
21. Foreign Investment Laws and Policies in China

Historical views and current issues

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Introduction

The Chinese Government has welcomed and encouraged foreign investment since the reform and opening-up began in 1978. There was a lift in the importance of inward direct foreign investment (DFI) in 1984 with deepening of urban reform, and again from 1992 with stronger commitment to developing an internationally oriented market economy. Foreign investment has played a significant role in China's economic growth and also to its overall social development. Foreign investment laws in China have been gradually improved along with the progressively deeper reform which has provided a legal environment that is better able to attract foreign investment. The development of foreign investment in China is closely related to and results from changes in foreign investment laws and policies. The amount of realised foreign capital coming into China since 1983 illustrates this correlation (Figure 21.1). Before 1992, the amount of realised foreign capital in China was small. After 1992 the amount increased significantly, as the Chinese Government accelerated movement to a market economy and sought to provide an efficient legal environment for foreign investment. Since then, the amount of realised foreign capital coming into China has increased substantially.

This chapter provides a comprehensive overview of China's foreign investment laws and policies, in three sections. The first section briefly introduces the basic framework of China's foreign investment laws and policies. The second reviews the historical developments of China's foreign investment laws and policies, providing a context for the past few decades. The third discusses the current issues China's foreign investment laws and policies are facing.

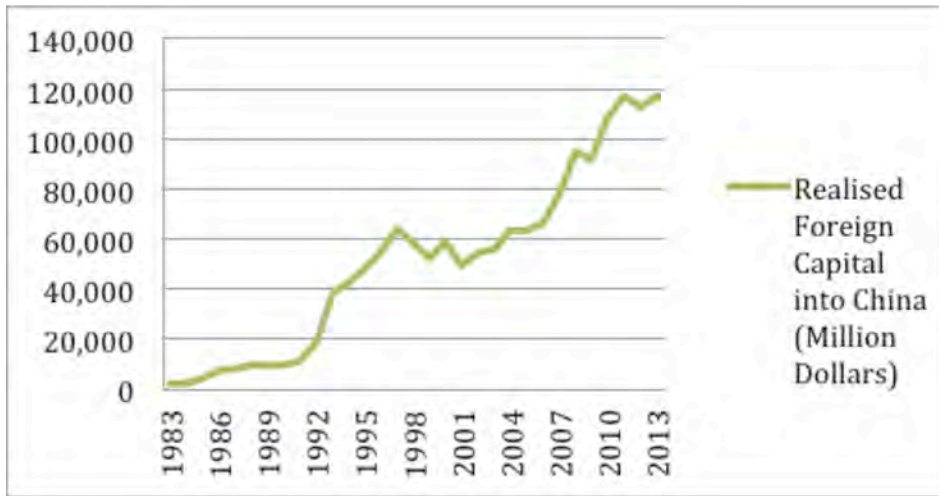


Figure 21.1 Realised Foreign Capital Coming into China, 1983–2013

Sources: NBS (2013); MOFCOM (2014).

Basic framework of China's foreign investment laws and policies

Within China's centrally planned economy before reform and opening-up, the number of foreign investments was small, and there was no body of laws or policy on foreign investment.¹ The framework of China's foreign investment laws and policies has been gradually built since 1978.

¹ For example, Provisions on the Establishment of Schools by Charitable Donations by Overseas Chinese (promulgated on 2 August 1957; expired); Consolidated Industrial and Commercial Tax Regulations of the People's Republic of China [Draft] (promulgated on 14 September 1958; expired).

Legislation

The first foreign investment law in China was the Law of the People's Republic of China on Chinese-Foreign Equity Joint Ventures (hereinafter 'Law of Equity Joint Ventures') promulgated in 1979.² Since then, the Chinese Government sequentially promulgated the Law of the People's Republic of China on Foreign-Capital Enterprises (hereinafter 'Law of Foreign-Capital Enterprises'), in 1986,³ and the Law of the People's Republic of China on Chinese-Foreign Contractual Joint Ventures (hereinafter 'Law of Contractual Joint Ventures'), in 1988.⁴ These three laws are collectively referred to as the 'Three Investment Laws' regulating foreign investment in China. To ensure the implementation of the Three Investment Laws, the State Council promulgated three regulations or rules: Regulations for the Implementation of the Law of the People's Republic of China on Chinese-Foreign Equity Joint Ventures (hereinafter 'Regulations of Equity Joint Ventures') in 1983,⁵ Rules for the Implementation of the Law of the People's Republic of China on Foreign-Capital Enterprises (hereinafter 'Rules of Foreign-Capital Enterprises') in 1990,⁶ and Rules for the Implementation of the Law of the People's Republic of China on Chinese-foreign Contractual Joint Ventures (herein after 'Rules of Contractual Joint Ventures') in 1995⁷ (collectively referred to as the 'Regulations of the Three Investment Laws'). The Three Investment Laws and the Regulations of the Three Investment Laws constitute the basic framework of Chinese foreign investment laws.

Article 18 of the Company Law of the People's Republic of China (1993)⁸ (hereinafter '1993 Company Law ') stipulated that it 'shall apply to limited liability companies with foreign investment. Where laws concerning Chinese-foreign equity joint ventures, Chinese-foreign contractual joint ventures and foreign-funded enterprises provide otherwise, such provision shall prevail.' This article specified the basic principle that foreign-invested companies must follow: there are special laws beyond the general laws applied to domestic

2 Law of the People's Republic of China on Chinese-Foreign Equity Joint Ventures (promulgated on 8 July 1979; amended on 4 April 1990 and 15 March 2001).

3 Law of the People's Republic of China on Foreign-Capital Enterprises (promulgated on 12 April 1986; amended on 31 October 2000).

4 Law of the People's Republic of China on Chinese-Foreign Contractual Joint Ventures (promulgated on 13 April 1988; amended on 31 October 2000).

5 Regulations for the Implementation of the Law of the People's Republic of China on Chinese-Foreign Equity Joint Ventures (promulgated 20 September 1983; revised on 15 January 1986, 21 December 1987, 22 July 2001 and 19 February 2014).

6 Rules for the Implementation of the Law of the People's Republic of China on Foreign-Capital Enterprises (promulgated on 21 December 1990; revised on 12 April 2001 and 19 February 2014).

7 Rules for the Implementation of the Law of the People's Republic of China on Chinese-Foreign Contractual Joint Ventures (promulgated on 4 September 1995, revised on 19 February 2014).

8 Company Law of the People's Republic of China (promulgated on 29 December 1993; amended on 25 December 1999 and 28 August 2004; revised on 27 October 2005; and amended on 28 December 2013).

companies. This principle still stands. The 1993 Company Law was amended in 1999 and again in 2004, but Article 18 stood untouched. The 2005 Revision of the Company Law (hereinafter '2005 Company Law') revised Article 18 by including the foreign-investment companies, both limited liability companies and corporation owned by shareholders. Article 218 prescribed that the 2005 Company Law 'shall be applicable to foreign-invested companies with limited liability and such companies limited by shares; and where laws on foreign investments provide otherwise, the provisions there shall be applicable'. Article 218 of the 2005 Company Law remained the same after its 2013 amendment.

In addition, China has also developed a large number of implementation regulations on foreign investment.⁹ These regulations, together with the Three Investment Laws, the Regulations of the Three Investment Laws and, most recently, the 2005 Company Law (2013 amendment), provide a relatively complete legal environment for foreign investment practice in China.

Guiding catalogues

The Three Investment Laws and Regulations of the Three Investment Laws provide guidance on the areas and industries in which foreigners may invest.¹⁰ In 1995, in order to provide further guidance for foreign investment and to ensure foreign investments are consistent with China's national economic and social development plans, the State Council and its responsible departments promulgated the Interim Provisions on Guiding Foreign Investment Direction (hereinafter 'Interim Provisions on Guiding Direction'). These provisions—for the first time—outlined in law 'encouraged, restricted and prohibited' industries for foreign investment (see Chinese Investment and Development

9 For example, Measures for Strategic Investment by Foreign Investors upon Listed Companies (promulgated on 31 December 2005); Measures for the Administration of Foreign-Capital Lease Industry (promulgated on 3 February 2005); Provisions on Mergers and Acquisitions of Domestic Enterprises by Foreign Investors (promulgated on 8 August 2006).

10 Article 3 of the Regulations of Equity Joint Ventures (promulgated 20 September 1983; revised on 15 January 1986, 21 December 1987, 22 July 2001 and 19 February 2014) stipulates that the main industries in which Chinese-foreign equity joint ventures are permitted to be established are energy development, machine manufacturing, electronics and computer industries, light industry, agriculture, tourism and service trades. Article 3 of the Law of Foreign-Capital Enterprises (promulgated on 12 April 1986; amended on 31 October 2000) stipulates, in principle, that foreign-capital enterprises shall be established to help the development of China's national economy, shall use advanced technology and equipment or market all or most of their products outside China. In addition, it also authorises the State Council to make regulations regarding this direction. Therefore, according to this authorisation, Articles 4 and 5 of the Rules of Foreign-Capital Enterprises (promulgated on 21 December 1990; revised on 12 April 2001 and 19 February 2014) outline industries that are prohibited and restricted. The prohibited industries are the press, publishing, broadcasting, television, movies, and so on; and the restricted industries are public utilities, communications and transportation, trust investment, and so on. Article 4 of the Law of Contractual Joint Ventures stipulates, in principle, that the establishment of productive contractual joint ventures that are export-oriented or technologically advanced is encouraged.

1995(7):52). The interim provisions provided that a ‘Guiding Catalogue for Foreign Investment Industries’ (hereinafter ‘Guiding Catalogue’) would be used to review and approve foreign investment applications.¹¹

On 11 February 2002, the State Council promulgated the Provisions on Guiding Foreign Investment Direction (hereinafter ‘Provisions on Guiding Direction’), which went into effect on 1 April 2002; the Interim Provisions on Guiding Direction ceased to be effective on the same day.¹² The Provisions on Guiding Direction provide that the Guiding Catalogue and the Catalogue of Priority Industries for Foreign Investment in the Central-Western Region (hereinafter ‘Central-Western Region Catalogue’) are to serve as the basic policies for reviewing, evaluating and approving foreign investment projects and enterprises.¹³

The Guiding Catalogue is a nationwide directory for foreign investments. It sets up three categories of industries—encouraged, restricted and prohibited. Those not included in the catalogue fall into a default fourth category: ‘permitted’ industries,¹⁴ which allow foreign investors to participate according to the principles of the market economy. The Guiding Catalogue, since its publication in 1995, has been revised five times, in 1997, 2002, 2004, 2007 and most recently in 2011.

The Central-Western Region Catalogue was first published in 2000 for the implementation of the ‘Western Region Development Strategy’ of the State Council. It was meant to improve the quality of the overall economic development of central and western regions. The industries listed in this catalogue are those that are seen to have significant advantages in each province in terms of environment, natural resources, human resources, production, technology, markets, and so on, and that may enjoy preferential policies as industries that are encouraged for foreign-investment.¹⁵ The Central-Western Region Catalogue has been revised three times—in 2004, 2008 and most recently in 2013.

Policies

The Twelfth Five-Year Plan 2011-15 regulates matters relating to foreign investment in China. It reiterates that China will continue to advance and deepen its opening-up policy, and affirms the strategic objectives of ‘bringing in’ and ‘going out’. Part XII of the Twelfth Five-Year Plan points out that:

11 Interim Provisions on Guiding Foreign Investment Direction (promulgated on 20 June 1995; expired), Art. 3.2.

12 Provisions on Guiding Foreign Investment Direction (promulgated on 11 February 2002), Art. 17.

13 *Ibid.*, Art. 3.2.

14 *Ibid.*, Art. 4; Interim Provisions on Guiding Direction (promulgated on 20 June 1995; expired), Art. 4.

15 See Provisions on Guiding Direction (promulgated on 11 February 2002), Art. 11.

[I]n order to sit well with the new situation of China's opening up—to equally steer imports, exports, and inbound and outbound investments—the Chinese Government must actively employ a more proactive opening up strategy, constantly explore new areas and places to open up, expand and deepen the convergence of interests for all parties, improve the mechanism to better adapt to the development of an open economy, and effectively prevent risks, so as to promote development, reform and innovation by opening up.¹⁶

The Decision concerning Deepening Reforms at the third Plenum of the 18th Party congress in 2013 provides additional guidance on matters of foreign investment. It indicates that China will further promote economic reform and opening-up, reduce the limitations on foreign investment in China, promote the unification of laws regarding foreign and domestic investors, expand the opening-up of financial sectors and interior borders, accelerate the negotiation and signature of free-trade agreements and the construction of free-trade zones. These principles send a positive signal to foreign investors aiming to invest in China.

Historical development of China's foreign investment laws and policies

Geographical areas expanded

The geographical areas permitting foreign investment have been expanded progressively (see State Council 2006; State Council Information Office 2008). After 1979, China first established four special economic zones: Shenzhen, Zhuhai, Shantou and Xiamen. In 1984, China further allowed foreign investment in 14 coastal cities. Also in 1984, China established the first group of 14 national economic and technological development zones. Then in 1988, the Chinese Government approved Shandong Peninsula and Liaodong Peninsula as coastal economic development zones and approved the establishment of Hainan Special Economic Zone. In 1990, the Chinese Government opened Shanghai's Pudong District to foreign investors. In 1992, it further opened five riverside cities, four provincial capital cities in border and coastal regions and 11 inland provincial capital cities, expanding the open areas from coastal to inland provinces. Since accession to the World Trade Organisation (WTO) in 2001, China has further expanded areas in which foreign investment is allowed; now the areas are 'broadened from limited areas to all-around areas; from a trial opening

16 See <http://www.gov.cn/2011lh/content_1825838_13.htm>.

led by government policies, into a foreseeable opening on a legal basis; from a self-unilateral opening into a mutual opening up among WTO members' (State Council Information Office 2008).

Investment field broadened

1) Guiding Catalogue

There were three categories outlined in the Guiding Catalogue in 1995: encouraged (A), restricted (B) and prohibited. No preferential policies are referred to in this catalogue, but relevant preferential treatments are still given in accordance with the previously promulgated and implemented laws and regulations.¹⁷ By comparing industries under each category with the amendments thereafter, it is clear that the authorities have gradually reduced restrictions on foreign investment.

The Guiding Catalogue published in 1997 added 15 industries to the 'encouraged' category (see Table 21.1). In 2002, in order to fulfil its WTO commitments, the Chinese Government for the second time revised the Guiding Catalogue. Seventy-five industries were added to the 'encouraged' category and 36 industries were removed from the 'restricted' category. There were two significant changes in this revision. First, an appendix was introduced to specify the organisational forms and equity ratios. Second, the division of the 'restricted' category into two types, A and B was abolished. In 2004, the catalogue was amended for the third time. Some industries were removed from the 'encouraged' list, including scrap-steel processing and aluminium production with a capacity of 300 000 t and over per annum. In 2007, the catalogue was amended for the fourth time. There was further opening-up in the services sectors, encouragement of foreign investment enterprises in the recycling and renewable energy industries and environmental protection, and the promotion of comprehensive utilisation of resources. In addition, the separate appendix to the Guiding Catalogue was integrated into each specific industry. By 2011, 10 years after China's accession to the WTO, the catalogue was amended for the fifth time to further expand the opening-up process. For example, financial leases and medical institutions were moved from the 'restricted' into the 'encouraged' category; 11 areas that had been subject to equity ratio limitations for foreign investment were removed.¹⁸

17 For example, product-for-export enterprises and technologically advanced enterprises could receive a reduction of or exemption from the site-use fees (except for those located in busy urban sectors of large cities) and enterprise income tax, and could receive a conditional refund of the total amount of enterprise income tax. Provisions of the State Council for the Encouragement of Foreign Investment (promulgated on 11 October 1986), Art. 4, 8–10.

18 See 'Interpretation of the Latest Catalogue for the Guidance of Foreign Investment Industries by the Development and Reform Commission and Other Departments' (<http://news.xinhuanet.com/fortune/2011-12/29/c_111334458.htm>).

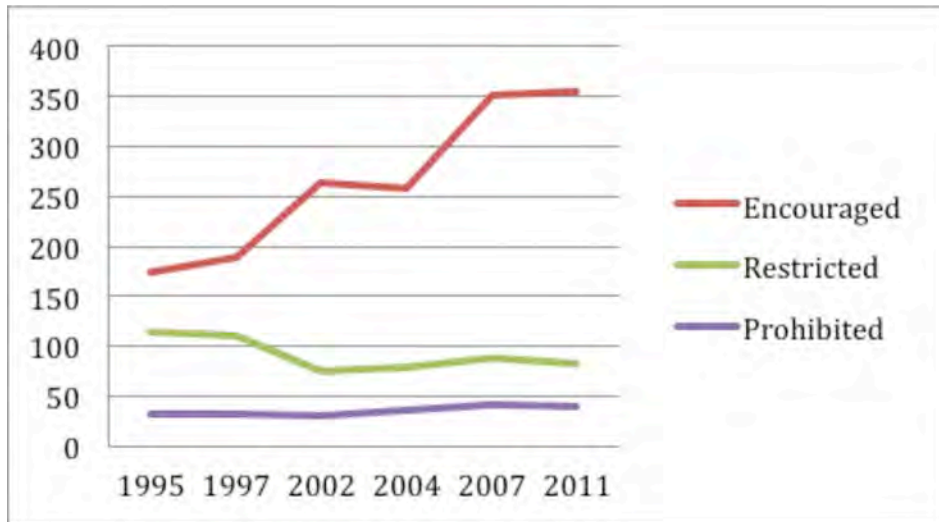


Figure 21.2 Numbers of Industries in Each Version of the Guiding Catalogue

Note: The authors analysed the data according to each version of the Guiding Catalogue since 1995. For more details, see Table 21.1.

Table 21.1 and Figure 21.2 compare the changes to industries with the previous Guiding Catalogue in the encouraged, restricted and prohibited categories. The comparison demonstrates that restricted industries are tending to be reduced and encouraged industries tending to increase. This suggests a trend towards encouraging foreign investment in China.

Table 21.1 Numbers of Industries in Each Version of the Guiding Catalogue

Version	Total	Encouraged	Restricted (A)	Restricted (B)	Subtotal of Restricted	Prohibited
1995	317	172	38	76	114	31
1997	329	187	25	86	111	31
2002	366	262	-	-	75	29
2004	370	257	-	-	78	35
2007	478	351	-	-	87	40
2011	476	354	-	-	83	39

Sources: Guiding Catalogues, published in 1995, 1997, 2002, 2004, 2007 and 2011.

2) Central-Western Region Catalogue

In June 2000, in order to implement the Western Development Strategy, the Chinese Government released the Central-Western Region Catalogue. This catalogue, together with the Guiding Catalogue, has since become the guide for directing and approving foreign investment projects and foreign invested

enterprises. The industries in the Central-Western Region Catalogue are chosen according to the peculiarities of each province; some of the industries also include restrictions on management or equity share ratios.

The Central-Western Region Catalogue is organised by region. In the catalogue published in 2000, the 'Central-Western region' refers to the following provinces and areas: Shanxi, Inner Mongolia Autonomous Region, Jilin, Heilongjiang, Anhui, Jiangxi, Henan, Hubei, Hunan, Guangxi Zhuang Autonomous Region, Chongqing Municipality, Sichuan, Guizhou, Yunnan, Tibet Autonomous Region, Shaanxi, Gansu, Ningxia Autonomous Region, Qinghai, and Xinjiang Uygur Autonomous Region. In 2005, the State Council released Opinions of the General Office of the State Council on Promoting the Opening-Up of the Old Industrial Base in Northeast China, which stipulated that by the end of the transitional period of China's entry into the WTO, Liaoning Province would be added into the Central-Western Region Catalogue, rather than listing it under the Catalogue of Priority Industries for Foreign Investment in Liaoning Province. In 2009, the State Council released Several Opinions of the State Council on Promoting the Construction and Development of the Hainan International Tourism Island, which further broadened the Central-Western region by adding Hainan Province. Therefore, there are 22 regions in the current Central-Western Region Catalogue published in 2013.

Each amendment to the Central-Western Region Catalogue is accompanied by the addition of a certain number of industries; some of the newly added industries are even available for the entire Central-Western region. One key feature of the amendments is that the number of encouraged industries has increased. For example, in the Central-Western Region Catalogue published in 2000, there were only 256 industries; however, the number went up to 268 in 2005, then to 412 in 2008. The number is now 500—almost double the number in 2000. Another key feature of the amendments is that the 'encouraged' category has broadened gradually, with some of the newly added industries available for the entire region. For example, according to the Central-Western Region Catalogue published in 2004, road transportation of passengers, and construction and business operation of urban gas supply, heat supply, water supply and drainage systems were added to the original list. According to the 2008 catalogue, value-added telecommunication¹⁹ was added. According to the 2013 catalogue, nursing homes were added. In addition, wholly foreign-owned investments are encouraged in medical institutions in all of the 22 Central-

¹⁹ Subject to China's WTO commitments.

Western regions in the 2013 catalogue, compared with seven regions and limited forms of Chinese-foreign equity joint ventures and Chinese-foreign contractual joint ventures in 2008.²⁰

Organisational forms increased

The types of business that foreign investors could invest in have gradually expanded in successive laws and regulations. Currently, the types of business permitted include but are not limited to: Chinese-foreign equity joint ventures; foreign-capital enterprises; Chinese-foreign contractual joint ventures; branches of foreign companies; companies limited by shares with foreign investment; investment companies by foreign investment; and foreign-funded partnership enterprises. In addition, foreign investors may invest in China by way of mergers and acquisitions.

Three types of business are listed in the Three Investment Laws and the Regulations of the Three Investment Laws: Chinese-foreign equity joint ventures; foreign-capital enterprises; and Chinese-foreign contractual joint ventures. Chinese-foreign equity joint ventures are limited-liability companies incorporated in China by foreign joint ventures (such as foreign companies, enterprises, other economic organisations or individuals) and Chinese joint ventures (such as Chinese companies, enterprises or other economic organisations), according to relevant Chinese laws.²¹ Foreign-capital enterprises are limited-liability companies or other forms established in China exclusively by foreign investors (such as foreign enterprises, other foreign economic organisations and individuals), according to relevant Chinese laws.²² Chinese-foreign contractual joint ventures are limited-liability companies or other forms established in China jointly by foreign parties (such as foreign enterprises and other economic organisations or individuals) and Chinese parties (such as Chinese enterprises or other economic organisations) and operated under their joint-venture contracts, according to relevant Chinese laws.²³ These three types of business are different from each other in organisational form, legal status, distribution of profits and loss, and operation and management model, (see Table 21.2).

20 The authors analysed the data according to each version of the Central-Western Region Catalogue since 2000.

21 Law of Equity Joint Ventures (promulgated on 8 July 1979; amended on 4 April 1990 and 15 March 2001), Art. 1, 4.1.

22 Law of Foreign-Capital Enterprises (promulgated on 12 April 1986; amended on 31 October 2000), Art. 1–2; Rules of Foreign-Capital Enterprises (promulgated on 21 December 1990; revised on 12 April 2001 and 19 February 2014), Art. 18.

23 Law of Contractual Joint Ventures (promulgated on 13 April 1988; amended on 31 October 2000), Art. 1–2; Rules of Contractual Joint Ventures (promulgated on 4 September 1995, revised on 19 February 2014), Art. 14.

Table 21.2 Comparison of Three Types of Foreign Investment Vehicles

	Chinese-foreign equity joint ventures	Chinese-foreign contractual joint ventures	Foreign-capital enterprises
Key regulations	Law of Equity Joint Ventures; Regulations of Equity Joint Ventures	Law of Contractual Joint Ventures; Rules of Contractual Joint Ventures	Law of Foreign-Capital Enterprises; Rules of Foreign-Capital Enterprises
Contributor(s)	Foreign companies, enterprises, other economic organisations or individuals, together with Chinese companies, enterprises or other economic organisations	Foreign enterprises and other economic organisations or individuals, together with Chinese enterprises or other economic organisations	Foreign enterprises, other foreign economic organisations and individuals
Proportion of foreign investor's investment	Not less than 25 per cent of its registered capital	According to the joint-venture contract	100 per cent
Transfer of rights	Consent of the other party; the other party has a pre-emptive right if transferred to a third party	Written consent of the other party	—
Distribution of profits, risks and losses	In proportion to their contributions to the registered capital	According to the joint-venture contract	—
Organisational form(s)	Limited-liability company	Limited-liability company or other forms	Limited-liability company or other forms (if approved)
Legal status	Legal persons	Legal persons if meet relevant conditions	Legal persons if meet relevant conditions
Nationalisation or requisition of assets	Nationalisation: no Requisition: no, subject to special circumstances and compensation	—	Nationalisation: no Requisition: no, subject to special circumstances and compensation
Examination and approval authorities	State's competent department in charge of foreign economic relations and trade	Department in charge of foreign economic relations and trade under the State Council or department or local government authorised by the State Council	Department under the State Council in charge of foreign economic relations and trade, or an institution authorised by the State Council
Review period (from the application received date)	Within three months	Within 45 days	Within 90 days
Operation and management	Board of directors	Board of directors or a joint managerial institution	In accordance with the approved article of association
Duration of entity	Through agreement by the parties (with approval); could be extended	Through agreement by the parties (with approval); could be extended	Foreign investor's report (with approval); could be extended

Sources: Law of Equity Joint Ventures 2001; Regulations of Equity Joint Ventures 2014; Law of Contractual Joint Ventures 2000; Rules of Contractual Joint Ventures 2014; Law of Foreign-Capital Enterprises 2000; Rules of Foreign-Capital Enterprises 2014.

As early as the 1993 Company Law, the Chinese Government had allowed foreign companies to establish a branch in China. A branch is not a legal person, but a division of a foreign company (which is a company registered and incorporated outside China in accordance with foreign laws).²⁴

In 1995, the Ministry of Foreign Trade and Economic Cooperation (MOFTEC)²⁵ issued the Provisional Regulations of the Ministry of Foreign Trade and Economic Cooperation on Certain Issues Concerning the Establishment of Companies Limited by Shares with Foreign Investment, which allowed foreign investment to take the form of companies limited by shares. These are companies established in China by foreign and Chinese shareholders in accordance with these provisional regulations, and which bear their liabilities with their total assets. The capital stock of such companies is made up of equal value shares by all the shareholders, and the foreign shareholders may purchase and hold more than 25 per cent of the company's total registered capital, which is raised by means of promotion or public offer.²⁶ Following the implementation of these provisional regulations, the Ministry of Commerce (MOFCOM) promulgated more notices or circulars in order to regulate matters such as the approval of such companies' establishment or alteration, the applications to issue A shares and B shares, and so on.²⁷

In 1995, MOFTEC also promulgated the Interim Provisions concerning the Establishment of Investment Companies by Foreign Investment, which allowed foreign investors to establish investment companies. Investment companies by foreign investment are limited-liability companies established exclusively by foreign investors or jointly by foreign and Chinese investors, for the purpose of direct investment. The registered capital of such companies should exceed RMB30 million.²⁸ In 2003, MOFCOM promulgated the Provisions on the

24 Company Law (promulgated on 29 December 1993; amended on 25 December 1999 and 28 August 2004; revised on 27 October 2005; and amended on 28 December 2013), Art. 199, 203.

25 The Ministry of Foreign Trade and Economic Cooperation was merged into the Ministry of Commerce in 2003.

26 Provisional Regulations of the Ministry of Foreign Trade and Economic Cooperation on Certain Issues concerning the Establishment of Companies Limited by Shares with Foreign Investment (promulgated on 10 January 1995), Art. 2, 5, 7.

27 Circular of the General Office of Ministry of Foreign Trade and Economic Cooperation on Relevant Issues of Joint Stock Companies with Foreign Investment (promulgated on 17 May 2001); Notice of the Ministry of Commerce on the Relevant Issues concerning the Conversion of Unlisted Foreign Capital Shares of Foreign-Funded Joint Stock Limited Companies into Tradable B-Shares (promulgated on 30 July 2008); Notice of the Ministry of Commerce on the Decentralisation of Approval on the Alteration of Foreign-Funded Joint-Stock Companies and Enterprises (promulgated on 5 August 2008).

28 Interim Provisions Concerning the Establishment of Investment Companies by Foreign Investors (promulgated on 4 April 1995), Art. 1, 3.

Establishment of Investment Companies by Foreign Investors,²⁹ which replaced the previously issued series of interpretations, notices and supplementary provisions concerning investment companies by foreign investment.³⁰

In 2009, the State Council promulgated the Measures for the Administration on the Establishment of Partnership Business by Foreign Enterprises or Individuals in China, which allow foreign investors (with foreign companies and foreign individuals included) to join established Chinese partnerships, or to jointly set up partnerships with other foreign investors, Chinese companies or Chinese individuals in China.³¹ In 2010, the State Administration for Industry and Commerce (SAIC) issued the Administrative Provisions on the Registration of Foreign-Funded Partnership Enterprises, amended in 2014, which regulates the establishment, modification and cancellation of foreign-funded partnerships.

In addition to the establishment of these forms of foreign investment, the Chinese Government also allowed foreign investors to invest in China by way of business restructuring, mergers and acquisitions. In 1998, the State Economic and Trade Commission (SETC) issued the Interim Provisions on State-Owned Enterprises' Utilising of Foreign Investment for Reshuffling, which allows state-owned enterprises (SOEs) to utilise foreign direct investment to acquire other domestic enterprises, to complement self-owned floating assets and to reimburse enterprise debts.³² In 2002, the China Securities Regulatory Commission, Ministry of Finance (MOF) and SETC jointly released Issues Related to Transferring State-Owned Shares and Institutional Shares of Listed Corporations to Foreign Investors (expired), which allows the transfer of state-owned shares and institutional shares of listed companies to foreign investors, subject to the requirements of the Guiding Catalogue.³³ In the same year, SETC, MOF, SAIC and the State Administration of Foreign Exchange jointly issued the Interim Provisions on Introducing Foreign Investment to Reorganise State-Owned Enterprises, which allows the introduction of foreign investment to 'reorganise state-owned enterprises and corporate enterprises with state-owned equities (financial enterprises and listed corporations are excluded) or turn them

29 Provisions on the Establishment of Investment Companies by Foreign Investors (promulgated on 10 June 2003; revised on 13 February 2004 and 17 November 2004). This regulation had been revised twice. Supplementary Provisions on the Establishment of Investment Companies by Foreign Investors (promulgated on 26 May 2006) were issued.

30 For example, Supplementary Provisions on the Interim Provisions Concerning the Establishment of Investment Companies by Foreign Investors (promulgated on 24 August 1999, expired); Second Supplementary Provisions on the Interim Provisions Concerning the Establishment of Investment Companies by Foreign Investors (promulgated on 31 May 2001, expired).

31 Measures for the Administration on the Establishment of Partnership Business by Foreign Enterprises or Individuals in China (promulgated on 25 November 2009), Art. 1–2, 12.

32 Interim Provisions on State-Owned Enterprises' Utilising Foreign Investment for Reshuffling 1998 (promulgated on 14 September 1998), Art. 2.

33 Issues Related to Transferring State-Owned Shares and Institutional Shares of Listed Corporations to Foreign Investors 2002 (promulgated on 1 November 2002; expired), Art. 2.

into corporations with foreign investment'.³⁴ Specifically, foreign investment could be introduced to reorganise SOEs into foreign-invested enterprises by transferring equity to foreign investors, increasing shares, and selling all or major assets of the SOE to foreign investors.³⁵

In 2003, MOFTEC and four other ministries issued the Interim Provisions on Mergers and Acquisitions of Domestic Enterprises by Foreign Investors, which were revised by the MOFCOM in 2006 by issuing the Provisions on Mergers and Acquisitions of Domestic Enterprises by Foreign Investors (hereinafter 'Provisions on M&A by Foreign Investors').³⁶ In 2009, in order to ensure the Interim Provisions on Mergers and Acquisitions of Domestic Enterprises by Foreign Investors sat well with the Anti-Monopoly Law of the People's Republic of China and the Provisions of the State Council on Standards for Declaration of Concentration of Business Operators, the Provisions on M&A by Foreign Investors were amended by MOFCOM.

Approval process improved

The Three Investment Laws are essential in regulating the review of foreign investment in China. Before these laws, local approval measures were the main source of regulations, but they were scattered and inconsistent.³⁷ After the introduction of the Three Investment Laws, foreign investment review processes in China have been unified and standardised.

The review and approval of foreign investment in China can be classified into two categories: approval before establishment and approval after establishment. Approval before establishment mainly refers to the article of association and/or agreement approval by MOFCOM, the provincial commerce department and local departments authorised by the State Council. Approval after establishment refers to the approval of such matters as major or substantial changes, equity transfer contracts and corporate liquidation.

34 Provisions on Introducing Foreign Investment to Reorganise State-Owned Enterprises (promulgated on 8 November 2002), Art. 2.

35 Ibid, Art. 3.

36 Provisions on Mergers and Acquisitions of Domestic Enterprises by Foreign Investors (promulgated on 8 August 2006; revised on 22 June 2009).

37 For example, Implementing Measures for the Regulations of Shanghai Municipality on Discussion and Examination and Approval Procedures of the Establishment of Chinese-Foreign Equity Joint Ventures and Foreign Enterprises (promulgated on 1 July 1984; expired).

According to the Three Investment Laws, review and approval of foreign investment in China is the responsibility of MOFCOM, the provincial commerce departments and the local authorities authorised by the State Council.³⁸ In recent years, MOFCOM has issued a series of regulations to gradually decentralise and allow lower-level departments to make decisions on foreign investment.³⁹ Now it reviews and approves only some foreign investment applications. The latest decentralisation was in 2010, referred to as the Notice of the Ministry of Commerce on Decentralising the Examination and Approval Power for Foreign Investment. According to the notice, the approval authorities are diversified according to the categories in the Guiding Catalogue and the value of investment capital involved.⁴⁰

Super-national treatment phased out

In the early years of economic reform and opening-up, in order to attract foreign investment, the Chinese Government gave foreign-invested entities specified super-national treatments regarding taxation and land use. After 1994, the Chinese Government began unifying the taxation system regarding domestic-invested and foreign-invested entities. By enriching implementation regulations and rules,⁴¹ the Government gradually unified different taxation categories: value-added tax, consumption tax, business tax, and urban and township land-use tax. On 1 December 2010, the super-national treatment for foreign investment, in terms of preferential taxation treatment ended with the unification of the urban maintenance and construction taxes and educational surcharges.

38 See Law of Foreign-Capital Enterprises (promulgated on 12 April 1986; amended on 31 October 2000), Art. 6; Law of Contractual Joint Ventures (promulgated on 13 April 1988; amended on 31 October 2000), Art. 5; Law of Equity Joint Ventures (promulgated on 8 July 1979; amended on 4 April 1990 and 15 March 2001), Art. 3.

39 For example, Notice of the Ministry of Commerce on the Decentralisation of Approval on the Alteration of Foreign-Funded Joint-Stock Companies and Enterprises (promulgated on 5 August 2008); Notice of the Ministry of Commerce on Further Simplifying and Regulating the Foreign Investment Administrative Licensing Issues (promulgated on 26 August 2008); Notice of the Ministry of Commerce on Decentralising the Examination and Approval Power for Foreign Investment (promulgated on 10 June 2010).

40 Notice of the Ministry of Commerce on Decentralising the Examination and Approval Power for Foreign Investment (promulgated on 10 June 2010), Art. 1–6.

41 The main unification of the taxation regime happened between 2006 and 2010. For example: 1) Decision of the Standing Committee of the National People's Congress concerning the Application of Interim Regulations on Such Taxes as Value-Added Tax, Consumption Tax and Business Tax to Enterprises with Foreign Investment and Foreign Enterprises (promulgated on 29 December 1993); 2) Enterprise Income Tax Law of the People's Republic of China (promulgated on 16 March 2007); 3) Notice of the State Council on Extending the Urban Maintenance and Construction Tax and Educational Surcharges from Chinese to Foreign-Funded Enterprises and Citizens (promulgated on 18 October 2010).

Sub-national treatment reduced

Before China's accession to the WTO, the Chinese Government also applied some sub-national treatments to foreign-invested entities, alongside major super-national treatments. For example, higher requirements on capital and local content were imposed on foreign-invested entities. The former required that the capital of foreign investment by shares should be higher than the required amount specified in the Company Law;⁴² and the latter required the foreign-invested entities to give first priority to purchasing material (such as required raw and processed material, fuel, parts and auxiliary equipment) in China.⁴³ After China's accession to the WTO, the aforementioned provisions were gradually eliminated in order to fulfil China's WTO commitments.

Further reform: China (Shanghai) Pilot Free Trade Zone

After China fully opened economically, it began to explore new ways of deepening the market economy. After the setting up of the Shanghai Waigaoqiao Free Trade Zone in 1990, the State Council approved the establishment of some types of special Customs-supervised bonded zones, such as bonded areas,⁴⁴

42 Article 7 of the Provisional Regulations of the Ministry of Foreign Trade and Economic Cooperation on Certain Issues concerning the Establishment of Companies Limited by Shares with Foreign Investment (promulgated on 10 January 1995) stipulates that '[r]egistered capital of a company shall be the total capital stock recorded with registering departments. The registered capital of a company shall be at least RMB30 million.' According to Article 78.2 of the Company Law 1993, however, '[t]he minimum amount of registered capital of a joint stock company limited shall be RMB10 million. Requirements for the minimum amount of the registered capital of a joint stock company limited to be higher than the above amount are provided for in separate laws or administrative decrees.' After the amendment of the Company Law 2005 in 2013, the registered capital for stock companies limited by shares was cancelled.

43 For example, Law of Foreign-Capital Enterprises (promulgated on 12 April 1986; amended on 31 October 2000), Art. 15; Law of Equity Joint Ventures (promulgated on 8 July 1979; amended on 4 April 1990 and 15 March 2001), Art. 9.2; Law of Contractual Joint Ventures (promulgated on 13 April 1988; amended on 31 October 2000), Art. 9.2.

44 A bonded area refers to special areas in China under the control of the Customs authorities, which are established upon approval by the State Council. The area is isolated, according to the supervision requirements of Customs, from other areas in the territory of the People's Republic of China. See Procedures on Customs Control over Bonded Areas (promulgated on 1 August 1997), Art. 2–3.

export processing zones,⁴⁵ bonded logistics centres,⁴⁶ bonded logistics parks,⁴⁷ bonded port areas⁴⁸ and comprehensive bonded zones.⁴⁹ On 29 September 2013, the China (Shanghai) Pilot Free Trade Zone (PFTZ) came into operation, which marked a milestone in China's economic reform.⁵⁰

PFTZ aims to accumulate experience in the next two to three years in boosting China's reform and opening-up within new legal structures compatible with international trade and investment standards. Pilot programs will be launched in this zone to transform the functions of government, the opening-up of financial services, the reform of the approval process, and the operation of foreign investment review systems. The aims of the PFTZ can be specified in more detail as follows.

45 An export processing zone is a certain area as approved by Customs within the territory of China in which to undertake export processing, which is under close supervision by Customs. See Interim Measures for the Administration of Processing Trade in Export Processing Zones (promulgated on 22 November 2005), Art. 2–3; Interim Measures of the General Administration of Customs of the People's Republic of China for the Supervision over Export Processing Zones (promulgated on 24 May 2000; revised on 2 September 2003), Art. 3–4.

46 Bonded logistics centres could be classified into bonded logistics centres (type A) and bonded logistics centres (type B). The former are places under Customs surveillance as approved by the General Administration of Customs, which are operated by legal enterprises within the territory of China to undertake business operations of bonded warehousing logistics. The latter refers to places under concentrated surveillance as approved by the General Administration of Customs, which are operated by a Chinese domestic enterprise with legal status and where many enterprises enter to undertake the business operations of bonded logistics warehousing. See Interim Measures for the Administration of Bonded Logistics Centres (Type A) by the General Administration of Customs of the People's Republic of China (promulgated on 23 June 2005), Art. 2; Interim Measures for the Administration of Bonded Logistics Centres (Type B) by the Customs of the People's Republic of China (promulgated on 23 June 2005), Art. 2.

47 A bonded logistics park is a special zone under Customs supervision, which is established within the planning areas of a bonded zone or a special port section adjacent to the bonded zone for the development of modern international logistics upon the approval of the State Council. See the People's Republic of China Customs Bonded Logistics Park Management Measures (promulgated on 28 November 2005), Art. 2.

48 A bonded port area is an area under special Customs supervision, which has the functions of a port for logistics, processing and so on, and is established within the port areas opened to the outside by the state and specific areas adjacent upon approval by the State Council. Such areas are isolated from other areas within the Customs territory of the People's Republic of China by checkpoints, fences, video surveillance systems and other facilities that meet the requirements for Customs supervision. See Interim Measures of the Customs of the People's Republic of China for the Administration of Bonded Port Areas (promulgated on 3 September 2007; amended on 15 March 2010), Art. 2, 4.

49 Currently, there is no specific regulation on comprehensive bonded zones. According to the State Council's announcements on the establishment of the Tianjin Binhai Comprehensive Bonded Zones, Beijing Tianzhu Comprehensive Bonded Zones and Haikou Comprehensive Bonded Zones, the functions, tax policies and foreign exchange policies of such zones are subject to the State Council's reply on the establishment of the Yangshan Bonded Port Area. See the State Council's Reply on the Establishment of Tianjin Binhai Comprehensive Bonded Zones (issued on 10 March 2008); the State Council's Reply on the Establishment of Beijing Tianzhu Comprehensive Bonded Zones (issued on 23 July 2008); and the State Council's Reply on the Establishment of Haikou Comprehensive Bonded Zones (issued on 22 December 2008).

50 Pilot Free Trade Zone (<<http://www.shftz.gov.cn/WebViewPublic/NewsPaper.aspx?new=1>>).

1. To explore protocols of cooperation, leading to a one-stop service, integrated review and approval, and efficient operation, and to perfect an information disclosure system with the participation of foreign investors and compatible with international rules.
2. To broaden the opening-up of the service sectors. Special measures will be imposed on 18 service sectors, such as finance, transportation, commerce and trade, professional, cultural and public services. Special measures refer to the suspension or cancellation of restrictions such as requirements concerning the qualification of investors, limitations on foreign participation, restrictions concerning business scope, and so on.
3. To implement a pre-entry national treatment to foreign investors and a 'Negative List' mechanism within PFTZ. For areas that are not in the negative list, foreign and domestic investors will receive the same treatment, by following filing procedures instead of approval requirements (with the exception of areas specifically defined by the State Council), and the Shanghai Municipal People's Government will be in charge of the project filing procedures.
4. To develop shipping-related industries such as shipping finance, international shipping, international ship management, and international ship brokerage, to simplify the application process permitting international shipping and to create a more efficient ship registration system.
5. To enhance the development of financial services by allowing certain foreign-invested financial institutions to incorporate foreign-invested and Chinese-foreign equity joint-venture banks in PFTZ; gradually permitting foreign-incorporated entities to participate in commodity futures trading; supporting equity escrow institutions to establish comprehensive financial platforms in the zone, and encouraging the RMB reinsurance business.
6. To strengthen protection by enhancing the regulatory system, and by terminating or modifying current laws and regulations.
7. To implement preferable policies on income tax, pilot policies of export tax refund for qualified financial leasing businesses and consumption taxes, so as to promote investment.⁵¹

51 Framework Plan for the China (Shanghai) Pilot Free Trade Zone [中国（上海）自由贸易试验区总体方案] (<http://www.shftz.gov.cn/WebViewPublic/item_page.aspx?newsid=635158957941988294&coltype=8>).

Foreign investment laws and policies in China: current issues

The laws and regulations regarding foreign investments in China have been gradually improved, and national treatment of foreign investors is increasing in prevalence. Notwithstanding all the accomplishments, certain issues remain to be resolved.

Cumbersome and inconsistent legislation

Foreign investment in China is regulated by the Three Investment Laws and the Regulations of the Three Investment Laws, together with the Company Law and hundreds of administrative regulations. The Three Investment Laws each cover one type of foreign investment entity, making the legal system very complicated. The complexity is demonstrated in the following ways (Qiu 2013). First, the separate settings of the Three Investment Laws are a waste of legislative resources, as more than half of the regulations are similar to one another and therefore could be combined. In addition, the regulations lack coordination, meaning different types of foreign-invested entities are treated differently (for example, there are different approval periods, and different rules regarding the board of directors). Second, the Three Investment Laws are not sophisticated enough to include many essential provisions, leading to unnecessary delegated agencies and delegated regulations and complexity of regulations, thus making it difficult to thoroughly understand the content of China's foreign investment laws. Third, the numerous local rules trump higher legal authorities, making it essential to understand the local regulations in addition to the statutes and administrative regulations when investing in China. And fourth, certain provisions in the Three Investment Laws are in conflict with the Company Law.

Ambiguous approval criteria

The criteria that can be used to block a foreign investment are ambiguous.⁵² Operationally, it is impossible for foreign investors to predict the results of their proposals under China's foreign investment approval system, which puts them in a difficult situation. For example, Article 9 of the Rules of Contractual Joint Ventures (2014) stipulates that:

⁵² It is, however, normal practice for the criteria to approve foreign investment to be vague. For example, in Australia's *Foreign Acquisitions and Takeovers Act 1975*, 'national interest' is adopted as a criterion; in the United States' *Foreign Investment and National Security Act* of 2007, 'national security' is followed in the review process; and in Canada's *Investment Canada Act 1985*, 'national security' is used as a criterion.

Under any of the following circumstances, approval will not be granted to an applicant for establishment of a contractual joint venture: (1) Harming state sovereignty or social public interests; (2) Endangering state safety; (3) Causing pollution to the environment; (4) Other circumstances which violate the law, administrative regulations or state industrial policies.

Article 4 of the Regulations of Equity Joint Ventures (2014) similarly stipulates that:

Applications to establish joint ventures shall not be granted approval if the project involves any of the following conditions: (1) detriment to China's sovereignty; (2) violation of the Chinese law; (3) nonconformity with the requirements of the development of China's national economy; (4) environmental pollution; (5) obvious inequity in the agreements, contracts and articles of association signed impairing the rights and interests of one party.

Article 5 of the Rules of Foreign-Capital Enterprises (2014) also stipulates that:

No application for the establishment of a foreign-capital enterprise shall be approved if the proposed enterprise is under any of the following circumstances: (1) injuring China's sovereignty or social and public interests; (2) endangering China's national security; (3) in violation of Chinese laws and regulations; (4) not in keeping with the requirements of China's national economic development; (5) may result in environmental pollution.

Restricted investment industries

Even though the industries opened to foreign investment have been greatly broadened, some industries are still restricted, or even prohibited from foreign investment. According to the latest Guiding Catalogue published in 2011, 83 industries under the restricted category allow foreign investment, subject to certain conditions. For example, foreign investors can invest in the area of exploration and mining of special and scarce coals, but in these activities the Chinese party shall hold the majority of shares. Foreign investors can invest in the development of real estate, but such investment should take the form of equity joint ventures or contractual joint ventures. These conditions have limited the ability of foreign investors control to the invested entity. Thirty nine areas are still prohibited from foreign investors.

Undefined compensation standards in requisition

In the case of requisition of foreign-invested entities, the compensation standard is ambiguous. For example, Article 2.3 of the Law of Equity Joint Ventures (2001) prescribes that '[t]he State shall not nationalize or requisition any equity joint venture. Under special circumstances, when public interests require, equity joint ventures may be requisitioned by following legal procedures and appropriate compensation shall be made.' Similarly, Article 5 of the Law of Foreign-Capital Enterprises (2000) prescribes that '[t]he State does not nationalise or requisition any enterprise with foreign capital. However, under special circumstances when public interests require, enterprises with foreign capital may be requisitioned through legal procedures and appropriate compensation shall be made.' It is clear that Chinese-foreign equity joint ventures and foreign-capital enterprises in China are principally beyond the scope of requisition by the Chinese Government. In some special circumstances, however, when required by the public interest, requisition could be applied, subject to legal procedures and appropriate compensation. The problem is that the standard of appropriate compensation in China is not specified.

Conclusion

Since 1978, economic reform has transformed China from a centrally planned closed system to an open and modern market economy. Chinese foreign investment laws and policies have also gone through steady improvements—from nothing to something, from good to better. Overtime, Chinese foreign investment laws and policies promote an increase in the areas, industries forms in which foreign investment is permitted, and approval processes have been improved towards prevalence of national treatment. Major decisions regarding the reform and opening-up, especially China's decision to establish a socialist market economy and to join the WTO, have played significant roles in the development of China's foreign investment legislation.

China's foreign investment laws now comprise the Three Investment Laws as the basic laws, the Company Law as the general law, supplemented by hundreds of administrative and local regulations. Reform is still needed on coordinating and reducing complexity of foreign investment laws and regulations, reducing ambiguity of foreign investment approval criteria, eliminating restrictions on investment in some industries, and defining compensation standards in the case of requisition. Thus, China still has some distance to travel in order to make its foreign investment laws becoming an integral part of the system of rules of law, which China is endeavouring to establish.

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Appendix Table 21.1 Realised Foreign Capital into China, 1983–2013

Year	Realised foreign capital into China (\$ million)	Year	Realised foreign capital into China (\$ million)	Year	Realised foreign capital into China (\$ million)
1983	2 260	1994	43 213	2005	63 805
1984	2 870	1995	48 133	2006	67 076
1985	4 760	1996	54 805	2007	78 339
1986	7 628	1997	64 408	2008	95 253
1987	8 452	1998	58 557	2009	91 804
1988	10 226	1999	52 659	2010	108 821
1989	10 060	2000	59 356	2011	117 698
1990	10 289	2001	49 672	2012	113 294
1991	11 554	2002	55 011	2013	117 586
1992	19 203	2003	56 140		
1993	38 960	2004	64 072		

Sources: NBS (2013); MOFCOM (2014).

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