other reputational penalty. Often, these are becoming more - these are recently becoming more popular in China. They have developed, in fact, a - what is essentially a blacklist initiative. Often, they found that Chinese, for instance, are much more sensitive to this kind of thing where there is a significant reputational penalty.

Then, of course, fines, monetary sanctions. These tend to be - in China these tend to be somewhat low. Again, they're gearing them towards the lowest common denominators, not often providing the variation to address companies that are very - actually able - that would not be deterred by the low fines. But, that is also changing. They're looking more at variable sanctions now, depending on the economics involved.

Shutdown orders. You often see these in the news. China, for example, shuts down 75 pulp and paper mills along certain river. These are often rescinded when compliance is verified but, sometimes, they're permanent. Where products are involved, they're looking more at import and manufacturer bans. For example, with a new chemical substance law, one of their ultimate weapons is a three-year import and manufacturer ban for that substance that has not been registered according to law.

And then, of course, criminal penalties. We're seeing these often with the recent spills in China. They're looking at a wide range of criminal sanctions against the - for instance, the entities that are deemed responsible for the Songhua river benzene spill.

Just to leave you with some general observations, we're moving to slide 17 here. With regard to the environmental legal system, the environmental law sector is receiving heightened attention from legislative and regulatory bodies. Everyone wants to get involved in this now. This is often creating what we see as a mission creep. In other words, it's not just the state Environmental Protection Administration any more than you need to monitor. It is a wide range of agencies, and we'll go through those shortly, that are getting involved in environmental efforts, environmental lawmaking.

There's a growing number of statutes implementing rules, standards and other legal norm-setting documents. We'll talk about the nomenclature soon. But, just to put a sharp edge on this, more than 1,000 such documents were issued in the EHS area last year alone.

The gradual greening of non-environment-specific statutes and regulations is also occurring. This would be contract law. This would be other areas of law. And now, when they're being revised, there are a number of environmental provisions that are often being included.

Government transparency and associated public participation efforts are more evident in the environmental area recently. Folks that are on the phone may know that, recently, China promulgated and also made effective public participation measures associated with the environmental impact assessment regime. This is something which before, previous to that, was only a mere comment in the environmental impact assessment law regarding the need to solicit public comment. But, now actually very detailed public participation measures are in force in China.

And this, as folks understand, given the background with China that we'll also talk about, in terms of accessing law, is quite a landmark event for them to actually push public participation to this level.

Just quickly now we'd like to review, just so folks know some of the key actors in the environmental area in China, first moving to slide 18 is the National People's Congress, which (Hongjun) was previous a member and legislative director. The Congress, for folks on the phone, is the national legislature, of course. It's the Environmental Protection And

Resource Conservation Committee, and also the Finance And Economic Committee, which are primarily responsible for drafting and reviewing environmental-related statutes. What you may not know, however, is that this entity also possesses supervisory authority over national and local implementation of environmental laws. Often, this is sort of like, again, the nuclear option for enforcement. If things aren't going well at the local level, the Congress can step in and take over implementation, supervision, and can even send missions to the local areas to supervise the implementation of the law.

Next, on slide 19 we have the State Council. As I mentioned, China's highest level executive body. It's composed of our Premier, Vice Premier, state counselors, totaling about 10, and a limited number of staff. What folks may not know, however, it's not a working body. In other words, they don't have a permanent staff that is rule-making every day. It instead convenes inter-government meetings on proposals and promulgates regulatory proposals submitted by state council agencies such as SEPA, or the State Environmental Protection Administration, if these proposals are generally supported by agency consensus. So, what - it will convene to review these proposals and act on them as requested.

A recent example is the - China's waste electrical and electronic equipment recycling law, which the National Development and Reform Commission drafted but then sent up to the state council for action, to put that in real terms.

Next slide we have, again, the State Environmental Protection Administration, the agencies everyone looks to as the environmental authority in China. A note here, as we motioned, that it's not a cabinet-level agency. There may be some changes upcoming that may make

this a ministry over those - have been long in the making. We'll see how things go. The administrator is (Xio Xionchen), who is recent - was recently appointed after the previous administrator, (Xi Zhenhua), stepped down after the controversy associated with the Songhua River benzene spill late last year.

As I mentioned, too, SEPA you'll find very sensitive concerning the mission creep among other agencies that SEPA perceives as eroding its regulatory responsibility. So, where SEPA is involved in peer review of another agency's environmental rulemaking, you'll often find that SEPA, at least politically, will often be one of the agencies that is very critical of that rulemaking. And we can talk about that rulemaking process in the Q&A period if needed. But, bottom line is that there is peer agency review of these rulemakings and, often, that can create significant delays in the rulemaking process.

Then, we have the National Development And Reform Commission. Just basically, the takeaway from this is it is the agency with responsibility for reform. You see that "R" in the acronym. Therefore, having the ability to influence greatly reorganization reform of agencies, other agencies tend to give it quite a lot of deference.

Next slide, we'll take a quick look at the Administration for Quality, Supervision, Inspection and Quarantine. This very long title, but a very - also a very influential agency. Among other things it's the gatekeeper for the promulgation, typically jointly with other agencies like SEPA, of Chinese national standards. We all have dealt with the Chinese standards. We'll talk about those later. It's also responsible for certification and accreditation so, if we're being certified as compliant, certified for a particular activity in China, often they are involved. They are also the port inspector. So, these are the folks that

often create issues for us as in-house counsel, where we're trying to get product into China and they are inspecting it for consistency with Chinese law and standards. Just a note that they're an increasingly significant player in the environmental sector.

We also include the Ministry of Health here. Typically they're more focused on, of course, the health and safety side of the equation. However, were there environmental health effects associated with spills, et cetera, they often get involved. They're also responsible for significant amount of the standards related to the toxicity classification, that kind of thing.

And then, just to make things complicated, on slide 24, we have also seen recent years the increasing involvement of the following agencies in environmental regulatory issues, including the Ministry of Information industry, which for the electronics folks on the phone, you may know is the lead agency for China's restriction of hazardous substances, or RHS regulation. The Ministry of Commerce, the Ministry of Land and Resources, the Ministry of Agriculture, the Ministry of Science and Technology and the Ministry of Communications, which is essentially China's Department of Transportation.

I'd also add here the Ministry of Finance, which can get involved in things such as green procurement, such as the development of a system to govern the application of recycling fees. Often, when you deal with financial issues such as that, you will also see the Ministry of Finance get involved in the rulemaking process.

And with all of that, I think some of the key takeaways from this is that lawmaking processes exist in China, but influences on these processes are difficult to determine with any

accuracy. However, trying to understand them can often help us in predicting some of the trajectories of the environmental law and policymaking in China.

Lawmaking is a multi-organization process so, whenever you're looking at advocacy, when you're looking at things that are affecting the company, remember to map out which agencies are involved. Each will bring to that rulemaking, and also to the interpretation of that regulation once it's in effect, their own slant. Sometimes it is helpful, for example, when we're dealing with the Ministry of Health, to know that they are involved, one, two, that they're going to be among the most conservative where health protections are - exist and, if the Ministry of Commerce is involved, to understand as well that they're going to have a more industry-sensitive viewpoint, and bring that - and be able to bring that to bear on the process.

Three, government stakeholders carry more weight in the process than private sector stakeholders. We always have to understand that in China, and that will not change any time soon. The public officials, as (Hongjun) can attest, in China do not see themselves as civil servants. Where they have meetings with your staff in China often, or even you, they often see that as a favor to you, and you have to understand this in terms of why, for example, you can't get a meeting till the last minute, why things like this are so challenging. That whole sense of public service is only now starting to develop in China as it pertains to private - the private sector.

Lawmaking process also may provide official opportunity for stakeholder, meaning - including our company input, but this opportunity is not certain. This is something, again, that we need to underscore. For example, with many lawmaking processes, a good example

is the recent labor contract law, which was put out for public comment. There may be these public comment opportunities, but then it will go back inside the box, so to speak, and they will change the law, but they won't necessarily put it out again, like they do here, so that you can see what happened with your comments. That may or may not happen.

Again, we're looking at the dire need for an administrative procedure act that deals with notice and comment. That is underway, but it's been, again, another initiative long in the coming, and something that, again, we can only hope for soon.

And lastly, just another takeaway is that earlier intervention in the lawmaking process is always best where company advocacy is concern. This again highlights the importance of the government affairs function in China and how that might be able to link with our - the legal function because, obviously, in China, particularly given the challenges to stakeholder input, if you can intervene early or before a rulemaking is issued, for example, or even early in the process of the rulemaking, it's easier to address changes in that rulemaking.

Some of this is obvious, but I think that, with many of our companies, the government affairs function is now starting to evolve in China, and it just highlights how that will be increasingly important in China in years to come.

We wanted to run through now probably one of the more important areas to discuss today, some of the key issues we see for corporate counsel arising from the Chinese environmental legal system, and I think that these are broadly applicable. You know, we didn't write this just to be - of course, everything has an environmental example, but I think generally in China these issues will be the same.

First is navigating national and local government relationships. We wanted to talk about that. That is often a hot button issue, how to deal with ambiguous legal provisions, three, a related issue, agency interpretations. Often with ambiguous legal provisions, you need to rely on agency interpretation. Nomenclature, what are all these different documents? How do you address this? Accessing the law. We're all lawyers, typically, or work with lawyers. Accessing the law is one of the primary functions to understanding the nature of an issue and addressing it, some issues related to that in China.

And then, keeping up with a very dynamic legal system. Obviously, if they've issued over 1,000 EHS-related legal measures, including interpretations last year, how do you keep up with that dynamic legal system?

First issue again being the whole issue of national-local government relationships. Important just to set some baselines. In the Chinese legal system, all legal norms are established via national laws. In other words, that's the baseline. Local authorities can set up legal requirements based on these principles. They can even enact, and some may be able to comment more stringent measures, just like in the U.S. But, the national government sets up the baseline.

Local authorities are also important. However, to understand their role in the system, because an increasing number of approvals under various legal measures are issues, or subject to approval or approval recommendations from local authorities. In other words, under a lot of the newer laws we see, local authorities are giving, just like states in the U.S., more leeway to approve projects, to approve different applications, et cetera, set up under national

laws, or they're the ones the government - local governments are the ones that submit their approval recommendations or disapproval recommendations to the national government for action.

And this creates a very - one, it sets up a system whereby, often, there is a tension that's created because of this between the national and local governments, particularly where the local governments do not correctly interpret the local law, or choose to ignore the local law, and that's one of the things we want to talk about because it often sets up a very hair-graying and complicated situation for in-house counsel.

For instance, looking at slide 29, it's not unusual for local government authorities to claim interpretive authority for national environmental laws, or to implement such laws in a fashion inconsistent from the text of national law. Just a note here, national government authorities typically do not delegate their authority to interpret national laws. In fact, if you look in standards, most of the standards you look at, and a lot of the key legal documents you'll look at will include a provision, often near the end, that indicates the official interpretive authority.

For example, if it indicates the State Environmental Protection Administration or it indicates the State Administration for Work Safety, that means they are the national - they are the official interpretive authority unless there's clear indication that they've delegated. Often, if you find that some other government authority, some other lower level government authority is interpreting that law, waiving a particular provision, et cetera, there is an issue there, and you need to deal with it on a risk management - in terms of risk management for the company.

It's impotent for headquarters to coordinate with their China-based teams. The protocol for engaging with the Chinese government just because of this, to do it up in advance, for example, is often much easier than doing it when an issue like this arises. This kind of planning can avoid situations in which the company is put in a situation where China-based teams must decide between undermining their relationships with the local government officials, and these are often the folks that they deal with day to day. For example, they're the people that come, knock on the door, kick the tires at the plant, et cetera, and between fulfilling corporate compliance commitments.

Often, of course, we need to fulfill our corporate compliance commitments, but putting the China teams in that situation can often create some havoc and intense stress between the headquarters and the field, so to speak.

A hypothetical situation here would be where the local government approves completion of a mid-level environmental impact assessment. There are three levels in China, one being where the minimal environmental impacts, and there's a mid-level form, and then the most detailed one being an EIA statement. If the local government approves completion of this mid-level form, for example, on the project, and you find, and there's a law dictating what level must be prepared for what kind of project, and you find that that law - your own team finds that that law requires the most detailed level of EIA, or others find this, that puts you in a situation where the local - you know, are you faced with going to the local government and saying, "Well, your interpretation of the law is wrong." That can often be a very awkward situation.

We also find that as well with Chinese judicial authorities who often are unfamiliar with environmental issues, and where counsel may be put in an uncomfortable situation to explain to them what the law is. Recent tensions, we must say, between the national and local authorities have made this even more critical an issue. This Songhua River benzene spill that we mentioned November of last year intensified national government scrutiny of local government implementation of environmental law.

So, you may find in a situation, though it's not the company that's an enforcement target because of this wrongful interpretation or waiver by the local government of national law. However, the national government may come in at some time later and choose to rectify situations incorrectly approved by the local government and, as a result, you have significant business interruptions to deal with.

Some statistics to consider. Pre-November 2005 when the benzene spill occurred on the Songhua River, SEPA officials commented that local government reports to SEPA numbered about 15. In other words, these were reports from the local governments required under law of spills, releases into the environment. Post-Songhua River spill, these reports numbered approximately 140. So, you see the local governments are taking this fairly seriously. However, they're also - in other words, like a hot potato, moving this quickly to SEPA, to let SEPA address this. So, things are - the national government is playing a far more prominent role in this kind of local issue.

One of the things that we'll talk about in this sense and how to deal with it is often that what you do if you go into a situation in China, often as multinationals, where we say, you know, we communicate clearly with the local government up front that, as a policy, we're a

big corporation or well-known corporation in China. It is part of our standard policy to let SEPA, the national authorities - you can just - it can be ambiguously worded - as the national authorities know what we're doing. They always give you the option to let the national authorities know in these kind of situations and advise the local authorities that you will do so so you're not put in this awkward situation of having to challenge the local authority after the fact, after they've apparently misinterpreted or ignored a key provision of the law.

Moving quickly to ambiguous legal provisions, legal documents, again as we mentioned, are generally much shorter in China. The implementing measures are often not promulgated together with the enabling statute. Indeed, they're often issued in phases at generally random intervals, and this is in part a result of the lawmaking culture in China, which favors leaving as much interpretive discretion as possible to the regulatory authorities.

This leaves us with a significant challenge. We of course favor written confirmation of a particular interpretation, but are often left with, for example, consultant or other third-party opinions on how the law in question should be interpreted. We'd much prefer to have the agency, for example, say, "This situation here is our confirmation of the definition of activity, and you are in or outside of that activity." Of course, you'd want to know where that opinion would be going before you ask for it, but we wanted to show that that generally is not something that's easily obtained in China.

Moving to the next slide, you'll see that agencies are generally reluctant to provide written interpretation. In most cases, interpretations from a national agency are in the format of a response to questions from the agency's local counterparts. In other words, the (Nanjing)

Environmental Protection Bureau questioned SEPA on the definition of pesticide product in the national law. SEPA then responds, or the Ministry of Agriculture responds, provides that interpretation.

We are, however, seeing occasionally requests for interpretation from companies. This is often something, however, that SEPA doesn't - and other agencies don't respond as quickly to, or even respond at all to. So, often we find where it is absolutely necessary and important to get such interpretation that we work with our local government counterparts to get the question sent upstairs.

Another approach where it is just impossible to get this kind of information is to take a verbal discussion with an agency official, fold that into a response letter, meaning a thank-you letter, and generally record that conversation for both the agency, sending it to the agency and confirming the receipt, and also recording it in your own file.

I would also note, however, that, particularly among some of the agencies like SEPA, the State Environmental Protection Administration, they are starting to compile these interpretive letters. So, that tradition is continuing, and we hope it can only expand to include the private sector more and more.

I'm moving now, for time purposes, to slide 35, for folks on the phone. If you'll move with me, that would be great, and the issue I would like to address here is that some things to note when you're looking for more written guidance from the Chinese authorities. One is that, if the issue in question is a subject of U.S. government advocacy that you know of, the agency is very likely to be reluctant to commit to a particular interpretation in writing. In

fact, in general, if there is U.S. government or other government engagement in this area, often that is quite an issue.

(Jackie), if you could, could you move it to slide 35? Thank you. Regardless, obtaining written interpretations from government authorities will involve significant advocacy efforts, as I mentioned. Going through the local government to do so is one option. Another is, again, recording the discussions in - with the interpretive authorities in a letter, thanking the authorities for their verbal guidance. It will all depend on how critical this is. And again, another reason for the whole issue of getting written interpretation as being a significant advocacy exercise is because you really want to be able to predict the outcome before you get the interpretation so that there are no unpleasant surprises, of course.

Next slide, please. We wanted to touch upon some of the nomenclature because that can often be very confusing. You'll see things out there like circulars, management methods, opinions, provisional measures, several opinions on. Often, this is described - this is a confusing array of names. There is a law, or actually a series of laws, that sets forth what certain kinds of laws should be called.

However, as with a lot of things in China, that gets lost in translation, even in Chinese, and the agencies go about naming these things as they wish. The key is, from the document name itself, for example circular, it is difficult to determine whether the requirements set forth in document of mandatory-voluntary. You need to really dig into the relationship among the various legal documents.

Often you'll look at an area of law, for example be it, let's say, hazardous waste. You need to look at the key documents in the area to determine the key documents, and then review them to identify their inter-relationships. In the hazardous waste characterization area, it would be, for example, the national catalog of hazardous waste, but then you'll see that that also refers internally to the Hazardous Waste Identification standards, and you'll need to review those, as well, to understand how that regime works.

And often, as noted earlier, for ambiguous provisions, then you'll need to reach out to the authorities perhaps to put a sharp edge on some of the ambiguous terms within the laws. Next slide, please.

Important issue for us all, as I mentioned, accessing the law. I mentioned earlier that we'd touch upon this but, historically, Chinese laws have been treated as government secrets. In fact, under the government secrets law, this has been one of the greatest challenges to accessing law in China, particularly draft laws. Still, even though they will often not do it, there remains sensitivity among government agencies with making informational laws widely available. Not long ago I remember a situation where I asked my friend at State Environmental Protection Administration to mail me a standard because I had to have a - participate in a meeting in the U.S. and I didn't have time to wait to go over and get it from him at SEPA. He sent it to me in the mail, and the Postal Administration returned it, telling my colleague at SEPA that it was unlawful to send Chinese laws overseas.

Now, things have changes slightly, and you can get laws mailed to you, typically, particularly if they're on less sensitive issues like environmental law. But, it's important to understand

that this sensitivity exists, particularly when we're dealing with draft laws because our colleagues sometimes can be very aggressive. You know, they want to get a draft law.

However, understand that there is an issue, particularly where it's not a law - a draft law that the Chinese agency has, at its own initiative, issued for the public. There can be some sensitivity, and we need to understand this, if that company representative then comments on that law or refers to that law or disseminates it broadly in terms of the Chinese government perhaps taking action based on the government secrets law. All of this is disconcerting, I know, but, hopefully, the situation is changing, particularly among, thankfully, agencies like the State Environmental Protection Administration.

Other baseline things to understand, there's no comprehensive gazette of environmental laws available now and, despite WTO (excession) agreements, there's still significant issues with their understanding what constitutes a law affecting international trade and, therefore, subject to WTO notification requirements. For folks that monitor the TBT Committee notifications, you'll note there are a lot of standards notified, but, if you really understand how many environmental laws are issued every month, you'll note that very few, if any of those, are notified to the WTO even though we would understand to affect - affecting our trade concerns.

And then, of course, laws are generally not translated into foreign languages. We'll talk about some exceptions. Next slide, please.

And also, we'll talk about some options for helping you access a lot of the key materials. Some things I would note, you should have your folks in China make regular visits to agency

publication or bookstores. Most law standards are not readily available to the Internet, but they are readily available in these bookstores if you go routinely. Again, because they often go out of print and the Chinese government has not yet reacted with printing more or less, it tends to just be an assumption of how many they need, they're published, and then, if they're out, they're out.

So, routinely visiting not only the bookstores but also the agency websites can be a good procedure to put in place if it is not already, websites particularly because we're seeing more and more agencies publish draft rulemakings on their Chinese websites. And I provide the SEPA, English and Chinese website access on this slide 39 - slide 40, and slide 41 for your view. Next slide, please.

Also give you on this slide 39 a book, a compilation that was published - yes, go ahead.

(Bruce Clafter): (Tad)?

(Tad Ferris): Yes?

(Bruce Clafter): Yes, this is Bruce. We're running out of time here. I did want to get a couple of questions in.

(Tad Ferris): Sure.

(Bruce Clafter): Could you sum up, perhaps?

(Tad Ferris): Yes, we'll sum up. Just one second.

(Bruce Clafter): OK.

(Tad Ferris): So, folks, on the next couple of slides can see some - we've presented some resources for folks to look at to find compilations of Chinese law in Chinese and in English. And then, just wrapping up, one thing to highlight in terms of trends shaping the future, on slide 43, if you can jump right now to slide 43, the European Union is particularly influential in China right now. That's why you'll see a lot of rulemakings that are mirroring, at least at the outset, although not in the actual requirements, for example the European RHS directive, the Energy Using Product directive, the REACH proposal, other things being extremely influential in China right now.

This is in part a characteristic of China wanting to look at foreign influence but, as one lawmaker put it, "Writing the law to reflect Chinese characters, literally and figuratively." And then also, in terms of their enforcement approach with the - with laws, we're seeing increasingly a guilty until proven innocent approach whereby, regardless of your past history, good, bad, et cetera, the authorities insist on certification of compliance approaches that require that all go through this certification approval, again regardless of whether you've had previous infringements.

And we see that, for example, with the evolving RHS regime in China, Restriction of Hazardous Substances regime in China, and then also in terms of developing characteristics, they are looking at a ground water - soil and ground water contamination remediation

approach now but, having to twist that to fit the Chinese model perhaps not inappropriately because of their understanding of the weaknesses of China's judicial system.

So, with that, future issues for safety and health, we'll leave to further discussion. You can review those slides.

(Bruce Clafter): Thank you very much. When you catch your breath for one second, (Tad) and (Hongjun) have graciously agreed to take any questions offline that you don't get answered on today's call. We're going to run over a few minutes and take some questions but, if you can't stay on the line, pull up their bios and feel free to send them an e-mail directly, and they'll do their best to respond to you. Remember, again, we have an evaluation that's posted here on the right side. Please click into that, take just a couple moments to fill it out and get it back to us.

So, let me pose a couple of quick questions for both of you. The first one was, "You talked about enforcement trends in China. Are there statutory minimum and maximum penalties or fines," in other words a schedule of some kind, like we have here in the States?

(Hongjun Zhang): Yes. You can, in each relations, normally a particular law they set up the minimum and the maximum penalty. But, generally, the mandatory penalty level is pretty low, so many ((inaudible)) prefer to even pay the penalty rather than run or ((inaudible)) area ((inaudible)) facility. For example, if you (related) a pollution permit, the penalty - I don't have the number in front of me, but there is - it's a relatively low number, but that they do have a minimum and a maximum of each set up in the Chinese law.

(Bruce Clafter): A question relating to corporate issues. One of the listeners asked whether or not environmental indemnities are typically used in merger and acquisition transactions, and are they typically enforceable.

(Tad Ferris): Hi, this is (Tad). I'll take the first part and let (Hongjun) take the enforceable part since he was on that - he was one of the enforcement officers.

We are - can folks hear me, because it's breaking up? (Bruce), can you hear me?

(Bruce Clafter): Yes, I can. Keep going.

(Tad Ferris): OK. We're seeing increased use of indemnities, warranties, indemnifications in merger and acquisition agreements in China. It will often depend on the sophistication of course of the parties involved in this. We've seen heavy resistance, for example, with regard to where one of the parties is a state-owned enterprise. Often that is just their different level of sophistication with regard to this, particularly understanding that China is moving toward the historical ground - soil and ground water contamination liability regime.

It is easier for us as U.S. counsel to understand, from our own experience, what that might mean and why it is important to get these things into an agreement up front. It is harder for many of the Chinese parties to understand since they're not used to provisions that address future laws. In other words, there's nothing really on the books now, but, knowing what we do, that this is definitely coming down the pike. That often puts us in a more challenging situation. But, we are seeing them put into the agreements more often. And (Hongjun) can talk a little bit about the enforcement before we move on.

(Hongjun Zhang): We understand such issue are largely ((inaudible)) ground water, the soil conservation issue. Actually, in China there were no much long - there's no long history regarding enforcement of such issue. Actually, in China ((inaudible)) a national law address this issue. However, multinational companies and also the local EPB, Environmental Protection Authorities, often advise for merger and acquisition purpose, you know, that some pre-agreement should be set up in order to reduce future dispute. The ((inaudible)) authority and the Arbitration Authority, we talk with them not for - it's a case basis, but for their general opinion. They are indicated they will respect - any future dispute happened, they will respect the agreement between parties and ((inaudible)) parties as long as the agreement among the parties are legal.

So, with that in mind, we would like to say, even though - by now we don't have much experience ((inaudible)), have much experience regarding the enforcement of agreement among the parties. However, we will generally say that these are something enforceable, or at least will be - get respect.

(Tad Ferris): And this is (Tad). Just - if I could just add one thing, one thing we've seen is where the party, particularly the Chinese party, is more resistant to adding these provisions, often engaging the local authorities, particularly if you're in a more developed area. We see this - you know, typically we as companies invest, build in economic and development zones or areas that are moving towards more foreign investment, or - and get the local authorities to also, particularly environmental authorities, safety authorities, depending on the issue, to also encourage this kind of fore-thinking. It often helps the Chinese parties agree to something more - that we're more comfortable with, as well.

(Bruce Clafter): A somewhat related issue, you talked before about the various influences on Chinese law. To the extent the U.S. law has been emulated, would you say that there are particular aspects of U.S. environmental law that have explicitly been rejected by the Chinese?

(Tad Ferris): That's a very interesting question. I'll let - (Hongjun's) been in contact almost day to day with law-drafting authorities. Typically, I'll just only say before I hand it to him, that typically, where there is a resistance to U.S. law approaches, it's more for political reasons, meaning they're already - they're just withdrawing their support of it because of sensitivity over, for example, a recent human rights report, et cetera.

But, it's not to say that the European Union is the only influence. U.S. still remains influential. We've seen that from the recent SEPA administrator visit. However, often we sometimes undermine that influence by, you know, there's just no funding for the initiative. You'll see that the recent agreement between the U.S. and China had a lot of caveats in it and, again, that is a signal that everything's contingent on funding. We've seen, conversely, a huge amount of funding being available from the European Commission, and that often helps grease the wheels, so to speak, in terms of Chinese review of different initiatives. We've also seen the Europeans placing agency (fissiles), (seconding) them, as it were, to the Chinese agencies, and that obviously is a great influence, as well.

Hongjun, anything that the Chinese have rejected from the U.S. specifically?

(Hongjun Zhang): We don't see much, you know, rejection regarding the influence. We - a basic situation is a European have ((inaudible)) influence to the China environmental legal system, particularly in the recent years, according - that the judgment from the Chinese authority, basically they've seen more new initiative from Europe rather than they've seen new initiative from the U.S. This is something different with just about five or six years ago. Previously they learn more and they see more from Chinese - from American experience. The early experience on the environmental legal regime, for example, you know, want impact assessment, for example ((inaudible)) the permit system, they largely borrow from U.S. rather than European. The situation just shift a little bit in the last five, six years.

(Bruce Clafter): Another question had to do with the role of the judiciary. Are there any significant interpretations of Chinese environmental laws that are coming out of Chinese courts? Do they really play the kind of role that we see in the United States at all?

(Tad Ferris): Well, I - sure. This is (Tad). And since we - I'll let (Hongjun) speak to if there's anything recent. We did see on the safety and health side significant interpretation with regard to child labor. But, mostly it was the supreme judicial - people's court basically playing the function of emphasizing how important compliance with this area of law was rather than actually providing for the clarity. But, I'll let (Hongjun) talk about the environmental side in the courts.

(Hongjun Zhang): In ((inaudible)) years there were - there was some interpretations from Chinese ((inaudible)) court regarding how environmental law should apply, and such and such. But, one notice - one note that we want to make is the case - China is not a case law system. Basically, the case decided by ((inaudible)) or whatever called, is not part of law. So, they

are very influential for the future decisions, but the local - but, the lower level court is not necessary to - how to follow is the previous case.

When we talk about interpretation, that means occasionally Chinese court, particularly (Supreme) Court, do issues and document which is not part of a case but, rather than interpretation, to direct the local court how a particular provisions of a law should be apply in the court decision. So, that decision is part of law. However, the case law is not.

(Bruce Clafter): A little more specific question is, "Does Chinese environmental law recognize the concept of joint and several liability, which we commonly see in multi-party sites here in the United States?"

(Hongjun Zhang): We haven't seen much case on the joint and the several responsibility, but China do have a so-called very broad principle called ((inaudible)), and that ((inaudible)) be often referred in the court decisions and the agency decisions. They determine basically, you know, where or how some responsibility for the pollution in whatever case, and then if technically it's capable to determine which party to have which responsibility. The court will generally decide in this way.

When we involve certain agreement among the parties regarding the future potential liability, they generally in their ((inaudible)) agreement cite - have the principle in this way by saying, you know, whoever contribute something, whoever will be responsible. So, they, technically ((inaudible)) then could be challenging.

(Bruce Clafter): Great. I think we've pretty much run out of time here. I wanted to mention one other thing to those of you who are still on the call. Holland & Knight is the sponsor of our national environmental committee this year, and we're going to be working with them very closely. To the extent you want them to address some other subjects later in the year, please put that on your evaluation form or send a quick e-mail to (Vince Gonzales), who's on our website. he's the national chairman this year. And we can arrange for (Tad) or (Hongjun) or one of their partners to be on one of our monthly conference calls and address those questions.

Again, you can direct specific questions to either of them at their e-mail addresses, which are in their biographies. You can print out all of the slides in PDF form and take a look at those. They did not cover all the materials. You might find something in there you'd like to ask them about.

So, we thank you very much for your participation today. Again, if you could fill out the evaluations, we'd be most thankful. And enjoy the rest of the day. Thanks.

(Tad Ferris): Thanks, everyone.

(Hongjun Zhang): Thank you.

(Bruce Clafter): Thanks, (Tad), (Hongjun).

(Tad Ferris): Thanks, (Bruce). Talk to you soon.

(Bruce Clafter): All right.

(Hongjun Zhang): ((inaudible))

END