DIRECTORATE GENERAL FOR TRADE
EUROPEAN COMMISSION

Summary of contributions to the European Commission's public consultation on "The future investment relationship between the EU and China"

Disclaimer:
This document does not present the official position of DG Trade or of the European Commission. It is designed to summarise the views of interested parties who gave comments on the future investment relationship between the EU and China. The suggestions in this document in no way prejudge either the nature or the form or content of any future action by the European Commission

1. INTRODUCTION

In the context of an Executive-to-Executive meeting on 29 April 2010, European Commission President Manuel Barroso and Chinese Premier Wen Jiabao instructed their respective teams to study the options for enhancing the bilateral investment relationship between the EU and China. To this end, a "Joint EU-China Investment Task Force" was launched in summer of 2010 to explore the scope for deeper cooperation on investment, including considerations of a possible standalone investment agreement.

In this context, the European Commission launched a broad public consultation to gather views from relevant stakeholders regarding the future EU-China investment relationship.

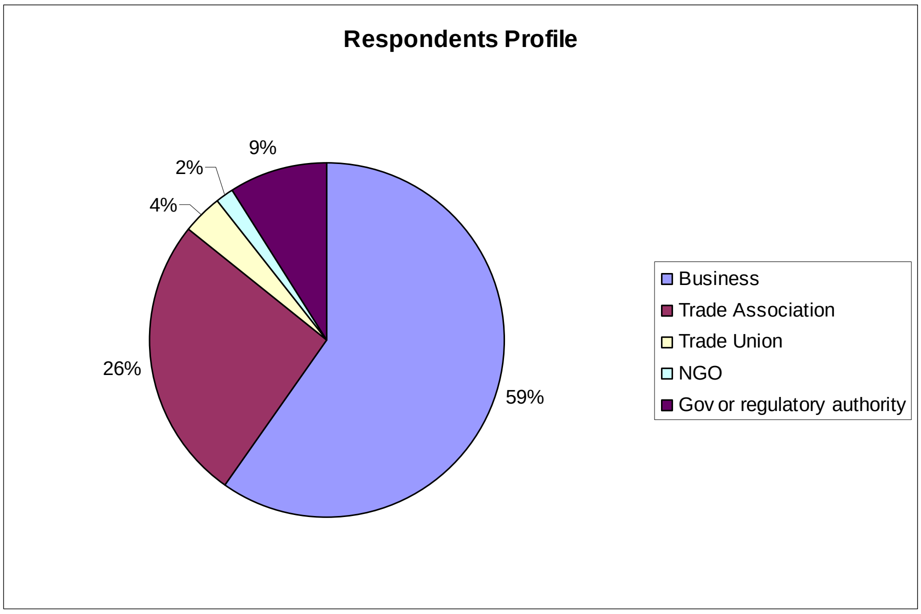
The replies to the questionnaire provide the European Commission with data, information and views of stakeholders about the current barriers and protection standards affecting EU direct investment in China, and about the (possible) effects of an EU investment agreement in China.

2. THE PUBLIC CONSULTATION AND THE QUESTIONNAIRE

The public consultation ran from 5 May to 5 July 2011. The exercise was open to all stakeholders, both within the EU and in third countries.

An on-line questionnaire, hosted by the European Union's Your Voice in Europe's web site, was open to all stakeholders interested. The questionnaire had 34 questions covering three main topics: investment environment in China, investment environment in the EU, and the potential impacts of an EU-China investment agreement. The written version of the on-line consultation is to be found at:
http://trade.ec.europa.eu/consultations/?consul_id=153

In all, 57 exploitable answers were received from a wide range of respondents. Submissions came from private companies having their headquarters in 16 different Member States, trade associations, trade union, governmental authorities and NGOs.



59% of the respondents were companies, 26% were trade associations. The business sectors represented were diverse, both in services and non-services, including among others the steel industry, distribution services, manufacturing, mining, automotive, banking and other financial services, pharmaceuticals and legal services. 75% of the respondent companies had already invested in China, mostly in the form of Greenfield investment (for 2/3 of them) and under a wholly foreign-owned status (for 70% of them).

In addition, 9% of the replies came from governmental or regulatory authorities, 4% from trade unions and one of the respondents was an NGO.

The full list of contributors is attached in the annex and links to those contributions where respondents agreed to have them published will be made available on the Trade website.The on-line consultation exercise made clear that all contributions would be published unless respondents indicated that they did not wish their contribution to be made public.

3. EXECUTIVE SUMMARY AND CONCLUSION

On the general **evolution of the investment climate in China** in the past 5 years, the views were quite balanced between those who believe that the climate has improved (36%) and those who believe that it has worsened (24%). The general perception was that China had modernized its investment and business environment as a result of its accession to the WTO and a general economic reform process. However this evolution seems to be uneven across sectors and many obstacles and difficulties remain for foreign investors. Some respondents even raised a "reform fatigue" phenomenon and recently increasing protectionism.

China seems to be an **increasingly strategic market for EU investors**, with 60% of business respondents foreseeing China as a Top 5 destination for investment in their sector in 10 years time compared to 46% in 2011. In addition, 11 business respondents predict for China to become a more important destination for investment in their sector in 10 years time than it is now. The five **most attractive aspects of the Chinese market** are the size of the Chinese market, the proximity to the clients/market, the lower labour costs, the costs of resources and the productivity.

Regarding the **barriers to investment in China**, most of the respondents indicate that they have experienced difficulties when investing, or trying to invest in China, some of them even stating that those difficulties deterred them from going through with investment plans. Most often, the barriers encountered arose both before investing (i.e. pre-establishment) and after having invested (i.e. post-establishment). The most problematic barriers identified by the respondents were: licensing requirements/procedures, foreign ownership limitations, regulatory approval procedures, prohibition to invest/limited scope of business, joint venture requirements, subsidies enjoyed by Chinese companies and technology transfer requirements. Half of the respondents also experienced a form of **unfair treatment** and several of them claim to have experienced issues linked to the protection of their **key technologies** when investing in China.

The public consultation also showed that the main **problem respondents saw in China related to barriers to the market** and the **lack of a level playing field** once they had managed to invest in China. On balance the added value therefore was felt to be in an agreement which would help create better access to the market and crucially **increase transparency, legal certainty** and fair treatment of foreign investors. It was also clear that instruments afforded by investment protection agreements, in particular investor to state dispute settlement, were considered as less crucial since resorting to investment arbitration against China was felt to be a last resort only given the fear of retaliation by China.

The **merger review procedures** are equally an area of concern for EU investors in China, with only 12% of respondents considering that those procedures are followed in a fair, reasonable, predictable and non-discriminatory way.

A substantial number of respondents consider that **China's subsidies policy** acts as a barrier to investment in China, stating that those subsidies which are not attributed in a transparent manner largely favour Chinese companies and that this distorts competition and creates an unlevel playing field between foreign and domestic companies in China.

On the **Chinese legal system**, 80% of the respondents said that they did not have confidence in it to protect their rights as investors because of the lack of transparency and consistency of the system which is subject to political pressure. They rely mostly on amicable settlement to deal with legal conflicts in China, and most of them indicated that they would consider starting **investment arbitration** proceedings against China only in case of complete expropriation, because of the fear that it would deteriorate their relationship with the Chinese Government.

Regarding the **investment climate in the EU**, a strong majority of respondents believe Chinese outward investment in the EU is increasing. However, when asked specifically about the investment in the EU by **Chinese state-owned enterprises (SOEs),** a majority of them replied that they see no particular issues. About 1/3 of them however indicated that they have concerns about the unfair competition created by the differences in the situation of EU companies and Chinese SOEs, notably because of the subsidies received by the latter, which do not face the same strict competition/state aid rules as companies in the EU.

The replies to the question regarding the **impact on the investment climate** of an EU-China investment agreement show strong support to an initiative which would aim to facilitate EU investment in China. Most of the respondents express a strong interest in obtaining better access to the Chinese market and in the elimination of unfair competition with domestic companies. They also emphasize the need to improve the legal framework for EU investors in China by ensuring more clarity and predictability, as well as a better implementation of the rules.

A majority of respondents considers that EU-China investment cooperation should focus specifically on facilitating EU **Small and Medium Enterprises'** investment in China. In general, the barriers encountered by SMEs in China are the same as the ones encountered by large companies, but those barriers are more pronounced for SMEs, which do not always have the financial and human resources needed to bear long and expensive administrative or legal procedures. They emphasized the need for simplified rules, better information and specific assistance for SMEs investing in China.

A large majority of respondents believes that it would be preferable to have **one single EU agreement covering investment protection** rather than 25 different Bilateral Investments Treaties (as at present) with China. An EU-China agreement would contribute to clarifying the legal and operational framework for EU investors in China, and reciprocally, thus increase efficiency and business confidence. Several respondents however stressed the need to ensure that the_level of protection is at least equivalent to the "best" BIT concluded by Member States and that such a new agreement would not negatively affect existing rights of investors provided in existing BITs. In addition to the standard investment protection provisions, several respondents pointed out that such an agreement would also need to focus on implementation and enforcement of commitments (including existing WTO commitments).

Regarding the potential **impact of an EU-China investment agreement on employment and labour standards,** the majority of the respondents believes that they could be positively affected by such an agreement, both in the EU and in China. The potential positive impacts mentioned relate mostly to the creation of employment opportunities, especially more qualified jobs and to the best practices exported by EU companies to China in terms of e.g. labour standards, safety and corporate governance. Some respondents however expressed concern that an EU-China investment agreement could create unfair competition due to the difference in the cost of labour, thus encouraging a lowering of social standards and a relocation of EU enterprises to China. Some respondents advocated the inclusion of a set of core labour and social standards in such an agreement, to which both parties would commit. At the same time other respondents (trade associations, in particular) stressed that social and labour issues fall outside the scope of an investment agreement and should not be covered by it.

Concerning the potential **impact of an EU-China investment agreement on the environment**, a majority of respondents believes that this agreement could have a positive effect in China and a positive or neutral effect in the EU. They highlighted the improved opportunities that this agreement could bring for better cooperation and integration by both EU and China on sustainable development objectives. They also thought that it could positively influence China's environmental policies by increasing policy transparency and encouraging the implementation of mutual standards. Some of the respondents however feared that if no global standards were set, such an agreement could encourage countries to lower environmental standards and policies in order to attract investment. As in the context of employment and labour standards, a number of respondents, while stressing the need to ensure equal treatment of domestic and foreign companies in the implementation of environmental regulation, advocated against the integration of environmental standards and mandatory requirements in such an investment agreement, since such issues should be addressed elsewhere.

Finally, asked about the potential **impact on human rights**, a majority of respondents replied that an EU-China investment agreement would have no impact in the EU. In addition, almost half of the respondents thought that an agreement could have a positive impact on China. They pointed out the opportunity for better cooperation and exchange of information, which could increase transparency and positively influence Chinese human rights policies. Contrary to these opinions, some respondents expressed concerns that such an agreement could encourage a lowering of EU practices and standards. In general they believe that the impact could be positive, provided that the agreement included specific provisions on human rights standards, whereas other believe that those standards should not be included in such an investment agreement because it could paralyse negotiations and potentially threaten or weaken the protection of EU investment abroad.

4. RESPONSES TO THE QUESTIONNAIRE

I) INVESTMENT ENVIRONMENT IN CHINA

In the online questionnaire, several questions in this part were shown only to respondents having indicated before that they were either a business or a trade association representing businesses. With a view to present the results more clearly, the order of the replies reproduced below does not match exactly the order of the online questionnaire.

A) Questions for companies and trade associations having already invested in China:

1. *Question: On a global basis, where do you rank China as a destination for investment for your sector? a) in 2011 and b) in 10 years*

In 2011, 16% of the business respondents (companies and trade associations) rank China as top destination for investment in their sector, 46% rank China as top 5 destination, 27% as top 10 destination and 11% indicate that China is not a top 10 destination for investment in their sector. Concerning future investment plans, China appears to be an increasingly strategic market for the business respondents. Indeed, 60% of them predict China to be a top 5 destination for investment in their sector in 10 years compared to 46% in 2011. Moreover, 25% of business and trade association respondents predict China to become a more important destination for investment in their sector in 10 years time than it is now.

2. *Question: What is the status of your operation in China?*
3. *Question: What kind of investment have you made in China?*
4. *Question: When did you start investing in China?*

75% of the respondent companies had already invested in China, and most of them started investing in China a long time ago: 42% started investing over 10 years ago and 50% between 2 and 10 years ago. The results obtained with this public consultation thus come for a large part from companies that have both a long term view for their investments in China, and a good knowledge/experience of the Chinese market and policies. 2/3 of investments were realised as Greenfield investments and 1/3 as mergers & acquisitions. Finally, 70% of the investments made by the respondents were constituted as wholly foreign-owned enterprises (WFOE), 25% as joint ventures (JV) with the EU investor holding a majority share and 5% as a JV with the EU investor holding a minority share. The domination of WFOE in the respondent companies is also interesting because it can give us a view on the specific difficulties encountered by these kinds of companies in China.

5. *Question: Which aspects and factors of the Chinese market attracted (or attract) you the most and made (or might make) you decide to invest?*

Out of the 15 elements and factors that were listed as possible replies to this question (in addition to the possibility of indicating extra factors), **five of them appear as the key factors: the size of the Chinese market, the proximity to the clients/market, the lower labour costs, the costs of resources and the productivity.** Others factors mentioned: the good infrastructure, the proximity to talent, the ease of doing business, research and development, the attitude of authorities and the attitude of local partners.

6. Question: *Have you experienced difficulties when investing, or trying to invest, into China?*

   If you answered yes, did these difficulties arise mostly:

   - *Before investing in China (i.e. pre-establishment)?*
   - *After having invested in China (i.e. post-establishment)?*

29 respondents indicated that they (or their members) have experienced difficulties when investing, or trying to invest, into China. Most of the respondents who experienced barriers indicate that they arose both pre-establishment and post-establishment.

Some of the respondents were completely prevented from investing in some sectors which are entirely closed to foreign investors. In particular, the *European Express Association*, a trade association representing the interests of the express integrators, mentioned the revised "Catalogue of Industries Guiding Foreign Investment", which added domestic express delivery to the prohibited list of sectors. A large company also mentioned the increased restriction for investment in *high and new technologies* such as the development of *genetically modified and bio agriculture*.

A large number of respondents stressed the foreign ownership limitations and/or the joint venture (JV) requirements that they faced when investing in China. For instance, based on China's steel industry policy issued in 2005, foreign investors in the *steel sector* cannot have a majority shareholding as the steel industry is considered a "strategic" industry related to "national security". One of the companies operating in the steel sector explained that the JV requirements they faced made them restrict their investment plans to areas open to wholly foreign-owned enterprises. Another company in the steel sector explained that they established a JV in 2002, but due to different cultures and lack of operational control they had to dissolve it after 4-5 years. They also complained about the limitations of access to strategic raw materials. Several companies from the *automotive sector* mentioned the new draft Catalogue, which limits foreign investment in "key new energy vehicle component manufacturing" to joint ventures with no more than 50% ownership by the foreign partner. Finally, a company operating in the *power and rail transport sector* raised the issue of the prohibition to hold majority share in power generation and rail and the excessive and unpredictable control of foreign investments according to the national security review mechanism.

The length of the licensing and regulatory approval procedures was another barrier to investment often mentioned by respondents. One of the companies even stated that it had to create an administrative department for the sole purpose of dealing with the ongoing government requirements.

Moreover, many respondents complained about the lack of regulatory transparency and predictability. They mention opaque regulations, often only published in Chinese, different standards and inconsistent implementation of laws at national, provincial and local level, as well as continuous modification of regulations with immediate effect. One of the examples given was the sudden change in the recently published *social insurance law* leading to a substantial increase in the company contribution to employees' insurance cost. A *packaging material and machinery* company also stated that it lost 1 million € because of discordance among different institutions about machinery duty free import.

Among the difficulties experienced by the respondents when investing in China, the infringements of intellectual property rights and poor enforcement of the existing legislation protecting intellectual property appear quite frequent. According to a trade association, the legislation exists but the application and enforcement is difficult and becomes expensive, therefore patents are often not registered, increasing the risk of being copied. According to a company from the *steel industry*, the issue of the forced technology transfer seriously blocks the market entry and the business expansion of foreign companies in China by rendering the conduct of mergers and acquisitions difficult for multinational companies in the steel business and by putting them in a passive position when negotiating with Chinese partners.

A company in the *automotive industry* stressed that foreign-invested companies cannot participate in national or the vast majority of local government R&D programs or receive government R&D funding. Besides, it added that local government officials tend to offer attractive incentives to foreign-invested companies to invest in China, however, some of the promises cannot be fulfilled in a timely manner once investment is made.

According to a company in the *steel industry*, the presence of state-owned enterprises makes it difficult for foreign investors to enter this sector, especially in merger and acquisitions activities and concerning government procurement.

Detailed answers concerning the difficulties experienced by investors in China were in particular given concerning two sectors.

Firstly, a respondent raised a number of issues regarding the transport sector – in particular in relation to rail transport citing a clear policy of technology transfer and local content requirements to ensure protection of local industry. Furthermore the sector seems to be prone to increasingly burdensome licensing procedures for foreign suppliers. These together have prevented foreign companies effectively from bidding on public transport contracts. The respondent also raised the issue of the protection of intellectual property rights, claiming that China is reported to be filling patent applications in several foreign countries (ex US, Brazil) on technologies that were originally provided by foreign suppliers. Finally, the respondent indicated that the currency restrictions create limits on profit repatriation.

Secondly, the trade association representing the recording industry worldwide (IFPI) mentioned an important number of investment barriers in the *recording industry*. Some sectors are entirely closed to foreign investors, according to the draft Investment Catalogue. Foreign companies are thus prohibited from investing in the business of publication and production of audiovisual products and electronic publications, in addition to be prohibited from setting up any digital or online music services. There are also foreign ownership limitations in the sub-distribution of audiovisual products and in value-added telecommunication services. The trade association then reported that the foreign record companies are being discriminated against because of the censorship regimes for both physical and digital formats of foreign sounds and video recording. Finally, foreign record companies are facing unclear and obscure procedures to apply for a permit or approval to import or distribute foreign audiovisual products.

7. *Question: Please rank the five investment barriers that you consider the most problematic in China (from 1 – the most problematic; to 5 – the least problematic)?*

In accordance with the difficulties described by the respondents in their replies to the previous question, four investment barriers appear to be the most problematic for companies investing, or tying to invest in China: **licensing requirements/procedures, foreign ownership limitations, regulatory approval procedures, prohibition to invest/limited scope of business and joint venture requirements**. If we consider that the licensing requirements and the regulatory approval procedures can be regrouped into one category, then it appears clearly that in the respondents' view, the difficulties that they are encountering in the Chinese market are not only linked to the access to this market (which is limited by the three other barriers mentioned), but also to the implementation of the rules and the transparency/clarity of the Chinese policies. Appearing next in the respondent's ranking of most problematic barriers are the subsidies enjoyed by Chinese companies and the technology transfer requirements, which are specifically addressed by questions 17 and 10 respectively. Finally, other barriers mentioned included: local partner requirements, registration requirements, tax measures, excessive capital requirements, nationality/residency requirements, national security control, and problematic requirements for qualification.

8. *Question:* *Have any barriers that you have encountered deterred you from going through with plans to invest in China?*

9 respondents stated that barriers encountered deterred them from going through with plans to invest in China. For instance, a small company operating in the food trade business indicated that excessive capital requirements stopped it from expanding further its investments in China. Moreover, a large company in the steel industry stated that the joint venture requirements made them restrict their investment plans to areas open to wholly foreign-owned enterprises, because they feared a forced technology transfer. As a result, they were not able to invest in their core business (specialty steel manufacturing). Another large company in the same sector indicated that it had decided to make new investments in Taiwan instead of investing further in China, because of their fear to be copied.

9. *Question:* *Have you experienced any unfair treatment in connection with your investment in China?*

17 business respondents (50%) claim to have experienced a form of unfair treatment in connection with their investment in China. In their replies, the respondents report a general asymmetry of treatment with local companies, notably in terms of foreign ownership limitations and joint venture requirements, as well as concerning tax benefits. In the *automobile industry* a company pointed out the new proposed restrictions on foreign investment in key new energy vehicles component manufacturing as a form of unfair treatment. A company from the *steel industry* stated that a State-owned enterprise can get policy and financial support when merging with small steel companies. In the *textile industry*, EURATEX, a large trade association, indicated that local companies that are directly or indirectly supported by the authorities have a competitive advantage as they have faster and more efficient ways to deal with the regulatory and bureaucratic procedures. Without a local partner, investment procedures are more complex and take longer and this is even more evident if the foreign company is a small or medium enterprise and thus not considered by local authorities as a “strategic investment”. Finally, the EU Chamber of Commerce in China recalled that in its 2011 Business Confidence Survey, firms reported that they viewed government policy towards FIE as becoming increasingly unfair, and also that they expected this development to continue in the future.

10. *Question:* *Have you experienced any issues linked to the protection of your key technologies when investing in China?*

13 business respondents (38%) stated that they have experienced issues linked to the protection of their key technologies when investing in China. Among those respondents, many of them complained of issues linked to copying. A company producing copper products stated that local companies had copied their brochure and modus operandi. A large automotive supplier reported that the company had encountered trademark/patent infringement and counterfeiting issues which resulted in a loss of know-how associated with high attrition. One large company in the steel industry stated that their plants have been copied in a very short period of time. Finally, in the textile industry, a big trade association stressed that copying and counterfeiting in China are key problems for its sector, because parts of its members' competitive assets are related to creativity and to the protection of designs and models. The association added that even if Chinese legislation and the public authorities' awareness of this problem are improving, they still faced serious threats and this was a factor that discouraged investment. Another trade association in the services sector indicated that its members encountered frequent violations of intellectual property rights in China. Beyond the infringement of IPRs, the procedures to assign and enforce those rights were also criticised by respondents. A company in the pharmaceutical industry stated that any assignment of intellectual property rights by a Chinese entity to an offshore entity will need to be registered with the MOFCOM which puts an extra burden on companies. Finally, the issue of technology transfers requirements was raised by a few respondents, notably by a company in the steel industry, which stressed that technology transfer requests are always part of cooperation discussions.

11. *Question: As an investor, how do you usually deal with legal conflicts in China?*

The respondents' most common approach to dealing with conflicts in China by far was amicable settlement. Only then did some respondents say they would respond with "end of contract/cooperation" as well as recourse to local legal proceedings. The replies received to the next question about the respondents' level of confidence in the Chinese legal system help explain why this way of dealing with legal conflicts in China only appears as a third choice in the respondents' answers, followed closely by recourse to "international arbitration" and "diplomatic support".

12. *Question: Do you have confidence in the Chinese legal system to protect your rights as an investor?*

80% of the respondents who expressed an opinion on the Chinese legal system said that they did not have confidence in it to protect their rights as investors. They explained that the Chinese legal system lacked transparency and consistency, both in the decisions and in the judicial process itself. They indicated that there was a gap between the written laws and their application and enforcement. Some respondents pointed at the existing bias towards local companies, stating that the Chinese courts and authorities are reported to be usually not neutral towards foreign companies. Finally a number of respondents stressed that the legal decision process was subject to political pressure, both from the local SOEs and from the administrative agencies at central, provincial and municipal level, which have a strong discretionary power to decide on foreign investment policies.

13. *Question: Would you consider starting international arbitration proceedings against the People's Republic of China on the basis of an investment treaty in the case of unfair and discriminatory treatment, or expropriation without compensation, of your investment?*

40% of the respondents who answered this question indicated that they would consider starting arbitration proceedings against China. While those of the respondents who answered “yes” did not give specific explanation, it is however interesting to look at the justifications brought by those who answered that they would not consider starting international arbitration proceedings against China. Several of them feared that starting such proceedings would prevent them from doing business again in China, or that it would impact other investments that they already had made in China. Others stated that such proceedings took too much times, resources and energy, therefore they would rather focus on projects with higher success rates. Other companies said that they would only start those proceedings in cases of complete expropriation, because this kind of legal complaint would seriously deteriorate the relationship with the State.

14. *Question: Have you ever used the provisions of any existing bilateral investment treaty to defend your rights as an investor?*

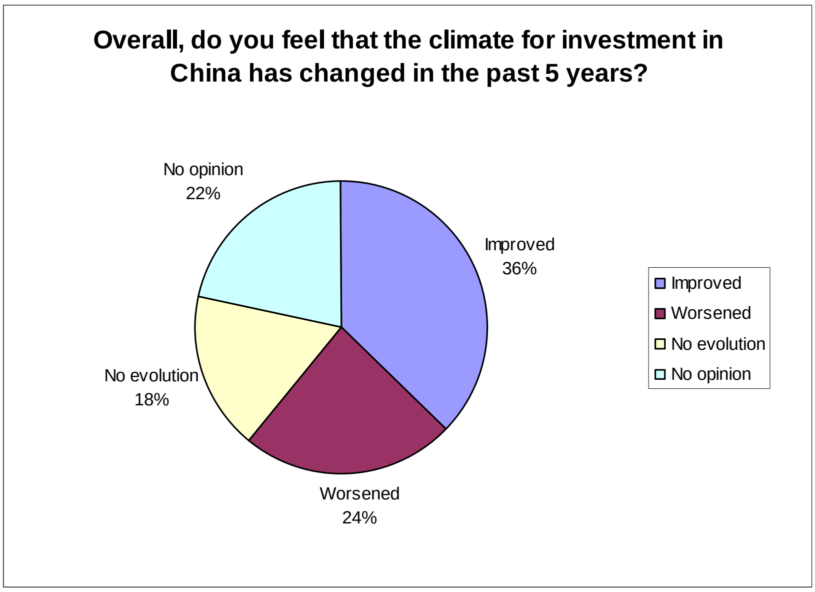
If you answered Yes: Have you ever used the provisions of a bilateral investment treaty concluded between an EU member state and China to defend your rights as an investor?

6 respondents stated that they have used the provisions of an existing BIT to defend their rights as investors in the past, but the information given about these legal cases is confidential. However it does not appear from the replies that any respondent ever used the provisions of a BIT between China and an EU Member State.

B) Questions for all respondents:

15. <u>Question:</u> *Overall, do you feel the climate for investment in China has changed in the past 5 years?*

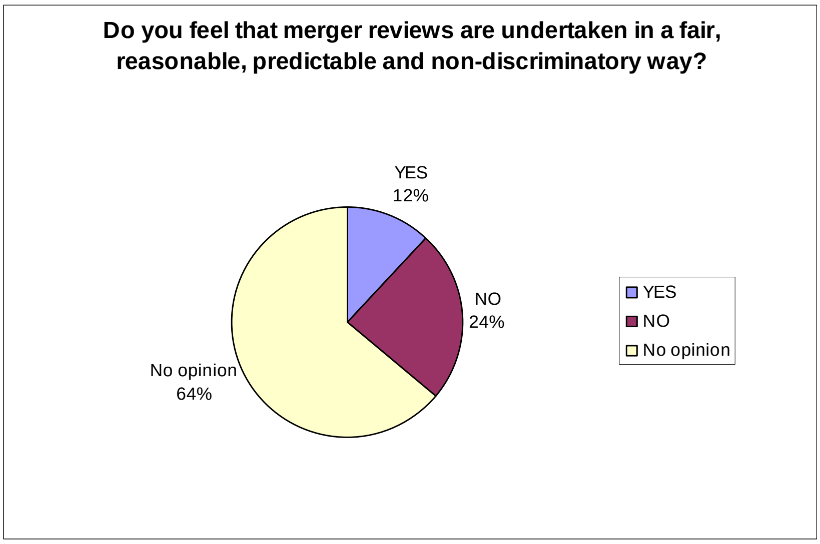
36% of the respondents felt that the investment climate in China had improved for the past 5 years, whereas 24% of the respondents felt that it had worsened.



In terms of improvement, respondents mentioned China's accession to the WTO and the economic reforms that occurred in the process. In general, they perceived a general modernisation of China's behaviour towards business. As a result of this evolution, they felt that the general investment climate had improved, but unevenly across sectors. Other respondents indicated some improvement concerning the scope of business for foreign investors in China. While a few of them mention a wider range of industry sectors now open to foreign investment (e.g. wine, steel), others pointed out the allowance of greater shareholding to foreigners in Chinese companies. The assessment of the evolution of the investment climate in China is therefore closely linked to the sector the respondents represent.

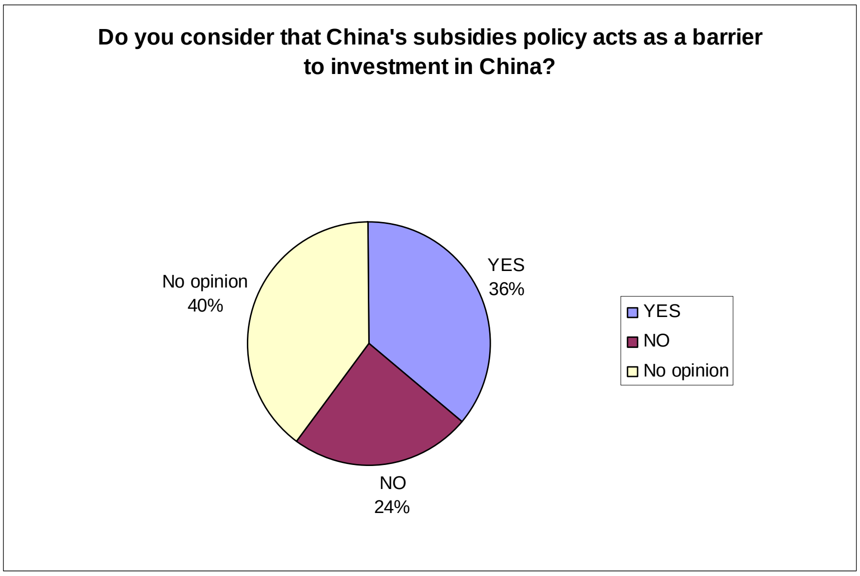
In terms of worsening, a few respondents believe that a “reform fatigue” phenomenon has taken place in China, with a general slowing down of reforms. Moreover, they stressed the relative implementation of the WTO commitments (e.g. intellectual property rights enforcement). They indicated that there were a lot of remaining issues across sectors, for instance the uncertainties, the lack of transparency and the sudden changes in policies that impact the companies' activities. For instance, a respondent mentioned the sudden change in the Social Insurance Law, to be effective in July, which requires companies to substantially increase their contribution to employee’s insurance. A number of respondents stated that certain policies (e.g. indigenous innovation measures, preferential financing conditions, licensing and regulatory procedures) have the effect of discriminating against foreign owned companies in favour of domestically owned companies. Moreover, these kind of policies seem to be part of a more general evolution that saw a recent increase in China's protectionism (persisting non-trade barriers, technology transfer obligations, on-going restrictions to foreign investments, access difficulties to public procurement, indigenous innovation etc.) and its desire to create national champions (subsidies, preferential treatment for SOEs). In the automotive sector in particular, a large company stressed that the new draft Catalogue limits foreign investment in key new energy vehicle component manufacturing to joint venture with no more than 50% ownership by the foreign partner. They state that this policy forces foreign companies in key new energy vehicle components to partner with Chinese companies that do not have equivalent capabilities in the area.

16. *Question:* *Do you feel that merger review and merger review procedures are undertaken in a fair, reasonable, predictable and non-discriminatory way?*



A good share of the respondents (notably those who were not companies having invested in China), did not have an opinion on those procedures (64%). However, **among the respondents who expressed an opinion on the Chinese mergers review procedures, 2/3 of them raised concerns regarding this process**. Those concerns related mostly to the lack of transparency and predictability that surrounds the mergers review procedures, which, in addition to be long, also entails undue delays. One of the respondents thus stated that the approval of its joint venture had been delayed for 2 years for no reason. The procedures followed vary according to the province concerned, which adds to the confusion. Other respondents raised the issue of the participation of Chinese competitors in the *ad hoc* committee performing the review, which reinforces the general suspicion that mergers reviews are used as a means of protecting domestic players and discriminating against foreign-invested enterprises. Respondents expressed general concerns about the fairness of the merger review process. One of the respondents stressed that the approval process for the merger between Motorola and Nokia Siemens Network, although approved by antitrust agencies in 8 countries, was unduly delayed by Chinese authorities. Another respondent referred to the Coca-Cola/Huiyuan merger approval process as a case of discrimination against foreign investors. Finally, some respondents indicated that they had concerns about the impact on the merger approval process of the recently release national security review mechanism.

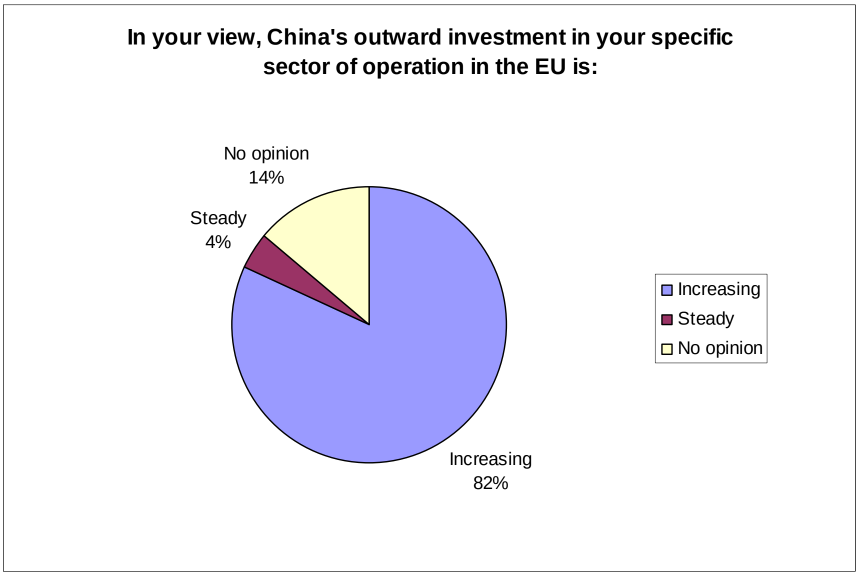
17. <u>Question:</u> *Do you consider that China's subsidies policy acts as a barrier to investment in China?*



As for the merger reviews procedures, a good share of respondents did not have an opinion on China's subsidies policy (40%). However, **60% of the respondents who expressed an opinion considered that China's subsidies policy acts as a barrier to investment in China**. As a general remark, subsidies policies were criticised by respondents for not being transparent. Moreover, a substantial number of respondents stated that subsidies largely favoured Chinese companies (especially State owned enterprises), and that this distorted competition and created an unlevel playing field between foreign and domestic companies in China. Respondents also indicated that subsidized companies had a strong financial advantage, especially in public procurement/bidding situations. State owned enterprises (SOEs) were notably often favoured in public tendering for projects and would not necessarily survive without subsidies. One respondent indicated that the unfair competition created by the subsidies received by domestic companies was particularly strong in the area of research and development. In the automotive industry for instance, it seems that the Chinese government provides substantial subsidies to domestic companies making new energy vehicles and components, whereas little subsidy is provided to foreign-invested companies in the same area. A trade association representing the interest of the automotive industry even indicated that the subsidies are granted exclusively to indigenous brands involved in new technologies.

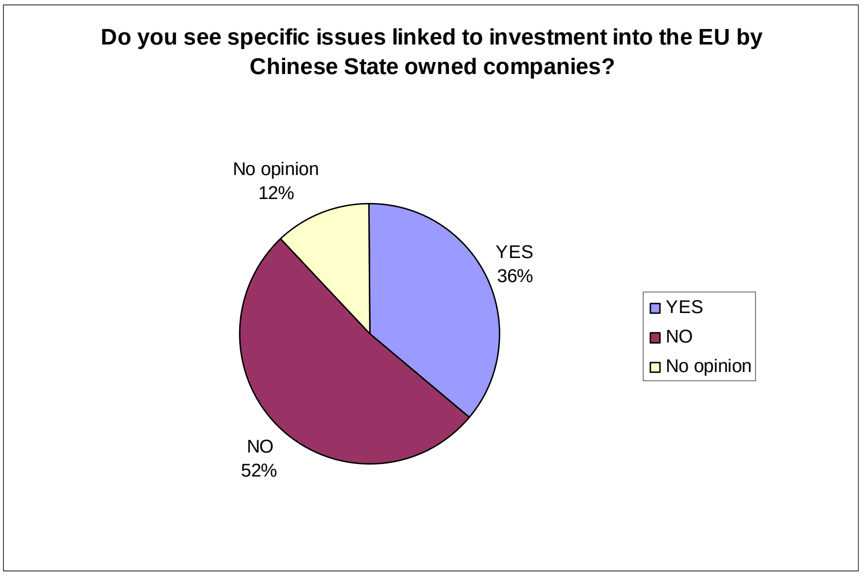
II) INVESTMENT ENVIRONMENT IN EU

18. *Question: In your view, China's outward foreign investment (i.e. Chinese companies investing abroad) in your specific sector of operation in the EU is:*
19. *Question Are there already Chinese companies that have invested in your sector in the EU that compete with you?*



Half of the business respondents (companies and trade association representing business) indicated that there were already Chinese companies that have invested in their sector in the EU and that competed with them. Moreover, **82% of the respondents felt that China's outward foreign investment in the EU in their sector of operation was increasing.** As an example, the French Permanent Delegation to the EU indicated that the Chinese outward investment flows in France amounted to 118 million Euro in 2009, compared to less than 20 million Euro in 2005.

20. *Question: Do you see specific issues linked to investment into the EU by Chinese state owned companies?*

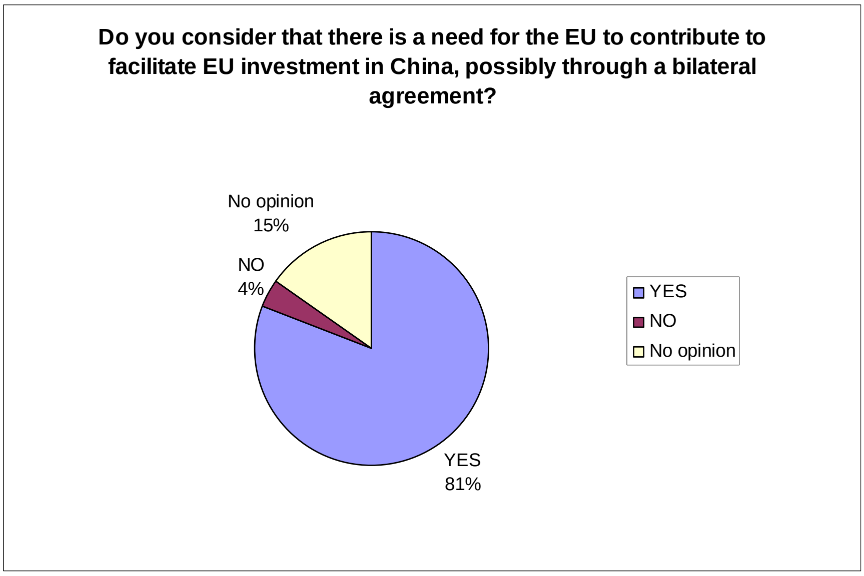


A majority of respondents (52%) did not see specific issues linked to investment into the EU by Chinese state owned enterprises (SOEs). Those of the respondents who expressed concerns stressed the unfair competition created by the differences in the situation of EU companies, which have to respect strict standards, and Chinese SOEs, in terms of prices, product quality, but above all concerning the subsidies received by those companies. A number of respondents advocated in favour of the application to these companies of the same competition rules that EU companies face when operating in the EU market, notably the EU anti-subsidies/state aid rules. They also pointed out that full transparency on the origin of the capital should be required from these companies. In particular, concerns were expressed by respondents that SOEs may benefit from the political and financial support of the Chinese authorities in public procurement tenders in the EU. As an example, one respondent mentioned the recent case of the public contract awarded to the Chinese SOE COVEC (China Overseas Engineering Group) by the Polish government due to a tender far below the minimum price expected, thus raising a debate about unlawful dumping practice. Finally, some respondents expressed concerns linked to the Chinese SOEs' investment in key technologies or critical infrastructures.

III. POTENTIAL IMPACTS OF AN EU-CHINA INVESTMENT AGREEMENT

A. Impacts on the investment climate

21. Question: *Do you consider that there is a need for the EU to contribute to facilitate EU investment in China, possibly through a bilateral agreement?*

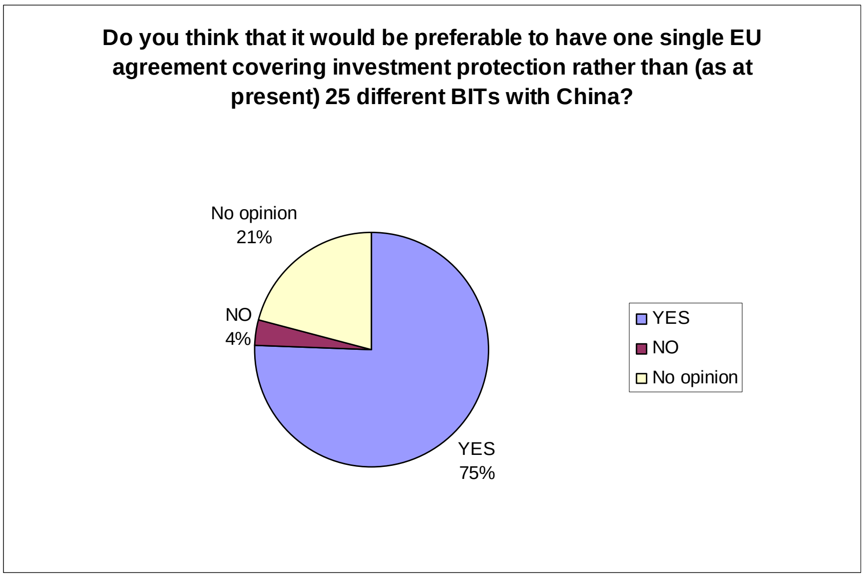


A very large majority (81%) of respondents considered there to be a need for the EU to contribute to facilitate EU investment in China, possibly through a bilateral agreement. Most of the respondents stated the need to ensure better access to the Chinese market for EU investors and to improve the legal framework for EU investors in China, by creating more stability and gaining better investment protection. According to them, an EU level initiative would contribute to eliminate unfair competition and raise general issues of concerns without affecting the status of EU companies affected. It would also contribute to increase clarity and predictability of the investment environment in China and the implementation of laws and commitments. Finally, for a few respondents, an EU level agreement could be a way of gaining more negotiating power and have more influence, also on other aspects, like environmental and labour policies in China. The two respondents who gave a negative answer did not give specific explanations.

22. *<u>Question:</u> Are there any specific issues that EU-China investment cooperation should focus on for facilitating EU small and medium enterprises' (SMEs') investment in China?*

A majority of respondents (51%) thought that there were specific issues that EU-China investment cooperation should focus on for facilitating EU Small and Medium Enterprises investment in China. A large number of respondents stated that in general, the barriers encountered by SMEs in China were the same as the ones encountered by large companies, but those barriers were even more problematic for SMEs, which do not always have the financial and human resources needed to bear long and expensive administrative or legal procedures. They mentioned a number of issues that are specifically difficult for SMEs: financing (notably the access to local banks), capital requirements, the procedures to set-up a company, visa restriction, double taxation, the lack of legal support/advice, regulatory controls and licensing requirements, the issue of intellectual property rights protection/enforcement and unfair competition with local SMEs. A respondent company pointed out the need for simplified rules, for instance a website in China with online payment for European SMEs, and reciprocally for Chinese SMEs in EU. EURATEX, a large trade association in the textile sector, stressed that the existence of focal points of information and assistance for SMEs was of key importance. It also insisted on the importance of cooperation and joint projects between EU and China, like the ongoing EU-China Trade Cooperation project. Another large trade association, BUSINESSEUROPE, stated that there had been recently some positive initiatives by the European Commission to give advice on investment and market access conditions for SMEs, such as the recently launched EU SME Centre. The association advocated for synergy effects to be triggered through effective coordination and cooperation between this Centre and other already existing help desks or European business service providers, notably at national level.

23. *<u>Question:</u> Do you think that it would be preferable to have one single EU agreement covering investment protection rather than (as at present) 25 different bilateral investment treaties with China?*



75% of the respondents thought that it would be preferable to have one single EU agreement covering investment protection rather than the present 25 separate BITs with China. Several respondents indicated that an EU-China agreement could contribute to clarifying the legal and operational framework for EU investors in China, and vice versa. They added that an EU bilateral investment treaty (BIT) would allow for more transparency and better implementation as well as enforcement of policies, thus increasing efficiency and improving business confidence. In addition, a large number of respondents stated that such an EU-level investment agreement would ensure a balanced treatment between all EU companies by harmonizing the protection standards. The general idea expressed by a large number of respondents is that the EU should have BITs with major countries, including China, provided that the level of protection as at least equivalent to the "best" BITs concluded by the Member States and that such agreement would not negatively affect existing rights of investors provided in existing BITs.

The views of respondents were however quite split in terms of the content and scope of a potential investment agreement. A trade union pointed out that an agreement would be an opportunity to advance recognition by both Chinese authorities and EU investors of the application of minimum social benefits in accordance with the law of the EU and the Protocol on Economic Social and Cultural rights ratified by China. A trade association also mentioned the need to cover the enforcement of international standards regarding child labour, environment, and anti-corruption. On the other hand, according to the European Services Forum and the Foreign Trade Association, the approach adopted should be based on practical considerations on strengthening commercial investment protection offered by the existing member state BIT network and not upon a purely abstract notion of a single EU-China agreement. Such negotiations should not in any cases diminish the existing protection and should not drag on for a long period. They also stated, along with other trade associations, that unrelated investment issues (human rights, labour conditions, etc.) should not be introduced into the negotiations. These non-commercial issues are not dealt with in the existing EU Member States' BITs and hence should not be part of a possible EU agreement (*see also the replies to the questions on the impacts of an EU-China agreement*). According to the EU Chamber of Commerce in China, an EU-China investment agreement should focus on creating a fair market environment. The EUCCC stressed that there would be a substantial positive impact only if market access were a key component, adding that specific concerns should be targeted, instead of having general statements and blanket coverage, and that there was also a need to ensure a full implementation.

24. *Question: Do you believe that there is a need to cover other aspects/standards relating to protection of investment currently not included in existing bilateral agreements?*

Several respondents, particularly trade associations, began by mentioning the common standards relating to investment protection generally included in BITs and which of these they would also like to find in an EU-China investment agreement: broad definition of investment, fair and equitable treatment, non-discrimination, investor to state dispute settlement with specific and limited time-frame, prompt, adequate and effective compensation in case of expropriation or measures of equivalent effect. They also stressed the need to ensure better transparency in the Chinese investment rules and policies, as well as the need to promote a dialogue on investment facilitation. Several respondents pointed out that such an agreement would need to focus on implementation and enforcement of the commitments, especially at the local level.

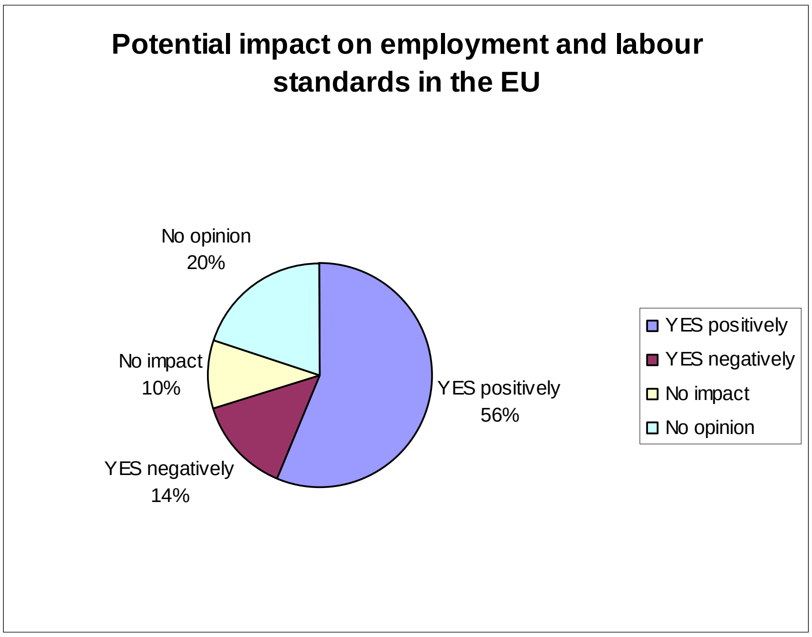
Intellectual property rights and their enforcement were also often mentioned as a specific issue to be addressed through an investment agreement with China. In the *pharmaceutical industry* notably, a large company called for an improved regulatory data protection from 6 to 10 years in order to create a level playing field between Chinese and European pharmaceutical companies.

In the *automotive industry*, a large company stated that an EU-China investment agreement should aim to take out the restriction to foreign investment in key New Energy Vehicles component manufacturing, treat foreign-invested companies (FICs) equally with domestic companies and allow FICs to compete with domestic companies in government research & development programs and funding.
Finally, a trade association representing the interests of the *electrical and electronic industry* indicated that a bilateral agreement should focus on the protection of intellectual property and the recognition of international standards for imported products, in addition to fostering the access to public procurement in China, both on the state and local levels. It also stressed that a bilateral agreement should address the issues of transparency in the administrative procedures and the compliance with basic competition and labour laws (notably corporate social responsibility requirements).

B. Social and labour aspects

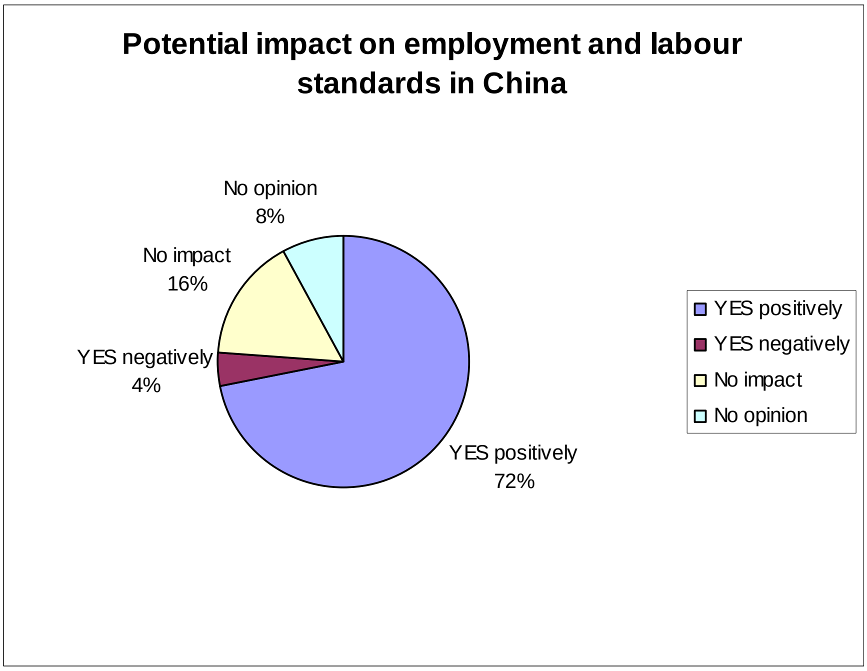
25. *Question: Do you think that employment (both the number and the quality of jobs) could be affected as a result of an EU-China investment agreement?*

a) In the EU



56% of the respondents thought that employment and labour standards in the EU could be positively affected by an EU-China investment agreement. 14% of them believe that employment would be negatively affected in the EU, 10% that it would not be affected and 20% did not have an opinion on this issue.

b) In China



72% of the respondents thought that employment and labour standards in China could be positively affected by an EU-China investment agreement. 4% of them believe that employment would be negatively affected in China, 16% that it would not be affected and 8% did not have an opinion on this issue.

In terms of positive impacts, a large number of respondents stated that in their view, an EU-China investment agreement would create employment opportunities, both in the EU and in China, due to the increase of investment activities. Moreover, they thought that an intensification of the investment flows between the two areas would lead to an increased demand for know-how and expertise and the creation of more qualified jobs. Beyond the effect on the level of employment and qualification, several respondents also thought that this agreement could have a larger impact on social and labour standards in China, influenced by EU standards. Indeed, they stressed that EU companies investing in China would bring along their best practices and apply them to their local activities, including better labour standards, safety and health conditions, training, corporate governance, etc.

Some respondents however suggested that an EU-China investment agreement could have negative impacts on employment and labour standards. In the EU, they expressed concerns that this agreement could encourage companies to relocate to China because of lower labour costs and that this could lead to a transfer of employment from the EU to China. They also feared that an increase of Chinese investors could result in a lowering of the EU labour and social standards due to the pressure from Chinese competitors. Concerning China, some respondents pointed out that better skilled workers could emigrate more easily from China to the EU and this could result in a loss of know-how for China, as a consequence of the concentration of qualified jobs in the EU.

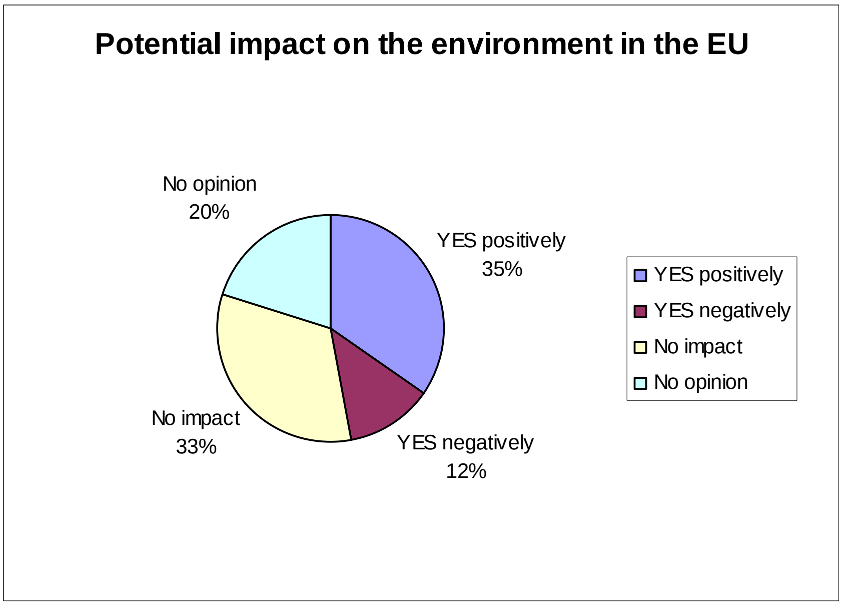
26. Question: *In your view, which issues linked to social and labour standards would require specific attention, in the context of an EU-China investment agreement?*

A number of respondents stated that in order to level the playing field between the two areas, a set of core labour and social standards should be accepted by both parties and included in an investment agreement. A number of issues and standards were mentioned as being potentially integrated in this set, e.g. working conditions (hourly wage, hours worked), workers' rights, child labour, social security, safety, healthcare and pensions. A few respondents stressed the need to protect the EU social system, while other stated that work and residence permits should be addressed in the agreement. Expressing a similar view as a small group of respondents, one large company from the chemicals industry stated that in order to implement internationally recognized labour and social standards and to ensure a level playing field for all economic actors, the recognition of international conventions (e.g. the OECD Guidelines for multinational enterprises, the ILO conventions, the United Nations Covenant on Economic, social and cultural rights) should be part of an EU-China agreement. However, the views on the possible inclusion of social and labour standards into an investment agreement were split overall, as several respondents took the opposite view, stating that social and labour issues were outside the scope of an investment agreement and should not be covered (e.g. European Services Forum, Foreign Trade Association, Eurochambres).

C. Environmental aspects

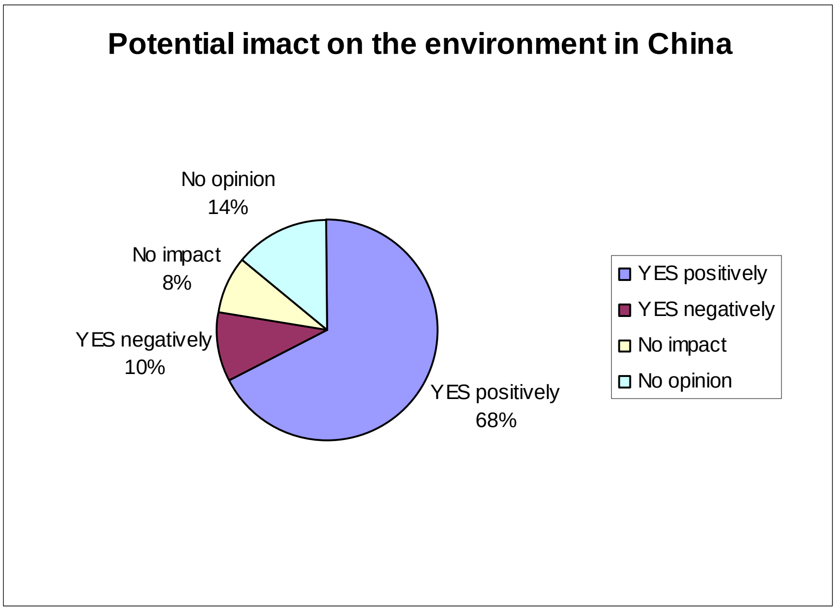
27. Question: *Do you believe that an investment agreement with China could affect the environment?*

a) In the EU



68% of respondents thought that an EU-China investment agreement could have a positive or a neutral impact on the environment in the EU. 12% of them believe that the environment would be negatively affected in the EU, 20% did not have an opinion on this issue.

b) In China



68% of respondents thought that an EU-China investment agreement could have a positive impact on the environment in China. 10% of them believe that environment would be negatively affected in China, 8% that it would not be affected and 14% did not have an opinion on this issue.

In terms of positive impacts, a number of respondents stated that an EU-China investment agreement represents an opportunity to foster the integration, by both the EU and China, of sustainable development objectives by promoting environment-friendly technologies and the implementation of mutual standards. In the same manner as for social and labour standards, some respondents pointed out that EU companies investing in China would bring along better environmental standards and practices, notably the use of new clean technologies, and that those practices would spread to local companies through spill-over effects. More globally, numerous respondents believe that a better investment relationship between EU and China, using an investment agreement, would enhance the bilateral cooperation between the two areas, resulting in an increased transparency in policies and a better exchange of information. As a consequence, such an agreement could encourage China to improve its environmental policies, in particular, as some respondents suggested, if it contained environmental standards.

Regarding the negative impacts, some respondents indicated that the unilateral internalization of environmental costs by the EU could influence investment decisions towards a location with different environmental costing factors, resulting in an increased relocation of polluting companies to China. Those respondents also generally believe that if no global environmental standards were set and accepted by both parties, the result of an increase in the investment flows between EU and China could lead to a degradation of the environment in China (because of the relocation of the most polluting EU industries) and a pressure in the EU to lower the environmental standards (because of the increased competition from Chinese companies).

28. *Question: In your view, which issues linked to the environment would require specific attention, in the context of an EU-China investment agreement?*

In the same manner as for employment and social impacts, a number of respondents stated that in order to level the playing field between the two areas, a set of core environmental standards should be accepted by both parties and included in the investment agreement. Some respondents gave examples of the mechanisms that could be introduced, including duty and tax-exemptions on green products, better allocation of subsidies for research and development, corporate responsibility principles. A number of key issues were also mentioned, e.g. CO2, contamination of air, soil, water, health (faked or tainted food), pollution (water safety, air pollution), general living environment, recycling. In particular, several respondents stressed that the cost for direct emissions should be the same for the Chinese companies as for EU companies.

29. ***Question: How could the EU and China seek to better integrate sustainable development considerations in their discussions on issues that concern their investment relations?***

Some respondent stated that environmental standards should be integrated in an EU-China investment agreement as well as commitments to implement multilateral agreements on the protection of the environment. They also advocated for this agreement to integrate periodic environmental impacts assessments, review mechanisms, legal liability of companies in case of damage to the environment, and real control mechanisms. The reply to this question by the NGO APRODEV, in particular, stated that an EU-China investment agreement should promote sustainable development in its three dimensions, economic, social and environmental, as well as the attainment of the Millennium Development Goals. The association stressed that such an agreement should not undermine governments' right to regulate and to apply domestic policies (e.g. positive discrimination, economic and women empowerment programmes, climate mitigation, etc.). APRODEV believes that the EU should use this investment agreement to promote and improve the monitoring of the conduct of European firms in the Chinese market, and of Chinese firms in the EU market, for example, with regard to taxation, financial reporting, anti-corruption, compliance with the OECD guidelines for Multi-national enterprises. In terms of renewable energy and climate mitigation measures, APRODEV believes that knowledge sharing rather than protection of intellectual property is needed to respond these global challenges.

However, the views of respondents on the integration of environmental standards and mandatory requirements were as divided as those on social and labour standards. For several of the major trade associations, an integration of sustainable development considerations needs to be a natural outcome of the investment, and they believe that mandatory requirements concerning environment should not be included in an investment agreement. They stated that there are other fora to deal with environmental policy issues. The only investment-specific issue that should be tackled concerns the application of environmental rules in a manner that discriminates against EU enterprises. Indeed, they stressed that it was necessary to ensure the equal treatment of domestic and foreign businesses in implementation, monitoring, and enforcement of environmental regulation. BUSINESSEUROPE, one of the trade associations, added that this investment agreement should not use wording or articles that have the effect of attracting investments by lowering environmental standards either in the EU or in China, and that Chinese investments into the EU must comply with European environmental legislation.

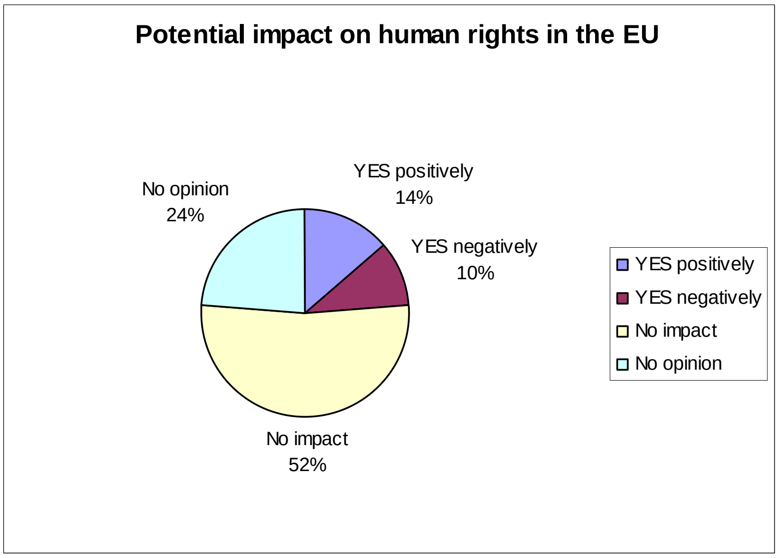
An alternative position, presented by the Automobile Manufacturers Association, favours the integration of sustainable development issues in the EU-China Partnership and Cooperation Agreement, to ensure that cooperation on the environment is reflected in the EU-China partnership. The association also stated that the EU investors have often faced challenges with conflicting

Chinese environmental regulations, for example the imposition of emissions standards for vehicles at a time when Chinese refineries were incapable of providing high enough quality fuels to match the standards. Therefore, they believe that a dialogue on the coordinated implementation of environmental rules across affected industry sectors (with industry participation) could facilitate the introduction of new environmental rules. In general, several respondents stressed the need to promote regular dialogue at sectoral level and encourage transparency and information exchange.

D. Human rights aspects

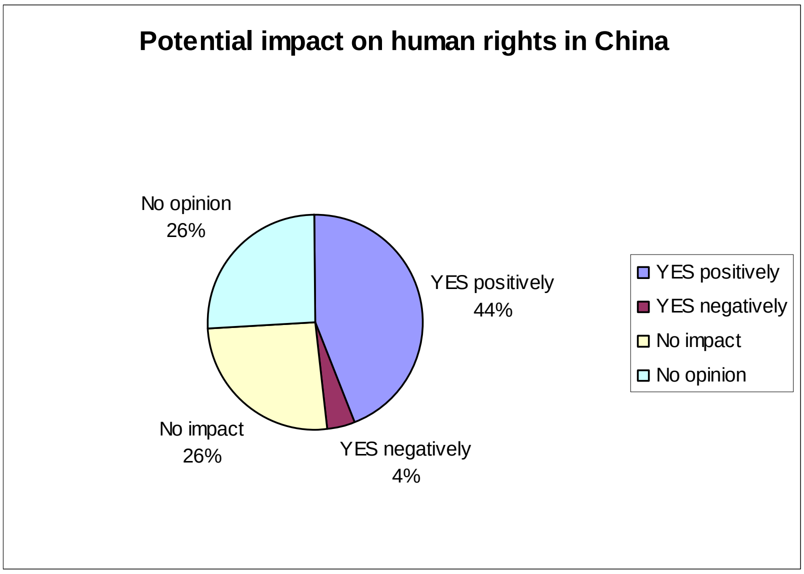
30. Question: *Do you think that human rights could be affected in the context of an EU-China investment agreement?*

a) In the EU



52% of the respondents thought that an EU-China investment agreement would have no impact on human rights in the EU. 14% of the respondents believe that the impact on human rights in the EU would be positive, 10% that the impact would be negative and 24% did not have an opinion on this issue.

b) In China



44% of the respondents thought that an EU-China investment agreement could have a <u>positive impact</u> on human rights <u>in China.</u> 26% of the respondents believe that such an agreement would have no impact on human rights in China, 4% that it would have a negative impact and 26% did not have an opinion on this issue.

Regarding the <u>positive impacts</u>, several respondents thought that an investment agreement was an opportunity for better cooperation and exchange of good practices and for influencing Chinese human rights policies. Other respondents added that bilateral investment agreement can positively influence the business relationship between the two areas which would lead to an increased exchange among people, contributing to a better and deeper common understanding also on fundamental issues. Moreover, they believe that fair and sustainable business relationships introduce more transparency and encourage companies to respect and promote human rights. A few respondents stated that the EU investors in China, bringing along their corporate standards and governance principle, would contribute to increase standards and cause spill-over effects for domestic companies. Other respondents stated that this agreement could have a positive impact on human rights in China if it includes specific provisions on human rights standards.

The <u>negative impacts</u> mentioned by a small number of respondents relate to a general pressure on EU practices and standards (e.g. unions, wages etc.) resulting from the increase possibility for EU companies to relocate in China.

31. ***<u>Question:</u> In your opinion, which issues relating to human rights might require specific attention in the context of an EU-China investment agreement?***

Respondents mentioned a number of issues to address in relation to human rights, some of which are also related to social and labour standards: <u>freedom of expression, freedom of the media (press and access to websites in particular), child labour, respect of labours laws and standards, better conditions for NGOs and the civil society, respect of the due process of law</u>, etc. The Austrian Federal Chamber of Labour stated that an EU-China investment agreement should reconcile the rights of investors with the policy space of states to allow for the protection and the promotion of human rights. The NGO APPRODEV stressed that <u>transparency and accountability</u> of business activities should be enhanced to avoid human rights violations, notably giving the <u>OECD guidelines</u>

for multi-national enterprises the status of binding standards. They also emphasized that human rights should be included in the impact assessment process, which should provide for a monitoring mechanism that goes beyond aggregated data. On the contrary, several of the major trade associations stressed that human rights issues should not be included in an EU-China investment agreement because it could paralyse negotiations and potentially threaten or weaken the protection of EU investment abroad.

IV. OTHER ISSUES

32. ***Question:* If there are any other issues that are not mentioned in this questionnaire that you would like to address, please use the space below to set them out.**

Very few respondents mentioned other issues. In particular, one large company, which started to invest in China more than 10 years ago, stated that treating a country the size of China as a single homogenous entity may sometimes over-simplify the specific situations in different areas with different development stages. It stressed that regional differentiation may be useful. Another large company pointed out that it was sometimes difficult to bring back dividends from China.