**US-China Business Council Comments on**
**the Draft Foreign Investment Law of the People's Republic of China**

February 24, 2019

The US-China Business Council (USCBC) represents more than 210 U.S. companies with significant operations in China and has a strong interest in the continued advancement of China's economic reform initiative to allow the market to play a decisive role in the economy. We submit these comments on behalf of our membership, as well as the membership of the Coalition of Services Industries (CSI), the American Council of Life Insurers (ACLI), and Insurance Ireland, which along with ACLI, belongs to the Global Federation of Insurance Associations.

We are pleased that the National People's Congress is taking significant steps to reform China's foreign investment regime. These reforms are essential for China's future economic development, and can play an important role in spurring more foreign investment. We are pleased to have the opportunity to offer comments on the draft Foreign Investment Law (draft law), which replaces three current foreign investment laws: the Wholly Foreign-Owned Enterprise Law ("WFOE Law"), the Sino-Foreign Equity Joint Venture Enterprise Law ("EJV Law"), and the Sino-Foreign Contractual Joint Venture Enterprise Law ("CJV Law").

This draft law has positive elements that will be helpful to foreign company operations by enhancing investment protections and addressing some significant concerns of our member companies, including concerns related to market access, intellectual property rights protection, and technology transfer. We are also pleased that this draft appears to streamline the approval process for a significant portion of foreign investment, and that it incorporates important principles such as pre-establishment national treatment and a negative list (the "Special Management Measures for Foreign Investment"). However, the draft language on these issues is vague, leaving too much room for divergent interpretations. Clearer and more specific guidance will help to establish and ensure a more stable environment for foreign investment.

Inherent in the draft law is terminology that USCBC has previously noted invites discrimination: foreign-invested enterprise (FIE). Use of this term invites discriminatory treatment of various types of domestic legal entities, based solely on ownership. We encourage China's policymakers to move toward eliminating the FIE classification and govern all legally-established companies in China under the same laws and regulations that apply to domestic enterprises, such as the Company Law.

In the interim, we propose the following general principles for the draft law:

- **Eliminate provisions that discriminate between foreign and domestic investment, even if the discrimination is in name only.** Foreign-invested companies should be subject to the same legal and reporting requirements as domestic companies. Eliminating extensive reporting requirements and additional supervision and inspection requirements that apply solely to FIEs will help to ensure that foreign companies are not treated differently from domestic companies. China's complex pre-establishment restrictions on market access, such as administrative approvals required before business can be conducted, impact many industries and undermine equal treatment by impeding foreign investors from investing in the first place. These pre-establishment requirements should be amended to reflect the goal of the draft law of treating foreign and domestic investments equally.

- **Increase transparency in all review procedures and standard setting processes.** Greater transparency in licensing procedures and implementation of laws, regulations and rules would

help foreign companies ensure their operations and procedures are compliant. Our members appreciated the government's establishment of a complaint mechanism for foreign companies to seek redress when they encounter problems, and would appreciate more guidance regarding how to use that mechanism to effectively protect their rights. We suggest providing more fulsome and detailed provisions for the complaint and feedback mechanisms available to foreign-invested companies, with responsibilities, authority, procedures and methods clearly defined. Foreign companies should also have a greater voice in national standards setting processes so that their views and experience are taken into account. We recommend include explicit provisions in the draft law and other relevant measures indicating that foreign-invested enterprises are to be treated equally in these processes.

- **Continue to improve intellectual property (IP) protections.** Strong IP protections are fundamental to protecting investors' rights. While USCBC has further comments on the draft law's provisions prohibiting forced technology transfers as a condition for foreign investment, the draft law should also prohibit IP infringement and be accompanied by improved enforcement of investors' rights in that area.

In addition to these general principles, we respectfully submit the following specific comments for consideration:

**Article 1**
The general provisions, beginning with Article 1, make clear that the law is intended to promote and protect foreign investment in China. We recommend adding additional language recognizing that foreign invested enterprises are equally important participants in China's national economic development.

**Article 2**
The definition of "foreign investor" and "foreign investment" are not clear and may cause confusion and divergent interpretations in implementation. First, it is not clear whether foreign investors can include foreign or regional governments and international organizations. Second, the definition of foreign investment includes "direct" and "indirect," but "indirect foreign investment" is described in vague terms.

To limit confusion and conflicting interpretations among different bureaus and provincial and local governments, we recommend that an investor be considered a "foreign investor' based on the investor's place of formation of the entity. This change should also eliminate any assessment of nationality based on the nationality of shareholders, directors, and management.

We also recommend clarifying when the Foreign Investment Law is applicable to a domestic Chinese company. Article 2 does not specify the threshold amount or percentage of shares, stock or property that a foreign investor must acquire in a Chinese company for the Foreign Investment Law to be applicable. If any amount of foreign investment makes an entity subject to the Foreign Investment Law, it should be explicitly stated. If there is a threshold amount of foreign investment, the threshold should be defined. If a foreign investor must have a "controlling" share in the company, the definition of "control" should be explained.

Article 2 also uses the term "merger and acquisition" (并购), but the Anti-Monopoly Law uses the term of "concentration" (经营者集中) to express the same meaning. We recommend maintaining consistent terminology between laws by using the term "concentration."

**Article 3**

Article 3 outlines general principles for the treatment of FIEs, including "building a stable, transparent and predictable investment environment for foreign investment." Since Articles 16 and 20 both identify "fair treatment" as a goal of the law, we recommend adding "fair treatment" to the general principles outlined in Article 3.

**Article 4**

Article 4 provides that the management scheme of pre-establishment national treatment plus negative list will be applied to foreign investment. The article also indicates the negative list applicable to foreign investment is published or approved to be published by the State Council. In reality, some free trade zones have reduced, or are in the process of reducing the negative lists used within their respective zones, raising questions about the legality of this practice. Article 4 should clarify that these modifications to the national negative list is endorsed by the central government. Such a change would improve predictability and certainty, which are critical for foreign investment.

**Article 6**

Article 6 requires foreign investors and foreign-invested enterprises to abide by Chinese laws and regulations and not endanger China's national security or harm the public interest. However, the definition of what would harm public interests is not provided. USCBC recommends clarifying what is meant by "harming the public interest" and clearly describing activities that would be considered as "harming the public interest.".

**Article 8**

Article 8 requires that foreign-invested enterprises should create the necessary conditions for employees to establish labor unions and facilitate labor activities. We recommend concluding the article with an additional sentence: "The provisions of this article shall supersede all other legal stipulations."

**Article 9**

Article 9 references the State's "various policies that promote the development of enterprises." This language is vague and broad. The policies referenced in the article should be clearly identified to clarify if it includes local government policy. In addition, for clarity and consistency with other policies, we recommend striking "except for where administrative regulations or the law stipulate otherwise," and replacing that language with a more specific stipulation, "unless otherwise stipulated by this law".

**Article 10**

Because many foreign industry associations represent the interests of foreign industry, we recommend amending Article 10 of the draft law to read, "For the purpose of formulating laws, regulations, and rules related to foreign investment, the opinions and suggestions of foreign-invested enterprises and foreign trade associations shall be taken into consideration according to procedures prescribed by law."

Article 10 also says "Normative documents or judicial rulings that are related to foreign investment shall by promptly published in accordance with law." We recommend amending this language to read, "Normative documents or judicial rulings that are related to foreign investment shall be promptly published in accordance with law, except for the cases that involve national secrets or trade secrets of the party(ies)."

**Article 11**

We appreciate language in Article 11 aimed at improving provision of services and information to foreign investors. We recommend clarifying which ministry or agency is responsible for providing which services to further define the Foreign Investment Service System and how it is implemented. It would be even more helpful if a "one-stop shop" were established to provide these services to foreign investors.

**Article 15**
We are encouraged that the draft law stipulates that FIEs are to participate equally in standards setting work. We recommend clarifying the rights and responsibilities of participants in the standards setting process, and specifying the rights and responsibilities that FIEs are to be accorded, such as voting rights and drafting rights.

To this end, we recommend the draft law create a designated unified channel to make draft versions of all standards (national, industry, and other types of standards) and standards-related policies and regulations set by government or government-affiliated organizations available to domestic, foreign-invested, and foreign-based companies for public comment for a period of at least 60 days. Additionally, adding language that requires all non-governmental bodies and organizations that set standards and standards-related policies and guidelines to increase transparency by making draft versions of these documents freely available for public comment by all stakeholders regardless of nationality would greatly increase the opportunities for foreign investors to engage in the standard setting process.

Although existing rules and practice such as State Council Circular No. 5 allow FIEs equal participation in standards development activities, FIEs are not consistently permitted full participation in China's standards development process, including as full voting members of technical committees responsible for standards setting. Permitting FIEs to participate in standards-setting activities on equal footing with their domestic counterparts would promote a more robust standards-setting process.

Finally, we recommend the draft law require all standards to be published in both Chinese and English.

**Article 16**
We welcome safeguards for FIEs' equal participation in government procurement activities. Article 16 should detail specifically what is meant by "products manufactured by foreign-invested enterprises in mainland China." We recommend that products sold by foreign invested enterprises in China, be afforded equal treatment in government procurement, not just products manufactured by foreign-invested enterprises in mainland China. We further recommend that "products manufactured by foreign-invested enterprises in mainland China" be defined with reference to China's Customs' regulations on "Country of Origin." In addition, products manufactured by FIEs that are eligible for government procurement activities should include products that are toll manufactured by foreign-invested enterprises inside and outside of mainland China.

There should also a clear bidding process available to FIEs seeking to participate in government procurement activities, as well as language articulating rules or remedies for foreign enterprises when they are denied equal participation in government procurement activities. We suggest adding the following text to Article 16, "For any discriminatory, prohibitive or restrictive requirement in government procurement activities, affected parties may apply for an administrative reconsideration to the competent department at a higher level within 60 days from the date when they become aware of such discrimination, or file an administrative litigation to the court at the same level within 90 days from the date when they become aware of such discrimination."

**Article 18**
It is unclear what kinds of foreign investment promotion policies local governments are authorized or unauthorized to formulate. When local governments develop foreign investment promotion policies or make promises that are beyond their authority in order to incentivize and attract foreign investment, foreign investors should be compensated for any actual damages they incur. We recommend adding language that provides this protection.

**Article 19**
We appreciate language in Article 19 aimed at improving the provision of services and information to foreign investors at various levels of government. We recommend clarifying which ministry or agency is responsible for providing which services. It would be even more helpful if a "one-stop shop" were established to provide these services to foreign investors.

**Article 20**
Regarding circumstances where the State is permitted to expropriate a foreign investment, the terms "special circumstances," "public interest," "legally prescribed procedures" and "fair and reasonable compensation" are extremely vague. We recommend amending Article 20 of the draft to read, "The State shall not nationalize or expropriate foreign investment; in special circumstances, if foreign investment is required to be levied on the grounds of societal public interest, it shall be conducted in accordance with provisions of relevant treaties or agreements, proceed according to non-discriminatory legal procedures, and shall entail fair and reasonable compensation."

**Article 21**
Article 21 proposes useful safeguards for the legal repatriation for foreign profits out of China, however, the defined scope of "capital contributions, profits, capital gain, and intellectual property right royalties" is too narrowly defined to capture all income generated by foreign enterprises in China. We recommend amending Article 21 of the draft to: "Foreign investors capital contributions, profits, capital gains, intellectual property rights gains, compensation or indemnification, and other operating income they receive in accordance with law may be freely transferred out of China in either RMB or foreign currencies according to the needs of foreign investors."

**Article 22**
Article 22 defines the terms for technical cooperation and sets a useful standard for partnerships but still risks technology transfer pressure. To limit that risk, we recommend changing the second clause of Article 22 of the draft to: "Terms for technical cooperation as it pertains to foreign investment shall be determined via equal negotiation between each of the parties involved. Neither administrative organs nor staff thereof shall use administrative means to force the transfer of technology."

The protection of foreign investors' intellectual property in China is currently challenged by differing provisions in Chinese laws, regulations, and Supreme Court interpretations, including interpretations by the Supreme Court of Article 329 of the Contract Law, and the current regulatory requirement to register all intellectual property agreements involving foreign parties at MOC as a pre-condition for Chinese parties to pay royalty and engineering service fees to foreign parties. To ensure the effectiveness of the protections afforded under Article 22, we recommend stipulating that Article 22 prevails over any conflicting rules.

**Article 24**
Article 24 clarifies that foreign companies will be compensated for losses suffered but is insufficiently clear on causation. We recommend changing the second clause of Article 24 that says, "...and provide compensation to foreign investors for losses suffered for [what this provision stipulates] in accordance with the law" to "and compensate foreign investors in accordance with the law for losses suffered due to [what this provision stipulates]". Compensation should also be fair and reasonable, in order to make the language consistent with Article 20 of the draft.

**Article 25**

Article 25 should include more specific language detailing the complaint mechanism for foreign-invested enterprises, what it does, and how it works. It is also unclear how the complaint mechanism created in the draft law will operate in relation to other paths for seeking remedies, such as administrative reconsideration and litigation. We suggest adding language stipulating that using the complaint mechanism for FIEs is not a prerequisite to seeking administrative reconsideration or pursuing litigation.

**Article 27**
The scope of the negative list for foreign investment in the respective trade zones is different from the scope of the negative list for foreign investment in the country. In reality, some free trade zones have or are in the process of reducing the negative lists used within their respective zones, raising questions about the legality of this practice. Article 27, like Article 4, should clarify that these modifications to the national negative list is endorsed by the central government. Such a change would improve predictability and certainty, which are critical for foreign investment.

**Article 28**
Article 28 provides that "the approval and filing of a foreign-invested project should be governed by other relevant rules." However, Article 2 Section 1 provides that the forms of "foreign investment" includes investment in new projects. USCBC recommends including specific details of the approval process and filing process in the draft law to ensure one process covers all the necessary filings and approvals adopting the one-stop shop principle.

**Article 29**
To ensure this law supersedes future administrative regulations, we suggest amending language in the second paragraph of Article 29 from, "Except as otherwise provided by laws or administrative regulations," to "Unless otherwise expressly stipulated by law."

**Article 31**
As stated in multiple places in the text of the draft law, foreign investors enjoy national treatment when investing in China. However, Article 31 requires all foreign investments to comply with an information reporting requirement that does not apply to domestic investments. This clearly contradicts the national treatment principle laid out elsewhere in the draft. We recommend deleting Article 31. If there is indeed a need to strengthen the information reporting requirements for companies registered in China, these requirements should be articulated in amendments to the Company Law and should be as simple as possible so as not to discourage investment.

**Article 33**
Article 33 establishes a national security review system for foreign investment, but does not specify the specific content of the national security review system, such as the scope of the review, the content of the review, the requirements for the application documents, the review procedures and time limits. It is also unclear on what legal basis the national security reviews of newly established FIEs outside of free trade zones would be conducted, since the current legal basis for national security reviews of foreign investment appears in only the Notice of the General Office of the State Council on Establishing a Security Review System for Foreign Investors to Acquire Domestic Enterprises (Guo Ban Fa [2011] No. 6) and the Office of the State Council on Printing and Distributing Free Trade Notice of the National Security Review Trial Measures for Foreign Investment in the Pilot Area (Guo Ban Fa [2015] No. 24). We ask that Article 33 be revised to provide more clarity on the scope, consequences and processes for this national security review, and suggest that the scope be limited to restricted industries as identified in the negative list.

Article 33 also stipulates that security review decisions made in accordance with law are "final decisions," suggesting but not clearly specifying that these decisions cannot be appealed for administrative reconsideration or administrative litigation. Generally, an administrative decision can be reviewed or appealed through litigation.

The absence of a meaningful system to appeal decisions contradicts China's efforts to promote more transparent administrative decision-making. We recommend revising this article to state that parties may appeal national security review decisions through China's court system, and to specify either in this law or in follow-up implementing regulations the specific mechanism and level of court that can hear these cases.

**Article 36**
Article 36 states that if an FIE breaches the law, a joint punishment will be carried out. We recommend clarifying what is meant by "joint punishment," what entity will enforce the punishment, and the scope and process for the punishment.

**Article 37**
The principle of reciprocity is a long-established rule of international law, which does not need to be reiterated with respect to foreign investments. The redundancy of Article 37 with those obligations may cause different interpretations when implementing the law. WTO panels are the appropriate forum for international trade disputes. We therefore recommend deleting the language in Article 37.

**Article 38**
While we recognize that the Chinese government may promulgate regulations applicable to foreign investment in specific sectors, we are concerned that such regulations may unfairly and unnecessarily discriminate against foreign investors and hamper China's ability to become a major international financial center. There is no need for rules further restricting foreign investment in specific industry sectors, as the purpose of the negative list is to contain an exhaustive list of such restrictions. Alternatively, the first part of Article 38 should refer to a definite and not an open-ended list of sectors (including banking, securities and insurance and online publishing) in which special provisions applying to foreign investors continue to apply. This would prevent the issue of further rules providing for restrictions on foreign investments in other sectors not covered by the negative list.

We therefore recommend appending a sentence to provide as follows: "Any such regulations shall be based on prudential considerations and impose no non-prudential requirements with the effect of discriminating against foreign invested financial institutions or foreign investment in securities and foreign exchange markets."

**Article 39**
Article 39 stipulates that once the Foreign Investment Law becomes effective, the Chinese-Foreign Equity Joint Ventures Law (EJV Law), the Wholly Foreign-Owned Enterprises Law (WFOE Law), and the Chinese-Foreign Contractual Joint Ventures Law (CJV Law) shall be abolished. However, certain issues remain unaddressed in the draft law, including the approval regime for restricted industries, and the governing law of joint venture contracts. We recommend articulating applicable provisions.

The second clause of Article 39 provides that Foreign-invested enterprises that are established in accordance with the EJV Law, WFOE Law and CJV Law prior to the Foreign Investment Law's implementation may retain their original corporate organizational forms for five years after the implementation of this Law. We propose that this provision be amended to provide that entities established prior to the promulgation of the new law should be grandfathered or that language be added

explicitly stating that investors in established entities may maintain their current corporate forms unchanged. If this is not explicitly allowed, then many existing foreign-invested companies will be forced to renegotiate their joint venture contracts and/or amend their constitutional documents. Allowing existing foreign-invested companies to maintain their current corporate organizational structures will eliminate the uncertainty brought by the mandatory requirement to comply with the company organization rules within five years.

Article 166 of the Company Law, which establishes that 10 percent of after-tax profit must be accrued in a statutory reserve fund, is not compatible with commonly accepted principles of corporate law and undermines companies' flexibility to provide remuneration to shareholders. This creates a disincentive for foreign investors. We recommend continuing the exemption for foreign-invested enterprises from Article 166 of the Company Law (in Article 8 of the EJV Law and Article 76 of the Implementing Rules of the EJV Law), which allow for the thresholds of companies' statutory reserve funds to be determined with the discretion of the companies' boards and shareholders.

USCBC, ACLI, CSI and Insurance Ireland thank the National People's Congress for providing this opportunity to comment on the draft Foreign Investment Law. We hope these comments are constructive and helpful. We would appreciate the opportunity to have further dialogue on these comments and issues, and we would be happy to follow up as appropriate.