

Introduction of Mainland China M&A Security Review Mechanism and Its Several Problems

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Abstract: In order to achieve an open policy in investment, the establishment for the M&A national security review system (which is always called “national security review”) is an important part of “wide open and strict supervision” new policy. This recall the needs to examine what is a national security review system, why to perfect it, and how to perfect. This article first of all to interpret and analyze, compare the legislative model of national security review system, and then explore the problems existing in its system of mainland China.

Key words: national security system; Shanghai free trade zone; M&A and investment

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Since the acquisition of Lenovo to IBM in 2004, Chinese enterprises overseas M&A increasing year by year, but they hit a wall repeatedly because of national security review of M&A, such as CNOOC bid for UNOCAL, Hair takeover Mike, HUAWEI’s acquisition of 3com, 2wire and 3leaf, all of which cause the attention of nationals a mechanism called National Security System in the U.S.. UNCTAD organization headquarters in Geneva issued the “world investment report 2013” in June 26, 2013, the report demonstrates that the developing countries’ attracting foreign investment in 2012 exceed the developed countries for the first time.¹ Among them, China’s foreign capital inflow ranked the second in the developing countries², outflow ranking rose from the sixth to the third³. Compared with the rapid development in transnational investment, the legislation system is still keep rigid and outdated. It is a time to reform the legislation in investment law. On September 13, 2013, the state council published “Framework Plan for China (Shanghai) Pilot Free Trade Zone” (hereinafter referred to as “Framework”) says to improve the system of national security review, carry out in pilot test area involving the national security review of foreign investment.⁴

Although there are many studies since 21st century regarding national security review system in Mainland

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¹ UNCTAD: World Investment Report 2013, Key Messages, “Developing countries take the lead. In 2012—for the first time ever—developing economies absorbed more FDI than developed countries, accounting for 52 percent of global FDI flows”, p. xi.

² Ibid, Overview, “Figure 2: Top 20 host economies”, p. xiv.

³ Ibid, Overview, “In the ranks of top investors, China moved up from the sixth to the third largest investor in 2012, after the United States and Japan”, p. xiii, and “Figure 3: Top 20 investor economies”, p. xv.

⁴ “Framework Plan for China (Shanghai) Pilot Free Trade Zone”: “c. Explore the ‘Negative List’ administrative approach...National security review system will be improved, and pilot national security review on foreign investment projects will be trialed in the China (Shanghai) Pilot Free Trade Zone to constitute a safe and efficient open economic system. A foreign investment administrative system that is aligned with international standard will be set up”.

China, but mostly from national security review system comparison of China and the U.S., trying to draw lessons from American national security review system⁵, some engaged to prevent the forbid from the U.S. national security review system⁶. There still little essay regard to the new policy of investment law beginning at the end of 2013⁷. This assignment try to exam the 2011 version, which is the existing national security review system, combining with the new situation of Shanghai FTZ policy, draw lessons from multinational national security system research.

1. Introduction of National Security Review System of Mainland China

1.1 The Concept of National Security Review System in Mainland China

The full name of national security review system in Mainland China is “Foreign investor M&A of domestic enterprises for national security review system”⁸, hereinafter referred to as “M&A security review”⁹regulated in “General office of the state council on establishing a foreign investor merger and acquisition of domestic enterprises safety review system notification” (hereinafter referred to as “Notification”) No clear definition either abroad or at home. From the legislative practice of each country, the system is a kind of national security review of foreign capital refer to a “foreign-capital M&A transactions of a country when there maybe threaten or damaging to national security, and then take measures such as suspension, prohibition, or changes to regulate the harmful actions”¹⁰

There are two types of investment, one is direct investment, and the other is portfolio investment. Direct invest includes green-land investment and M&A. In Mainland China, the existing foreign investment national security review is focuses on M&A. Literally speaking, M&A is the combination of merger and acquisition¹¹. In the U.S., it also including “takeover” (purchase control or ownership of enterprise¹²). For the concept of “merger”, some counties take a broad meaning, namely mergers including absorption merger as well as consolidation¹³,

⁵ Biancheng, “A comparison of Sino-American National Security Review System”, *Law and Society*, March, 2014.

⁶ Xie Hao, Yang Wen: Research on American National Security Review System regarding to cross-border M&A, Asia Pacific Economic, January 2014, Huang Zhijin: China state-owned investors overseas investment legal issues research, Ph.D. Dissertation of Eastern China Political science and Law University, May, 2013, etc.

⁷ One piece of paper of Professor Song Xiaoyan discuss the Shanghai FTZ in its paper, regarding to how to build a national security review system: China (Shanghai) free trade area of foreign security review mechanism law, Law, January 2014.

⁸ See “General office of the state council on establishing a foreign investor merger and acquisition of domestic enterprises safety review system notification”.

⁹ General office of the state council on establishing a foreign investor merger and acquisition of domestic enterprises safety review system notification: to guide the orderly development of foreign investors M&A to domestic enterprises, safeguarding state security, agreed to by the state council, the foreign investor merger and acquisition of domestic enterprises can build up safety review (hereinafter referred to as M&A security review) ...

¹⁰ Wang Xiaoqiong: the latest development and its revelation of Western counties national security review system of foreign capital's M&A, Hubei people's publishing house, in December 2010, p. 11.

¹¹ “Mergers and acquisitions, merger and acquisition (or takeover) es.... atmosphere absorb merger and merger by consolidation, absorption merger refers to a company to absorb another enterprise (target), the target enterprise; a consolidation is the merger of two or more enterprises to form a new company, the original enterprise disappeared.... acquisition refers to a company by buying shares of listed companies and make the company control the timing of the transfer behavior.” Citing (a), Shanghai Dictionaries Press, the first edition, August 2010, p. 0276.

¹² Bryan A. Garner: “takeover: The acquisition of ownership or control of a corporation”, Black's Law Dictionary, Standard Ninth Edition, June 25, 2009, p. 1591; Similar in the United Kingdom, Judy Pearsall: “an act of assuming control of something especially the buying out of one company by another”, *The Concise Oxford English Dictionary* (revised 10th edition), Oxford University Press, May, 2004, p. 1460.

¹³ Judy Pearsall: “merger n. the combining of two things, especially companies, into one”, *The Concise Oxford English Dictionary* (revised 10th edition), Oxford University Press, May, 2004, p. 892.

while some countries take a narrow definition, that is, only including the absorption merger¹⁴, such as the U.S., it only represent the newly established merger. For the concept of “Acquisition”¹⁵, the broader meaning is get property ownership of an asset¹⁶, but the narrow one only means the business acquisition. Merger and Acquisition is a new word together as a combined meaning, takes the broad meaning of merger and narrow meaning of acquisition, which is only mean to gain control of the other enterprise’s property rights by a transaction behavior.¹⁷

Why enterprise behavior needs to rise to the national security review of mergers and acquisitions? This is a matter of necessity. Early scholars have conducted case well. M&A maybe refer to the interests of public employees, consumers, environmental protection¹⁸. Cross-border M&A has been shown to create greater value¹⁹, but also proved to cause greater risk, such as the threat to industry monopoly, the core technology, misappropriation of national brands, increasing financial risk, leading to loss of state-owned assets²⁰, which makes the private law nature of mergers and acquisitions have a certain content of public law, need to intervene in public power to regulate. At present, many countries in the world establish the system of the national security review for foreign capital M&A.

1.2 Definition of “National Security”

National Security concept has been widely explored, but no uniform standards. It is so extensive, is decided by the diversity of security elements, political, military, economic, scientific, technological, cultural and even physical environment and other factors will affect the national security of a country. Vagueness of its definition is inherent in its nature, so does in the area of M&A.

Nations varies on this definition. More and more countries do not define this phrase of National Security review in investment law, such as the U.S. and Canada. “National security” is not explicit defined, so that to leave a largest space for discretion. International discussions on national security mostly focus on multinational and bilateral investment agreements, are scattered across the treaties. In Mainland China, “Notification” defines “national security” as follows: “national security, including domestic production capacity for defense needs, internal service delivery and related equipment and facilities” and “economic stability” and “social order” and “design and key technologies research and development capabilities for national security.”²¹

¹⁴ Bryan A. Garner: “merger (8): The absorption of one organization (esp. corporation) that ceases to exist into another that retains its own name and identity and acquires the assets and liabilities of the former.” *Black’s Law Dictionary* (Standard Ninth Edition), June 25, 2009, p. 1078.

¹⁵ Ibid, “corporate acquisition (1911) the takeover of one corporation by another if both parties retain their legal existence after the transaction”, p. 269.

¹⁶ Ibid, “acquisition: 1 The gaining of possession or control over something <acquisition of the target company’s assets>”, p. 26; see also Judy Pearsall: “a recently acquired asset or object”, *The Concise Oxford English Dictionary* (revised 10th edition), Oxford University Press, May, 2004, p. 12.

¹⁷ “Mergers and acquisitions:... enterprise to gain control of other enterprises and the capital market mechanism for all of the property rights transaction activity”, Citing(a), Shanghai Dictionaries Press, August 2010, the first edition on, p. 0276.

¹⁸ Wang Xiaoqiong: the latest development and its revelation of Western countries national security review system of foreign capital’s M&A, Hubei people’s publishing house, in December 2010, p. 4.

¹⁹ Laurence Capron: *Using Acquisitions to Access Multinational Diversity: Thinking Beyond the Domestic versus Cross-Border M&A Comparison*, Insead Faculty & Research, 2004/58/SM.

²⁰ Xia Shen: “multinational corporations’ invasion ‘and the economic security of our country’”, “international economic review, 1996, 8; Zhang Changyu, Shen Zhibin: “the introduction of foreign capital and national economic security”, “management modernization, 1999 (3); Jiang Yongdeng: “economic security and its assessment, statistical research, 1999, 9; Liu Yanling: “under the background of economic globalization to China’s national security agreement”, “realistic”, 2004 s4 period and so on, Max Weber XieHao, Ellen Pau: “across the U.S. national security review mechanism of the M&A research”, “Asia Pacific economic”, 2014, p. 1.

²¹ “Notification”: “II. Content of M&A security review: a. the impact of M&A on national defense, including domestic production capacity for defense need, internal service delivery and related equipment and facilities. b. the impact of mergers and acquisitions on the country’s economic stability. c. the impact of mergers and acquisitions on the basic social order. d. M&A deals involving national security impact of key technologies research and development capabilities.”

2. The Other Two Review Mechanisms and Its Relation to National Security Review in Mainland China

There are three main types of review system for foreign investment: market-access review, concentration review and national security review. Concentration review and national security review are promulgated by the national people's Congress of "the People's Republic of China (PRC) Anti-monopoly Act" ("Anti-monopoly Act"), and therefore is often collectively known as the antitrust review in a broad prospective. The real antitrust review here is only concentration review.

2.1 Market Access Review

Market Access Review, strictly speaking, is not a systematic mechanism, it is collectively, access requires the admission from administration to approval of Greenland foreign investment, there is no uniform law, detailed rules are scattered in, separate regulations as well as legal documents relating to a series of entry requirements.

At the national level, Commerce Department identifies that foreign investors or M&A, investment, equity funding need to obey market access requirement in the legal document "Catalog of Industries for Foreign Investment" ("Catalog"), which is the effective law in China except for Shanghai FTZ. Besides, "the PRC Sino-foreign joint venture enterprise law" (published March 15, 2001) and "the PRC Sino-foreign joint venture enterprise regulation" (revised January 8, 2011), "the PRC Chinese-foreign cooperative ventures law" (October 31, 2000) and "the PRC Chinese-foreign cooperative ventures regulation" (published April 12, 2001), the "PRC Company Law" (revised October 27, 2005), which are called "Foreign Investment three laws" in Mainland China, are laws that specifically governs the foreign investment.

In Shanghai FTZ, National Standing Committee authorized Shanghai FTZ to suspend many of the market access requirements in the "Foreign Investment three laws"²², instead, it promulgated "China (Shanghai) free trade zone foreign investment access special management measures (negative list)" ("Negative List", published in September 29, 2013), introduced "Pre-establish national treatment" and "negative list" model. This is the first time that Mainland China accepts this model. Pre-establish National treatment was first accepted by the North American Free Trade Agreement ("NAFTA"). It extends the principle of national treatment to as early as Greenland investment stage. The Negative list does not apply to M&A stage, instead, it illustrate that the M&A investment should obey relevant regulation²³. The word "relevant" means that it does not include the negative list reminded here. Therefore, there is no new marched law with negative list guiding the foreign capital M&A, the national level's existing National Security Review still apply in Shanghai FTZ.

2.2 Concentration Review

Concentration Review Mechanism was established by two legal instruments: Regulation of the state council on the criteria for notification concerning a concentration" ("Concentration Regulation") and "PRC Antitrust Law" (published on August 3, 2008). Both of which generally apply to domestic and foreign investment, the former has developed detailed process and scope. "Concentration" that needs to notify should be reviewed by anti-monopoly law enforcement authority. The objective of the review is to prevent the concentration of business which

²² The standing committee of the National People's Congress regarding the authorization of the state council in China (Shanghai) free trade area temporarily adjust the decision of the administrative examination and approval of the relevant law, published in August 30, 2013.

²³ "Negative List": Free-trade test in the foreign capital merger and acquisition of foreign investors to invest in the listed company's strategic foreign investors by its holdings of China equity capital contribution, shall conform to the requirements of the relevant provisions; Involving national security review of antitrust review, in accordance with the relevant regulations.

“eliminates or restricts market competition”,²⁴

According to Article 20 of PRC Antitrust Law and “Concentration Regulation” Article 2: operators concentrated refers to “(a) operators merged; (ii) operators through made equity or assets of way made on other operators of control right; (three) operators through contract, way made on other operators of control right or can on other operators imposed decisive effects.

2.3 Relationship among the Three Review System

Though the three functions overlap somehow, but their focal points are not the same. The relationship between these three types of review is parallel. Their objective, effects to be achieved are different. Market access review is for preventing the entry of access that may negatively affect a certain industry, which focus on certain industry. Concentration review is for anti-monopoly, intended to create an orderly Market development. National Security Review is to “guide the orderly development of M&A for domestic enterprises by foreign investors and safeguard the national security.”²⁵ with the intention of balancing foreign and national interests.

The three review systems do not have chronological order. Each one is an independent mechanism, with its own characteristics. A typical case was Matheson Company acquisition United States Hercules Corporation and South Africa’s Minorco intentional merge and acquit the company United Kingdom GoldFields, U.S. government has launched a national security review and the a concentration review, the investment fail the latter one but win the national security review²⁶. It is the same in Mainland China, law does not specify the sequence of these three review. Article 31 of the Antitrust Law says “foreign mergers and acquisitions of domestic companies or otherwise participate in the concentration of business operators, involving national security, concentration review except in accordance with the provisions of this law, a national security review should also be in accordance with the relevant provisions of the State.”²⁷ This provision uses subject to In addition to “embody both side-by-side and independent relationship.

In comparison, in the content, national security has a fallback character among these three. For example, no monopoly but cases affecting national security, centralized review will helpless, launched a national security review is required to save the crisis.

3. Legislation Model of National Security Review

3.1 Legislation History of National Security Review in Mainland China

Foreign investment used to be Greenland investment in early stage until the early 90’s from Hong Kong China, strategic investment company once bought 101 State enterprises which earned huge profits. After the successive

²⁴ Antimonopoly Law: Article 28: A concentration has or may have effect of eliminating or limiting competition, the anti-monopoly enforcement authority under the state council shall prohibit the centralized decision.

²⁵ The preamble of the Notification: “in recent years, with the in-depth development of economic globalization and China’s opening to the further expansion of foreign investors with investment increasing by way of mergers and acquisitions, contributed to the diversification of means of utilizing foreign capital in China, in optimizing the allocation of resources, promoting technological progress, improve the enterprise management level has played a positive role. To guide the orderly development of mergers and acquisitions of domestic enterprises by foreign investors, the interests of national security, the State Council agreed, in respect of building safety review of mergers and acquisitions of domestic enterprises by foreign investors (hereinafter referred to as mergers and acquisitions security review) system related matters as follows:

²⁶ Wang Fang: “National security review in foreign capital M&A and antitrust review of the coordination mechanism research”, Master’s degree thesis in East China university of Political Science and Law, April 15, 2013.

²⁷ Antitrust Law Article 31: “foreign mergers and acquisitions of domestic companies or otherwise participate in the concentration of business operators, involving national security, in accordance with the provisions of this law, should also review by a national security review in accordance with the relevant provisions of the State.”

“travel deals”²⁸, “jiangling deals”²⁹, forced Mainland to focus on mergers and acquisitions by foreign capital.

After a series of reforms, in 2008, the antitrust Act take into effect, it is the first time to admit the legal status of national security review. In 2009, in order to match Antitrust Act, Mainland promulgated “Concentration Regulation” and “Regulation of mergers and acquisitions of domestic enterprises by foreign investors.” (June 22, 2009). On February, 2011, the State Council issued a legal document: namely “Establishment of mergers and acquisitions of domestic enterprises by foreign investors of the safety review notification system (hereinafter referred to as the notification)”, for the first time for a national security review regime, establishes the general framework of the system. In August 2011, for supporting the notification, the Ministry of Commerce has issued the Department of Commerce to implement “security review system of mergers and acquisitions of domestic enterprises by foreign investors”, set out in some detail such matters as procedures for national security review regime. Since then, the Chinese mainland national security review regime formally established. Effective documents is aimed specifically at national security review regime are under section 31 of the anti-trust law, normative documents of the State Councils’ “Notification” as well as sectorial normative documents of the regulations.

According to law, State Council has the legislation power for regulation. As the state council authorized the Shanghai FTZ to enact a new regulation for national security, it means that Shanghai FTZ government now has the power to enact it so that its model can be extent to the whole country in the future.

3.2 Legislation Model of Foreign Capital M&A in Other Countries

Model I: Regulation specifically in M&A for foreign capital national security review

Many county has enacted law specifically for M&A, For example, the typical country is the U.S., it uses the Acts including Exon-Florio Amendment³⁰ and Foreign investment and the national security law of 2007³¹ and its implement regulation, Foreign mergers and acquisitions takeover regulations of 2008³² to build its national security review system. Committee on Foreign Investment in the U.S. (CFIUS) is the apartment take charge of this system authorized by No. 12661 order in 1993. Australia is similar to the U.S., the foreign investment review committee is specifically in charge of the system. The laws are including 2013 revised In 1975 foreign capital M&A and Takeover Act and its foreign capital M&A and Takeover Relation which regulated the M&A threshold. Mainland China is also in this model.

Model II. The national security system both apply to abroad or at home, such as Canada. The law are including Investment Canada Act³³ and its implement regulation³⁴ (Regulation Respecting Investment in Canada) and National Security Review of Investments Regulations³⁵ to manage the national security. The last one is

²⁸ In August 1995, Japan Isuzu and Itochu trading agreement acquired travel 25% of shares, becomes the largest shareholder, according to travel Japanese parties reached a transfer agreement, the Northern Brigade land per acre only 50,000 RMB of discounted shares, premium obviously low, and there is also a device to be underestimated. Northern Brigade has 4 Germany’s large equipment, the actual price is RMB 100 million, but its assessing price was only 8 million Yuan. Travel assets loss seriously.

²⁹ In August 1995, Ford spent \$40 million offer investors about 139 million class b shares issued by jiangling motors, whose b shares accounted for jiangling Motors the offering 80% of the total, per cent of total issued share capital of 20%. Subscription price is slightly higher than net assets per share of jiangling motors. At the same time, Ford nominated 3 people to the JMC 9 person Board of Directors. In October 1998, jiangling Motors b share issuance to 170 million shares, Ford to 0.454 dollars each to subscribe to 120 million shares.

³⁰ 50 U.S.C. app. 2170.

³¹ 121 Stat. § 246 (2007).

³² 31 C.F.R. § 800 (2008).

³³ Investment Canada Act (R.S.C., 1985, c. 28 (1st Supp.)).

³⁴ Investment Canada Regulations (SOR/85-611).

³⁵ National Security Review of Investments Regulations (SOR/2009-271).

specifically for national security.

Model III. National security system is inherent in general economic law. Germany International Economic Law, Foreign Trade and Payment Act and their amendments have review system for national security. Russia use its Russian Federation guarantees Russia defense and national security programs with strategic business law to regulate national security review. Japan's Foreign Exchange and foreign trade law and Import and export trade law established a pre-notification review system for national security review.

Model IV. No specific national security review regulation, but have its in facto form, such as England and France. India used the pre-establish national treatment and automatic access channel. But if you are a country that is deemed as dangers or sensitive, it cannot pass this channel, and need to be reviewed.

4. Problems of Chinese National Security Review System

4.1 Legislation and Scope

4.1.1 The Legislation Level of National Security Review Is Too Low

In the Sino-US bilateral investment agreements negotiation, China is asked to transfer its investment law to "pre-establishment market access national treatment add a negative list" model, Shanghai FTZ is the pilot to accept this model. China (Shanghai) approach to record foreign investment in the free trade zone says: Chapter I General provisions article 3 "within the scope of national security reviews of foreign-invested projects, should be in accordance with the relevant provisions. "Therefore, before the new system of national security is established in Shanghai FTZ, it should still use the existing provisions at national level.

Though this system is for the all nation which is very important, but it is not strictly a law, but rather a series of legal documents. The only provision promulgated in law is Article 31 of Antitrust Law, but antitrust law's objective is for regulating the antitrust actions which may not relevant to national security. Also, the scope of the exiting national security review was established was for M&A, some of them not breach the concentration law may also threaten national security. The relation between these two kinds of review is neither inclusive nor exclusive. It is not proper to let the antitrust law leading the national security system for foreign investment.

4.1.2 Scope That Cannot Cover the Area besides Negative List

In the national level, "Catalog" list detailed information about where to ban or restrict some of the industry for foreign investment, it is not a negative list, all of the investment need to get permission in advance, therefore, in fact, Mainland China is included the national security review already in its market access period.³⁶ Therefore, the national security review system has not been used, it is only for supplement the Catalogue.

However, the new negative list model does not need permission from the government if the investment is not in the list. Therefore, these investments are out of censor according to the law. Most of the countries using the model of negative list have national security review system in case if the un-regulated investment is dangerous for national security, it can launch the national security review system to prevent or cure the damages, such as the U.S.. If Shanghai FTZ pilot promote its negative list to the whole nation, the unexpected area of non-regulated investment will need a buffer to prevent the most dangerous situation to national security lawfully instead of only by administration document, or non-document refer to this scope at all. The existing national security system only established by administration document, and it's only scope is M&A. It is far from enough comparing with the

³⁶ Ding Ding and Pan Fangfang: "On the analysis of the system of our country's national security review of foreign capital's M&A and suggestion", *Contemporary Law*, the first edition in 2012, p. 131.

scope of other countries accepting the same model.

Negative list only gives the investment which cannot access or need a further review, but it is not an open list, the objective is to encourage more investment, there is possibility that new area of investment may enter into as no regulation restrict its market access. This area will totally out of governance of law in the country respect to the existing Chinese investment law. Except for the U.S., Australia and German, National Security Review are not limited in its foreign investment law in the area of M&A, such as Canada also apply to market access, India combine these two, Russia clearly lists the area that under the national security review, England and France scattered this kind of review in many economic laws, Japan regulates that all direct investment that relating to national security need previous review.

In the Shanghai FTZ zone, the negative list remind the “national security review” which is except for the special measures to control foreign investment that explicitly set out, it is forbidden for the foreign investors to engage in social activities that may threat national security and public interest.³⁷ It is not clear in this document that how to evaluate such investment whether it compromise the national security, and there is no legal reference implement this provision.

4.2 Lack of Definition

“Notification” regulate the kind of investment in the scope of national security review, regulation implement more detailed procedure, these two compose a complete system of national security review system, but neither of them define “foreign investor” and “Domestic Corporation” refer to this system.

In Antitrust Law, none of such definition exist, neither does the laws that reminded in regulation. The regulation reminds two laws, so called regulation of mergers and acquisitions of domestic enterprises by foreign investors, Several Rules refer to investors of enterprises with foreign investment shareholding modification and Interim provisions on investment of foreign-funded enterprises in China. Except for the first one, the other two refer to Foreign Investment Three Law³⁸, but is also says that the definition is only for this specific law.³⁹

Mainland China legal document related to “foreign investors merger or acquit domestic industry” including one central government document namely Notification and three department administration document, all of these

³⁷ Apart from the special administrative measures listed in the Negative List, foreign investors are prohibited (or restricted) from investment in industries which are prohibited (or restricted) by China, or by international agreements/treaties China concluded with other countries/jurisdictions. Foreign investors are also prohibited from investment in projects which would compromise China's national or social security, and from business operations which would compromise the public interest.

³⁸ First times appeared in second article “place business competent sector in according to on foreign investors merger territory enterprise of provides under, and foreign investment enterprise investors equity change of several provides under, and on foreign investment enterprise territory investment of provisional provides under, about provides accepted merger trading applications Shi, for belonging to merger security review range, but applications people is not to Commerce made merger security review applications of, should suspended handle.....” second times in seventh article “..... (A) does not affect national security, the applicant may, in accordance with the provisions on mergers and acquisitions of domestic enterprises by foreign investors and the foreign-invested enterprises investors shareholding modification of certain provisions, the interim provisions concerning the investment in foreign-invested enterprises, the relevant provisions of, to the relevant authorities with the appropriate administrative privileges to handle mergers and acquisitions procedures.”

³⁹ Foreign investment enterprise investors equity change of several provides under second article: “This provides by said of foreign investment enterprise investors equity change, is refers to pursuant to China legal in China territory established of Sino-foreign joint venture operating enterprise, and Sino-foreign cooperation operating enterprise, and foreign-funded enterprises (following collectively for enterprise) of investors or its in enterprise of funded (including provides cooperation conditions) share (following called equity) occurred changes. “And on foreign investment enterprise territory investment of provisional provides under second article:” This provides by said foreign investment enterprise territory investment, is refers to in China territory law established, take limited responsibility company forms of Sino-foreign joint venture operating enterprise, and Sino-foreign cooperation operating enterprise and foreign-funded enterprises and foreign investment Corporation, to this enterprise of on behalf of, in China territory investment established enterprise or purchased other enterprise (following abbreviation “was investment company”) investors equity of acts.”

do not have such definition. In 401 legal document of Mainland China in the national level law, no definition exists. Only one ambiguous definition is in “Law on Foreign-funded Enterprises”, it says that the People’s Republic of China allow foreign enterprises and other economic organizations or individuals (hereinafter referred to as foreign investors) foreign-funded enterprises ‘establish within the territory of China’⁴⁰. Here, it defined it as foreign enterprises and other economic organizations or individuals. In case law, there is a case in appellate court of Shanghai, so called “Jin Steel co., LTD. and Shanghai equity inheritance disputes case”, court cannot find the definition, so Judge uses the principle of domicile to decide the case.

Domicile principle is easier to follow in law, but it is too simple and not practical for this system. The purpose of this kind of review is for “guide the orderly development of mergers and acquisitions of domestic enterprises by foreign investors so that to maintain national security”⁴¹ the fallback and serious feature as well as the buffer characteristic of this system needs a wide scope so that it can really perform its function. If no clear definition on its scope, the ambiguous will cause huge uncertainty both for investors and the country. Some scholar think that it is better not to define the term so that to extend the scope⁴², but here, without definition will leading to diverse applications in practice because mainland China is not a case law legal system, court may apply only the domicile principle that looser or overly broad definitions on its application. Some worried that too detailed national security law will scare away foreign investors, but the fact is, without a clear law, dangerous and threaten is still exist, the measures to deal with them will out of law that only depends on the discretion of administration, which may cause more possibility of unfair or bribe without law’s regulation. The proper way to protect the interests of foreign investors is to enact clear guidance by law with soft, loose, convenience design, considerate relief measure as well as reasonable consultation and fair communications procedural design.

Almost all the countries define its scope for “foreign investor”. The U.S. use a very broad definition, it regulated that foreign investor are represented for any individual or entity, entity are including any subsidiary, partnership, group or union, real estate, trust, corporate, department of a corporate, organization or any of the referred entity’s assets or service or products, any government. Australia also gives a detailed definition, Foreign investors are defined as non-Australia nationality to natural persons, one or several companies owned by non-Australian citizens, a trustee of the trust assets or number of non-Australian citizens or foreign companies hold significant benefits or accumulated the important interests of the company⁴³. German gives the definition as

⁴⁰ Article 1: to expand foreign economic cooperation and technological exchanges, promote the development of China’s national economy, People’s Republic of China allows foreign enterprises and other economic organizations or individuals (hereinafter referred to as foreign investors) foreign companies in Chinese territory, protecting the legitimate rights and interests of foreign-funded enterprises.

⁴¹ the preamble of the notice: “in recent years, with the in-depth development of economic globalization and China’s opening to the further expansion of foreign investors with investment increasing by way of mergers and acquisitions, contributed to the diversification of means of utilizing foreign capital in China, in optimizing the allocation of resources, promoting technological progress, improve the enterprise management level has played a positive role. To guide the orderly development of mergers and acquisitions of domestic enterprises by foreign investors, the interests of national security, the State Council agreed, in respect of building safety review of mergers and acquisitions of domestic enterprises by foreign investors (hereinafter referred to as mergers and acquisitions security review) system related matters as follows:”

⁴² Ji Rongrong: Jurisdiction refer to ICSID, Arbitration and Law, No. 92, p. 1.

⁴³ Foreign Acquisitions and Takeover Act 1975:26A Compulsory notification of certain section 21A transactions

(1) In this section, person to whom this section applies means: (a) a natural person not ordinarily resident in Australia; (b) a corporation in which a natural person not ordinarily resident in Australia or a foreign corporation holds a substantial interest; (c) a corporation in which 2 or more persons, each of whom is a natural person not ordinarily resident in Australia or a foreign corporation hold an aggregate substantial interest; (d) the trustee of a trust estate in which a natural person not ordinarily resident in Australia or a foreign corporation holds a substantial interest; or (e) the trustee of a trust estate in which 2 or more persons, each of whom is either a natural person not ordinarily resident in Australia or a foreign corporation, hold an aggregate substantial interest.

receiving possession of acquirers are foreign investors from outside the European Union or the European free trade association; or the acquirer was from the aforementioned enterprises in the area, but the business itself is at least 25% of the voting shares are controlled by foreign investors outside of this area.

Also, Mainland China do not have a clear definition refer to “domestic enterprise”. Canada provide a very broad definition of domestic enterprise, as long as part of the enterprise is operated in Canada, and there are several Canada people hired by the company, or operation of the company’s assets in Canada, it can be realized as domestic enterprise.⁴⁴ German also uses principle of place to decide the domestic enterprise. Russia regulate 42 types of “strategic company”, if foreign investor invest on these companies they need review.

Without a clear definition, ridiculer results will happen, for example, if one enterprise registered in Mainland China but controlled by foreigner, if it harms national security, whether we need to look it as foreign investor considering the diplomacy or only look it as nationals regardless of such foreign capital. Or if one company is a Chinese capital enterprise registered outside China, it may have to go through the national security process just like a foreigner.

5. Conclusion

National Security Review in investment activities is a crucial system in regulating foreign investment in hundreds of countries. Though it varies in each country, it plays a role as a buffer between foreign investor’s interest and domestic interests. However, the system in Mainland China is still imperfect with several problems. New national security review system is needy for matching the new model of investment policy in the future.

⁴⁴ Canada Investment Law 25.1 This Part applies in respect of an investment, implemented or proposed, by a non-Canadian...to acquire, in whole or in part, or to establish an entity carrying on all or any part of its operations in Canada if the entity has (1) a place of operations in Canada, (2) an individual or individuals in Canada who are employed or self-employed in connection with the entity’s operations, or (3) assets in Canada used in carrying on the entity’s operations.