

## II. TRADE POLICY REGIME: FRAMEWORK AND OBJECTIVES

### (1) INSTITUTIONAL AND LEGAL FRAMEWORK

1. There have been no major changes to China's institutional and legal framework regarding trade since 2010.<sup>1</sup>

2. Under the 12<sup>th</sup> Five-Year Plan, issued on 16 March 2011, China aims to enhance its administrative efficiency by optimizing its structure, administration layers, and functional responsibilities, and promote the reform of big ministries/departments, with an emphasis on solving the problem of redundant agencies, overlapping competence, and conflicting policies.<sup>2</sup>

3. The WTO Agreements and China's Protocol of Accession are implemented domestically through enabling legislation. Both the Civil Procedure Law and the relevant judicial interpretations accept the principle that, when an international treaty concluded or acceded to by China contains provisions that differ from the provisions of the Civil Procedure Law, the provisions of the international treaty will apply, except for cases in which China has made reservations.

#### (i) Transparency

4. Since its previous Review, China has taken some small steps to improve transparency. The State Council issued a few circulars to direct government agencies at all levels to enhance, *inter alia*, government information disclosures; public consultations for drafting regulations and rules; and administrative reconsideration (appeal).<sup>3</sup>

5. Nonetheless, many aspects of China's trade and investment policy regime remain complex and opaque, leaving scope for administrative discretion and corruption. According to a 2011 Corruption Perception Index, which measures perceptions of corruption among public officials and politicians in 183 countries, China ranked 75<sup>th</sup>, with a score 3.6 out of 10, almost identical to its ranking in 2009.<sup>4</sup>

#### (a) Information dissemination

6. Under the Provisions on the Disclosure of Government Information, which entered into force on 1 May 2008, governments at the central and local levels must: establish the processes for information disclosure; formulate guides and catalogues on the information to be disclosed; and improve the publication of information and systems concerning performance review, public comments, annual reporting, and accountability. Government agencies must disclose, on their own

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<sup>1</sup> The National People's Congress and its Standing Committee exercise legislative power; the State Council, i.e. the Central People's Government, is the executive body of the highest organ of state power and the highest organ of state administration; China's judicial system consists of the Supreme People's Court, the local people's courts at different levels, and special courts such as military, railway, and maritime courts.

<sup>2</sup> The 12<sup>th</sup> Five-Year Plan, Section 1, Chapter 46.

<sup>3</sup> The General Office of the State Council is in charge of guiding and supervising the disclosure of government information. The National Corruption Prevention Bureau, which reports directly to the State Council, is responsible for assuring the transparency of government information at various levels; with a view to preventing corruption, it monitors the flow of suspicious assets and corruption activities. The Legislative Affairs Office of the State Council is responsible for checking coherence of regulations, and carrying out public consultations for draft regulations.

<sup>4</sup> Transparency International online information. Viewed at: <http://cpi.transparency.org/cpi2011/results>.

initiative, information that, *inter alia*: involves the vital interests of citizen, legal persons or other organizations; need to be broadly known to the public; reflects the structure, functions, procedure, and condition related to the administrative agencies; and is required to be disclosed in accordance with other laws and regulations. Such "voluntary" disclosure of information to the public must be conducted within 20 working days from the day the information is formed or revised. Government agencies must respond to disclosure requests from the public within 15-30 working days.<sup>5</sup>

7. The Provisions on the Disclosure of Government Information define government information and a mechanism of related administrative remedies. The Government has identified problems of administrative disclosure including implementation, comprehensiveness of disclosure, procedural problems, and the balance between information disclosure and confidential information.<sup>6</sup> On judicial procedures regarding information disclosure, the Regulations on Trials over Administrative Litigation Cases of Government Information Disclosure, a judicial interpretation of the Supreme People's Court (entered into force on 13 August 2011), stated that the People's Courts must register litigation claiming that the Government did not provide appropriate information in time, in response to the applicant's request.

8. The website of the China Legislative Information Network System, which is maintained by the Legislative Affairs Office of the State Council, publishes mainly the central government's trade-related laws and regulations as well as some trade-related departmental rules by the central governmental agencies, in Chinese. In addition, it provides on-line or off-line links to other agencies and ministries that are responsible for drafts of administrative regulations and departmental rules proposed for public comments; it also has links to local government legislative affairs offices. According to the authorities, all draft administrative regulations have been published on the website for public comments since 2008.<sup>7</sup> In addition, MOFCOM's China Foreign Trade and Economic Gazette publishes China's trade-related laws, regulation, and rules.

9. Neither *ex ante* nor *ex post* economic evaluations of policies and measures (including tax and non-tax incentives) are published, indicating that this form of transparency is not a major feature of China's institutional framework, to the detriment of public accountability and thus governance.

10. Upon accession to the WTO, China established enquiry points and enquiry websites under the Ministry of Commerce (MOFCOM), and the General Administration of Quality Supervision, Inspection and Quarantine (AQSIQ).<sup>8</sup>

(b) Consultations with the private sector, including notice and comment procedures

11. In accordance with the Legislation Law and its relevant regulations<sup>9</sup>, when administrative regulations, rules of the State Council ministries and local governments are drafted<sup>10</sup>, the opinions of

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<sup>5</sup> Article 14 of the Provisions excludes information regarding national security, commercial secrets, and personal privacy.

<sup>6</sup> See the Circular of Opinions on Deepening Administrative Disclosure and Strengthening Administrative Service, issued by the General Office of the State Council on 2 August 2011. Viewed at: [http://www.gov.cn/jrzq/2011-08/02/content\\_1918496.htm](http://www.gov.cn/jrzq/2011-08/02/content_1918496.htm).

<sup>7</sup> WTO document S/C/M/92, 12 December 2008, paragraph 24.

<sup>8</sup> The enquiry points are: <http://sms.mofcom.gov.cn/> (MOFCOM), and <http://www.tbt-sps.gov.cn/sites/english/Contact/Pages/default.aspx> (AQSIQ).

<sup>9</sup> Relevant regulations include the Regulations on Procedures for Formulation of Administrative Regulations (State Council Decree 321), and the Regulation on Procedures for Formulation of Departmental Rules (State Council Decree 322), effective 1 January 2002.

relevant authorities, other organizations, and citizens must be solicited extensively, particularly regarding major issues in the regulations. Consultations may be carried out through symposiums, workshops, "expert" discussion meetings, seminars, and public hearings. If the regulations or rules are "directly involved with immediate interests of citizens, legal persons or other organizations", or if relevant authorities, organizations or citizens have major differing opinions on them, the drafting authority must publish such regulations/rules for public comments; it may also hold public hearings.<sup>11</sup> It would appear that regulatory agencies have discretion to decide whether a hearing is held, whom to invite (e.g. affected foreign parties), and how the hearing is organized.<sup>12</sup>

12. On 10 October 2010, the State Council issued Certain Opinions on Strengthening the Building of a Government Ruling by Law with a view to clarifying obligations of ministries and agencies to solicit public comments on draft administrative regulations and departmental rules. Under the Opinions, administrative agencies at the central and provincial levels must solicit public comments when developing administrative regulations and departmental rules; they are also required to broaden the scope of information disclosure and to enhance administrative reconsideration and litigations. Although, according to the authorities, all draft administrative regulations have been published on the China Legislative Information Network for public comments since 2008, it would appear that not all departmental rules have been published (e.g. on the China Legislative Information Network or on ministry/agency websites) for public comment. The authorities state that "expert hearings" have been conducted for all trade-related laws and regulations in the drafting process. It was not clear to the Secretariat to what extent affected foreign investors were involved in the consultations, or whether proceedings or minutes of the hearings were available to the public.

13. All drafts of trade-related administrative regulations and departmental rules that are published for public comment must provide a comment period of not less than 30 days, subject to exceptions.<sup>13</sup> With some exceptions, regulations and rules enter into force 30 days after promulgation.<sup>14</sup>

14. The authorities maintain that suggestions from the public on legislation are usually sufficiently reflected in drafts of laws and administrative rules. However, according to the OECD, public participation in policy formulation in China is still at a relatively early stage, characterized by informing the public rather than collecting opinions for improving policy making.<sup>15</sup>

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<sup>10</sup> For a more detailed explanation of China's legal structure and legislative process, see WTO (2006), p. 36.

<sup>11</sup> The drafting agencies must give the public a 30-day notice about the date, time, venue, and topics of public hearings. If regulatory agencies, in the process of drafting, do not publish the draft to the public, and do not conduct any public hearing, the legislative organization may seek approval from the corresponding ministry or the government at its corresponding level to publish the drafts, and conduct public hearings. Minutes of the public hearings must be made; and responses to and treatment of comments from public hearing must be explained and justified when the draft rules are sent for verification.

<sup>12</sup> OECD (2009b), p. 103.

<sup>13</sup> Agreement on the 4<sup>th</sup> Sino-US Strategic Economic Dialogue, June 2008. Viewed at: <http://www.america.gov/st/texttrans-english/2008/June/20080619150342xjsnommis0.7032129.html> [3 August 2011].

<sup>14</sup> Regulations and rules that are related to national security, foreign exchange, monetary policies, or whose implementation will be hindered by non-immediate effect, will enter into effect on the day of promulgation. The Legislative Affairs Office of the State Council issued a circular (Guo Fa Han 2002/134) to the legislative affairs agencies of ministries (at the central level) and local governments (at the provincial level) to urge strict adherence to the 30-day notice for all departmental rules/provincial regulations.

<sup>15</sup> OECD (2010b), p. 220.

(c) Appeal procedures

15. In accordance with the Interim Measures Concerning Complaints from Foreign-invested Enterprises<sup>16</sup>, the Complaint Coordination Office for Foreign-invested Enterprises and the National Complaint Centre for Foreign-invested Enterprises under MOFCOM supervise and handle complaints from foreign-invested enterprises that consider their rights have been impaired by the authorities. Data on actual complaints were not made available to the Secretariat.

16. In accordance with the Law on Administrative Reconsideration<sup>17</sup>, any citizens, organs, or other organizations may file appeals with a view to preventing and correcting specific administrative acts that are deemed illegal or improper, within 60 days of the occurrence of the administration action that they believe has damaged their legitimate rights. A pilot programme to establish "administrative reconsideration commissions", which are independent from other government agencies, was launched in 2008 in Beijing, Heilongjiang, Jiangsu, Shandong, Henan, Guangdong, Hainan, and Guizhou.<sup>18</sup>

(ii) Central-provincial relationships

17. The Constitution of China provides that all levels of administration are subordinated to the State Council. It would appear that responsibilities at the sub-national government level are not precisely defined and may differ among provinces.<sup>19</sup> Where the division of responsibilities between the central and local governments is not clear, delegation from the central executive is the most common manner of policy implementation. In effect, China has a shared governance structure that requires continuous negotiations among different levels of government.<sup>20</sup>

18. Laws are passed and enacted by the National People's Congress and its Standing Committee. The State Council promulgates national regulations and policies. For the implementation of laws, regulations, and "national policies", the authorities at the provincial level may enact implementation measures with effect within the local administrative territories. These implementation measures may vary across regions, reflecting the different local interests. The Constitution and other relevant statutes clarify that local regulations must yield before regulations of higher status.<sup>21</sup> The Legal Affairs Office of the State Council reviews local regulations to assure policy coherence.

19. Ministerial-level administrative agencies promulgate administrative rules, which are expected to be applied uniformly nationwide. Implementation and enforcement of national policies and measures are carried out mostly by counterpart agencies of local governments, except for those ministerial agencies that have local branches. Nonetheless, coordination between the agency at the central level and its counterparts at the local level remains weak, raising issues of policy coherence. According to the authorities, higher level agencies tend to use the argument "local yields to central" to solve conflicts.

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<sup>16</sup> MOFCOM Decree 2006/2, effective 1 October 2006 (in Chinese). Viewed at: [http://www.gov.cn/gongbao/content/2007/content\\_494436.htm](http://www.gov.cn/gongbao/content/2007/content_494436.htm).

<sup>17</sup> National People's Congress online information. Viewed at: [http://www.npc.gov.cn/englishnpc/Law/2007-12/11/content\\_1383562.htm](http://www.npc.gov.cn/englishnpc/Law/2007-12/11/content_1383562.htm).

<sup>18</sup> Online information viewed at: [http://news.xinhuanet.com/legal/2008-12/12/content\\_10494653.htm](http://news.xinhuanet.com/legal/2008-12/12/content_10494653.htm).

<sup>19</sup> Yang (2002), p. 333; and OECD (2010c), p. 220.

<sup>20</sup> OECD (2010c), p. 222.

<sup>21</sup> WTO (2006), pp. 34-37.

20. Provincial protectionism may result in barriers to internal trade and investment.<sup>22</sup> Local governments are dependent on revenues produced by their local SOEs and on income generated from economic activities in their local area. On 28 August 2010, the State Council issued a Circular of Opinions on Promotion of Enterprises Restructuring through Mergers and Acquisitions (State Council Circular 2010/27), requiring local authorities to abolish local regulations that hinder cross-province investment activities, in particular cross-provincial mergers and acquisitions. The authorities also state that various programmes, such as reform of the system of transfer payments, have been introduced to reduce inter-provincial trade and investment barriers.

## **(2) DEVELOPMENT AND ADMINISTRATION OF TRADE POLICIES**

### **(i) Main trade laws**

21. China's main laws covering international trade include the Foreign Trade Law, the Customs Law, and the Regulations on Import and Export Tariffs, which contain the tariff schedules, as well as laws and regulations relating to standards, SPS, anti-dumping measures, countervailing and safeguard measures, and intellectual property rights. During the period under review, various trade-related laws, regulations and departmental rules have been adopted or amended covering, *inter alia*, border measures, taxation, competition, and intellectual property protection (Table AII.1); China also abolished a number of trade-related administrative regulations and rules.<sup>23</sup>

### **(ii) Trade policy objectives**

22. China's overall trade policy objective has remained largely unchanged since 2010: to accelerate its opening to the outside world (with a view to introducing foreign technology and know-how); develop foreign trade; and promote sound economic development. Within this overall trade policy objective, the 12<sup>th</sup> Five-Year Plan (covering 2011-15) places emphasis on exports and inward foreign investment but also on imports and outward foreign investment.<sup>24</sup> In this context, China aims to stabilize exports, expand imports, and thus reduce the trade surplus.<sup>25</sup> The authorities intend to achieve this objective through import facilitation measures, as well as further preferential trading agreements.

### **(iii) Agencies involved in trade policy formulation and implementation**

23. Agencies involved in China's trade policy formulation remained unchanged during the review period.<sup>26</sup> The Ministry of Commerce (MOFCOM) has main responsibility for policy coordination and

<sup>22</sup> For a more detailed explanation, see WTO (2006), Box II.2, p. 41.

<sup>23</sup> These include: the Regulation on Administration of Financial Institutions' Trading Spot and Forward Foreign Exchange on Behalf of Clients (promulgated by SAFE on 5 March 1988); the Administration Measures on Foreign Exchanges for Overseas Investments (promulgated by SAFE on 6 March 1989); the Administration Measures on Overseas Financial Institutions (PBC Decree 1990/1); the Interim Measures for the Quota Administration of Import Tariff on Agricultural Products; the Rules on Collection of Fees for International Vehicle Transport of Containers; the Interim Measures for Administration of Highway and Waterway Infrastructure Projects with Foreign Loans; the Interim Measures for Supervision of Exchange Payment and Writing-off for Import Trade; and the Measures for Administration of Agencies for Application of Safety and Quality Licenses for Imported Commodities.

<sup>24</sup> The 12<sup>th</sup> Five-Year Plan, Part XII.

<sup>25</sup> Minister Chen Deming answered journalists' questions at a press conference during the 11<sup>th</sup> National Congress, 7 March 2011. Transcripts viewed at: <http://www.gov.cn/2011lh/zhibo/20110307a.htm> [25 May 2011].

<sup>26</sup> WTO (2010), p. 14.

implementation of all trade-related issues. Also involved in trade policy formulation and implementation are, *inter alia*, the ministries of Agriculture; Environmental Protection; Finance; Industry and Information Technology; Land and Resources; and Transportation, as well as the National Development and Reform Commission (NDRC), which is in charge of overall national economic and social development policy.

24. Several industry associations also collect and share information, identify and deal with problems related to industries, discuss trade policy issues that affect their industries, and represent the interest of their sectors in relation to the Government.<sup>27</sup>

### **(3) TRADE AGREEMENTS AND ARRANGEMENTS**

#### **(i) Participation in the World Trade Organization**

25. China became a WTO Member on 11 December 2001. It is not a signatory to the plurilateral Agreement on Government Procurement (GPA); it submitted a revised offer to join the GPA in December 2011. It is an observer to the Agreement on Trade in Civil Aircraft. China is a participant in the Agreement on Information Technology (ITA); it is not a party to the Pharmaceutical Agreement.

26. The authorities consider that the completion of Doha Round negotiations is important to support the multilateral trading system, and that "only after the Doha Round is completed will Members be confident to engage in in-depth discussions on new issues of the 21<sup>st</sup> century".<sup>28</sup> China emphasizes the importance of respecting the development mandate and the progress made so far.

27. China has submitted a number of notifications during the period under review, including notifications on agriculture, services, technical regulations, regional trade agreements, and intellectual property legislation (Table AII.2). A total of 482 notifications were registered during January 2010 to February 2012, including a new notification on subsidies adopted for 2005-2008. Nonetheless, in some areas (e.g. state trading), notifications are considerably outdated or overdue.

28. In the WTO Dispute Settlement Mechanism, China was involved in 6 cases as a complainant<sup>29</sup>, and 12 as a respondent between 2010 and 2011.<sup>30</sup> In addition, China participated as a third party in 24 disputes during the period under review.<sup>31</sup>

#### **(ii) Regional arrangements**

29. China was a latecomer to regional trade agreements but has become an active participant. It has also enlarged the geographic scope of its agreements. Its earliest agreements were signed with its

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<sup>27</sup> For a list of China's industries associations and chambers of commerce, see MOFCOM online information. Viewed at: <http://english.mofcom.gov.cn/chamberofcomm.shtml>.

<sup>28</sup> WTO document WT/MIN(11)/ST/106: Statement by China's Minister of Commerce at the WTO Ministerial Conference, Eighth Session, Geneva, 15-17 December 2011.

<sup>29</sup> WT/DS379, WT/DS392, WT/DS397, WT/DS399, WT/DS405 and WT/DS422.

<sup>30</sup> WT/DS387, WT/DS388, WT/DS390, WT/DS394, WT/DS395, WT/DS398, WT/DS407, WT/DS413, WT/DS414, WT/DS419, WT/DS425, and WT/DS427. The authorities note that disputes regarding WT/DS387, WT/DS388, and WT/DS390 were settled bilaterally.

<sup>31</sup> WT/DS353, WT/DS369, WT/DS371, WT/DS375, WT/DS376, WT/DS377, WT/DS381, WT/DS384, WT/DS386, WT/DS389, WT/DS391, WT/DS396, WT/DS400, WT/DS401, WT/DS402, WT/DS403, WT/DS404, WT/DS412, WT/DS415, WT/DS416, WT/DS417, WT/DS418, WT/DS421, and WT/DS423.

neighbours (Hong Kong, China; Macao, China; ASEAN; and the Asia Pacific Trade Agreement). It has since moved further afield, negotiating agreements with New Zealand, Chile, Peru, and most recently Costa Rica. Its current negotiations also confirm this broader search for RTA partners (including with the EFTA states, the GCC, India, the Republic of Korea, and SACU). The structure of its agreements has changed, and become deeper over time, as the more recent agreements include commitments in services. As stated in its 12<sup>th</sup> Five-Year Plan, China intends to accelerate the implementation of the Free Trade Area Strategy, strengthen economic linkages with major trading partners, and deepen cooperation with emerging markets and developing countries.

30. The authorities consider that regional trade agreements serve as a complement to the multilateral trading system while China pursues its opening-up policy; in regard to free-trade agreements (FTAs)/regional trade agreements (RTAs), China maintains that it follows the principle of inclusiveness and openness. While in general, the agreements notified by China to the WTO especially under Article XXIV of the GATT 1994 have relatively high tariff line and bilateral import coverage, this is not the case for all its agreements. In its agreements with Chile, Peru, and New Zealand, China commits to eliminate duties on 94.6% to 97.2% of its tariffs, corresponding to 88% to 99.1% of its bilateral imports from these trading partners; however, duties on only 35.4% of its tariffs will be eliminated in the agreement with Pakistan, corresponding to 44.4% of China's imports from Pakistan. That Pakistan has also committed to relatively low levels of tariff elimination in the agreement suggests that China's commitments to eliminate tariffs in its RTAs are based on reciprocity rather than a general policy of openness in its RTAs.

31. China has notified to the WTO its involvement in 11 FTAs/RTAs (Table AII.3).

32. China has concluded two new FTAs since 2009, i.e. the free-trade agreement with Costa Rica (signed April 2010, entered into force August 2011), and the Cross-Straits Economic Cooperation Framework Agreement (ECFA) with Chinese Taipei (signed June 2010, entered into force September 2010). The two agreements were the object of early announcements to the WTO.

33. In addition, China has signed China-ASEAN FTA complementary agreements: the memorandum on strengthening cooperation in standards, technical regulations, and conformity assessment (25 October 2009); the memorandum of understanding on the cooperation in the field of intellectual property (21 December 2009); the agreement on investment (15 August 2009); and the second protocol to amend the agreement on trade in goods (29 October 2010).

34. China has signed supplementary agreements to the Closer Economic Partnership Arrangement between Hong Kong and the Mainland (Hong Kong CEPA) and between Macao and the Mainland (Macao CEPA). Supplementary Agreement VI to Hong Kong CEPA (signed 9 May 2009, effective 1 January 2010); Supplementary Agreement VII to Hong Kong CEPA (signed 27 May 2010, effective 1 January 2011); and Supplementary Agreement VIII to Hong Kong CEPA (signed 13 December 2011, effective 1 April 2012); Supplementary Agreement VI to Macao CEPA (signed 11 May 2009, effective 1 January 2010); Supplementary Agreement VII to Macao CEPA (signed 28 May 2010, effective 1 January 2011); and Supplementary Agreement VIII to Macao CEPA (signed 17 December 2011, effective 1 April 2012).

35. China is pursuing negotiations or undertaking joint-studies on possible RTAs/FTAs with: Australia; Norway; Switzerland; Iceland; the Gulf Co-operation Council (GCC); India; the Republic of Korea; SACU (individually); and the Republic of Korea and Japan (for a future tripartite agreement).

36. China has been a member of APEC since 1991. In 2011, 64.3% of China's merchandise imports were from APEC members, and 61.3% of its merchandise exports went to them. China has been a member of ASEM since 1996.

**(iii) Unilateral preferences**

37. As of 1 January 2011, unilateral preferential tariffs on 60% of products (in terms of national tariff lines) were offered to 36 least developed countries (LDCs).<sup>32</sup> On 1 January 2012, Niger and Somalia were offered similar treatment.<sup>33</sup> According to the authorities, about 90% of tariffs (in terms of national tariff lines) on imports from Lao PDR, Cambodia, and Myanmar have been eliminated unilaterally since 1 January 2010 under the China-ASEAN FTA framework.<sup>34</sup> During the Eighth WTO Ministerial Conference, China indicated that it would reduce tariffs to zero on 97% of imports (in terms of national tariff lines) from LDCs that have diplomatic ties with China.<sup>35</sup>

**(4) FOREIGN INVESTMENT REGIME**

**(i) Recent developments in FDI policy**

38. In 2010 (the latest year for which data are available), China was the world's third largest recipient of FDI after the EU and the United States.<sup>36</sup> China has been "encouraging" inward FDI, mainly in manufacturing, with particular emphasis on high-value-added production and new technology, and in certain services such as telecommunications, tourism, "modern" logistics, and service outsourcing. On 1 January 2008, China eliminated preferential treatment to FDI projects in regard to the enterprise income tax, except for some "grandfathering" of incentives during a five-year transition period. Since 1 December 2010, foreign enterprises pay urban maintenance and construction tax and education levies at the same rates as domestic enterprises.<sup>37</sup>

39. Since 1 January 2011, foreign investors have been "permitted" to invest in health care services in China on a pilot-project basis; previously, they were listed in the "restricted" category.<sup>38</sup>

<sup>32</sup> Online information. Viewed at: [http://www.gov.cn/zwqk/2010-06/24/content\\_1635985.htm](http://www.gov.cn/zwqk/2010-06/24/content_1635985.htm).

<sup>33</sup> Tariffs on some imports from Niger and Somalia were already zero-rated.

<sup>34</sup> An FTA between China and "old members" of ASEAN, i.e. Brunei, Indonesia, Malaysia, Philippines, Singapore, and Thailand was fully implemented on 1 January 2010, whereas the FTA between China and "newer members", i.e. Cambodia, Lao PDR, Myanmar, and Viet Nam is to be fully implemented on 1 January 2015 (WTO document WT/COMTD/51, 21 December 2004).

<sup>35</sup> WTO document WT/MIN(11)/ST/106: Statement by China's Minister of Commerce at the WTO Ministerial Conference, Eighth Session, Geneva, 15-17 December 2011.

<sup>36</sup> UNCTAD (2011).

<sup>37</sup> State Council Circular on Unifying the Urban Maintenance & Construction Tax, and Education Levies between Domestic and Foreign Enterprises (State Council Circular 2010/35, 18 October 2010).

<sup>38</sup> The General Office of the State Council Circular on Several Opinions on Further Encouraging and Guiding Social Capital to Invest in Healthcare Sector, 26 November 2010, "encourages" foreign investment to establish joint-venture healthcare institutions (either equity or contractual), and the equity share ceiling is to be removed gradually. A pilot programme of wholly foreign-owned healthcare institutions is being carried out. As of 1 January 2011, healthcare service providers from the Hong Kong SAR and the Macao SAR have been allowed to set up wholly owned hospitals in Shanghai, Chongqing, Guangdong, Fujian, and Hainan, and wholly owned care homes in Guangdong. Service providers from Chinese Taipei have been allowed to set up wholly owned hospitals in Shanghai, Jiangsu, Guangdong, Fujian, and Hainan. Foreign-invested healthcare institutions may set up as profitable or non-profit organizations.



40. A revised *Catalogue for the Guidance of Foreign Investment Industries* (2011 version), which entered into force on 30 January 2012, added 44 subsectors and projects (e.g. services for intellectual property right protection, services of marine oil pollution clean-up technology, and new-energy automobiles) to the "encouraged" category, whereas 41 subsectors and projects (e.g. manufacturing of complete automobiles, and of polysilicon) were removed from the "encouraged" category. The authorities noted that the foreign equity share ceiling for 11 subsectors in the "encouraged" and "restricted" categories were also removed on 30 January 2012.

41. Since 6 April 2010, the Government has encouraged foreign-invested enterprises (FIEs) in joint ventures with Chinese enterprises or research institutes to participate in government-funded projects under the "national technology development programme" and the "innovation capacity-building programme".<sup>39</sup> The national technology development programme and the innovation capacity-building programme are subsidy programmes managed by NDRC with the aim of promoting innovation. The programmes are open to enterprises and research institutes. Upon approval of projects put forward by enterprises, NDRC grants subsidies that partially cover the cost of innovation activities. Since 31 August 2010, some manufacturing subsectors (e.g. textiles and apparel, toys, and domestic appliances) and banking services in the central and western regions have been classified as "encouraged", in accordance with the State Council's Guiding Opinions on Central and Western Regions' Receipt of Industrial Transfers.<sup>40</sup> This reclassification will be reflected in the next revision of the Catalogue of Advantaged Industries for Foreign Investment in Central-Western China.

42. The Government intends to increase decentralization and simplify verification procedures for foreign investment. Since 4 May 2010, provincial authorities have been delegated to approve certain FDI projects below US\$300 million (previously US\$100 million).<sup>41</sup> Since 14 February 2011, outward FDI below US\$300 million in natural resources, and below US\$100 million in non-natural resources may be approved by the authorities at the provincial level, except, *inter alia*, for projects on basic telecom network operation, cross-border hydro power development, large-scale agricultural development, major power grid, and news media. Previously, all outward FDI projects had to be verified and approved by the NDRC, in accordance with the Interim Measures for Administration on Examination and Approval of Overseas Investment Projects.

43. With a view to clarifying the procedures and scope of anti-trust reviews and national security reviews on M&A activities involving FDI, detailed measures for national security reviews over foreign mergers and acquisitions<sup>42</sup>, and a guideline for impact assessment of anti-trust reviews<sup>43</sup>, entered into force in September 2011.

## (ii) Regulatory framework

44. Main laws and regulations specifically related to FDI in China remained unchanged during the period under review. They include: the Law on Chinese-Foreign Equity Joint Ventures, the Law on Chinese-Foreign Contractual Joint Ventures, the Law on Foreign-Capital Enterprises, and the Law on Partnership Enterprises, and their implementing regulations. Under these laws, FIEs include

<sup>39</sup> Certain Opinions on Further Improving the Use of Foreign Capital (State Council's Circular 2010/9).

<sup>40</sup> State Council Circular 2010/28, 31 August 2010.

<sup>41</sup> See Certain Opinions on Further Improving the Use of Foreign Capital (State Council Circular 2010/9).

<sup>42</sup> MOFCOM Provisions on National Security Review over Acquisitions of Domestic Enterprises by Foreign Investors, 1 September 2011.

<sup>43</sup> The Interim Provisions on the Assessment of the Impact of Concentration of Undertakings on Competition, 5 September 2011.

equity joint ventures (with foreign investment no less than 25% of registered capital), contractual joint ventures and wholly foreign-owned enterprises, participation in partnership enterprises<sup>44</sup>, and mergers and acquisitions of Chinese domestic enterprises. The authorities noted that foreign investors may also be allowed to own some shares in state-controlled enterprises in certain sectors.<sup>45</sup>

45. The Provisions on Guiding Foreign Investment Direction classify foreign investment projects into four categories: encouraged, permitted, restricted, and prohibited.<sup>46</sup> The current *Catalogue for the Guidance of Foreign Investment Industries*, which entered into force on 30 January 2012, lists industries that are encouraged, restricted, and prohibited<sup>47</sup>; projects that do not fall into these three groups are "permitted".

46. The authorities intend to promote FDI in the central-western region of China. To this purpose, all sectors listed in the Catalogue of Advantaged Industries for Foreign Investment in Central-Western China are "encouraged"; thus, preferential policies towards "encouraged" sectors are applied to all sectors, notably labour-intensive sectors, in this catalogue. Tax incentives are in place for FDIs investing in the central-western region.<sup>48</sup> The current Catalogue entered into force on 1 January 2009. Processing trade in central-western region is also encouraged by special customs supervision zones or bonded warehousing.<sup>49</sup>

47. In general, projects in the encouraged category are those that use improved technology and are less polluting<sup>50</sup>, while "restricted", and "prohibited" projects employ outdated technologies, over-exploit scarce natural resources, and tend to harm the environment. Foreign equity limits tend to be intricate and vary by industry, and are not necessarily related to the category.

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<sup>44</sup> Detailed regulations are contained in Measures of Management of Partnership Enterprises Established by Foreign Investors within the Territory of China, State Council Decree 567, effective 1 March 2010.

<sup>45</sup> State-controlled enterprises are enterprises in which the State, or another state-owned enterprise (SOE), holds more than 50% of equity; or, if the equity share is less than 50%, the State or another SOE has controlling influence on its management and operation.

<sup>46</sup> Provisions on Guiding Foreign Investment Direction. Viewed at: [http://english.gov.cn/laws/2005-07/25/content\\_16873.htm](http://english.gov.cn/laws/2005-07/25/content_16873.htm) [11 February 2008].

<sup>47</sup> The *Catalogue for the Guidance of Foreign Investment Industries* is formulated based on the *Catalogue of Guiding Industry Structure Adjustment*. The latest version of the latter entered into force on 1 June 2011.

<sup>48</sup> Certain Opinions on Further Improving the Use of Foreign Capital (State Council Circular 2010/9), Section 2, Point 8 and Point 9.

<sup>49</sup> See the State Council's Guiding Opinions on Central and Western Regions' Receipt of Industrial Transfers (State Council Circular 2010/28, 31 August 2010).

<sup>50</sup> Encouraged industries include: projects to develop new agriculture technologies and agriculture, or to develop energy, transportation or important raw material industries; those for high and new technologies, or advanced application of technologies to improve product quality, increase technology efficiency, or produce new equipment or new materials that cannot be produced domestically; those helping to meet domestic and export market demand; those adopting new technology or equipment for saving energy and raw materials; and those making full use of human and natural resources in central and western parts of China. Restricted industries include: those that use outdated technology, or do not favour resource-conservation and the environment; those using resources protected by law or regulations; and "industries that shall be opened gradually". Prohibited industries include: those that endanger the safety of the State or damage social and public interests; those that pollute the environment, destroy natural resources or impair human health; those that occupy large amounts of arable land, or are unfavourable to protection and development of land resources; those that endanger the safety of military facilities and their performance; and those that use Chinese craftsmanship or technology to make products.

48. FIEs in the encouraged category may import capital equipment duty free. All foreign-invested enterprises may enlarge their scope of business, subject to approval. Foreign investment in the restricted category may be permitted, subject to approval, if export sales are over 70% of total sales of the product.<sup>51</sup>

**(iii) Examination and approval procedure**

49. FDI in "important or restricted" projects<sup>52</sup> requires verification by the authorities, as stipulated in the Decision on Reforming the Investment System and the Catalogue of Investment Projects Requiring Government Verification (issued by the State Council), which includes non-government-funded, important or restricted fixed-asset investment projects, in several industries or sectors.<sup>53</sup> All other investment projects, irrespective of the amount of investment, need to be registered only with the relevant authorities, such as the local development and reform commissions (DRCs).

50. The main regulations for FDI in "important or restricted" projects, the Interim Measures for the Administration of Examining and Verifying Foreign Investment Projects, based on the Decision and on the Administrative Permission Law, stipulate examination and approval procedures for FDI in China.<sup>54</sup> To establish an FIE in such projects, applications must be submitted for examination and verification to the NDRC, or to other government agencies, such as the local DRCs.

51. Projects valued at US\$300 million or more (for FDI projects approved as of 4 May 2010 and after, compared with US\$100 million previously) for encouraged and permitted sectors (US\$50 million for restricted industries) must be verified by the NDRC or other relevant agencies (e.g. industry regulators) at the national level; projects below these thresholds may be verified and approved by local DRCs.<sup>55</sup> Applications for permitted and encouraged industries valued at over US\$500 million (US\$100 million for restricted industries), after examination by the NDRC, are submitted for verification to the State Council. The NDRC must complete its examination and verification within 20 working days after accepting the application; this may be extended by 10 working days if it is difficult to reach a decision (the project applicant is informed of the delay). The NDRC examines and verifies FDI applications against, *inter alia*, the following provisions: relevant laws and regulations; the *Catalogue for the Guidance of Foreign Investment Industries*; the *Catalogue of Advantaged Industries for Foreign Investment in Central-Western China*; the medium-and long-term development plan for national economy and society (the five-year plans); policies related to industry planning and restructuring; public interests and competition provisions; land-use planning, city planning, and environment protection policies; national standards; and rules on capital account management and foreign debt management.<sup>56</sup>

<sup>51</sup> The authorities note that this is not common.

<sup>52</sup> The authorities note that these restricted sectors are listed in the restricted category in the *Catalogue of Guiding Industry Structure Adjustment* and the *Catalogue for the Guidance of Foreign Investment Industries*.

<sup>53</sup> These include: agriculture and forestry; energy; transportation; information technology; raw materials; manufacturing; light industry and tobacco; high and new technology; urban infrastructure; social projects (including tourism), and financial services.

<sup>54</sup> These measures apply to Chinese-foreign contractual joint ventures, Chinese-foreign equity joint ventures, wholly foreign-owned enterprises, mergers between enterprises, acquisitions of domestic enterprises by foreign investors, and increases in capital of foreign-owned enterprises.

<sup>55</sup> The power to verify restricted industries may not be delegated to a department below provincial DRC level. For projects of more than US\$30 million involving FDI, local governments must submit a copy of the examination and verification document to the NDRC within 20 working days.

<sup>56</sup> Provisions in the Interim Measures for the Administration of Verification and Authorization of Foreign Investment Project (NDRC decree No. 2004/22), entered into force on 9 October 2004.

52. In addition, FIEs (excluding in the financial sector) seeking to establish in China must submit an application simultaneously to MOFCOM or local commercial departments<sup>57</sup>, for an FIE Approval Certificate. This allows the FIE to complete all the other procedures necessary to commence operations, such as registration of the enterprise.

53. Foreign investment in China can be made in renminbi (RMB). Except for investments valued at ¥300 million or more or in industries that require approval from MOFCOM, the authorities at the provincial level may complete the approval procedure similar to that for investment in foreign currencies. Foreign investments with RMB are not allowed "directly or indirectly" in equities and financial derivatives, except those used for strategic investment in listed companies.

54. The authorities state that there are no restrictions on lending by domestic banks to foreign-invested enterprises.

55. FDI in the form of mergers and acquisitions (M&As) of enterprises is subject to anti-trust reviews, as per the Anti-Monopoly Law.<sup>58</sup> Anti-trust reviews are intended to assess the influences on market competition of M&A operations. In addition to anti-trust reviews, FDI involving M&A with Chinese domestic enterprises is subject to national security reviews, if the FDI is related to defence, or is deemed to have influence on national security, such as controlling firms engaged in key commodities (e.g. agriculture, energy, and natural resources), key infrastructures, key transports, and key equipment manufacturing with essential technologies. Anti-trust reviews and national security reviews are to be completed within a defined time-frame (Chapter III(3)(vi)). In the period 2008-2011, MOFCOM reviewed 382 cases, of which 371 were unconditionally cleared, 10 were cleared subject to conditions, and 1 case was rejected.<sup>59</sup>

56. The Government encourages the development of foreign-invested high-tech enterprises<sup>60</sup>, as well as R&D cooperation between domestic and foreign enterprises. It supports eligible foreign-invested enterprises, jointly with domestic enterprises and research institutes, to apply for government funded/sponsored R&D projects, innovation capacity-building projects, and authentication of national technology centres. The authorities maintain that there are no mandatory requirements for technology transfer associated with FDI approval. Eligible foreign-invested R&D centres were exempted from duties, value-added tax, and consumption tax on imported inputs needed

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<sup>57</sup> Projects valued at US\$300 million or more in the encouraged or permitted sectors (and US\$50 million for restricted industries) are approved by MOFCOM. Projects valued below the threshold are approved by the commercial departments at the provincial level (since 10 June 2010).

<sup>58</sup> Administrative regulations with regard to FDI involving M&As include: the Provision on Mergers and Acquisition of Domestic Enterprises by Foreign Investors; Measures on the Examination of Concentration of Undertakings; Measures on the Notification of Concentration of Undertakings (entered into force in January 2010); and Provisions on National Security Review over Acquisitions of Domestic Enterprises by Foreign Investors (entered into force on 1 September 2011).

<sup>59</sup> The M&A case rejected by MOFCOM concerned an application by Coca Cola to merge with Hui Yuan. For details see MOFCOM Announcement 2009/22 (in Chinese). Viewed at: <http://fldj.mofcom.gov.cn/aarticle/ztxx/200903/20090306108494.html>.

<sup>60</sup> Authentic high-tech enterprises may be granted preferential tax treatment, such as enterprise income tax exemption or reduction, within the validity of high-tech enterprise status. Any enterprise registered in China for longer than one year may apply for authentication as a high-tech enterprise; the status of high-tech enterprise is valid for three years, and may be renewed. Six conditions must be met including, products (or services) supplied by the enterprises must be on the list of High-Tech Fields with Essential Support by the State; and the authentic high-tech enterprises must possess "self-owned" intellectual property rights over the "core technology" acquired through in-house R&D, transfer or gift, M&A operation, or exclusive licence for more than 5 years.

for R&D consumables before 31 December 2010. Nonetheless, concerns have been raised about *de facto* technology transfer requirements on foreign investment projects, e.g. in the new-energy automotive sector.<sup>61</sup> The authorities maintain that China currently has no measures that impose technology transfer requirements; preferences may be accorded to innovators depending on whether the relevant technology is domestically owned or licensed by foreign investors. China plans to conduct studies between 2012 and 2013 on whether to continue these measures.

57. The State Council supports FIEs to be listed, and/or to issue corporate bonds on Chinese market. It also continues to "guide" financial institutions to enhance credit supports to FIEs. At the time of this review, details of measures were not available to the Secretariat.

**(iv) Bilateral investment treaties**

58. China had signed 131 bilateral investment agreements by the end of December 2011.<sup>62</sup> Between 2010 and 2011, China concluded bilateral investment agreements with Chad, Libya, Uzbekistan, and Congo (DRC).<sup>63</sup>

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<sup>61</sup> WTO documents G/L/977, 16 November 2011; and IP/C/60, 17 November 2011.

<sup>62</sup> UNCTAD International Investment Agreement Database. Viewed at: <http://www.unctad.org/Templates/Page.asp?intItemID=2339&lang=1> [01.12.2011].

<sup>63</sup> Investment treaties with France and Switzerland entered into force in 2010. The three newly concluded investment treaties have not yet entered into force.