Executive Summary

China maintains a more restrictive foreign investment regime than its major trading partners, including the United States. In 2013, the flow of new Chinese direct investment into the United States eclipsed that of the United States into China, according to widely-cited estimates by the Rhodium Group, a leading private consultancy focused on U.S.-China investment. However, the total stock of U.S. investment in China remains significantly higher than the total stock of Chinese investment in the U.S., at US $70 billion compared to just US $17 billion as of the end of 2012, according to the Ministry of Commerce (MOFCOM) China Commerce Yearbook 2012 (the latest year for which China's bilateral data is available). China relies on an investment catalogue to encourage foreign investment in some sectors of the economy, while restricting or prohibiting it in many other industries. China's investment approval regime appears designed to foster economic growth but may also shield inefficient or monopolistic Chinese enterprises from competition, particularly those China is trying to cultivate as market leaders. Foreign investors cite concerns about rising costs, difficulty in finding qualified human resources, and the discretionary authority Chinese regulators have to discriminate against foreign investors, both in the establishment and operational phases.

Over the past year, there were several positive signs that China's new leaders are committed to redefining the State's role in the economy. Xi Jinping, in his first year as State president and head of the Communist Party, has worked to consolidate power and pushed for economic reform to further open the economy to private capital, including international investors in some sectors. Major developments in 2013 include:

- In July, China made a landmark decision to negotiate a high-standard bilateral investment treaty (BIT) with the United States that would be based on the U.S. model BIT approach to national treatment, which covers both the "pre-establishment" and post-establishment phases of investment, and delineates a clear "negative list" of negotiated exceptions.
- In September, China established the Shanghai Pilot Free Trade Zone, partly to test reforms to the investment registration regime and to open previously closed sectors to foreign investment.
- In November 2013, at the Third Plenum meeting of the 18th Party Congress, the Chinese Communist Party unveiled an ambitious reform agenda that directs the authorities to broaden foreign investment access and underscores the leadership's commitment to allow market forces to play a "decisive" role in allocating resources and driving economic growth.

Although the Chinese Communist Party says it expects to "fulfill" the Third Plenum reform agenda by 2020, a detailed reform roadmap and reform timing is lacking for many economic sectors. Foreign investors remain concerned about discriminatory industrial policies, opaque investment approval procedures used to achieve industrial policy goals and a lack of effective administrative and legal recourse if an investment approval is conditioned or denied. Poor enforcement of intellectual property rights (IPR), the forced transfer of technology, and lack of rule of law are additional concerns.

The United States government has raised concerns about China’s investment restrictions and discriminatory policies at high levels, in bilateral fora such as the U.S.-China Joint Commission on Commerce and Trade (JCCT), the U.S.-China Strategic and Economic Dialogue (S&ED) and the U.S.-China Investment Forum. BIT negotiations are an additional opportunity to encourage China’s economic reforms, integrate China into a global rules-based system, and level the playing field for U.S. businesses. The United States Government emphasizes the need for China to open new sectors to foreign investment, increase transparency, and improve the enforcement of existing laws to protect investors’ rights. For China to achieve its ambitious economic growth goals, its investment regime will have to change to permit greater competition across a broader range of sectors.

1. Openness to, and restrictions upon, foreign investment

Attitude Toward FDI

The Chinese government has stated that it welcomes foreign investment. China attracted US $118 billion in worldwide foreign direct investment (FDI) in 2013, second only to the United States. China's sustained high economic growth rate and the expansion of its domestic market help explain its attractiveness as an FDI destination. However, foreign investors often temper their optimism regarding potential investment returns with uncertainty about China's willingness to offer a level playing field vis-à-vis domestic competitors. In addition, foreign investors report a range of challenges related to China's current investment climate. These include industrial policies that protect and promote state-owned and other domestic firms, equity caps and other restrictions on foreign ownership in many industries, weak IPR protection, a lack of transparency, corruption, and an unreliable legal system.

For more information, AmCham China’s 2013 American Business in China White Paper can be found here: http://www.amchamchina.org/whitepaper

FDI Statistics from MOFCOM can be found here:
http://www.fdi.gov.cn/1800000121_10000177_8.html

Other Investment Policy Reviews

Organization for Economic Cooperation and Development (OECD)

China is not a member of the Organization for Economic Cooperation and Development (OECD). The OECD Council decided to establish a country program of dialogue and co-operation with China in October 1995. The most recent OECD Investment Policy Review for China was completed in 2008. The OECD Investment Policy Review noted that the policy changes in China between 2006-2008 tightened restrictions on inward direct investment, including cross-border mergers and acquisitions.

The report can be found here:
http://www.oecd.org/daf/inv/internationalinvestmentagreements/oecdinvestmentpolicyreviews-china2008encouragingresponsiblebusinessconduct.htm

World Trade Organization (WTO)

China became a member of the World Trade Organization (WTO) in 2001. WTO membership boosted China's economic growth and advanced its legal and governmental reforms. The most recent WTO Investment Policy Review for China was completed in 2012. The report states that there were few changes to China's policies on inward foreign investment in the period under review (2010-2011).

The report can be found here:
http://www.wto.org/english/tratop_e/tpr_e/tp364_e.htm

IMF information can be found here:
http://www.imf.org/external/country/Chn/

Laws/Regulations of FDI

Overview

China has a legal and regulatory framework that provides the government with discretion to promote investment in specific regions or industries it wishes to develop, and to restrict foreign investment deemed not to be in its national interest or that might compete with state-sanctioned monopolies or other favored domestic firms. Foreign investors report that many regulations contain undefined key terms and standards, and that regulations are often applied in an inconsistent manner by different regulatory entities and localities. Potential investment restrictions in China are thus much broader than those of many developed countries, including the United States.

The Constitution of the People's Republic of China was adopted by the 5th National People's Congress on December 4, 1982, with several revisions through 2004. China's accession to the WTO spurred significant transformations in various areas of Chinese domestic law. The current Chinese leadership has emphasized the need to strengthen the rule of law in China. Nonetheless, foreign investors have expressed concern that the legal system allows regulators significant discretion to adapt decisions to changing circumstances, which results in an unpredictable business climate and rulings that can appear arbitrary or discriminatory. Generally, unlike the United States, the legal system is designed to serve State and Chinese Communist Party interests, and as such, does not consistently protect individual rights or effectively resolve disputes. The current system is still developing as a venue to address investment and commercial disputes.

FDI laws

Article 18 of the Constitution states that China permits foreign enterprises and other economic organizations or individuals to invest in China. The issuance of the China-Foreign Equity Joint

Venture Enterprise Law in 1979 marked the beginning of the establishment of China's foreign investment legal regime. Since then, China has established a foreign investment legal regime based on three central laws. These are: the China-Foreign Equity Joint Venture Enterprise Law, the China-Foreign Cooperative Joint Venture Enterprise Law, and the Foreign-Invested Enterprise Law.

The administrative regulations and regulatory documents issued by the State Council include, but are not limited to:

- the Implementation Regulations of the China-Foreign Equity Joint Venture Enterprises Law
- the Implementation Regulations of the China-Foreign Cooperative Joint Venture Enterprise Law
- the Implementation Regulations of the Foreign-Invested Enterprise Law
- the State Council Provisions on Encouraging Foreign Investment
- the Provisions on Guiding the Direction of Foreign Investment
- the Administrative Provisions on Foreign Investment to Telecom Enterprises

There are over 1,000 rules and regulatory documents related to foreign investment in China issued by government ministries. They include, but are not limited to:

- the Guiding Catalogue of Foreign Investment Industries
- the Provisions on Mergers & Acquisition of Domestic Enterprises by Foreign Investors
- the Administrative Provisions on Foreign Investment in Road Transportation Industry
- the Interim Provisions on Foreign Investment in Cinemas
- the Administrative Measures on Foreign Investment in Commercial Areas
- the Administrative Measures on Ratification of Foreign Invested Projects
- the Administrative Measures on Foreign Investment in Distribution Enterprises of Books, Newspapers and Periodicals
- the Provision on the Establishment of Investment Companies by Foreign Investors
- the Administrative Measures on Strategic Investment in Listed Companies by Foreign Investors

In addition, local legislatures and governments also enact their own regulations and rules to regulate foreign investments in their areas, in accordance with national laws and policies, including, for example, Wuhan's Administration Regulation on Foreign-Invested Enterprises and Shanghai's Municipal Administration Measures on the Land Usage of Foreign-Invested Enterprises.

Under this foreign investment legal regime, China approves foreign investments on a case-by-case basis following review by multiple government agencies. China claims to provide national treatment after an investment has been established, but not before. Foreign investors may only invest where allowed by laws, regulations, and rules, in specified areas or industries, and are required to obtain ratification for planned investment projects and to establish companies. In some industries, such as the telecommunication industry, foreign investors are also required to obtain approval from relevant industry regulators. Separate approval processes govern land use and other administrative areas. Reviews may overlap, resulting in potentially redundant examinations. Low transparency limits the predictability of outcomes.

A list of Chinese laws and regulations, central and local can be found here:
http://www.gov.cn/zhengce/

FDI Reform Announcements in 2013

In November 2013, following the Third Plenum of the 18th Party Congress, the Chinese Communist Party issued a report which is described by the Chinese leadership as one of the largest and most ambitious economic reform programs since Deng Xiaoping's pioneering market-oriented reforms in 1978. Among other things, the report directs China to broaden foreign investment access in China, to explore the possibility of a model for allowing foreign investment that would provide national treatment at all phases of investment, including market access (i.e., the "pre-establishment" phase of investment), and employ a "negative list" approach in identifying exceptions (meaning that all investments are permitted except for those explicitly excluded), and to set up more free trade zones like the newly-established and still-evolving Shanghai Pilot Free Trade Zone. The report also stated China intends to unify laws and regulations governing foreign and domestic investment. The United States is encouraged by these broad policy pronouncements and will closely monitor China's implementation measures to determine how and to what extent China follows through on them.

An abridged English version of the Third Plenum *Decision on Major Issues Concerning Comprehensively Deepening* Reforms (Third Plenum Decision) can be found here:
http://www.china.org.cn/china/third_plenary_session/2013-11/16/content_30620736.htm

In December 2013, MOFCOM solicited comments on revisions to three basic laws on foreign investment, with a view of unifying domestic and foreign investment regulatory regimes. These revisions could significantly change China's foreign investment management regime by extending national treatment to the market access phase, subject to limited exceptions spelled out in a "negative list." There is no timetable to complete the revision.

Industrial Strategy

Five-Year Plan

China defines its broad economic goals through five-year macro-economic plans. The most significant of these for foreign investors is China's Five-Year Plan (FYP) on Foreign Capital Utilization. *The 12th FYP for Utilization of Overseas Capital and Investment Abroad*, issued by the National Development and Reform Commission (NDRC), promises to guide more foreign direct investment (FDI) to an identified set of strategic and newly emerging industries (SEIs), namely energy efficiency and environmental technologies, next-generation information technology, biotechnology, advanced equipment manufacturing, new energy sector, new materials, and new-energy vehicles, while "strictly" limiting FDI in energy and resource-intensive and environmentally damaging industries; to encourage foreign multinationals to set up regional headquarters and research and development (R&D) centers in China; to encourage foreign investment in production services such as modern logistics, software development, engineering design, vocational skills training, information consulting, technology, and intellectual property (IP) services; to “steadily open up” banking, securities, insurance, telecom, fuel, and logistics industries; to “gradually open up” education and sports; to guide foreign capital to enter healthcare, culture, tourism, and home services; and to encourage foreign capital to enter creative design.

Innovation

A major goal of China's investment policies, stated in the 12th FYP, is to encourage the domestic development of technological innovation and know-how. Investment projects that involve the transfer of technology or the potential for "indigenous innovation" tend to be favorably received by China's investment authorities. China seeks to promote investment in higher value-added sectors, including high technology research and development, advanced manufacturing, clean energy technology, and select modern services sectors. Foreign investors have said they must often weigh China's market potential and its interest in attracting technology against China's inability or unwillingness to protect investors' IP.

Regional growth

China also seeks to spread the benefits of foreign investment beyond its relatively wealthy coastal areas by encouraging foreign companies to establish regional headquarters and operations in Central, Western, and Northeastern China. China publishes and regularly revises a *Catalogue of Priority Industries for Foreign Investment in the Central-Western Regions*, which outlines incentives to attract investment in targeted sectors to those parts of China.

The *Catalogue of Priority Industries for Foreign Investment in the Central-Western Regions* can be found here:
http://www.ndrc.gov.cn/zcfb/zcfbl/201305/W020130516388520815145.pdf

Limits on Foreign Control

Catalogue for the Guidance of Foreign Investment in Industries

China outlines its specific foreign investment objectives primarily through its *Catalogue for the Guidance of Foreign Investment in Industries* (Foreign Investment Catalogue, or Catalogue), most recently revised in December 2011, and maintained by MOFCOM and NDRC. The catalogue delineates sectors of the economy where foreign investment is "encouraged," "restricted," and "prohibited." Investment in sectors not listed in the Catalogue is considered permitted. China "encourages" investment in sectors where it believes it will benefit from foreign assistance or technology. Investment is "restricted" and "prohibited" in sectors that China deems sensitive, that touch on national security, or that do not meet the goals of China's economic development plans.

The English version of the 2011 Foreign Investment Catalogue can be found here:
http://english.mofcom.gov.cn/article/policyrelease/aaa/201203/20120308027837.shtml

Problems with the Catalogue

The Catalogue reflects China's market access restrictions. Contradictions between it and other measures have confused investors and added to the perception that investment guidelines do not provide a secure basis for business planning. Even in “encouraged” and “permitted” sectors, regulations apart from the Catalogue often detail additional restrictions on the specific forms of investment that are allowed. Chinese regulators have maintained the flexibility to ignore the Catalogue’s guidance in some instances, and to restrict or approve foreign investment for reasons other than those specified. The government may also adopt new regulations or establish industrial policies that supersede the most recently published edition of the Catalogue. Uncertainty as to which industries are being promoted and how long such designations will be valid undermines confidence in the stability and predictability of the investment climate.

Equity Caps

In addition to dividing industries into “encouraged,” “restricted,” and “prohibited” categories, the Catalogue may also require that investment take certain forms (such as a domestic-foreign equity joint venture) and/or that the foreign shareholder’s proportion of investment in the enterprise be limited to a minority share. Agency-specific regulations may also require that investment take certain forms. For example:

- In the oil and natural gas exploration and development industry, foreign investment is required to take the form of equity joint ventures and cooperative joint ventures.

- In the accounting and auditing sectors, foreign investment is required to take the form of cooperative joint ventures and partnerships.

- In the distribution of audio-visual products, foreign investment is only permitted in the form of cooperative joint ventures.

- In some sectors, the Chinese partners individually or as a group maintain control of the enterprise; for example, construction and operation of civilian airports, construction and operation of nuclear power plants, establishment and operation of cinemas, and the design and manufacture of civil-use satellites.

- In some sectors, the foreign shareholder’s proportion of the investment may not exceed a certain percentage. For example, foreign stakes are limited to:

    - 50% in value-added telecom services
    - 49% in basic telecom enterprises
    - 50% in life insurance firms
    - 49% in security investment fund management companies

Mandatory IP/technology transfer requirements

Mandatory joint venture structures and equity caps give Chinese partner firms significant control, often allowing them to benefit from technology transfer. In addition, the relative opacity of the approval process and the broad discretion granted to the authorities foster an environment where government authorities can impose deal-specific conditions beyond written legal requirements, often with the intent to force technology transfer as a condition of market access or to support industrial policies and the interests of local competitors.

Privatization Program

Early indications following China's November 2013 Third Plenum reform pronouncements suggest China will attempt to sell shares in state-owned enterprises (SOEs) to outside investors, improve SOE management structures, emphasize the importance of SOEs meeting financial goals, and take steps to bring private capital into some sectors traditionally monopolized by SOEs, such as energy, telecoms, and finance. Practically, the government must still work out how to implement its SOE reform vision, but a recent move to restructure a major state-owned conglomerate, Citic Group, by listing its assets in Hong Kong, where it will be subject to greater transparency rules and heightened regulatory scrutiny, suggests a possible mechanism to improve SOE corporate governance and transparency. The government also committed at the Third Plenum to raise the portion of earnings that SOEs pay out as dividends to the public budget, although here, too, the pace and method of implementation remains uncertain.

Screening of FDI

Overview

As mentioned, foreign investors are required to obtain approvals for their investment projects and to establish an enterprise. In some industries, such as telecommunications, foreign investors are also required to get approval from industry regulators.

Catalogue of Investment Projects subject to Government Ratification

In July 2004, the State Council issued its *Decision on Investment Regime Reform* and the *Catalogue of Investment Projects subject to Government Ratification*. According to the *Catalogue of Investment Projects subject to Government Ratification*, all proposed foreign investment projects in China must be submitted for "review and ratification" byNDRC or provincial or local Development and Reform Commissions, depending on the sector and value of the investment. In October 2004, the NDRC issued *Interim Measures for the Administration of Examining and Ratifying Foreign Investment Projects* to guide the ratification of foreign investment projects. NDRC's approval process includes assessing the project's compliance with China's laws and regulations, its national security implications, and its economic development ramifications. In some cases, NDRC also solicits the opinions of relevant Chinese industrial regulators and "consulting agencies," which may include industry associations that represent domestic firms. The State Council may also weigh in for high-value projects in "restricted" sectors.

In December 2013, China released a revised Catalogue of Investment Projects subject to Government Ratification, which narrows the scope of foreign investment projects subject to NDRC ratification and no longer requires approval for every foreign investment project. According to the revised *Catalogue of Investment Project subject to Government Ratification*, NDRC ratification only applies to projects over $300 million for the "encouraged" category of the Foreign Investment Catalogue or projects and over $50 million for investments into "restricted" categories in the Foreign Investment Catalogue. Provincial governments can ratify real estate projects in the "restricted" category of the Foreign Investment Catalogue and other projects in this category below $50 million. Local governments can ratify projects in the "encouraged" category under $300 million. Any other foreign-invested project not listed in the *Catalogue of Investment Projects subject to Government Ratification* no longer requires ratification, and instead only requires "filing-for-record" with local governments. This is significant progress. When announcing the reforms, NDRC stated that the latest revision was conducted in accordance with the principles of "pre-establishment" market access and a "negative list"-based approach, and estimated the number of projects requiring approval by the central authorities would decrease by 60%.

The *Catalogue of Investment Projects subject to Government Ratification* can be found here: http://www.gov.cn/zwgk/2013-12/13/content_2547379.htm

Approvals

Based on the three foreign investment laws, once NDRC approves the foreign investment project, foreign investors must apply to MOFCOM for approval to legally establish a company. Next, foreign investors apply for a business license from the State Administration of Industry and Commerce (SAIC), which allows the firm to operate. Once a license is obtained, the investor registers with China's tax and foreign exchange agencies. Greenfield investment projects must also seek approval from China's Environmental Protection Ministry and its Ministry of Land Resources. The actual implementation of China's foreign investment approvals process may vary in specific cases, depending on the details of a particular investment proposal and local rules and practices.

The U.S. Chamber of Commerce's report on *China's Approval Process for Inbound Foreign Direct Investment can be found here*:
http://www.uschamber.com/sites/default/files/reports/020021_China_InvestmentPaper_hires.pdf

MOFCOM revision plans

In December 2013, MOFCOM initiated a process to revise China's three main laws governing foreign investment. One of the goals of its revisions is to update China's laws to reflect a system whereby some foreign investments require approval, while others merely require filing for record.

Anti-monopoly review and the national security review

MOFCOM conducts anti-monopoly and/or national security reviews of proposed mergers or acquisitions of domestic enterprises by foreign investors. The anti-monopoly review is detailed in the section further below, on Competition Law. Article 31 of China's Anti-monopoly Law (AML) also notes that if a merger or acquisition of a domestic enterprise by a foreign investor poses national security concerns, a separate national security review is also required. MOFCOM's *Rules on Mergers and Acquisitions of Domestic Enterprises by Foreign Investment Article 12* stipulates that parties are required to report a transaction to MOFCOM if:

- foreign investors obtain actual control, via merger or acquisition, of a domestic enterprise in a key industry;

- the merger or acquisition affects or may affect national economic security;

- the merger or acquisition would cause the transfer of actual control of a domestic enterprise with a famous trademark or a Chinese time-honored brand.

If MOFCOM determines that the parties did not report a merger or acquisition that affects or could affect national economic security, MOFCOM, together with other government agencies, may require the parties to terminate the transaction or adopt other measures to eliminate the impact on national economic security.

In February 2011, China released the *State Council Notice Regarding the Establishment of a Security Review Mechanism for Foreign Investors Acquiring Domestic Enterprises*. The notice established an interagency Joint Conference, led by NDRC and MOFCOM, and with the authority to block foreign mergers and acquisitions of domestic firms that it believes may impact national security. The Joint Conference is instructed to consider not just national defense security but also national economic security and basic social order implications when reviewing transactions.

Local commerce departments are responsible for screening whether relevant transactions require a national security review when they examine transactions under China's foreign investment approval process. Some provincial and municipal departments of commerce previously posted on the Internet a Security Review Industry Table listing non-defense industries where transactions may trigger a national security review, but MOFCOM has declined to confirm whether these lists reflect official policy. In addition, third parties such as other governmental agencies, industry associations, and companies in the same industry can seek MOFCOM's review of transactions. Investors may also voluntarily file for a national security review.

Competition Law

Competition Policy, Laws, and Regulations

China has many laws and regulations that concentrate production in certain sectors into monopolies, near-monopolies, or authorized oligopolies. These measures are concentrated in capital intensive sectors, like electricity and transportation, or in industries such as fixed-line telephony and postal services, in which this approach may be used to ensure national coverage. Examples of such laws and regulations include the Law on Electricity (1996), Civil Aviation Law (1995), Regulations on Telecommunication (2000), Postal Law (1986), Railroad Law (1991), and Commercial Bank Law (amended in 2003), among others.

Anti-monopoly Law

China's Anti-monopoly Law took effect in August 2008 and established an anti-monopoly commission with oversight and coordinating responsibilities. Three agencies share enforcement responsibilities: MOFCOM reviews mergers; NDRC reviews cartel agreements to fix prices, abuse of dominance, and abuse of administrative power involving pricing; and SAIC reviews these same types of activities when they are not directly price-related. After the Anti-monopoly Law was issued, MOFCOM, SAIC, NDRC, and other Chinese government ministries and agencies began to formulate implementing regulations, departmental rules, and other measures. Generally, these ministries and agencies have been willing to seek public comment on their proposed measures.

China's Anti-monopoly Law establishes that merger reviews may consider the impact of deals on China's national economic development. As a step to improve the transparency of enforcement, MOFCOM has committed since November 2012 to disclose information about unconditionally approved cases on a quarterly basis going forward. The NDRC launched several high-profile anti-monopoly investigations in 2013, which focused on the prices charged to Chinese customers. The result of these investigations was often that targeted companies, both foreign and domestic, lowered prices in China for their goods, services, and IP.

Enforcement

China's enforcement of laws and regulations related to monopolies is uneven. Inconsistent local and provincial enforcement may be exacerbated by local protectionism. Government authorities at all levels in China may also restrict competition with favored firms through various forms of regulation. Official statements frequently suggest these efforts are tied primarily to employment concerns. However, the ultimate beneficiaries of the resulting measures are often unclear. In addition, local governments frequently enact rules that restrict inter-provincial trade, which may also restrict market access for certain imported products, raise production costs, and limit market opportunities for foreign-invested enterprises.

Since the Anti-monopoly Law went into effect, MOFCOM's oversight of mergers has yielded the most enforcement activity, largely due to the requirement to pre-notify merger transactions. Under the Anti-monopoly Law, through March 2014, China has "unconditionally" approved 728 merger cases and "conditionally" approved 23. Twenty of the 23 cases approved with conditions have involved offshore transactions between foreign parties. The other three transactions involved foreign companies merging with Chinese enterprises. MOFCOM blocked one acquisition when a U.S. company tried to acquire a well-known Chinese firm. Observers have expressed concern over the speed of MOFCOM's review process. MOFCOM's March 2014 *Provisional Rules on the Applicable Criteria of Streamlined Cases Regarding Concentrations of Undertakings* established a procedure for accelerated review.

In 2013, NDRC increased its enforcement activity noticeably, particularly against foreign enterprises. In addition, U.S. industry has expressed concern about insufficient predictability, fairness, and transparency in NDRC's investigative processes, including NDRC pressure to "cooperate" in the face of unspecified allegations or face steep fines. U.S. industry also has reported pressure from NDRC against seeking outside counsel, in particular international counsel, or having counsel present at meetings.

It remains unclear how China will implement the Anti-monopoly Law with respect to SOEs and government monopolies in industries deemed nationally important. One provision in the Anti-Monopoly Law protects the lawful operations of SOEs and government monopolies in industries deemed nationally important. Although another, ambiguous provision of the Anti-monopoly Law suggests such enterprises may be subject to a different standard, the three Anti-monopoly Law enforcement agencies have publicly stated that the law applies to SOEs, and have pursued enforcement actions against them. To date, China has enforced the Anti-Monopoly Law against SOEs, but concerns remain that enforcement against SOEs will be more limited and regarding the role of industry trade associations in the enforcement process. On the flip side, Anti-monopoly Law provisions restricting regulators from abusing administrative monopolies, which also appear in NDRC's and SAIC's implementing regulations, could help promote the establishment and maintenance of increasingly competitive markets in China if they are enforced.

Additional Laws Related to Foreign Investment

China's State Secrets Law gives the government broad authority to classify information as a "state secret," creating uncertainty and potential risk for investors negotiating with SOEs or operating in sensitive sectors. The Contract Law encourages contractual compliance by providing legal recourse for a breach of contract, although enforcement of judgments continues to be a problem. Additional investment-related laws include, but are not limited to: the Administrative Permissions Law; the Arbitration Law; the Corporate Income Tax Law; the Enterprise Bankruptcy Law; the Foreign Trade Law; the Government Procurement Law; the Insurance Law; the Labor Contract Law; the Law on Import and Export of Goods; and the Securities Law.

Investment Trends

Investment Climate Indices and Rankings

Measure	Year	Rank or value	Website Address
TI Corruption Perceptions index	2013	(80 of 177)	http://cpi.transparency.org/cpi2013/results/
Heritage Foundation's Economic Freedom index	2013	(137 of 178)	http://www.heritage.org/index/ranking
World Bank's Doing Business Report "Ease of Doing Business"	2013	(96 of 189)	http//doingbusiness.org/rankings

Global Innovation Index	2013	(35 of 142)	http://www.globalinnovationindex.org/content.aspx?page=gii-full-report-2013#pdfopener
World Bank GNI per capita	2012	5,720 USD	http://data.worldbank.org/indicator/NY.GNP.PCAP.CD

2. Conversion and Transfer Policies

Foreign Exchange

Foreign-invested enterprises in China do not need pre-approval to open foreign exchange accounts and are allowed to retain income as foreign exchange or convert it into renminbi without quota requirements. Foreign exchange transactions on China's capital account no longer require a case-by-case review by the State Administration of Foreign Exchange (SAFE). Instead, designated foreign exchange banks review and directly conduct foreign exchange settlements. The Chinese government registers all commercial foreign debt and limits foreign firms' accumulated medium- and long-term debt from abroad to the difference between total investment and registered capital. However, China has been gradually liberalizing foreign exchange controls, and in April 2014, announced new rules (the *Regulations on Forex Capital Pooling Operations and Management of Multinational Companies*) that provide greater flexibility in transferring foreign currency for large domestic and foreign multinational firms. Foreign firms must report their foreign exchange balance once per year.

Remittance Policies

The following operations do not require SAFE approval: purchase and remittance of foreign exchange as a result of capital reduction, liquidation, or early repatriation of an investment in a foreign-owned enterprise, or as a result of the transfer of equity in a foreign-invested enterprise to a Chinese domestic entity or individual where lawful income derived in China is reinvested. This would include profit, proceeds of equity transfer, capital reduction, liquidation, and early repatriation of investment.

3. Expropriation and Compensation

Chinese law prohibits nationalization of foreign-invested enterprises except under "special" circumstances. Chinese officials have said these circumstances include national security and obstacles to large civil engineering projects, but the law does not define the term. Chinese law requires compensation of expropriated foreign investments, but does not describe the formula to be used in calculating the amount. The Department of State is not aware of any cases since 1979, in which China has expropriated a U.S. investment, although the Department has notified Congress of several cases of concern.

4. Dispute Settlement

Overview

Chinese officials typically urge firms to resolve disputes through informal conciliation. If formal mediation is necessary, Chinese parties and the authorities typically promote arbitration over litigation. Many contracts prescribe arbitration by the China International Economic and Trade Arbitration Commission (CIETAC). Some foreign parties have obtained favorable rulings from CIETAC, while others question CIETAC's procedures and effectiveness. Other arbitration commissions exist and are usually affiliated with the government at the provincial or municipal level. For contracts involving at least one foreign party, offshore arbitration may be adopted. Arbitration awards are not always enforced by Chinese local courts. Investors may appeal to higher courts in such cases.

CIETAC, established by the State Council in 1956 under the auspices of the China Council for the Promotion of International Trade (CCPIT), is China’s most widely-utilized arbitral body for foreign-related disputes. CIETAC is based in Beijing and has four sub-commissions (Shanghai, Shenzhen, Tianjin, and Chongqing). In 2012, CCPIT, under the authority of the State Council, issued new arbitration rules that granted CIETAC headquarters significantly more authority to hear cases vis-à-vis its sub-commissions. Expecting a loss in revenue, CIETAC Shanghai and CIETAC Shenzhen declared their independence, issued their own rules, and changed their names. As a result, CIETAC Beijing disqualified CIETAC Shanghai and CIETAC Shenzhen from administering arbitration disputes.

This dispute between CIETAC Beijing and its sub-commissions has raised serious concerns in the U.S. business and legal communities. The dispute is particularly concerning for foreign companies with existing contracts that identify Shanghai or Shenzhen as the location for arbitration, as it is unclear whether CIETAC Shanghai or CIETAC Shenzhen would have the legal authority to arbitrate, whether a court would enforce an arbitral decision by either of those bodies, or whether such an arbitration clause would be deemed null and void for vagueness under China’s Arbitration Law. Formal commercial disputes between investors are heard in economic courts. In practice, China's court system is not independent of the government, and the government often intervenes in disputes. Corruption may also influence local court decisions, and local officials may disregard the judgments of domestic courts. China's legal system rarely enforces foreign court judgments.

Reports of business disputes involving violence, death threats, hostage-taking, and travel bans involving Americans continue to increase, although American citizens and foreigners in general do not appear to be more likely than Chinese nationals to be subject to this treatment. Police are often reluctant to intervene in what they consider to be internal contract disputes.

Investor-state disputes leading to arbitration are rare in China. China has never lost an arbitration case resulting from an investment dispute. China is a member of the International Center for the Settlement of Investment Disputes (ICSID) and has ratified the United Nations Convention on the Recognition and Enforcement of Foreign Arbitral Awards (the New York Convention).

Legal Code

China lacks a unified written “Commercial Law.” Rules governing commercial activities are present in various laws, regulations, and judicial interpretations, including China’s Civil Law, Contract Law, Partnership Enterprises Law, Security Law, Insurance Law, Enterprises Bankruptcy Law, Labor Contract Law and Implementing Regulations, and Supreme People’s Court Interpretation on Several Issues Regarding the Application of the Contract Law.

China does not have specialized commercial courts or IPR courts. Instead, local courts usually convene specialized tribunals to hear or try commercial disputes and IPR tribunals to hear or try IPR disputes. The Chinese Communist Party’s Third Plenum Decision, released in 2013, announced initiatives to strengthen IPR protection and explore establishing specialized IPR courts. The 2014 Working Report of the Supreme People’s Court recommended establishing specialized IPR courts.

Lack of Judicial Independence

China’s Constitution provides a legal basis for China’s courts to independently exercise adjudicative power, and several laws have provisions stating that courts are not subject to interference by administrative organs, public organizations, or individuals. However, in practice, China’s court system is not independent of the government or the Chinese Communist Party, which often intervene in disputes. Interference takes place for many reasons, including:

- Courts fall under the jurisdiction of local governments.

- Courts budgets are appropriated by local administrative authorities.

- Judges in China have administrative ranks and are managed as administrative officials. The Chinese Communist Party is in charge of the appointment, dismissal, transfer, and promotion of administrative officials.

- China’s Constitution stipulates that local legislatures appoint and supervise the courts.

- Corruption may also influence local court decisions, and local officials may disregard the judgments of domestic courts.

Third Plenum reforms

The Chinese Communist Party’s November 2013 Third Plenum Decision announced reforms to judicial management, including plans for unified provincial management of personnel and budgets for local courts and the intention to explore establishing judicial jurisdiction separate from administrative divisions, to ensure consistent and proper implementation of Chinese law. Some local courts, such as Shanghai, have already embarked on the reform process. If successful, reforms would enhance judicial independence.

Enforcing judgments of foreign courts

There are few precedents where Chinese courts have recognized and enforced foreign court judgments. Articles 281 and 282 of China's Civil Procedure Law covers the recognition and enforcement of the effective judgments of foreign courts by the court system of China. According to these laws, if the courts conclude, after reviewing the effective foreign courts' judgments in accordance with international treaties concluded or acceded by China or in accordance with reciprocity principles, that the judgments do not violate the basic principles of Chinese laws or China's sovereignty, security, and social public interest, the Chinese courts shall issue verdicts to recognize the effectiveness of foreign court judgments and issue enforcement orders if enforcement is needed.

China has concluded 27 bilateral agreements on the recognition and enforcement of foreign court judgments, but none with the United States. China's recognition of judgments by U.S. courts can be inconsistent, according to anectodal reports.

Bankruptcy

In June 2007, China's new Enterprise Bankruptcy Law came into force. For both foreign investors as well as domestic companies, the bankruptcy process is rarely used to wind down company operations or seek protection from creditors, due to the incomplete nature of the legal regime and judicial inexperience in this area of corporate law.

Investment Disputes

The Chinese government and judicial system do not maintain a public record of investment disputes. The Supreme People's Court maintains a count of the annual number of cases involving foreigners tried throughout China, but does not specify the types of cases, identify civil or commercial disputes, or note foreign investment disputes. The verdicts or rulings of most cases are open to the public.

Duration of Dispute Resolution

Article 270 of China's Civil Procedure Law states that time limits in civil cases do not apply to cases involving foreign investment.

According to the new 2012 CIETAC Arbitration Rules, in an ordinary procedure case, the arbitral tribunal shall render an arbitral award within six months (in foreign-related cases) from the date on which the arbitral tribunal is formed. In a summary procedure case, the arbitral tribunal shall make an award within three months from the date on which the arbitral tribunal is formed. In a domestic arbitration case, the arbitral tribunal shall render an arbitral award within four months from the date on which the arbitral tribunal is formed. At the request of the arbitral tribunal and with the approval of the Secretary General of the CIETAC, the time period of rendering an arbitral award may be extended.

5. Performance Requirements and Investment Incentives

WTO/TRIMS

When joining the World Trade Organization (WTO) in 2001, China committed to eliminate and cease the enforcement of trade and foreign exchange balancing requirements; local content and export performance offsets; and technology transfer requirements made effective through laws, regulations, and other measures. China also committed to lift within two years all measures applicable to motor vehicle producers that restrict categories, types, or models of vehicles permitted for production, and to increase limits within which investment in motor vehicle manufacturing could be approved by provincial governments.

Investment Incentives

Many localities – including special economic zones, development zones, and science parks – court foreign investors with packages of reduced income taxes, resource and land use fees, and import/export duties, as well as priority treatment in obtaining basic infrastructure services, streamlined government approvals, and funding support for start-ups. These packages may also stipulate export, local content, technology transfer, or other requirements.

Performance Requirements

China has committed to eliminate export performance, trade and foreign exchange balancing, and local content requirements. China has also committed to enforce only technology transfer rules that do not violate World Trade Organization (WTO) standards on IP and trade-related investment measures. In practice, however, local officials and some regulators prefer investments that develop favored industries and support the local job market. Provincial and municipal governments often restrict access to local markets, government procurement, and public works projects even to firms that have invested in the province or municipality. In addition, Chinese regulators have reportedly pressured foreign firms in some sectors to disclose IP content or license it to competitors, sometimes at below market rates.

Data Storage

In China, as elsewhere, there are vast opportunities in cloud computing, and information and communications technology (ICT) companies are faced with increasing competitive pressure to migrate services to the cloud to take advantage of the cost benefits and greater flexibility of online data storage and service provision. However, regulatory restrictions, including mandatory source code or IP disclosure requirements in testing and certification regimes related to government procurement, prescriptive technology adoption requirements (often in the form of domestic standards that diverge from global standards), and operational restrictions such as privacy measures, data center colocation, and cross-border data flow restrictions, conspire to limit foreign companies' ability to invest in China's emerging cloud industry. At the 24th U.S.-China Joint Commission on Commerce and Trade (JCCT), China agreed to provide foreign enterprises fair and equitable participation in the development of its SEIs, including cloud computing.

6. Right to Private Ownership and Establishment

In China, all commercial enterprises require a license from the government. There is no broad right to establish a business. Disposition of an enterprise is also tightly regulated.
The Administrative Permissions Law requires reviews of proposed investments for conformity with Chinese laws and regulations, and is the legal basis for China's complex approval system for foreign investment.

7. Right Protection of Property Rights

The Chinese legal system mediates acquisition and disposition of property. Chinese courts have an inconsistent record in protecting the legal rights of foreigners.

Tangible Property Rights

All land in China is owned by the State. Individuals and firms, including foreigners, can own and transfer long-term leases for land, structures, and personal property, subject to many restrictions. China's Property Law stipulates that residential property rights will be automatically renewed while commercial and industrial grants shall be renewed absent a conflicting public interest. A number of foreign investors have seen their land-use rights revoked when neighborhoods are slated by the government for development. Investors report compensation in these cases has been nominal.

China's Securities Law defines debtor and guarantor rights and allows mortgages of certain types of property and other tangible assets, including long-term leases as described above. China does not have laws or regulations prohibiting foreigners from buying non-performing debt, which they may acquire through state-owned asset management firms. However, in practice, China uses bureaucratic hurdles that limit foreigners' ability to liquidate assets in order to discourage them from purchasing non-performing debt.

Intellectual Property Rights

China has updated many of its laws and regulations to comply with the Agreement on Trade Related Aspects of Intellectual Property Rights (TRIPS) and other international agreements. However, there are still aspects of China's IPR legal and regulatory regime that the United States believes fall short of international best practices, and, if improved, would provide greater protection to IPR. Furthermore, effective enforcement of China's IPR laws and regulations remains a significant challenge.

In general, criminal penalties for infringement are not applied on a frequent and consistent enough basis to significantly deter ongoing infringement. Furthermore, administrative sanctions are typically non-transparent and are so weak as to lack a deterrent effect. Because of relatively low damage awards, civil litigation against IPR infringement continues to have a limited effect. For detailed information on China's environment for IPR protection and enforcement, please see the following reports:

Office of the United States Trade Representative's (USTR) 2013 Special 301 Report (see section on China):
http://www.ustr.gov/sites/default/files/05012013%202013%20Special%20301%20Report.pdf

USTR's 2014 National Trade Estimate Report on Foreign Trade Barriers in China (see section on IPR):
http://www.ustr.gov/sites/default/files/2014%20NTE%20Report%20on%20FTB%20China.pdf

USTR's 2013 Report to Congress on China's WTO Compliance (see section on IPR):
http://www.ustr.gov/sites/default/files/2013-Report-to-Congress-China-WTO-Compliance.pdf

For additional information about treaty obligations and points of contact at local IP offices, please see WIPO's country profiles:
http://www.wipo.int/directory/en/

Embassy point of contact: Bridget Davis (DavisBM@state.gov)

Local lawyers list: http://beijing.usembassy-china.org.cn/acs_legal.html

8. Transparency of the Regulatory System

China's legal and regulatory system is complex and Chinese regulators and other government authorities inconsistently enforce regulations, rules, and other regulatory documents. Foreign investors rank inconsistent and arbitrary regulatory enforcement and lack of transparency among the major problems they face in China's market.

The State Council's Legislative Affairs Office (SCLAO) has issued instructions to Chinese agencies to publish all foreign trade- and investment-related laws, regulations, rules, and policy measures in the MOFCOM Gazette, in accordance with China's WTO accession commitment. In addition, it has also issued notices to require its own departments and other central government agencies to post proposed trade- and economic-related administrative regulations and departmental rules and policies on the official SCLAO website for public comment. However, the SCLAO and ministries falling under the State Council continue to post only a fraction of draft administrative regulations and departmental rules on the SCLAO website for a 30-day public comment period. Likewise, Chinese agencies rarely solicit public comment on draft regulatory documents that directly implicate citizens' rights and obligations. Comment periods can be extremely brief, and the impact of public comments on final regulations is not clear.

Moreover, there are an increasing number of regulatory policies for which public comment is not sought before they are finalized. Foreign investors report that Chinese regulators at times rely on unpublished internal guidelines that nonetheless affect their businesses.

State actions motivated by a perceived need to protect social stability or achieve other political goals can affect foreign investors. Access to foreign online resources, including news, cloud-based business services, and virtual private networks (VPNs), is often and increasingly restricted without official acknowledgement or explanation. Foreign-invested companies have also reported threats of retaliation by the government for actions taken by the U.S. and other foreign governments at the WTO and in regards to outbound Chinese investment.

9. Efficient Capital Markets and Portfolio Investment

China’s leadership aims to build a modern, developed, multi-tiered capital market. Bank loans continue to provide the majority of credit in China, although other sources of capital, such as corporate bonds, trust loans, equity financing, and private equity financing, are expanding their scope, reach, and sophistication. Regulators use administrative methods to control credit growth, although market-based tools such as interest rate policy play an increasingly important role.

The People's Bank of China (PBOC), China's central bank, has gradually increased flexibility for banks in setting interest rates; the floor on the lending rate was removed in 2013, and the PBOC has said that the ceiling on deposit rates will be gradually lifted and removed within the next several years. Increased flexibility has squeezed the net interest margin of banks (i.e., the gap between deposit and lending rates), which has cut into the profits of China’s banking sector. Favored borrowers, particularly SOEs, benefit from greater access to capital and lower financing costs, as lenders perceive these entities to have an implicit government guarantee and hence lower risk profiles. Small- and medium-sized enterprises (SMEs), by contrast, experience the most difficulty obtaining bank financing, and instead, often finance investments through retained earnings or informal channels, including other Chinese firms or private lenders. In recent years, China’s “shadow banking” sector, which includes vehicles such as wealth management products and trust products, has grown rapidly. The Chinese authorities have taken successive steps to increase the transparency and strengthen the supervision of these activities, while also permitting their continued development, as in many cases, these products increase channels for private firms to obtain capital at market rates. In 2014, the government also announced a pilot program that will allow private investors to establish small commercial banks.

Non-bank financing has expanded over the last few years, including through public listing of stock, either inside or outside of China, and more firms are issuing bonds. Most foreign portfolio investment in Chinese companies occurs on foreign exchanges, primarily in New York and Hong Kong. In addition, China has significantly expanded quotas for certain foreign institutional investors to invest in domestic stock markets, and has approved a two-way cross-border equity direct investment scheme between Shanghai and Hong Kong, which will allow Chinese investors to trade designated Hong Kong-listed stocks through the Shanghai Exchange, and vice versa. Direct investment by private equity and venture capital firms is also rising rapidly, although from a small base.

10. Competition from State-Owned Enterprises

Overview

China's leading SOEs benefit from preferential government policies and practices aimed at developing bigger and stronger national champions. SOEs enjoy favored access to the most essential economic inputs (land, hydrocarbons, finance, telecoms, electricity) and considerable power in the markets for others (steel, minerals). SOEs have long enjoyed preferential access to credit and the ability to issue publicly traded equity and debt. According to some Chinese academics, provincial governments have used their power to manipulate industrial policies to deny operating licenses in order to persuade reluctant owners to sell out to bigger state-owned suitors.

The November 2013 Third Plenum agenda calls for SOEs to remain a key part of China's economic system, even as China makes them more efficient and transparent by limiting their monopoly power and preferential access to factors of production to improve their contribution to economic development. The Third Plenum meeting called for a "mixed ownership" economic structure, which would allow for private and state-owned businesses to co-exist in the domestic economy and proposed greater balance between private and state-owned businesses, including access to factors of production, competition on a level-playing field, and equal legal protection. The Third Plenum Decision explains that SOEs will focus resources in areas that "serve state strategic objectives." However, experts point out that SOEs continue to hold dominant shares in their respective industries, regardless of whether they are strategic, which may further restrain private investment in the economy. Moreover, the application of China's Anti-monopoly Law, together with other industrial policies and practices that are selectively enforced by the authorities, protect SOEs from private sector competition.

Investment Restrictions in "Vital Industries and Key Fields"

The December 2006 *Guiding Opinions Concerning the Advancement of Adjustments of State Capital and the Restructuring of State-Owned Enterprises* called on China to consolidate and develop its state-owned economy, including enhancing its control and influence in "vital industries and key fields relating to national security and national economic lifelines." The document defined "vital industries and key fields" as "industries concerning national security, major infrastructure and important mineral resources, industries that provide essential public goods and services, and key enterprises in pillar industries and high-tech industries."

At the time the document was published, the Chairman of the State-owned Assets Supervision and Administration Commission (SASAC) listed industries in which the State should maintain "absolute control" (aviation, coal, defense, electric power and the State grid, oil and petrochemicals, shipping, and telecommunications) and "relative control" (automotive, chemical, construction, exploration and design, electronic information, equipment manufacturing, iron and steel, nonferrous metal, and science and technology). China maintains that these lists do not reflect its official policy. In some cases, more than 50 percent ownership in some of these industries has been permitted on a case-by-case basis, especially if a particular expertise or technology is deemed important at the time.

China's current agriculture trade rules, regulations, and limitations on foreign agricultural investment severely restrict the contributions of American agriculture companies and, subsequently, the many potential benefits to China's agriculture sector. China's agriculture investment restrictions also appear to be at odds with the objectives of China's 12th FYP, which emphasizes the need to shift more resources to agriculture and food production in order to improve people's lives and meet China's food security and food safety needs.

China's State Assets Law is intended to safeguard China's economic system, promote the "socialist market economy," fortify and develop the state-owned economy, and enable SOEs to play a leading role in China's economy, especially in "vital industries and key fields." The law requires China to adopt policies to encourage SOE concentration and dominance in industries vital to national security and "national economic security."

Sovereign Wealth Funds

China's principal sovereign wealth fund is China Investment Corporation (CIC), which was established in 2007. CIC is overseen by a board of directors and a board of supervisors and invests on a 10-year time horizon, using rolling annualized returns to evaluate performance. China's sovereign wealth is also invested by a subsidiary of SAFE, a government agency that reports directly to the PBOC. The SAFE Administrator serves concurrently as a PBOC Vice Governor. While CIC publishes an annual report containing information on its structure, investments, and returns, SAFE does not. China's National Social Security Fund also makes investments using China's sovereign wealth.

11. Corporate Social Responsibility

Corporate social responsibility (CSR), or what is increasingly known as sustainability, is a relatively new concept for domestic companies in China and is less widely accepted there than in the United States. Investors looking to partner with Chinese companies or expand operations with Chinese suppliers face challenges ensuring domestic firms meet internationally recognized, voluntary industry standards in such areas as labor, the environment, and good manufacturing practices. China's 12th FYP highlights sustainability issues as a means to draw attention to the subject. Foreign-invested enterprises tend to follow generally accepted CSR principles, and most report annually on their CSR policies and achievements.

12. Political Violence

The risk of political violence directed at foreign companies operating in China remains small. Occasional violent but unconnected protests have occurred in all parts of China, but such mass incidents generally involved local residents protesting corrupt officials, environmental and food safety concerns, confiscated property, and disputes over unpaid wages. In several recent examples, workers and mid-level managers have protested against corporate merger and acquisition decisions on the grounds that employees were not consulted. In the fall of 2012, against a backdrop of rising tensions between China and Japan over territorial issues, some businesses owned or perceived to be owned by Japanese in multiple Chinese cities faced Chinese protests. Economic activity between China and Japan has suffered as a result.

13. Corruption

Overview

Corruption remains endemic in China. The lack of an independent press, as well as the fact that all bodies responsible for conducting corruption investigations are controlled by the Chinese Communist Party, hamper anti-corruption efforts. Senior officials and family members are suspected of using connections to avoid investigation or prosecution for alleged misdeeds.

According to Chinese law, accepting a bribe is a criminal offense with a maximum punishment of life in prison or death in "especially serious" circumstances. The maximum punishment for offering a bribe to a Chinese official is five years in prison, except when there are "serious" or "especially serious" circumstances, when punishment can range from five years to life in prison. A February 2011 amendment to the Criminal Law made offering large bribes to foreign officials or officials of international organizations a punishable offense, although there has yet to be a prosecution.

The Supreme People's Procuratorate and the Ministry of Public Security investigate criminal violations of laws related to anti-corruption, while the Ministry of Supervision and the Chinese Communist Party Discipline Inspection Committee enforce ethics guidelines and party discipline. China's National Audit Office also inspects accounts of SOEs and government entities.

Anti-corruption measures

China has stepped up efforts against corruption in Party ranks. President Xi Jinping has said that endemic corruption threatens the Party's survival and has vowed to go after high-flying “tigers,” as well as lowly “flies.” New anti-corruption measures, part of November 2013 Third Plenum reforms, signaled an intensified push to fight graft. The Third Plenum documents implored public officials to “keep power within the cage of regulations,” criticized material excess, and called for senior officials to disclose their wealth. Premier Li Keqiang said China has “zero tolerance” for corruption. However, individual citizens who have called for officials to disclose their public assets in support of the government’s anti-corruption goals have been subject to criminal prosecution.

In 2013, China engaged in an intensive and large-scale anti-corruption campaign, during which 31 central government SOE officials of director general rank or higher were investigated for graft by the Party’s Organization Department. Eight cases were transferred to the judicial authorities. High profile SOE executives were investigated and charged with corruption. Overall in 2013, Chinese Communist Party discipline organs investigated 173,000 corruption cases and disciplined 182,000 officials, of which 9,600 criminal suspects were transferred to judicial authorities. Nationally, prosecutorial authorities accused 51,000 officials of graft and job-related crimes, and courts nationwide concluded 23,000 graft and bribery cases.

China’s anti-corruption crackdown could curb abuse of administrative powers by government officials aligned with private sector patrons; however, selective application of anti-corruption rules may also raise concerns among foreign companies in China.

UN Anticorruption Convention, OECD Convention on Combatting Bribery

China ratified the United Nations Convention against Corruption in 2005 and participates in Asia-Pacific Economic Cooperation (APEC) and Organization for Economic Cooperation and Development (OECD) anti-corruption initiatives. China has not signed the OECD Convention on Combating Bribery.

14. Bilateral Investment Agreements

China has signed bilateral investment agreements with over 100 countries and economies, including Austria, the Belgium-Luxembourg Economic Union, Canada, France, Germany, Italy, Japan, South Korea, Spain, Thailand, and the United Kingdom. China's bilateral investment agreements cover expropriation, arbitration, most-favored-nation treatment, and repatriation of investment proceeds. They are generally regarded as weaker than the investment treaties the United States seeks to negotiate.

A list of China signed BITs can be found here:
http://tfs.mofcom.gov.cn/article/Nocategory/201111/20111107819474.shtml

The United States and China concluded a bilateral taxation treaty in 1984. The two countries resumed negotiations toward a bilateral investment treaty (BIT) in October 2012, following the conclusion of the U.S. model BIT review process. At the 2013 U.S.-China Strategic and Economic Dialogue, China agreed to conduct negotiations based on the concepts of “pre-establishment” national treatment, which would expand market access for foreign investors, and a “negative list” of negotiated exceptions to national treatment and other core treaty obligations.

15. OPIC and Other Investment Insurance Programs

The United States suspended Overseas Private Investment Corporation (OPIC) programs in the aftermath of China's crackdown on Tiananmen Square demonstrators in June 1989. OPIC honors outstanding political risk insurance contracts. The Multilateral Investment Guarantee Agency, an organization affiliated with the World Bank, provides political risk insurance for investors in China. Some foreign commercial insurance companies also offer political risk insurance, as does the People's Insurance Company of China.

16. Labor

Human resource issues remain a major concern for American companies operating in China. Labor costs are the problem most often cited, followed closely by difficulties in finding and retaining talent, particularly at the management level and highly skilled technical staff. Navigating evolving labor and social insurance laws and implementation rules is an enduring challenge.

In particular, the rocky implementation of new visa rules introduced in the past year led to significant delays for foreign employees waiting to obtain visas. Companies have more frequently cited China’s poor air quality and pollution generally as causing difficulties in trying to attract and retain qualified foreign talent. Together, these issues contribute to high labor costs.

Independent trade unions are illegal in China. The Trade Union Law gives the All-China Federation of Trade Unions (ACFTU) control over all union organizations and activities, including enterprise-level unions. The ACFTU is a Chinese Communist Party organ chaired by a member of the Politburo, and its priority task is to "uphold the leadership of the Communist Party." The ACFTU and its provincial and local branches aggressively organize new constituent unions and add new members, especially in large, multinational enterprises. The right to strike is not protected by law. However, worker protests and work stoppages occur regularly. Official forums for mediation, arbitration, and similar mechanisms of alternative dispute resolution are generally ineffective in resolving disputes.

China has not ratified core International Labor Organization conventions on freedom of association and collective bargaining, but has ratified conventions prohibiting child labor and employment discrimination. Apart from a lack of freedom of association and the right to strike, Chinese labor laws generally meet international labor standards. Enforcement of existing labor laws and regulations, however, is inconsistent.

17. Foreign Trade Zones/Free Trade Zones

China's principal customs bonded areas include Shanghai, Tianjin, Shantou, three districts within Shenzhen (Futian, Yantian, and Shatoujiao), Guangzhou, Dalian, Xiamen, Ningbo, Zhuhai, and Fuzhou. Besides these official duty-free zones identified by China's State Council, numerous economic development zones and open cities offer similar privileges and benefits to foreign investors.

In September 2013, the Shanghai Municipal government and the State Council announced the establishment of the China (Shanghai) Pilot Free Trade Zone (SFTZ), which condensed four previously existing bonded areas into a single free trade zone. The goal of the SFTZ is to provide a trial ground for trade and investment liberalization measures and to introduce services sector reform, especially in financial services, that China expects to eventually introduce in other parts of the domestic economy. Shanghai officials tout the use of a negative list, to spell out sectors where national treatment does not apply, as a key reform introduced in the zone. While the current negative list closely mirrors China's Foreign Investment Catalogue, Shanghai officials have committed to working with relevant ministries in Beijing to release a revised negative list by mid-2014, although the municipal government has not indicated the sectors or investment areas where foreign market access will expand. As of September 2013, 7,772 companies had registered in the free trade zone, including 661 foreign-invested firms. To date, the municipal and central government have released a number of administrative and sector-specific regulations and circulars that outline the procedures and regulations in the zone.

18. Foreign Direct Investment Statistics

Data Limitations

Investment from and to some economies, including but not limited to the British Virgin Islands, the Cayman Islands, Hong Kong, and Macau, may mask the ultimate source/destination of the investment. Some analysts have noted that investment from and to Taiwan may be underreported. Chinese FDI data do not include much of the high dollar-value minority equity stakes that American financial services firms have taken in major Chinese lenders. In addition, China does not classify reinvested locally-generated profits as new investment. MOFCOM's data tracks 2003 forward.

FDI as a Percentage of Gross Domestic Product

According to MOFCOM's 2013 China Commerce Year Book, China's FDI stock equaled 16 percent of its gross domestic product (GDP) in 2012.

Foreign Direct Investment Flows for 2012 (Top 10 Sources of Origin)

Country/Economy of Origin	**Millions of U.S. Dollars**
Hong Kong	65,561
British Virgin Islands	7,831
Japan	7,352
Singapore	6,305
South Korea	3,038
Taiwan	2,847
United States	2,598
Cayman Islands	1,975
Samoa	1,744
Germany	1,451

Source: China Commerce Yearbook 2013

Cumulative* Foreign Direct Investment for 2012 by Selected Source of Origin

Country/Economy of Origin	**Millions of U.S. Dollars**
Hong Kong	874,596
British Virgin Islands	129,402
Japan	87,246
United States	70,190
Singapore	59,261
Taiwan	57,046

South Korea	52,892
Cayman Islands	25,805
Samoa	19,928
Germany	19,761

Source: China Commerce Yearbook 2013

*Cumulative values are totals of the data collected each year, are not adjusted for inflation, and do not account for divestment.

Flow of Outbound Direct Investment for 2012 (Top 10 Destinations)

Destination	Millions of U.S. Dollars
Hong Kong	51,238
United States	4,048
Kazakhstan	2,996
United Kingdom	2,775
British Virgin Islands	2,239
Australia	2,172
Venezuela	1,542
Singapore	1,519
Indonesia	1,361
Luxembourg	1,133

Source: China Commerce Yearbook 2013

Stock of Outbound Direct Investment for 2012 (Top 10 Destinations)

Destination	Millions of U.S. Dollars
Hong Kong	306,372
British Virgin Islands	30,851
Cayman Islands	30,072
United States	17,080
Australia	13,873
Singapore	12,383
Luxembourg	8,978
United Kingdom	8,934

Kazakhstan	6,251
Russia	4,888
South Africa	4,775

Source: China Commerce Yearbook 2013

Key Macroeconomic Data: U.S. FDI in host country economy

	National Bureau of Statistics of PRC		USG or international statistical source		USG or international Source of data (Source of Data: BEA; IMF; Eurostat; UNCTAD, Other)
Economic Data	Year	Amount	Year	Amount	
Host Country Gross Domestic Product (GDP) (*Millions U.S. Dollars)*	2012	8,220,900	2012	8,227,000	http://www.worldbank.org/en/country
Foreign Direct Investment	China Commerce Year Book		USG or international statistical source		USG or international Source of data: BEA; IMF; Eurostat; UNCTAD, Other
U.S. FDI in partner country (*Millions U.S. Dollars, stock positions)*	2012	70,190	2012	51,363	BEA (click through below selections to reach) • Bureau of Economic Analysis • Balance of Payments and Direct Investment Position Data • U.S. Direct Investment Position Abroad on a Historical-Cost Basis • By Country only (all countries) (Millions of Dollars)
Host country's FDI in the United States (*Millions U.S. Dollars, stock positions)*	2012	17,080	2012	5,154	BEA (click through below selections to reach) • Balance of Payments and Direct Investment Position Data • Foreign Direct Investment Position in the United States on a Historical-Cost Basis • By Country only (all countries) (Millions of Dollars)
Total inbound stock of FDI as % host GDP (***calculate)***	2012	16%			

Sources and Destination of FDI

Data Limitations

The IMF does not track data for China's outbound direct investment.

According to MOFCOM's 2013 China Commerce Year Book, the top five destinations for China's Outward Direct Investment from 2003-2012 are: Hong Kong, British Virgin Islands, Cayman Islands, United States, and Australia.

Direct Investment from/in Counterpart Economy Data					
From Top Five Sources/To Top Five Destinations *(US Dollars, Millions)*					
Inward Direct Investment			**Outward Direct Investment**		
Total Inward	2,068,027	100%			
China, P.R.: Hong Kong	952,275	46%			
Virgin Islands, British	318,875	15%			
Japan	129,388	6%			
Singapore	87,020	4%			
United States	62,960	3%			
"0" reflects amounts rounded to +/- USD 500,000.					

19. Contact Point at Post for Public Inquiries

Bridget Davis
Investment Officer
Economic Section, U.S. Embassy Beijing

55 Anjialou Road, Chaoyang District, Beijing, P.R. China
0086-10 8531-3000
Beijinginvestmentteam@state.gov

Other Useful Online Resources

Chinese Government:

- Chinese Embassy in Washington, D.C.: **http://www.china-embassy.org/eng/**
- Ministry of Commerce: **http://english.mofcom.gov.cn/**;
- Invest in China: **http://www.fdi.gov.cn/pub/FDI_EN/default.htm**
- National Development and Reform Commission: **http://en.ndrc.gov.cn/**
- State Administration of Foreign Exchange: **http://www.safe.gov.cn/**
- State Administration of Taxation **http://www.chinatax.gov.cn/n6669073/index.html**

United States Government:

- U.S. Embassy in Beijing (Doing Business in China): **http://beijing.usembassy-china.org.cn/business.html**
- U.S. Department of State travel information: **http://travel.state.gov/**
- U.S. Trade Representative: **http://www.ustr.gov/**
- U.S. Department of Commerce: **http://www.export.gov/**
- U.S. Department of the Treasury: **http://www.treasury.gov/Pages/default.aspx**
- Export Import Bank: **http://www.exim.gov/**
- Overseas Private Investment Corporation (OPIC): **http://www.opic.gov/**
- U.S. Trade and Development Agency: **http://www.ustda.gov/**