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A new dimension of foreign investment law in China – evolution and impacts of the national security review system

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ABSTRACT

This article discusses the evolutional trajectory of China's national security review system (NSRS) and its potential impacts on inward foreign investment. By analysing the law-making process as well as merger cases of major significance, this article explores the emergence of China's NSRS in 2003, followed by its decade long (2006–2015) legal construction. The formation process of the NSRS that has evolved from interim administrative regulations to national law complies with the pragmatic, incremental character of the law-making in China in general. The key features of the NSRS provided in the 2015 draft Foreign Investment Law (FIL) is examined in detail to demonstrate the legislative headway as well as room for further refinement. In response to the ongoing concerns on the potential impacts of the NSRS on future foreign investment in China, this article attempts to argue that China's newly established NSRS, set forth in Chapter 4 of the draft FIL, is an anticipated and rational outcome, though further modification of the relevant provisions in the final text of the FIL could be expected. While the NSRS might cause rejection or delay of approval to some foreign investment projects, the clarified and delineated NSRS offers greater legal certainty and predictability. In view of China's continuous and adamant policies of attracting foreign direct investment (FDI), the NSRS is unlikely to have a significant impact on most foreign investment projects in the future.

KEYWORDS

National security review system; draft Foreign Investment Law in China; mergers and acquisitions; foreign direct investment

I. Introduction

In January 2015, the Ministry of Commerce of the People's Republic of China (MOFCOM) published a draft version of the Foreign Investment Law (FIL) for public comment.[1] Chapter 4 of the draft FIL reasserts that China will apply a national security

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[1] Foreign Investment Law of the People's Republic of China (Draft) (中華人民共和國外國投資法) (草案徵求意見稿) (Issued by MOFCOM on 19 January 2015) (hereafter 'Draft FIL'). The (unofficial) English translation of the full text of the draft FIL can be found on Wolters Kluwer, China Law & Reference, Foreign Investment Law of People's Republic of China (Exposure Draft) <http://law.wkinfo.com.cn/document/show?aid=MTAxMDAxMTMzMjY%3D&bid=&collection=legislation&language=%E4%B8%AD%E6%96%87&tokens=a024ea63d5a6062aa9aabc42f41721e9&modules=&showType=1> accessed 15 April 2016.

review system (NSRS) to all foreign investment that infringes or may infringe upon national security.[2] Once effective, the FIL will establish for the first time the national security review mechanism on the national law level,[3] though the embryo of the national security review occurred in 2003, which has later evolved over one decade from 2006 till 2015.

Notably, national security has been an issue addressed in several recently promulgated legislations. For instance, in July 2015, the Standing Committee of the National People's Congress promulgated the State Security Law, which includes the definition of state security, the tasks and duties of safeguarding state security, the establishment of a state security framework, the assurance of state security, etc.[4] Article 59 of the State Security Law particularly proposes to establish a state security review and oversight mechanism with regard to foreign investment, specific items, key technologies, network information technology products, etc. In November 2015, the Seed Law was revised and promulgated by the Standing Committee of the National People's Congress.[5] Analogously, Article 62 of the Seed Law proposes the establishment of a review system concerning foreign investment in the seed industry, which conforms to the NSRS stipulated in the draft FIL since agricultural security is codified as one of its considerations. Furthermore, in July 2016, the Standing Committee of the National People's Congress promulgated the Cyber Security Law (2nd Review Draft) for public comment, in which the term 'national security' is mentioned five times.[6] The purpose of the Cyber Security Law is to guarantee cyber security, national security, public interests, etc., which means cyber security is elevated to a salient position equivalent to national security.[7] This new draft law has invoked 46 business groups in the U.S.A., Europe and Asia to complain that if implemented 'would weaken security and separate China from the global digital economy'.[8] The ever increasing national security concerns reflected in these legislations demonstrate the consistency as well as the persistency of China's stance towards a comprehensive protection of its national security.

This article focuses on the NSRS stipulated in the draft FIL. Chapter 4 of the draft FIL radically alters China's national security review regime. First, according to the draft FIL, all foreign investment in China, including greenfield investment, mergers and acquisitions (M&As) and indirect investment, will be subject to a national security review, while only inward M&As in China have been subject to such censorship under the current legal framework. Second, the sectors subject to review have been confined to military

[2] Draft FIL (n 1) art 48.

[3] National law in China's legal system refers to law which is exclusively promulgated by the National People's Congress of the People's Republic of China and its Standing Committee. The national law has the supreme legal authority in the hierarchy of the Chinese legal system.

[4] State Security Law of the People's Republic of China (中華人民共和國國家安全法) (Promulgated by the Standing Committee of the National People's Congress on 1 July 2015, effective immediately). For a more detailed discussion on the State Security Law, see Zhou Yezhong and Pang Yuanfu, 'State Security Law, Patterns, Systems and Principles' (2016) 43(3) Journal of Sichuan Normal University (Social Science Edition) (周葉中、龐遠福, '論國家安全法：模式、體系與原則', 《四川師範大學學報(社會科學版)》, 2016 年第43(3)期).

[5] Seed Law of the People's Republic of China (2015 Revision) (中華人民共和國種子法) (2015修訂) (Promulgated by the Standing Committee of the National People's Congress on 4 November 2015, effective on 1 January 2016).

[6] The Cyber Security Law of the People's Republic of China) (Second Review Draft) (中華人民共和國網絡安全法) (草案二次審議稿) (Promulgated by the Standing Committee of the National People's Congress on 6 July 2016).

[7] Ibid art 1.

[8] Joe McDonald, 'Business Groups Appeal to China over Cybersecurity Law' <http://www.usnews.com/news/business/articles/2016-08-11/business-groups-appeal-to-china-over-cybersecurity-law> accessed 19 August 2016.

industry, agriculture, resources, infrastructure, transportation, key technology and major manufacturing, while the draft FIL expands the sectors subject to review to any foreign investment, as long as it is deemed a potential threat to national security.[9] And finally, the number of criteria for evaluation during a national security review has increased from four to 11 in the draft FIL, which means there will be more factors to be taken into consideration.[10] Hence, it appears that the draft FIL would substantially broaden the scope of China's NSRS. Such expansion of reference may facilitate the clarification of benchmarks to be used and enhance the transparency of the review process, it may also increase the susceptibility of arbitrary abuse.

While it still remains to be seen how such a security review regime will be designed in the final version of the FIL, much light has been shed on the language of the draft itself. Critiques indicate that the regulatory ambivalence and inconsistency, as well as the excessive generalisation of a mechanism as such would inevitably and significantly increase the unpredictability and uncertainty of China's foreign direct investment (FDI) regulatory regime that is already considered to be non-transparent and cumbersome; and such a NSRS is susceptible to be abused by the Chinese authorities based on political or even retributive considerations, rather than sheer national security reasons. As a result, a new NSRS would possibly become a regulatory hurdle to be feared by foreign investors who wish to enter the capital market in sensitive or strategic sectors.[11]

Contrary to the aforementioned criticism, this article contends that China's newly established national security review regime set forth in Chapter 4 of the draft FIL is rational, justifiable and a reflection of international practice; it will have a rather insignificant impact on most of the future inward FDI. Hence, the potential negative effects of such a review system are limited. To substantiate these contentions, the rest of this article is arranged as follows: section II explores the emergence of China's NSRS in 2003, followed by its decade long (2006–2015) legal construction in the context of inbound FDI; section III delves into the key features of the NSRS provided in the draft FIL, and some necessary refinements to be made to the final FIL; section IV assesses the potential impact of the NSRS on future incoming foreign investment and contends that any impact will be minor and not significant; this article ends with a concluding remark in section V.

II. The emergence and evolution of China's NSRS

A. The expansion of FDI and its accompanying national security concerns

China's FDI policies have always been a combination of attracting FDI by providing various incentives at different times on the one hand, and variable control and restrictions of FDI on the other hand. This has resulted in the dual-track legal regime where foreign and domestic

[9] Draft FIL (n 1) art 48.
[10] Ibid art 57.
[11] Shai Oster, 'China Fuels Concern for Planning Tougher Security Reviews' *Bloomberg Business* (10 February 2015) <http://www.bloomberg.com/news/articles/2015-02-10/china-s-plan-to-toughen-national-security-review-fuels-concerns> accessed 11 March 2016. See also, Chris Russell (additional research by Georgie Barber), 'Rules of the Game, Changes in China's Foreign Investment Law' *CKGSB Knowledge* (25 June 2015) <http://knowledge.ckgsb.edu.cn/2015/06/25/finance-and-investment/rules-of-the-game-changes-in-chinas-foreign-investment-law/> accessed 20 March 2016.

investments are separately regulated. Foreign investment is subject to a case-by-case approval by the central or local authorities in accordance with the size of the investment. Prior to China's admission to the World Trade Organisation (WTO) in 2001, policymakers in China did not pay specific attention to national security or economic security in the context of FDI. This was mainly due to the fact that China was at an initial stage of attracting FDI in large quantities, expecting to acquire advanced industrial technology and managerial expertise from western economies at the cost of domestic market share. Furthermore, due to the case-by-case examination and approval system for all inbound FDI in general, the necessity for a national security review was not recognised.

Three significant developments in the post-WTO period have precipitated the incremental introduction of a national security review regime vetting incoming foreign investment projects in China: the swift increase of FDI in China in the post-WTO period; the expansion of M&As of Chinese enterprises by foreign investors; and the failed attempts of China's outbound investment thwarted by national security implications in the recipient countries.

First, China promised to liberalise its FDI regulatory regime as part of its WTO accession commitments. In order to implement these commitments, the Chinese government revised existing laws and promulgated new laws to simplify the approval process of FDI as well as to open its domestic market to more sectors, especially the service sector, to foreign investors, which has resulted in the drastic expansion of inward FDI. For instance, according to Chart 1, in the first decade since the commencement of China's economic reform and opening-up policies from 1979 to 1988, the amount of FDI China received was 12.5 billion USD. In 1999, the value increased to about 40 billion USD. In 2002, the amount jumped to 52.7 billion USD. Since then the annual FDI inflow has been continually increasing, in 2010, it reached 105.7 billion USD. After a decade since China's accession to the WTO, the annual amount of FDI inflow in China has doubled.

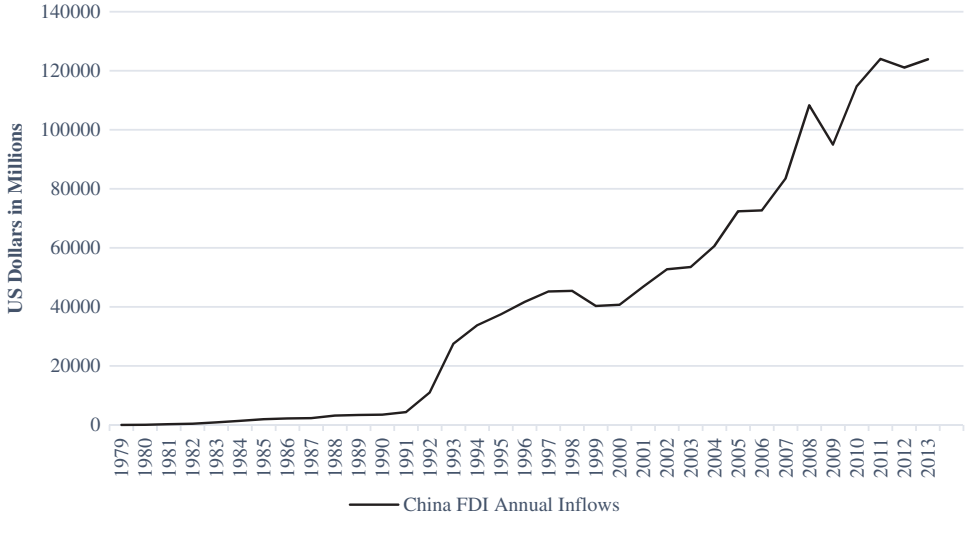

Chart 1. Annual FDI inflow in China, 1979–2013.

UNCTAD Statistics, Foreign Direct Investment – Inward and Outward FDI Stock, Annual, 1970–2013 <http://unctadstat.unctad.org/wds/fViewer/tableView.aspx> accessed 11 March 2016.

Accompanied by the dramatic proliferation of the amount of FDI in China, the form of FDI in China has also changed. Since 1979, China has implemented its three primary FILs, namely the Sino-Foreign Equity Joint Venture Law, the Sino-Foreign Cooperative Joint Venture Law and the Wholly Foreign-Owned Enterprise Law.[12] These laws focus on the regulation of greenfield investment as the main form of FDI in China. However, from the beginning of the 21st century, merger and acquisition activities, including both domestic and cross-border, inbound and outbound, have significantly increased. For the period of 2000–2010 such an increase in M&A transition values was almost parallel to that of utilised FDI.[13] The announced M&A deals (including both domestic and cross-border M&As) and their total values for the period of 2000–2010 are illustrated in Table 1 which shows that in 2000, there were only 250 M&A deals but the number jumped to 2409 in 2010; almost a ten-fold increase. With regard to the transition value, it increased from about 47 billion USD in 2000 to 193 billion USD in 2010, an increase of four times.

Furthermore, takeovers of Chinese indigenous companies conducted by foreign investors in the last decade from 2000 to 2010 has accounted for 23% of all M&A transactions that took place in mainland China, which is illustrated below in Table 2. Propelled by the fifth global M&A wave that commenced in the early 90's and peaked in the year 2000, a dramatic surge in cross-border M&A deals in China was observed in 2003, and a continuous increase has been witnessed until 2012, when cross-border M&As took approximately 8.8%

Table 1. Announced M&A deals and transaction values in mainland China, 2000–2010.

Year	Number of deals	Transaction values (in millions USD)	Year	Number of deals	Transaction values (in millions USD)
2000	250	47,430	2006	1304	60,471
2001	305	12,806	2007	1841	128,464
2002	580	30,350	2008	1978	155,895
2003	1014	32,262	2009	1925	150,845
2004	1404	31,001	2010	2409	19,3218
2005	1117	70,729	2000–2010 total	14,127	913,471

Only transactions of one million USD or higher are included. Tang and Metwalli (n 13) 30–31 (quoting from Thomson Reuters Financial Service, which is considered as the most comprehensive, authoritative and up-to-date source of M&A transactions).

Table 2. Composition of domestic and cross-border M&As in mainland China, 2000–2010.

Type of transactions	M&A value (millions USD)	Percentage
Mainland Chinese firms acquiring other mainland Chinese firms	621,441	59%
Mainland Chinese firms acquiring non-mainland Chinese companies	193,212	18%
Non-mainland Chinese firms acquiring mainland Chinese companies	244,217	23%
Total	1,058,870	100%

Tang and Metwalli (n 13) 39.

[12] Law of the People's Republic of China on Chinese-Foreign Equity Joint Ventures (中華人民共和國中外合資經營企業法) (Promulgated by the Standing Committee of the National People's Congress on 8 July 1979, effective immediately); Law of the People's Republic of China on Sino-Foreign Contractual Joint Ventures (中華人民共和國中外合作經營企業法) (Promulgated by the Standing Committee of the National People's Congress on 13 April 1988, effective immediately); Law of the People's Republic of China on Wholly Foreign-Owned Enterprises (中華人民共和國外資企業法) (Promulgated by the Standing Committee of the National People's Congress on 12 April 1986, effective immediately).

[13] Roger Y W Tang and AliM Metwalli, 'M&A in Greater China: An Update' (2012) 23(2) Journal of Corporate Accounting & Finance 39–40.

of total FDI inflows in China.[14] In comparison, cross-border M&As in China in 1990 recorded eight million USD, taking only 0.22% of the total FDI inflows in China that year.[15]

While the takeovers of Chinese companies by foreign investors bring about positive effects such as liquidising remnant assets of State-Owned Enterprises (SOEs), promoting innovative technology and introducing advanced managerial expertise to Chinese companies, there are also increased fears that under-regulated M&As will result to foreign monopolies, unemployment of Chinese workers, environmental destruction and the sell-out of state assets.[16] Specifically, since 2000, several world-renowned multinational enterprises (MNEs) have successfully acquired Chinese corporate champions, large-scale enterprises and State-owned listed companies, resulting in monopolies of foreign capital in sectors such as heavy machinery manufacturing, integrated circuit manufacturing and petrochemical equipment production; the debilitation of research and development (R&D) and independent innovating capacity of indigenous Chinese firms, as well as the dropout of Chinese national brands and Chinese time-honoured brands.[17] As a result, some of these M&A projects have influenced the government policy on restricting foreign investment for national security concerns.

Last but not least, several highly publicised Chinese outbound investment projects were blocked by the national security review regimes in the U.S.A., Australia and the U.K. in recent years, which may have incentivised the Chinese government to consider introducing a similar alternative as a countermeasure to protect China's national security.[18] Specifically, commentators speculate that China's gradually tougher stance on cross-border M&A deals may be associated with the failed acquisition of Unocal by China National Offshore Oil Corporation (CNOOC) in June 2005. CNOOC, a Chinese SOE that engages in offshore oil and gas production, offered to acquire Unocal, a U.S.-based MNE, which created unprecedented public debate regarding the proposed acquisition. It also swirled up vehement political opposition in the Congress, that the proposed deal would compromise the domestic oil supply of the U.S.A. and inevitably put the energy security of the U.S.A. at risk.[19] CNOOC did voluntarily apply for a national security review to the Committee on Foreign Investment in the United States (CFIUS), but eventually

[14] The statistic is calculated according to the original data obtained from Zhang Jinxin, 'Report on China's M&A Market 2014' *China Economy Weekly* (9 February 2015) (張金鑫, '2014年中國並購市場報告', 經濟網, 2015年2月9日) <http://www.ceweekly.cn/2015/0209/103894.shtml> accessed 11 March 2016.

[15] Huan Zhou and Paul Simpson, 'Cross-Border Mergers and Acquisitions in China: An Industry Panel Study, 1991–2005' (2008) 14(4) Asia Pacific Business Review 492.

[16] Cathleen Hamel Hartge, 'China's National Security Review: Motivations and the Implications for Investors' (2013) 49(1) Standford Journal of International Law 245.

[17] To name but a few, these acquisitions include: Alcatel-Lucent (French based) acquiring Shanghai Beier (a Chinese SOE); Emerson Electric Company (U.S. based) acquiring Ansheng Electric Company (a well-known Chinese private company); American Aviation LDC (U.S. based) acquiring Hainan Airlines (a well-known Chinese private company); Coca-Cola (U.S. based) acquiring Huiyuan Juice (a private Chinese company considered as a national corporate champion and a well-known brand). See, Li Ningshun, 'Discussion on Issues Pertaining to the Acquisitions of State-Owned-Enterprises by Foreign Investment' (2010) 29 (3) Commercial Times 108–109 (李寧順 '外資並購國有企業相關問題探討', 《商業時代》, 2010年第29(3)期, 108–109).

[18] Take the U.S.A. as an example, from 1988–2013, the U.S. President only officially blocked two deals based on national security concerns, in both cases, the acquirers were Chinese companies. Often times, proposed deals are forfeited and the notifications are withdrawn by investors themselves because of the overwhelming political backlash and pressure from various interest groups in the U.S.A., and Chinese companies are no strangers to such events. Some highly publicised mergers include CNOOC's failed attempt at acquiring Unocal in 2005; Huawei's failed attempts at acquiring 3Com in 2007 and 3Leaf in 2010; and Northwest's failed attempt at acquiring First Gold in 2009.

[19] For a detailed discussion of the political opposition in the Congress, see, Edward M Graham and David M Maechick, US National Security and Foreign Direct Investment (Peterson Institute for International Economics, 2006) 131–134.

withdrew the application as well as its bid for Unocal in August 2005 before CFIUS officially responded to its application, due to the overwhelming political meddling.[20] Commentators fear that CNOOC's failed attempt at acquiring Unocal would likely encourage the Chinese government to act in retaliation because of the nationalistic repercussions, by introducing a review mechanism similar to CFIUS to block undesired foreign investment based on national security considerations.[21]

In Australia, Chinese investors have encountered rejections due to national security implications similar to that in the U.S.A. Under the Foreign Acquisitions and Takeovers Act 1975 (FATA), the Treasurer of Australia may prohibit a particular transaction when such transaction fails to comply with the National Interest Test, a concept which is not specifically defined, but could be identified in multiple legislative references. In 2009, China Minmetals Non-Ferrous Metals Co. Ltd. proposed to acquire Oz Minerals Ltd in Australia, the deal was refused by the Australian government 'on national security grounds on the basis that it included mining operations located within the Woomera Prohibited Area weapons testing range'.[22] In August 2016, amid prevalent opposition, Australia blocked China's State Grid Corporation, a state-owned enterprise, from taking a controlling stake in Ausgrid, which is Australia's largest electricity network that provides critical power and communication services to businesses and government.[23] This decision, which could be the latest sign of the rising protectionism in Australia, was said on the consideration that the sale would jeopardise national security.[24]

In August 2016, it is reported that the British government postponed its approval for a new nuclear-power station project at Hinkley Point, a project through which China General Nuclear would acquire a one-third share.[25] Details of the government review process of this China–U.K. nuclear power deal remain confidential, due to its national security intricacies. These cases illustrate that more and more states are citing national security concerns in blocking sensitive foreign investment projects.

B. Emerging and intensifying regulatory power on national security review

Parallel with the aforementioned developments, a succession of legislative efforts is also identifiable to incrementally establish the NSRS concerning foreign investment in China.

The very concept of 'national security' first appeared in Chinese legislation in 1995. The Interim Provisions on Guiding the Orientation of Foreign Investment categorised the

[20] Souvik Saha, 'CFIUS Now Made in China: Duelling National Security Review Frameworks as A Countermeasure to Economic Espionage in the Age of Globalization' (2012) 33(1) Northwestern Journal of International Law and Business 221.

[21] Nikul Patel, 'Suggesting a Better Administrative Framework for the CFIUS: How Recent Huawei Mergers Demonstrate Room for Improvement' (2013) 38(3) North Carolina Journal of International Law and Commercial Regulation 958.

[22] Vivienne Bath, 'Foreign Investment, the National Interest and National Security – Foreign Direct Investment in Australia and China' (2012) 34(1) Sydney Law Review 15.

[23] Perry Williams, Brett Foley and Aibing Guo, 'Australia Blocks Foreign Bids for Electricity Supplier Ausgrid' *Bloomberg Market* (11 August 2016) <http://www.bloomberg.com/news/articles/2016-08-11/australia-rejects-bids-for-electricity-supplier-ausgrid> accessed 17 August 2016.

[24] Ibid.

[25] 'Whatever China Says, We Need to Dump Hinkley Point' *The Spectator* (13 August 2016) <http://www.spectator.co.uk/2016/08/whatever-china-says-we-need-to-dump-hinkley-point/> accessed 18 August 2016.

foreign-invested projects into four clusters, namely encouraged, permitted, restricted and prohibited ones.[26] It was stipulated specifically that investment 'harming national security or impairing the public interest'[27] or 'harming the safety and usage of military facilities'[28] should be prohibited. However, the purpose of this regulation was 'to guide the orientation of foreign investment, to keep the orientation of foreign investment in line with the national economy and social development planning of China, and to protect the lawful rights and interests of investors'.[29] Ostensibly, the protection of national security was not the primary concern of the government back then, besides merely the mentioning of it.

A notion that was most similar to 'national security review' first appeared in 2003, which was briefly mentioned in the Interim Provisions on Mergers and Acquisitions of Domestic Enterprises by Foreign Investors (Interim Provisions 2003).[30] Article 19 provided that, if the Ministry of Foreign Trade and Economic Cooperation (MOFTEC – the predecessor of MOFCOM) or the State Administration for Industry and Commerce (SAIC) believed that a merger transaction by a foreign investor involved 'major factors which seriously impact market competition, the national economy and people's livelihood, or state economic security, etc.', then the investor involved might be required to report the transaction to MOFTEC and SAIC. Article 20 further stipulated that after receiving such a report, MOFTEC and other pertinent agencies would jointly organise a hearing to decide whether a takeover should be approved or rejected.

However, the Interim Provisions 2003 did not generate an immediate practical impact. It was not until 2005 when a high-profile merger deal lifted the national security concern to a wider debate. In October 2005, the Carlyle Group (Carlyle) announced its intention to buy 85% stock of Xugong Construction Machinery Group (Xugong) at the price of 375 million USD. Xugong is a leading enterprise in China's machinery sector, which also happens to be a SOE wholly owned by the Xuzhou local government.[31] Carlyle is a U.S.-based private equity firm. After rashly announcing it to the public, this proposed deal invoked serious concerns from 'what nationalists derided as the sale of strategic assets at knock-down prices',[32] and that it would threaten 'China's national economic security'.[33] The deal was then submitted to MOFCOM for approval, which marked the beginning of an interminable three-year approval process. During this period, a potential Chinese rival bidder, Sany Group, has expressed its willingness to acquire the same stock of Xugong for 400 million USD via an

[26] Interim Provisions on Guiding the Orientation of Foreign Investment (指導外商投資方向暫行規定) (Issued by the Ministry of Civil Affairs, the National Development and Reform Commission and the State Economic and Trade Commission on 20 June 1995, effective immediately), art 4.
[27] Ibid art 7(1).
[28] Ibid art 7(3).
[29] Ibid art 1.
[30] Interim Provisions on Mergers and Acquisitions of Domestic Enterprises by Foreign Investors (外國投資者併購境內企業暫行規定) (Issued by the Ministry of Foreign Trade and Economic Cooperation on 2 January 2003, effective on 12 April 2003).
[31] Wang Zhihong, 'Carlyle Abandons Xugong Dream' *China Daily* (24 July 2008) <http://www.chinadaily.com.cn/china/2008-07/24/content_6871755.htm> accessed 11 March 2016.
[32] Sundeep Tucker, 'Carlyle Learns Bitter Chinese Lesson' *Financials* (23 July 2008) <http://www.ft.com/cms/s/0/76342814-58d2-11dd-a093-000077b07658.html#axzz3Xr5Xovnt> accessed 11 March 2016.
[33] CSC Staff, 'Carlyle's Proposed Stake Acquisition in Xugong Falls Through' *China Stakes* (23 July 2008) <http://www.chinastakes.com/2008/7/carlyles-proposed-stake-acquisition-in-xugong-falls-through.html> accessed 11 March 2016.

unofficial public statement, but Sany never made an official offer to Xugong and the matter ended with nothing eventually.[34] Carlyle then made concessions and revised its offer on two different occasions, which resulted in a substantial reduction of Carlyle's proposed stake in Xugong to a minority of 45% finally.[35] However, this gesture obviously did not sufficiently answer the concerns which MOFCOM and other relevant ministries of the State Council raised in their unprecedented gathering, which aimed to break the deadlock.[36] What had been reached in this central government officials gathering was merely further delay of approval from MOFCOM, and the whole deal finally fell through as Xugong declared in July 2008, that the proposed deal would not be implemented because the acquiring agreements signed between Carlyle and Xugong three years previously had expired.[37]

Judging from the reactions of both Xugong and Carlyle towards this much anticipated but failed transaction, both parties did express, at least implicitly, their disappointment and frustration towards MOFCOM's interminable and undisclosed approval process. Indeed, no official explanations have ever been released regarding this particular deal, leaving the public much space to conjecture what was the real concern MOFCOM had to have spent almost three years reviewing one deal, and ending with no final conclusions at all.

The heated debate amid the failed deal, however, seemed to be quite bipolar. Some scholars expressed their concerns that Carlyle's insidious attempt at gobbling up Xugong was nothing but a potential annihilation of a Chinese national champion, a convenient sacrifice of state assets of China, and a hostile and appalling exploitation of a successful Chinese company under the guise of regular commercial activities.[38] Some hence praised MOFCOM's adamant endeavour at protecting national economic security by preventing a potentially dangerous sell-out of the strategic state assets.[39] Others who disagree contended that there was hardly any national security implications involved in this proposed deal since Xugong was merely a heavy machinery manufacturer with absolutely no sensitive or strategic significance; MOFCOM was merely acting in retaliation to a 'nationalistic backlash'[40] because the CNOOC/Unocal debacle between China and the U.S.A. was only a few months prior to this deal.[41]

[34] Chen Haomin, 'Carlyle's Acquisition of Xugong Group Fell Through' *Sina Finance* (24 July 2008) (陳昊旻, '凱雷投資入股徐工集團告吹', 新浪財經, 2008年7月24日) <http://finance.sina.com.cn/chanjing/b/20080724/09565127210.shtml> accessed 18 August 2016.

[35] CSC Staff (n 33).

[36] Ibid.

[37] Ibid.

[38] Chen Yugang and Sun Xiaohui, 'A Failed Acquisition: Protectionism of Regulators or Disarming National Security Threats? A Carlyle Acquiring Xugong Case Study' (2009) 31(11) Contemporary Economy and Management (陳玉罡、孫曉輝, '併購失敗：管理者利益保護還是經濟安全威脅解除？— 凱雷收購徐工案例研究', 《當代經濟管理》, 2009年第31(11)期).

[39] Du Yang, 'A Domestic Gradation Analysis of Economy Securitization of China: A Carlyle Acquiring Xugong Case Study' (2010) 27(3) Foreign Affairs Review 133 (杜暘, '中國經濟議題安全化的國內層次分析：以凱雷併購徐工案為例', 《外交評論》, 2010年第27(3)期, 133).

[40] Sundeep Tucker, Andrew Hill and John Thornhill, 'Carlyle–Xugong Saga Has Become a Never-Ending Story' *Financial Times* (3 July 2008) <http://www.ft.com/intl/cms/s/0/7eaf5a02-4961-11dd-9a5f-000077b07658.html#axzz3Xr5Xovnt> accessed 11 March 2016.

[41] Kevin B Goldstein, 'Reviewing Cross-Border Mergers and Acquisitions for Competition and National Security: A Comparative Look at How the U.S.A., Europe and China Separate Security Concerns from Competition Concerns in Reviewing Acquisitions by Foreign Entities' (2011) 3(2) Tsinghua China Law Review 247.

While it is difficult, if not impossible, to figure out what the true intentions of MOFCOM might have been back then, it is reasonable to say that MOFCOM's hands were tied because there were few legal grounds on which to forbid the Carlyle–Xugong deal, since neither a national security review regime nor an Anti-Monopoly Law (AML) had officially been established yet. And due to the lack of a legitimate basis, the damages MOFCOM's 'silent treatment' had incurred in this particular case were more than obvious: the accusation of retaliation, nationalism, bureaucracy and protectionism. To conclude, concerns about national economic security were most likely on many Chinese officials' minds while they were evaluating the proposed deal, and so was the urgent necessity to build a legalised and systematic national security review regime in China.

In 2005, Hu Jintao, the then president of China, indicated at the Central Conference of Economic Affairs that M&As have become an important modality of inward FDI in China; to better adapt and accommodate such a trend, relevant laws and regulations pertaining to cross-border M&As should be stipulated and promulgated for the purpose of more effective utilisation of FDI.[42] Against this backdrop, MOFCOM and five other ministerial-level authorities jointly promulgated the Provisions on the Takeover of Domestic Enterprises by Foreign Investors in August 2006 (Provisions 2006).[43] For the first time in the law-making process of China's NSRS, Article 12 of the Provisions 2006 specifically stipulates that foreign investors are obliged to seek approval from MOFCOM if proposed takeovers may have an impact on national economic security, or involve the transfer of domestic enterprises that hold famous trademarks, Chinese time-honoured brands or any other important industries. Otherwise, MOFCOM and other relevant authorities have the power to terminate the transaction, or divest the relevant equity or assets.

In 2007, after nearly 20 years of deliberation, China adopted its first AML[44] that 'promises to float its markets in a procompetitive environment'.[45] Article 31 of the AML provides that 'where a foreign investor participates in the concentration of business operators by merging or acquiring a domestic enterprise or by any other means and national security is involved, besides the examination of the concentration of business operators, the examination of national security shall also be conducted according to relevant provisions'. Article 31 reaffirmed China's determination to conduct national security reviews for inbound M&A transactions for the first time ever in a law promulgated by the National People's Congress, the highest legislative body in China.

In September 2008, the same year as the end of Carlyle's failed attempt to acquire Xugong, another world-renowned U.S.-based MNE, the Coca-Cola Company (Coca-Cola) proposed to wholly acquire Huiyuan Fruit Juice Group Limited (Huiyuan), a leading Chinese brand in juice beverage production, for 2.3 billion USD. Coca-Cola then voluntarily submitted the paperwork

[42] Wen Xiantao, 'Discussion about the No. 10 Decree — Views on the End and Renascence of a Regime' (2016) 9(1) China Law Review 223 (溫先濤, '話說10號令 — 兼論一個體制的終結與新生', 《中國法律評論》, 2016年第9(1)期, 223).

[43] Provisions on Foreign Funded Mergers and Acquisitions of Domestic Enterprises (關於外國投資者併購境內企業的規定) (Issued by MOFCOM, the State Assets Supervision and Administration Commission of the State Council, the State Administration of Taxation, State Administration for Industry and Commerce, China Securities Regulatory Commission, and State Administration of Foreign Exchange on 8 August 2006, effective on 8 September 2006).

[44] Anti-Monopoly Law of the People's Republic of China (中華人民共和國反壟斷法) (Promulgated by the Standing Committee of the National Congress of the People's Republic of China on 30 August 2007, effective on 1 August 2008).

[45] Eleanor M Fox, 'An Anti-Monopoly Law for China – Scaling the Walls of Government Restraints' (2008) 75(1) Antitrust Law Journal 174.

required by the AML to MOFCOM for an anti-monopoly review. Quite similar to the Carlyle–Xugong deal, this proposed takeover quickly caught public attention and caused heated discussion in the media, mostly opposition to the deal, concerning the possibility of the gradual disappearance of a national champion and a national brand due to the proposed takeover by foreign investment. However, contrary to MOFCOM's three-year-long silent reaction in the Carlyle–Xugong deal, it took MOFCOM just six months to reach a decision this time, announcing the prohibition of the proposed acquisition in March 2009.

In the official announcement of the prohibition of the proposed deal, the Anti-monopoly Bureau of MOFCOM proclaimed that the prohibition was made under Article 28 of the AML, which stipulates that 'the Anti-monopoly Bureau of MOFCOM shall prohibit the concentration of proprietors if the said concentration restricts or may restrict market competition'.[46] It seems at first glance that this particular case had little to do with national security, since MOFCOM specifically stated that the prohibition is based on competition concerns. Some scholars called it a milestone in China's anti-monopoly regulatory scheme in terms of consumer protection; a legitimate, successful and laudable action of MOFCOM in thwarting a hostile takeover and defending a renowned domestic brand; and a victorious battle against the threat of China's national economy security.[47] Meanwhile, criticism also emerged soon after MOFCOM's announcement that some political agenda such as protectionism and preservation of a leading national brand was also involved in MOFCOM's consideration, because competition concerns alone would not suffice to explain what had happened.[48]

Notably, the Chinese government went from its consistently discreet and low-profile approach in its decision making in the past to an immediate and specific response to public criticism in this particular case. First, Xinhua News, China's state-owned and official national media, published a commentary defending MOFCOM's decision against the accusation of protectionism,[49] followed by a Q&A press conference with the spokesman of MOFCOM online only one week after the official announcement of the prohibition, clearing the widespread conjecture that the decision was made in the context of preserving a national champion and downright protectionism.[50] However, despite all these efforts made by the Chinese government defending its rejection of the deal, many still contended that the account of competition concerns alone could not sufficiently justify this failed merger deal.[51]

[46] MOFCOM Announcement (2009) No. 22: Announcement Barring Acquisition of Huiyuan by Coca-Cola (中華人民共和國商務部公告(2009年)第22號：商務部關於禁止可口可樂公司收購中國匯源公司審查決定的公告) (Issued by the Anti-Monopoly Bureau of MOFCOM on 18 March 2009, effective immediately) <http://fldj.mofcom.gov.cn/aarticle/ztxx/200903/20090306108494.html> accessed 11 March 2016.

[47] Sun Zhangwei, 'General Analyses of Coca-Cola's Acquisition of Huiyuan' (2011) 23(1) Management Review (孫章偉, '可口可樂-匯源收購案的綜合分析', 《管理評論》, 2011年第23(1)期).

[48] Pan Zhicheng, 'An Analysis of Relevant Reasons Why MOFCOM Banned the Acquisition of Huiyuan by Coca-Cola' (2009) 32(7) Law Science (潘志成, '析商務部禁止可口可樂收購匯源的相關理由', 《法學》, 2009年第32(7)期).

[49] Ming Jinwei, 'Commentary: It's Anti-monopoly Review, Not Protectionism' *Xinhua Net* (21 March 2009) <http://news.xinhuanet.com/english/2009-03/21/content_11045411.htm> accessed 11 March 2016.

[50] 'Q&A Conference on the Anti-Monopoly Review of the Coca-Cola - Huiyuan Merger Case by the Spokesman of MOFCOM Yao Jian' ('商務部新聞發言人姚堅就可口可樂公司收購匯源公司反壟斷審查決定答記者問') (Issued by MOFCOM on 25 March 2009) <http://www.mofcom.gov.cn/aarticle/zhengcejd/bj/200903/20090306124140.html> accessed 11 March 2016.

[51] Goldstein (n 41) 247–248. See, also, Sun Jin and Yu Zhe, 'The Ambiguity of China's Anti-Monopoly Regulation Regarding Mergers and Acquisitions of Foreign Investment — From the Standpoint of Prohibited Coca-Cola's Acquisition to Huiyuan' (2010) 3(3) Oriental Law 99-103 (孫晉、余喆, '我國外資併購反壟斷規制的不確定性及對策 — 從被禁止的可口可樂併購匯源案談起', 《東方法學》, 2010年第3(3)期, 99–103).

Presumably, at least one of the reasonable considerations left for MOFCOM to have blocked the deal is its clandestine intention to protect a nationally well-known brand like Huiyuan against foreign ownership. But why was MOFCOM reluctant to explicitly express such concern to justify its final decision?[52] One highly possible explanation to this question would be that MOFCOM deliberately evaded the application of Article 31 of AML in the review of the Coca-Cola – Huiyuan case to avoid greater ambiguity and even more public scepticism. Far away from a NSRS, Article 31 of AML is merely a conceptualisation, which leaves MOFCOM little regulatory initiative in practice. It is imaginable that, had MOFCOM invoked Article 31 of AML to justify its prohibitive decision of the Coca-Cola – Huiyuan deal, a succession of doubts would have flooded MOFCOM. To name a few, how does MOFCOM define 'national security', why does this particular deal fall within the purview of a national security scrutiny, who has the authority to conduct a national security review and how is it conducted? As a result, MOFCOM forbade the deal on competition grounds only to spare itself from possible criticism regarding the politicisation, unpredictability and unaccountability of citing national security concerns.

The Coca-Cola – Huiyuan case could serve as an emblematic example of MOFCOM's institutional deficiency and lack of professionalism in the context of a mixed review of national security concerns and competition concerns in China's inbound M&As screening regime.[53] Contrary to the argument that China does not need a separated and additional national security review mechanism at all because a considerably intertwined and highly regulated foreign investment regime with repetitive references of 'public interest', 'national economic security', 'national security', 'national energy resource security' and 'national cultural security' has already existed for decades, as some scholars are contending,[54] the Coca-Cola – Huiyuan case could serve as an example of the embarrassment and dilemma Chinese authorities had faced when security concerns are involved in China's inbound M&A approval process, as well as solid evidence of the regulative necessity and emergency of a defined and formalised national security review regime.

In such a context, in 2009, MOFCOM revised the Interim Provisions 2006, and issued the Provisions on the Takeover of Domestic Enterprises by Foreign Investors (2009 Revision).[55] Article 12 of the 2009 Revision inherits Article 12 of the Interim Provisions 2006, which requires foreign investors to submit a petition of approval voluntarily to MOFCOM when national economic security is at stake.

In 2011, to further guide the orderly development of M&As of domestic enterprises by foreign investors and safeguard national security, the General Office of the State Council issued the Circular on the Establishment of the Security Review System for Mergers and Acquisitions of Domestic Enterprises by Foreign Investors (2011 Circular).[56] The 2011

[52] Contrary to the Carlyle–Xugong failure years ago, MOFCOM was authorised by law to conduct a national security review when deemed necessary during a concentration review, since Article 31 of AML specifically provided a legal merit to do so.

[53] Goldstein (n 41) 250–251.

[54] Bath (n 22) 19–20.

[55] Provisions on the Takeover of Domestic Enterprises by Foreign Investors (關於外國投資者併購境內企業的規定) (Issued by MOFCOM on 22 June 2009, effective immediately).

[56] Circular of the General Office of the State Council on the Establishment of the Security Review System for Mergers and Acquisitions of Domestic Enterprises by Foreign Investors (關於建立外國投資者併購境內企業安全審查制度的通知) (Issued by the General Office of the State Council on 3 February 2011, effective on 2 March 2011) (hereafter 'The 2011 Circular').

Circular is the first legislation specifically stipulated for the purpose of the establishment of a comprehensive and exercisable framework of China's NSRS. It contains five articles, in which the Inter-Ministerial Joint Conference, China's national security review body, has been officially founded. Article 2 of the 2011 Circular provides four criteria for evaluation during a national security review, including the influence of M&A transactions on: (1) national defence security, including the ability for producing domestic products and providing domestic services required for national defence and the relevant equipment and facilities; (2) the stable operation of the national economy; (3) the order of basic social life; and (4) the capacity of research and development of key technologies involving national security.

In order to fully execute the 2011 Circular, MOFCOM issued the Provision on the Implementation of the Security Review System for Mergers and Acquisitions of Domestic Enterprises by Foreign Investors in August 2011 (2011 Provisions).[57] This departmental regulation has finally clarified certain elucidations in previous references, and has provided additional information for foreign investors as potential applicants, containing required application documents and application procedures. Deriving from a mere verbal concept, China's NSRS has progressively developed to a systematic and fully functioning regulatory mechanism that protects China's national security against hostile takeovers by foreign investors from both substantial and procedural perspectives.

However, both the 2011 Circular and the 2011 Provisions belong to a lower level of law-making compared with laws promulgated by the National People's Congress and its Standing Committee. Arguably, considering the significance and the sensitive and political nature of this topic, the NSRS should be legitimatised by the national law. Chinese scholars point out that a review system of FDI could be categorised as market-entry administrative system, in which the approval (or denial) of administrative license is expected. According to the Administrative Licensing Law however,[58] ministerial rules as the 2011 Circular and the 2011 Provisions which have not reached the level of national law generally do not possess the authority to deal with the issuance of administrative licenses, except that the State Council may grant temporary administrative licenses. Inevitably, the legitimacy of the 2011 Circular and the 2011 Provisions could be challenged.[59]

In 2013 after Xi Jinping became the President of China, he set out a new wave of deepening economic reform. At the Third Plenary Session of the 18th Communist Party of China (CPC) Central Committee held in November 2013, the CPC Central Committee passed the Decision on Major Issues Concerning Comprehensively Deepening Reforms (the 18th CPC Decision), which underlined that 'a liberalised new economic system shall be established … foreign investment policies shall be uniform (with domestic investment policies), stabilised, transparent and predictable … the approval regime of foreign investment shall be reformed … and a pre-establishment national treatment

[57] The Provisions of MOFCOM on the Implementation of the Security Review System for Mergers and Acquisitions of Domestic Enterprises by Foreign Investors (商務部實施外國投資者併購境內企業安全審查制度的規定) (Issued by MOFCOM on 25 August 2011, effective on 1 September 2011) (hereafter 'The 2011 Provisions').

[58] Law of the People's Republic of China on Administrative Licensing (中華人民共和國行政許可法) (Promulgated by the Standing Committee of the National People's Congress on 27 August 2003, effective on 1 July 2004), art 14.

[59] Qi Tong, 'Several Important Issues Concerning the Legislation on National Security Review on Foreign Investment' (2015) 5(3) China Law Review 79 (漆彤, '外資國家安全審查立法中的若干重要問題', 《中國法律評論》, 2015年第5(3)期, 79).

accompanied with a negative list approach shall be explored to regulate foreign investment activities'.[60]

To thoroughly implement the 18th CPC Decision, in January 2015, MOFCOM published the first draft FIL for public comment, in which the NSRS as part of the FIL is redesigned in Chapter 4, providing both substantial and procedural rules concerning a national security review of foreign investment. The draft FIL will be revised, and eventually be promulgated by the National People's Congress in the foreseeable future.[61]

III. The key features of the NSRS in the draft FIL

Chapter 4 of the draft FIL contains 26 articles. It sets forth a relatively detailed and comprehensive national security review regime on foreign investment. Since the draft provisions have largely embraced its U.S. counterpart, the Foreign Investment and National Security Act of 2007 (FINSA),[62] similarities and differences between the two regimes will be briefly noted for the sake of understanding the origin of the newly established Chinese system.

A. The review body

The idea of establishing the Joint Inter-Ministerial Conference (the Joint Conference) to fulfil the review function formerly appeared in the 2011 Circular, and it was further confirmed in Article 49 of the draft FIL. However, Article 49 does not provide more details than the 2011 Circular on the composition and functions of the Joint Conference. First of all, Article 49 is rather ambiguous about the composition of the Joint Conference by stating that 'the reform and development authority and the main foreign investment regulatory authority under the State Council jointly act as the conveners of the Joint Conference to specifically conduct the national security review of foreign investment in conjunction with the pertinent authorities involved in the foreign investment'. Obviously, 'the reform and development authority' refers to the National Development and Reform Committee (NDRC) while 'the foreign investment regulatory authority' refers to the MOFCOM. Avoiding explicit use the title of these two departments is probably because that the draft FIL was made by the MOFCOM itself and it tends to leave it to the State Council or the National People's Congress to further pinpoint this at a later stage.

Second, the stipulation of 'pertinent authorities' in Article 49 can refer to various ministries. It is desirable if the final FIL can provide a clearer and more detailed composition of the Joint Conference. In this respect, the U.S. national security review body – CFIUS can serve as an example. CFIUS has 11 permanent members, including the Secretary of the Treasury, the Secretary of Homeland Security, the

[60] 'The Communist Party of China Central Committee's Decision on Major Issues Concerning Comprehensively Deepening Reforms' *Xinhua Net* (15 November 2013) ('中共中央關於全面深化改革若干重大問題的決定', 新華網, 2013年11月15日) http://news.xinhuanet.com/politics/2013-11/15/c_118164235.htm> accessed 16 April 2015.

[61] For an overview of the innovative features of the draft FIL, see, Yuwen Li and Maarten Kroeze, 'The First Uniform Foreign Investment Law in China is in the Making' (2015) 14 Ondernemingsrecht.

[62] Section 721 of the Defence Production Act of 1950, as amended by the Foreign Investment and National Security Act of 2007 (FINSA), P.L. 110–49, 121 Stat. 246, 26 July 2007, codified at 50 U.S.C. App. § 2170.

Secretary of Commerce, the Secretary of Defense, the Secretary of State, the Attorney General of the United States, the Secretary of Energy, the Secretary of Labor, the Director of National Intelligence, the U.S. Trade Representative and the Director of the Office of Science and Technology Policy; and five observing members comprising the Director of the Office of Management and Budget, the Chairman of the Council of Economic Advisers, the Assistant to the President for National Security Affairs, the Assistant to the President for Economic Policy and the Assistant to the President for Homeland Security and Counterterrorism.[63] Permanent members are conducive to maintaining a stable and experienced board to ensure consistency in the interpretation and implementation of the law. Observing members compensate for the lack of special expertise of the permanent members in cases when extra discretion is demanded.

Third, the shared leading position of the MOFCOM and NDRC in the Joint Conference has its pros and cons. On the one hand, in view of the prudence the review process needs, the fact that MOFCOM and NDRC co-chair the Joint Conference may strengthen the institutional force in conducting the review. On the other hand, however, the dual leadership of the Joint Conference may possibly lead to a bureaucratic gap between the responsibilities of MOFCOM and NDRC, resulting in poor efficiency in fulfilling the functions of the Joint Conference.

Lastly, by the wording of Article 49, the ambiguity of whether the Joint Conference will be a permanent body or organised on an *ad hoc* basis whenever a review is to be conducted remains. Moreover, the chairperson of the Joint Conference remains undesignated, which needs to be further clarified either in the final text of the FIL or the subsequent implementing regulation to be issued by the State Council. It can be contemplated that the Joint Conference will be gradually strengthened from a monitoring body and a 'paper dragon' to a gatekeeper against threats to national security with substantial regulatory powers.

B. Foreign investment subject to review

Prior to the draft FIL, only M&As of domestic enterprises by foreign investors were subject to a national security review. The 2011 Circular confines the scope of the review to foreign M&As of domestic enterprises in the national defence sector; or in the sectors of key agricultural production, key energy and resources, vital infrastructure, important transportation services, core technologies and significant equipment manufacturing, provided that the actual controlling rights of the enterprises may be obtained by foreign investors.[64]

The draft FIL has substantially expanded the purview of the national security review regime, to 'any foreign investment that jeopardises or may jeopardise national security'.[65]

[63] Ibid art (k)(2).
[64] The 2011 Circular (n 56) art 1.
[65] Draft FIL (n 1) art 48. However, foreign investment in the financial sector is an exception. Article 74 of the draft FIL provides that the State Council will separately stipulate the NSRS for foreign investment in the financial sector. Furthermore, on 22 April 2015, the State Council issued the Decision of the State Council on the Market Access Administration for Bankcard Clearing Institutions (effective on 1 June 2015), of which Article 4(2) explicitly stipulated that when a foreign investor acquires a bankcard clearing institution, a national security review shall be conducted according to relevant provisions.

Notably, the notion of foreign investment has been defined in Article 15 of the draft FIL with a broad coverage of direct and indirect investment.[66] Why has the draft FIL extended the purview of NSRS to any foreign investment in general? To understand this rather drastic modification, it should be noticed that the draft FIL has revoked the long-lasting and currently valid case-by-case approval system; instead national treatment in the pre-establishment phase will be granted to foreign investors, with limited exceptions in designated industry sectors or to large investment which will be later provided in a separately formulated negative list.

The negative list approach is rather new in China's recent legislation. In October 2015, the State Council promulgated the Opinion on Carrying out the Negative List System for Market Access (2015 Opinion).[67] The 2015 Opinion further delegates the formulation and promulgation of the negative list for market access to the State Council, with the NDRC and MOFCOM assuming the drafting of the negative list for market access.[68] In March 2016, the NDRC and MOFCOM jointly issued the Notice on the Distribution of the Draft Negative List of Market Access (A Pilot Version), in which the draft negative list for market access is enclosed as attachment.[69]

Applicable to all investment proposed by either domestic or foreign investors, the negative list for market access consists of a prohibited catalogue and a restricted one. The negative list for market access comprises 96 items in the prohibited catalogue and 232 items in the restricted catalogue, covering over 100 pages altogether, and applies now only in Tianjin, Shanghai, Fujian Province and Guangdong Province.[70] The negative list for market access now serves as a pilot practice from 1 December 2015 to 31 December 2017, and will be formally implemented nationwide from 2018 onwards.[71] Its current form covers a broad scope of sectors and activities, including (but not limited to) agriculture, energy, manufacturing, construction, transportation, infrastructure, logistics, retail, real estate, finance, scientific research, service, environmental management, education, medicine and healthcare, entrainment, etc.[72] In view of the probationary nature of the negative list for market access, it still remains to be seen as how the negative list for market access will be implemented in the future.

Meanwhile, the draft FIL delegates the State Council to separately publish 'the category of special administrative measures' in the foreseeable future, a terminology that is alternatively referred to by the media and popularly known by the general public as the negative list for foreign investment.[73] This negative list proposed in the

[66] Article 15 of the draft FIL stipulates that foreign investment includes: 'the establishment of a domestic enterprise; the acquisition of shares, equity, share of property, voting power or other similar equities of a domestic enterprise; providing financing that involves the provision of equities; the acquisition of a franchise which involves the exploration and development of natural resources, infrastructure construction or operations; the acquisition of the right to use land or house ownership; and the control of domestic enterprises or holding of equities in domestic enterprises by way of contracts, trust or other methods'.

[67] Opinions of the State Council on Carrying out 'Negative List' System for Market Access (國務院關於實行市場准入負面清單制度的意見) (Promulgated by the State Council on 2 October 2015, effective on 1 December 2015) (hereafter 'The 2015 Opinion').

[68] Ibid art 10.

[69] The Notice of the NDRC and MOFCOM on the Distribution of the Draft Negative List of Market Access (A Pilot Version) (國家發展改革委員會、商務部關於印發《市場准入負面清單草案（試點版）》的通知) (Issued by the NDRC and the MOFCOM on 2 March 2016, effective immediately).

[70] Ibid.

[71] Ibid.

[72] Ibid.

[73] Draft FIL (n 1) arts 6, 20, 22–24.

draft FIL is applicable to investment and its operational activities carried out by foreign investors as an administrative measure *lex specialis*.[74] *Videlicet*, foreign investment will be subject to the scrutiny of both negative lists in terms of its market access.[75]

C. Criteria for evaluation

The draft FIL does not provide a definition of national security. Instead it enumerates a total of ten factors, plus one open-ended provision, namely 'other factors that the Joint Conference deems appropriate to be considered'. These ten factors include the potential impact on national defence, R&D ability for key technologies, leading status of domestic technology, dual-use goods and technology, key infrastructures and key technologies, information and Internet security, long-term demand of energy, food and other key resources, whether the foreign investment is controlled by the foreign government, stable functioning of the national economy, and social public interest and public order.[76]

The enumerated list of criteria for evaluation in the draft FIL bears some similarities with its U.S. counterpart. For instance, both the Joint Conference and CFIUS consider the traditional sensitive or strategic sectors, such as national defence sector, advanced key technology, critical infrastructure, energy and resources, and whether a proposed transaction is foreign government controlled as top priorities in its criteria for evaluation, and both of them contain an open-ended clause in the end which involve other factors to be decided by the review body.[77] However, differences exist where the U.S. list overtly mentions the prevention of terrorism, while the draft FIL exclusively refers to whether a transaction will have an impact on the stable functioning of national economy, or on the social public interest and public order.[78]

It is clear that China's evolving definition of national security will not confine itself to traditional national defence security. Instead, a broader definition of national security has been adopted, reflecting the wide scope of industries that Chinese legislators wish to protect and preserve against incoming foreign investment.[79] Some commentators appraise the expanding scope of the criteria of review, which reflects the flexibility and great discretion the Joint Conference holds in determining whether to institute a review, and the effective prevention of investors circumventing the law. Some even suggest that the final version of FIL should be even broader, encompassing cultural security and

[74] The 2015 Opinion (n 67) art 8.
[75] Guo Guannan and Xie Haiyan, 'Crucial Relations to Be Clarified in Formulating and Implementing the Negative List System' (2015) 22(10) Chinese Public Administration (郭冠男、謝海燕, '制定和實施負面清單制度必須理清的重大關係', 《中國行政管理》, 2015年第22(10)期).
[76] Draft FIL (n 1) art 57.
[77] Hartge (n 16) 261.
[78] There are total 11 enumerated and codified factors to be considered when CFIUS conducts a national security review. These factors involve national defence security; the extent of foreign control to U.S. companies and commercial activates; the effects on trade to terrorism countries and countries as regional military threats; the U.S. international technological leadership; the U.S. critical infrastructure; the U.S. critical technologies; whether the M&A transactions are foreign government-controlled; the possible diversion of technologies with military applications; the safety of energy and other critical resources; and any other factors deemed necessary to be considered. See, 50 U.S.C. App. § 2170 (f).
[79] Goldstein (n 41) 240.

ecological security into the criteria for evaluation, as countermeasures to similar considerations for which Chinese investors have been accounted when investing in the U.S.A.[80]

In May 2015, the State Council issued the Trial Measures for the National Security Review of Foreign Investments in Pilot Free Trade Zones (FTZs).[81] The criteria provided in the Trial Measures are generally similar to those in the draft FIL, in terms of the impact of national defence security, the stability of the national economy, basic public order, etc.; it particularly includes national cultural security and public morality.[82] It seems plausible that the State Council would also consider incorporating the impact of cultural security and public morality in the consolidated version of the FIL.

D. Initiation of the review procedure

There are three ways to trigger the review process, either by foreign investor's voluntary submission, or by the *ex officio* launch of the Joint Conference, or by third-party intervention.

A foreign investor may file an application for a national security review to MOFCOM if it considers its investment a potential threat to national security, in which case, the foreign investor is synonymous to an applicant.[83] This means the evaluation of such 'threats' or 'potential threats' to national security actually is at the investor's discretion. Once all required application materials are received, MOFCOM should first notify the applicant concerned whether a national security review is required within 15 working days; then submit a national security review request to the Joint Conference within five working days after the delivery of notification to the applicant.[84]

The Joint Conference may unilaterally initiate a review process whenever it deems that a foreign investment threatens or may threaten national security.[85]

When relevant government departments, industrial associations, peer enterprises, upstream or downstream enterprises and other relevant parties deem it necessary to conduct a national security review, they may suggest one via MOFCOM to the Joint Conference, who may then initiate a review process based on such suggestions.[86] This third-party intervention provision may in practice stimulate investors to submit voluntary notifications in order to avoid any potential and unexpected reviews later.

In comparison, a CFIUS review will be triggered by either a voluntary notification submitted by investors or a unilateral notification initiated by CFIUS itself.[87] In practice,

[80] Qi (n 59) 84. However, some commentators have questioned the necessity of encompassing 'cultural security' into national security considerations. The takeover case of AMC Entertainment by Chinese Dalian Wanda Group can shed some light. AMC was proposed to be acquired by the Chinese firm of large shares in an industry symbolic of American culture: entertainment. In 2012, CFIUS reviewed, and ultimately cleared this transaction. Critics questioned how 'AMC's ownership and operation of 338 movie theatres around the United States could be considered "so vital" that the incapacitation of the business would have a debilitating impact on national security?'. See, Hunter Deeley, 'The Expanding Reach of the Executive in Foreign Direct Investment: How Ralls V. CFIUS Will Alter the FDI Landscape in the United States' (2015) 4(1) American University Business Law Review 146.

[81] Trial Measures on National Security Review for Foreign Investment in Pilot Free Trade Zones (自由貿易試驗區外商投資國家安全審查試行辦法) (Issued by the General Office of the State Council on 8 April 2015, effective on 8 May 2015).

[82] Ibid art 2.

[83] Draft FIL (n 1) art 50.

[84] Ibid art 53.

[85] Ibid art 55.

[86] Ibid.

[87] 50 U.S.C. App. § 2170 (b), (1).

the overwhelming majority of notifications are voluntarily submitted by foreign investors themselves.[88] It remains to be seen whether MOFCOM would be flooded with review applications submitted voluntarily by foreign investors, who out of precaution wish to avoid any additional delays and transaction costs caused by an otherwise unexpected national security review conducted mandatorily by the Joint Conference.

E. General review and special review

The draft FIL is relatively clear and explicit in providing a two-step review process. The Joint Conference first conducts a general security review, followed by a special review if the proposed transaction fails to pass the general review.[89] Foreign investors and other relevant parties should cooperate with the Joint Conference during the review process by providing materials and information required and accepting relevant inquiries and investigations.[90] A general review should be completed within 30 working days from the day when the Joint Conference formally receives a review request from MOFCOM or from the day when the Joint Conference opts to initiate a national security review.[91] Two types of decisions result from the general review. One is that the Joint Conference will clear an investment when no threat to national security is involved. When the Joint Conference deems a foreign investment a potential threat to national security, subsequently a special review procedure will be commenced by the Joint Conference.[92]

A special review procedure should be completed within 60 working days from the commencement date of such a special review. A national security appraisal of the proposed foreign investment will be organised by the Joint Conference during the special review, and the appraisal opinions will be incorporated in the review process.[93] After completing a special review, the Joint Conference should notify MOFCOM of the final decision in writing given that the proposed foreign investment does not endanger national security. Otherwise, the Joint Conference should refer the proposed foreign investment to the State Council for a final decision when the proposed foreign investment is deemed to be a potential threat to national security. The State Council possesses the final authority to make the decision whether a proposed foreign investment should be cleared or declined.[94] Thus, despite the fact that the Joint Conference assumes the review process, it has no power to reject a foreign investment for the sake of national security. Obviously, the draft FIL intends to centralise the power of disapproval of a foreign investment to the State Council, the highest executive power in China. This can be understood as illustrating that China will take the decision to reject foreign investment with extreme prudence. However, the draft FIL is silent about the timeframe for the State Council to reach the decision, nor does it denote who is to represent the State Council to make such decision.

[88] This is because parties involved are always well advised to file voluntary notifications to CFIUS in order to avoid any unexpected unilateral CFIUS review in the future, so that there will be no additional transaction costs regarded.
[89] Draft FIL (n 1) art 60.
[90] Ibid art 59.
[91] Ibid art 61.
[92] Ibid art 62.
[93] Ibid art 63.
[94] Ibid art 64.

F. Review decision and implementation

The final results of a review, whether reached by the Joint Conference or by the State Council, could be one of the following three scenarios: (1) Clearance, if foreign investment does not threaten national security; (2) Clearance with conditions, if foreign investment threatens or may threaten national security, but such threats could be eliminated by conditional restrictions; (3) Rejection, if foreign investment threatens or may threaten national security, and such threats could not be eliminated.[95] Any decisions reached are exempted from administrative reconsideration and litigation.[96] Thus, under no circumstances could the finality of the decision be challenged.

In the second scenario, additional and restrictive conditions are proposed by applicants to MOFCOM before a final review decision is made. The Joint Conference evaluates the effectiveness and feasibility of such proposed conditional restrictions. Then based on the results of the evaluation, the Joint Conference could negotiate such additional and restrictive conditions with relevant parties, and if necessary modify the proposed foreign investment, in order to eliminate the potential threats to national security.[97] The Joint Conference then may reach the decision of clearance with conditions after coming to a consensus with the applicant.[98] Commentators fear that such conditional clearance might be so rigorously stipulated that foreign investors will choose to forfeit the entire deal outright, thus creating the same result as to a rejection of a deal.[99] For an overview of the aforementioned review procedure, see Chart 2.

G. The supervisory procedure and possible re-opening of review

If foreign investment projects pass the national security review under restrictive conditions, the foreign investors and the foreign-invested enterprises are obliged in their annual report to illustrate relevant circumstances regarding the adherence to the conditional restrictions in the previous year. The foreign investment regulatory authority under the State Council (which is synonymous with MOFCOM), jointly with other relevant departments, supervise with appropriate measures the implementation of the conditional restrictions. If the party concerned violates the restrictive conditions, which endangers or might endanger national security, the foreign investment regulatory authority under the State Council may propose a further national security review.[100]

In addition, foreign investment having already been cleared by a national security review could be subjected to another review when (1) foreign investors and other relevant parties intentionally or unintentionally conceal pertinent information or provide falsified materials or statements; (2) foreign investors and other relevant parties violate the conditional restrictions.[101] Thus, there is no 'safe harbour' clause that prevents a reopening of a review in China's NSRS, which is provided in the U.S. counterpart.[102]

[95] Ibid art 58.
[96] Ibid art 73.
[97] Ibid art 65.
[98] Ibid art 66.
[99] Hartge (n 16) 257.
[100] Draft FIL (n 1) art 67.
[101] Ibid art 56.
[102] The safe harbour clause in the U.S. legislation is a provision that ensures the exemption of a reopening or a revisit by CFIUS to transactions already undergone an official CFIUS review, provided that certain conditions are satisfied. See, 50 U.S.C. App. § 2170 (g), (1).

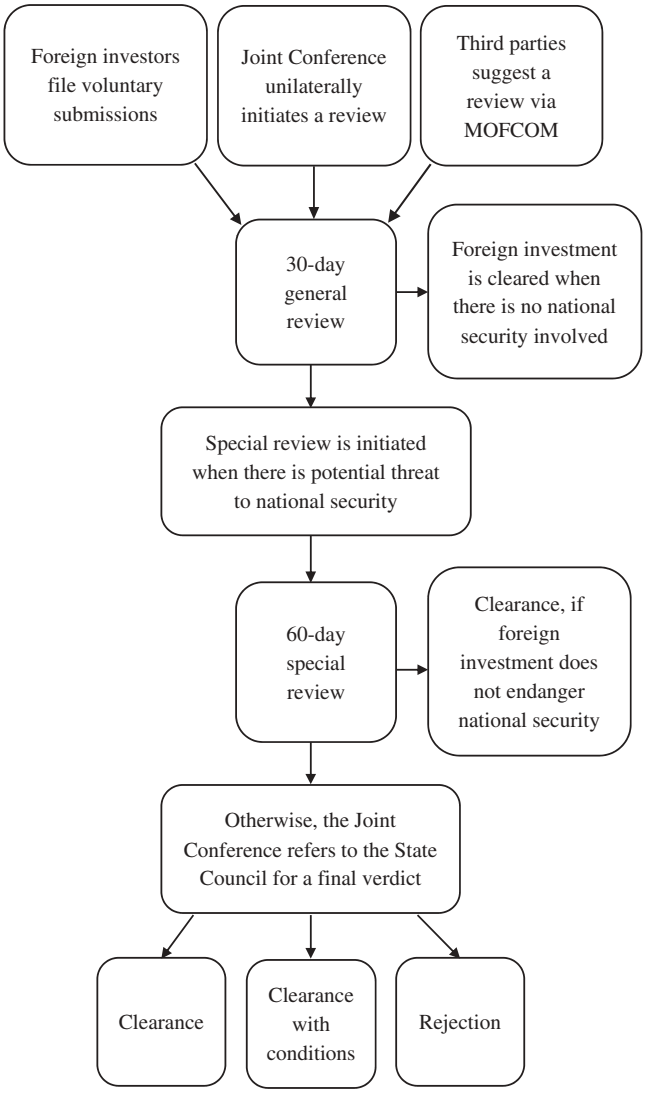

Chart 2. China NSRS flowchart according to the draft FIL.

H. Provisional measures and compulsory measures

MOFCOM is authorised to take temporary measures necessary to secure national security during the review process.[103] In case the Joint Conference determines that foreign investment is reckoned as already having produced or may produce significant detriments to national security, MOFCOM should forbid or terminate such foreign investment, or transfer the relevant equities and assets, or adopt other effective measures to neutralise such significant detriments.[104] MOFCOM is also entitled to collaborate with other relevant departments of the State Council, taking measures to eliminate or avoid

[103] Draft FIL (n 1) art 70.
[104] Ibid art 71.

any threats posed to national security.[105] The detriments caused by the aforementioned provisional measures and compulsory measures will be borne by foreign investors when a national security review is not initiated by the foreign investor's voluntary submission.[106]

I. Guidance and annual report on NSRS

According to previous references, the Chinese authorities are not required to publish any information about any completed national security review, which means foreign investors might encounter difficulties understanding the procedure from previous clearance patterns. The draft FIL requires MOFCOM to compile guidance explaining the mechanism of the review process for potential foreign investors, as well as to issue annual reports regarding transactions having been subjected to review in previous years.[107] Whether such guidance and annual reports are open to the public remains to be clarified in the final text of the FIL. However, in view of the interest of foreign investors, it is highly desirable that the guidance and annual reports will be accessible to the public. This is also in line with the government endeavour to fulfil the requirements of transparency and certainty in regulating foreign investment.

IV. The potential impact of the NSRS on foreign investment

Since the statutory establishment of the Joint Conference in 2011, barely any substantive information has been disclosed by any official outlet, with regard to how China's NSRS works in practice. Often, due to the complexity of China's FDI approval process, denial of approval can be explained by any reasons, or in some extreme cases, no reasons at all.[108] Hence, it is simply not possible to assess the functioning of China's NSRS in practice by examining the track record of its past clearances and refusals.

Considering the absence of empirical statistics, this article attempts to examine the potential impact of China's newly fledged NSRS set forth in the draft FIL on foreign investment from a normative perspective.

A. NSRS provides better transparency, predictability and accountability

As stipulated in the draft FIL, China's NSRS has, at the very least, set up a viable, consistent and unitary national security review mechanism in the form of national law for the first time in history. Though far from fully fledged, it establishes the 'rules of the game' and brings greater predictability and transparency to foreign investors. More importantly, a distinct national security review mechanism could 'act as a lightning rod', which separates national security concerns from other types of concerns in terms of regulating incoming foreign investment, for instance, monopoly or competition

[105] Ibid.
[106] Ibid art 72.
[107] Ibid arts 68 and 69.
[108] For example, in 2009, Tengzhong attempted to purchase General Motor's brand Hummer but both the NDRC and MOFCOM claimed that they never received any application. See, Eric Pekar, 'The Chinese Investment Regime and the U.S.–China BIT Negotiations' in Wenhua Shan and Jinyuan Su (eds), *China and International Investment Law-Twenty Years of ICSID Membership* (Brill Nijhoff, 2015) 276.

concerns, thus isolating national security concerns, which are otherwise considered to be the most politicised pretext of foreign investment, from outside pressures and complications by delineated statutory responsibility and accountability.[109]

Nonetheless, this article does not proclaim that China's NSRS is a cure to resolve all politicisation of foreign investment regulation. As a matter of fact, 'domestic policies, manifested through legislation and regulation … constitute a political response to the public, the press, industry associations, competing companies, opposition political parties, regional governments and other groups'.[110] It is no surprise that China's NSRS could possibly generate a sensational political mix, given the attention it attracts. Furthermore, the political meddling in the national security review process can hardly be ignored in other countries where a national security review or similar measures are adopted. For instance, CFIUS is constantly being questioned and accused of being over-politicised and prejudiced, and China has claimed that the U.S.A. has discriminated against Chinese investment through backdoor politics.[111] In Canada, the objection to BHP's bid for Potash Corp based on the 1985 Investment Canada Act (ICA) reflected obvious political motivation and government intervention. Commentators pointed out that 'while political opposition is not an unusual basis for a government's decision, "politics" is not one of the factors of consideration provided for in the ICA. However, this case demonstrates that domestic politics can and do play an influential part in the review process'.[112] The National Interest Test in Australia stipulated in the FATA 1975 also received its fair share of criticism. Specifically, it is susceptible to 'arbitrary political influence over investment' and 'the reference to community concerns through the nomination of sensitive sectors is purely a political response rather than a reflection of national security concerns'.[113] In conclusion, the tendency of over-politicisation regarding foreign investment regulation is ubiquitous and inevitable, due to the sensitive nature itself; the establishment of a national security review regime is likely neither to aggravate the susceptibility of political interference, nor to eradicate it. However, a clearly defined and unitary national security review regime, much like China's up-to-date legislative endeavour, could prevent, to a certain extent, the over-politicisation and the possible abuse when conducting a national security review.

B. The irrelevance of NSRS on most foreign investment projects

China's national security review will have a rather insignificant influence on future foreign investment as a whole. Some commentators contend that 'China's plan to broaden its ability to review incoming foreign investments for national security threats (in the draft FIL) is fuelling concern that the broader scope of the national security review would give ample leeway to China to reject unwanted investment without much of an explanation'.[114] Such perceived concern is exaggerated and unsubstantiated. For a

[109] Goldstein (n 41) 252.
[110] Bath (n 22) 32.
[111] Pekar (n 108) 278.
[112] Simone Collins, 'Recent Decisions under the Investment Canada Act: Is Canada Changing its Stance on Foreign Direct Investment?' (2011) 32(1) Northwestern Journal of International Law & Business 161.
[113] Julie Novak, 'Australia as a Destination for Foreign Capital' (October 2008) Institute of Public Affairs: Australia's Open Investment Future (AOIF) Paper 1, 11.
[114] Oster (n 11). See also, Orion Berg et al, 'National Security Clampdown on Foreign Deals' *White and Case LLP Publications and Events* (11 November 2015) <http://www.whitecase.com/publications/insight/national-security-clampdown-foreign-deals> accessed 11 March 2016.

start, when tracing the evolutionary trajectory of China's national security review mechanism, it is doubtless that such a regulatory regime has been developed for over one decade since 2003. Consequently, Chapter 4 of the draft FIL is not an invention of a sudden spur of the moment, but a logical outcome from a gradual and incremental jurisprudential development. Furthermore, the draft FIL has explicitly stipulated in its very first article that the purpose of the law is 'to promote and regulate foreign investment, to protect the legitimate rights and interests of foreign investors and to safeguard national security …'[115] Obviously, the underlining intention of the law's drafters is not to create a new regulatory hurdle by which foreign investors would be intimidated, but to establish an appealing, liberalised and predictable investment environment. Moreover, the most recent record of implementation of the AML can provide an indication of how NSRS may be applied in the future. Since the AML became effective in 2008, the government has had wide latitude to bar inward M&As. However, so far, few foreign acquisitions of Chinese companies have been affected. It is reported that up to December 2010, MOFCOM had reviewed more than 140 M&A cases, approved 95% of the cases without conditions and seven cases with conditions to remedy competition issues. The only banned case is the Coca-Cola's proposed acquisition of Huiyuan as discussed above.[116]

Nevertheless, it is undeniable that the NSRS prescribed in the draft FIL does encompass a much broader scope than earlier regulations, which could possibly lead to flexible discretion, even the abuse of the system in an arbitrary or retaliatory manner. This is an issue that should be strictly monitored in the enforcement of the FIL in the future. As far as law-making is concerned, the broader coverage should be better understood in the context of other provisions stipulated in the draft FIL. For instance, according to Article 6 of the draft FIL, foreign investors are entitled to national treatment unless otherwise stipulated in the negative list approach. This means instead of the case-by-case approval system for each foreign investment, the draft FIL applies comprehensive national treatment to all foreign investors in general in all stages of their investment.[117] Foreign businesses now 'may proceed to corporate registration without the need for any market entry approval', and 'be subject to a generic body of Chinese corporate law … in terms of incorporation, corporate governance, liquidation and other corporate matters', just like Chinese domestic enterprises.[118]

Given that a much more liberalised regulatory regime would otherwise dramatically reduce government control over market entry, a more stringent national security review regime that encompasses a broader scope of considerations is subsequently anticipated to regulate inward foreign investment that wishes to enter strategic or sensitive sectors. Moreover, the negative list approach will identify which foreign investment projects are

[115] Draft FIL (n 1) art 1.

[116] Christine Kahler, 'Foreign M&A in China Face Security Review' *China Business Review* (1 April 2011)<http://www.chinabusinessreview.com/foreign-ma-in-china-face-security-review/> accessed 21 March 2016.

[117] Ren Qing, 'Three Key Words in the Draft Foreign Investment Law of China' (2015) 5(3) China Law Review (任清, '外國投資法(草案)中的三個關鍵詞', 《中國法律評論》, 2015年第5(3)期). See also, Ren Qing and Wu Liyun, 'Great Leap in Foreign Investment Regime: From Case to Case Approval to Comprehensive Reporting' *Caixin Net* (27 January 2015) (任清、吳麗雲, '外資管理大跨越：從逐案審批制到全面報告制', 財新網 2015年1月 27日) http://opinion.caixin.com/2015-01-27/100778771_all.html> accessed 11 March 2016.

[118] Qiang Li et al, 'China's New Foreign Investment Law' *O'Melveny Alerts and Publications* (22 January 2015) <https://www.omm.com/resources/alerts-and-publications/publications/chinas-new-foreign-inv/> accessed 18 April 2016.

'restricted' or 'prohibited', which are either subject to a case-by-case approval or banned from market entry in the first place. Consequently, even though the national security review may cover a broad range of sectors and various considerations, only in extreme circumstances will the national security review be activated. The reason is that the majority of foreign investment that has the potential to encounter a national security review is highly likely to be classified as either 'restricted' or 'prohibited' according to the negative list approach, because these foreign investment projects are incongruent with general national interests (in a broader sense, such as national economic security, public interests, public policies, and indubitably, national security). As a result, these foreign investment projects will either still undergo a case-by-case approval (being classified as 'restricted'), or be downright prohibited from market entry (being classified as 'prohibited'), in neither cases will the NSRS be applicable.

C. *NSRS is in conformity with international practice*

Chapter 4 of the draft FIL 'represents a major step in China's efforts to rationalise its foreign investment regulatory regime in line with prevailing international best practices'.[119] First of all, major trading partners with China, including the U.S.A., Australia, Canada, France, Germany, the U.K. and Russia, have either adopted statutory NSRSs or similar alternatives within their domestic law long before China has done so. As a matter of fact, since the late 1990s when China's outbound FDI began to explode, Chinese companies' overseas investment has been incessantly challenged and scrutinised by the NSRSs of the aforementioned trading partners, not the other way around. China's newly established NSRS is merely an equivalent counterpart, not premeditated retribution.

Second, China's NSRS is compatible and consistent with prevailing international investment law. Under many international agreements, signatory states often negotiate local exclusion clauses which stipulate that states are allowed to take measures at times of necessity in order to protect their essential security interests, and such measures are exempt from the treaty commitments and obligations which the states have entered into.[120] Embedded in a significant number of investment agreements, such clauses are often referred to as essential security provisions, or non-precluded measures. The essential security provision applies when the host country considers it necessary (in its own judgment) for the protection of its public policy, national interests and national security, consequently abrogating certain substantial investor rights temporarily.[121]

On a multilateral level, 'virtually all regional and inter-regional International Investment Agreements (IIAs) contain general national security and public health (or public morals) exceptions to the non-discrimination standard'.[122] On a bilateral level, an essential security provision is found in the model Bilateral Investment Treaties (BITs) of Canada (2004),

[119] Ibid.
[120] Katia Yannaca-Small, 'Essential Security Interests under International Investment Law' in The Organization for Economic Co-Operation and Development (OECD) (ed), *International Investment Perspectives: Freedom of Investment in a Changing World 2007 Edition* (OECD Publishing, 2007) 94.
[121] José E Alvarez, *The Public International Law Regime Governing International Investment* (Hague Academy of International Law, 2011) 282.
[122] Peter Muchlinski, 'Policy Issues' in Peter Muchlinski, Federico Ortino and Christoph Schreuer (eds), *The Oxford Handbook of International Investment Law* (Oxford University Press, 2008) 24.

Germany (2005), India (2003) and the United States (2004 and 2012).[123] Since the first BIT signed with Sweden in 1982, China has approximately entered into more than 130 BITs, ranking in the second place of the number of signed BITs globally, following Germany.[124] And the most recent BITs China has entered into usually include such essential security provisions. In conclusion, the extensive inclusiveness of the essential security clause in IIAs demonstrates that the prevailing international practices confer on states the ability to control inbound FDI for national security considerations, and China's NSRS is a legitimate manifestation at its domestic law level of such ability embedded in international law.

In addition, one can hardly ignore the conspicuous resemblances from both procedural and substantial perspectives between the Chinese and the U.S. national security regimes, as discussed in section III of this article. As a matter of fact, since the Trading with the Enemy Act of 1917, the national security review regime of the U.S.A. has been evolving for almost one century.[125] Despite the fair share of criticism which CFIUS has received in recent years, it is widely acknowledged in the international business community as one of the best-known national security review processes. While the close resemblance between the two systems is susceptible to criticism that involves the accusation of retributive intentions, it also proves the point that China's NSRS is not disparate among analogical schemes of other countries.[126] Actually, these mutual similarities demonstrate the effort China has been making to improve its NSRS based on the existing U.S. counterpart that has long been acknowledged by investors.

V. Concluding remarks

In parallel with the expansion and integration of foreign investment in China's market, national security concerns cannot be ignored. Since the beginning of the 21st century, the Chinese government has addressed these concerns through positive law-making. However, the currently effective regulatory framework pertaining to NSRS is fragmented and incomplete. The draft FIL for the first time at the national law level sets out relatively clear and detailed rules to regulate foreign investment relevant to national security.

In addition, the draft FIL has liberalised China's foreign investment regulatory system by introducing national treatment in the pre-establishment phase, with limited restrictions numerated in the negative list, and most of the foreign investment projects can be expected to enter into China more easily once the FIL becomes effective. This will drastically change the fact that under the current regulatory regime all foreign investment, regardless of its sector and scale, are subject to government approval and oversight for matters such as establishment, operation, liquidation, capital increase and reduction, change of share or ownership, etc. This excessively restrictive examination and approval system will be revoked, which will significantly benefit most of the foreign investment in China. The NSRS is thus anticipated to apply as an exception rather than a norm.

[123] Yannaca-Small (n 120) 98.
[124] United Nations Conference on Trade and Development (UNCTAD), 'Recent Development in International Investment Agreements (2008–June 2009)' (No. 3 of 2009) *International Investment Agreements (IIA) Monitor* 3.
[125] Trading with the Enemy Act of 1917, ACT 6 October 1917, CH. 106, 40 STAT. 411.
[126] Hartge (n 16) 252.

China has greatly benefited from foreign investment over the past three decades, and it is most likely that China will continue its endeavour to attract and promote more foreign investment into its domestic market. However, the investment environment in China has become less attractive compared with other developing countries in recent years due to the fact that the cost of labour, energy, environment protection requirements, as well as other transactional cost have been rising for foreign investors. Hence, to maintain its competitiveness to potential investors, China will reject foreign investment for national security purposes in a very cautious and prudent way. Furthermore, driven by the 'going-out' policy, more and more Chinese companies have been seeking investing opportunities abroad. As a rational speculation, this momentum of China's outbound FDI would incentivise the Chinese government to substantially alleviate unnecessary restrictions on foreign investment and to incrementally liberalise its FDI regulatory regime, based on reciprocal considerations.

However, in the light of the recent legislative move in which national security issue in a number of new laws and regulations is highlighted, more substantiated rules on NSRS in the final version of the FIL is called for, since a clearly delineated system can provide better certainty, predictability and transparency for law compliance and enforcement. Meanwhile, it is advisable that in the implementation of the NSRS, the Chinese government should strike a balance between the promotion of foreign investment and the protection of national security as its core principle, rejecting only foreign investment projects that potentially threaten national security in rare and exceptional circumstances. The agencies involved in the security review process should be responsible to guarantee the transparency of the procedure so as to make the system understandable and accountable for potential foreign investors.