

Preparing the Toolkit in Case of Need: Foreign Investment Security Review Mechanism in China in the Context of the Sino-US Strategic Competition

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Abstract: In 2019, against the backdrop of strategic competition between China and the United States (US), the Sino-US trade war escalated further, while the number of cases in which the US imposed strict national security reviews on Chinese companies operating in the US increased significantly. Meanwhile, China promulgated the Foreign Investment Law (FIL) of the People's Republic of China and surpassed the US to become the world's largest recipient of foreign direct investment (FDI). In response to the furtherance of investment liberalization characterized by the modality of pre-establishment national treatment plus negative list, and the US' strengthened national security review of Chinese investment, the FIL and the Measures for the Security Review of Foreign Investment mandate the establishment of a formal national security review system for foreign investment. Modeling the US counterpart, the SRM leaves a few terms ambiguously defined or subject to the discretion of the authorities. Like the current toolkit, the national security review system can be activated when necessary to control unwanted foreign investment in the context of Sino-US strategic competition.

Keywords: Foreign Direct Investment (FDI), National Security Review, Foreign Investment Law (FIL), Security Review Measures, Toolkit

I. INTRODUCTION

For decades, there has been a growing emphasis on the risks posed by FDI to the host state and the impact of foreign investment on the national security of the host state. Accordingly, national security reviews have been made

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among regulatory measures for the admission of foreign investment. In light of the experiences of the US and other countries, a national security review system, which mainly reviews foreign investment activities and evaluates their impact on the host state's national security, is an essential tool for foreign investment management. In the Chinese context, the necessity of national security reviews stems from the fact that China is facing increasingly severe national security threats from foreign investment, which are rooted in the "intensification of geopolitical competition", as the US has already established comprehensive strategic competition with China. National security reviews are a manifestation of the host state's economic sovereignty. They are not only an important part of the traditional system for foreign investment management, but also a key issue that must be considered in the negotiation of international investment agreements. In recent years, many jurisdictions have witnessed the strengthening of security review system, such as the US, European Union (EU), United Kingdom (UK), and Australia. It is not difficult to find that in these jurisdictions, the security review system on foreign investment has either been upgraded or strengthened.

Take the US as an example. In December 2017, the then US President Donald Trump, an anti-establishment politician, released the National Security Strategy, marking the launch of a comprehensive strategy for competition with China centered on strategic competition and based on long-term competition. Against the backdrop, after the US launched an unprecedented trade war against China in a "wild" way, President Donald Trump signed both the Foreign Investment Risk Review Modernization Act (FIRRMA)¹ and the Export Control Reform Act (ECRA)² passed by the US Congress, respectively. The FIRRMA was designed to modernize and strengthen the Committee on Foreign Investment in the United States (CFIUS) to more effectively guard against the

1 US Department of the Treasury, FIRRMA, https://home.treasury.gov/sites/default/files/2018-08/The-Foreign-Investment-Risk-Review-Modernization-Act-of-2018-FIRRMA_0.pdf (Last Visited on July 16, 2025). For a study of FIRRMA, see, for example, J. Russell Blakey, The Foreign Investment Risk Review Modernization Act: The Double-edged Sword of US Foreign Investment Regulations, *Loyola of Los Angeles Law Review*, Vol. 53, No. 4, 2020, pp. 998-999.

2 The ECRA aims to authorize the President to control the export, reexport, and transfer of commodities, software, and technology to protect national security, and to promote the foreign policy of the United States, and for other purposes.

perceived risks to the national security of the US posed by certain types of foreign investment from targeted countries. The signing of FIRRMA into law by President Donald Trump on August 13, 2018 reinforced the implementation of the well-established security review system under Section 721 of the 1950 Defense Production Act.

Amid the trend of intensifying the national security review systems, China did not make itself an exception. On March 15, 2019, the 2nd Session of the 13th National People's Congress adopted the FIL of the People's Republic of China. As a basic law governing foreign investment, the FIL came into effect on January 1, 2020, upgrading the existing foreign investment regime and replacing the Law on Chinese-Foreign Equity Joint Ventures (EJV Law), the Law on Chinese-Foreign Contractual Joint Ventures (CJV Law), and the Law on Wholly Foreign-Owned Enterprises (WFOE Law). In the face of legislators, China's economic development goals require attracting significant amounts of foreign investment, while the increasing national security concerns China is experiencing necessitate strengthened management of foreign investment. To balance these two priorities, the FIL adopts a "risk-based and balanced approach" that introduces a mixed regulatory system of pre-establishment national treatment plus negative list and a strengthened management system with the "national security review" for foreign investment as the center. The negative list, which refers to the special management measure for the admission of foreign investment in specific fields that the State Council is mandated to issue or approve in light of foreign investment policies and evolving situations, signifies investment liberalization. Against this backdrop, the FIL further stipulates the establishment of a national security review system for foreign investment.³

The security review system, mandated by the FIL, shall be understood in conjunction with the modality of pre-establishment national treatment plus negative list for foreign investment, which was established by Article 4 of the FIL. While the pre-establishment national treatment plus negative list, which is designed to enhance transparency of the system for admission of foreign investment and further the accessibility of the Chinese market to foreign

³ The FIL, Article 35.

investment, highlights high-level opening-up and investment liberalization, the security review system is set to ensure the regulatory power of the government, thus striking a balance between the right to entry of foreign investors and the power of the government to regulate foreign investment.

Article 4 offers a detailed interpretation of the Chinese foreign investment security review system.

II. EVOLUTION OF THE SECURITY REVIEW SYSTEM IN CHINA

A. Emergence of a National Security Review System in the Context of Anti-monopoly Regulation

National security is among the most concerning issues involving foreign investment. However, China's first international investment law, the Law on Chinese-Foreign Equity Joint Ventures, adopted in 1979, was focused less on national security than on attracting foreign investment. The Law on Wholly Foreign-Owned Enterprises adopted in 1986, was the first to mention national security. According to Article 6 of the WFOE Law, an application for the establishment of a wholly foreign-owned enterprise that endangers China's national security would not be approved.

In fact, national security review is not a new concept in China. In early 2007, the Anti-Monopoly Law (AML) of the People's Republic of China provided that "Where a foreign investor participates in the concentration of business operators by merging or acquiring a domestic enterprise or by any other means and the national security is involved, besides the examination on the concentration of business operators according to this Law, the examination on the national security shall also be conducted according to the relevant provisions of the State".⁴

It is not difficult to find that the emergence of the first national security review system was, to a greater or lesser extent, prompted by the US practice towards proposed mergers and acquisitions (M&A) transactions involving

⁴ The AML, Article 31; The AML (2022 Amendment), Article 38.

Chinese companies.⁵ In this regard, embodying national security review in the anti-monopoly regulation is a makeshift arrangement, signifying that the authorities had realized the need for security review for foreign investment, so that a temporary legal basis was provided via the AML.

A comparison between national security review and anti-monopoly review will lead to the conclusion that the former is more onerous than the latter in terms of its effect on foreign investment. In this connection, the arrangement of embodying national security review in the anti-monopoly regulation might have given rise to the overuse of security review in lieu of anti-monopoly review.

Given the risk, in an apparent effort to be in line with the provisions of the AML, the General Office of the State Council promulgated Notice on the Establishment of the Security Review System for Mergers and Acquisitions of Domestic Enterprises by Foreign Investors in February 2011 (hereinafter referred to as “State Council Notice”), thus embarking on China’s first legislative move on national security review for foreign investment. Subsequently, the Ministry of Commerce (MOFCOM) issued the Interim Provisions on Issues Related to the Implementation of the Security Review System for Mergers and Acquisitions of Domestic Enterprises by Foreign Investors (hereinafter referred to as “MOFCOM Interim Provisions”), which took effect on March 5, 2011. In August 2011, just a few months later, the MOFCOM issued the Provisions on the Implementation of the Security Review System for Mergers and Acquisitions of Domestic Enterprises by Foreign Investors (hereinafter referred to as “MOFCOM Provisions”), which replaced the Interim Provisions and signified the formal establishment of the national security review system for foreign investment in connection with M&A of domestic enterprises.

B. An Overview of China’s First Security Review System for Foreign Investment

The State Council Notice and the MOFCOM Provisions formed the legal

⁵ Suvik Saha, CFIUS Now Made in China: Dueling National Security Review Frameworks as a Countermeasure to Economic Espionage in the Age of Globalization, *Northwestern Journal of International Law & Business*, Vol. 33, No. 1, 2012, p. 215.

framework of China's first security review system. They were in the form of ministerial rules and in a low position in the hierarchy of normative documents.⁶

It is not difficult to note that the first security review system, which focused on M&A by foreign investors, was narrow in scope of coverage. According to the State Council Notice, "mergers and acquisitions of domestic military industrial enterprises and supportive military industrial enterprises, enterprises surrounding major and sensitive military facilities, and other entities relating to the national defense security; foreign investors' mergers and acquisitions of domestic enterprises relating to important agricultural products, important energies and resources, important infrastructural facilities, important transportation services, key technologies, manufacturing of major equipment, etc., which relate to the national security, and whose actual controlling power may be obtained by foreign investors" are subject to national security review.⁷ This Notice listed four circumstances for the M&A of a domestic enterprise by a foreign investor: "(i) where a foreign investor purchases the equity shares of a domestic non-foreign-funded enterprise or subscribes to the increased capital of a domestic non-foreign-funded enterprise, and thus changes such domestic enterprise into a foreign-funded enterprise; (ii) where a foreign investor purchases the equity shares from the Chinese shareholders of a domestic foreign-funded enterprise or subscribes to the increased capital of a domestic foreign-funded enterprise; (iii) where a foreign investor establishes a foreign-funded enterprise and through which it purchases by agreement the assets of a domestic enterprise and operates such assets, or through which it purchases the equity shares of a domestic enterprise; or (iv) where a foreign investor directly purchases the assets of a domestic enterprise, and then invests such assets to establish a foreign-funded enterprise to operate such assets".⁸

This State Council Notice also enumerated the specific instances where the acquisition of actual controlling power of domestic enterprises by foreign investors is within the scope of security review. In this context, actual

⁶ The normative documents at the center level are fixed in a hierarchical structure, from top to bottom: the constitution, laws, administrative regulations and ministerial rules.

⁷ The State Council Notice, Article 1.1.

⁸ *Ibid.*, Article 1.2.

controlling power is defined by the State Council Notice as a state where “a foreign investor becomes the controlling shareholder or actual controller of a domestic enterprise through merger or acquisition”.⁹ It is further divided into four circumstances: “(i) where the total shares held by a foreign investor and its parent holding company and controlled subsidiary companies after merger or acquisition account for not less than 50%; (ii) where the total shares held by multiple foreign investors after merger or acquisition account for not less than 50% in total; (iii) where the total shares held by a foreign investor after merger or acquisition account for less than 50%, but the voting power it holds according to the stocks it holds is enough to have a material impact on the resolution of the shareholders’ meeting, the general assembly of shareholders, or the board of directors; or (iv) any other circumstance which leads to the transfer of the actual controlling power of a domestic enterprise on business decisions, financial affairs, personnel, technologies, etc. to a foreign investor”.¹⁰ These provisions have laid the foundation of the Chinese security review system.

The MOFCOM Provisions, which were derived from the State Council Notice, mainly further clarified the competent agency in charge, the documents to be submitted by the applicant and the procedures for security review.

C. Pilot Program of National Security Review of Foreign Investment in Free Trade Zones

In 2013, two years after the security review system came into being, China decided to introduce and carry out a reform of free trade zones (FTZs). FTZs are China’s testing grounds for new and groundbreaking legal and regulatory reforms, specifically, investment management systems using a negative list approach, the trade regulation system focusing on trade facilitation, the financial innovation system aimed at capital account convertibility and the liberalization of financial services, and a system of ongoing and *ex post* supervision with the transformation of government functions at its core. In this regard, the negative list approach is notable. The negative list, which is a catalogue of special

⁹ *Ibid.*, Article 1.3.

¹⁰ *Ibid.*

management measures for foreign investment access, replaced mandatory foreign investment screening requirements that were then applied elsewhere in China with mere filing-for-recordation requirements in a broad range of sectors in the FTZs. The goals of the new reform are to introduce institutional innovations in line with commonly accepted international rules on investment and trade, use key functional areas such as finance and trade, advanced manufacturing and technological innovation to exert maximum influence on other sectors, and to create FTZs characterized by the highest degree of openness, investment and trade facilitation, currency conversion freedom, convenient and efficient regulation, and a sound legal environment.

After the establishment of pilot FTZs, on April 8, 2015, the General Office of the State Council issued the Notice on Issuing the Measures for the Pilot Program of National Security Review of Foreign Investment in Pilot Free Trade Zones (hereinafter referred to as “FTZ Notice”), which further adopted an approach to national security review in the FTZs different from the original national security review system.

The FTZ Notice provides an opportunity for the Chinese government to assess the performance of the new national security review system on a trial basis, before considering whether to replace the existing national security review regime. More broadly, the FTZ Notice indicates China’s willingness to exercise its authority to review and control foreign investment under the national security review system as a means to balance the FTZs’ more liberalized approach to foreign investment, where the process of foreign investment has been simplified. Therefore, while the reforms in the FTZs facilitate foreign investment, such investments must nevertheless comply with national security requirements, which in certain respects are more stringent within the FTZs than outside them.

According to the FTZ Notice, “security review shall be conducted on foreign investment which affects or may affect national security and the capabilities to ensure national security, or involves sensitive investors, sensitive targets of merger and acquisition, sensitive industries, sensitive technologies, and sensitive areas”.¹¹ Specifically, subject to security review are

¹¹ The FTZ Notice, Article 1.

“foreign investors’ investment in pilot FTZs in military industry, supportive military industry, and other fields relating to national defense security, or in areas surrounding major or sensitive military facilities; and foreign investors’ investment that is made in pilot FTZs in the fields relating to national security such as important agricultural products, important energies and resources, important infrastructural facilities, important transportation services, important culture, important information technology products and services, key technologies, and manufacturing of major equipment, and through which foreign investors obtain the actual controlling power of the enterprises they invest in”.¹²

The FTZ security review system expanded the scope of application of the national security review system so as to subject both M&A and greenfield investment to security review, where “(i) Foreign investors solely or jointly invest with other investors in new projects or formation of enterprises; (ii) Foreign investors have obtained, through merger and acquisition, equities or assets of the enterprises which have been established; (iii) Foreign investors make investment through agreement-based control, holding shares for others, trust, reinvestment, overseas transaction, lease, subscribing for convertible bonds, and other means”.¹³ In some cases, the FTZ’s security review measures may require applications for national security clearance to be made for an investment in the relevant FTZ, where clearance would not have been required if the investment had been made elsewhere in places outside the FTZs. The expansion of the new security review system was apparently tailored to balance the freer movement of foreign investment into the FTZs.

Compared with the original security review system, the FTZ Notice also simplified the materials to be submitted, optimized the review procedures, and standardized the review norms and so on, thus further improving China’s foreign investment management system and paving the way for the institutionalization of a national security review system for foreign investment that is compatible with the negative list approach to admission of foreign investment.

¹² *Ibid.*, Article 1.1.

¹³ *Ibid.*, Article 1.2.

III. THE NEW NATIONAL FOREIGN INVESTMENT SECURITY REVIEW SYSTEM

A. Mandates of the Laws for Establishing a National Security Review System

Not long after the 18th National Congress of the Communist Party of China in 2012, the new leadership of China prioritized national security issues in its policy agenda, which led to the establishment of a National Security Commission by the Central Committee of the Communist Party of China in November 2013, which is tasked with mapping out China's national security strategy and ensuring the security of the state, and adoption of the National Security Law of the People's Republic of China (hereinafter referred to as "NSL") in 2015. It was the NSL that specifically required establishing rules and mechanisms to conduct a national security review of foreign investment in China that may impact national security. The NSL provided the legal mandate for a new national security review system for foreign investment.

Due to the promotion of the Belt and Road Initiative from the end of 2013 to the enactment of the FIL in 2019, China experienced steady growth in both the volume of FDI attracted and the number of foreign-invested enterprises established. As a matter of fact, China had become the second largest recipient of FDI, which highlighted the importance of security review system as an essential tool to mitigate potential security risks associated with increased foreign investment.

Also, when the proposed FIL was still in the process of drafting and deliberation, it was known that the pre-establishment national treatment combined with the negative list would become the core of the law. This approach was introduced not only to enhance the transparency of the policy concerning admission of foreign investment, but in a way to encourage, promote and attract foreign investment by minimizing restrictions thereon. However, increased market access may also heighten national security risks and thus require more stringent foreign investment management. The national

security review system must be able to address the national security risk that may be posed by foreign investment under the framework of FIL.

Moreover, when the Chinese authorities were contemplating a basic law for foreign investment, major jurisdictions like the US strengthened their own national security review systems, which will be discussed later. As a matter of fact, during the time-span when the draft FIL was being elaborated and reviewed by the National People's Congress for adoption, the US significantly increased its national security reviews against Chinese investment in the US.¹⁴ China has noticed the development.¹⁵ It is not difficult to understand that China's proposed new national security review system could also be considered as a strategic leverage in response to US' prohibitive or restrictive investment measures against China's overseas investment.

The program of security established in FTZs had laid down the foundation for a comprehensive national system for foreign investment security review. Given that the existing national regulatory systems for security review, low in the hierarchy of normative documents and limited scope of application, were inadequate to satisfy the needs of the superpower for national security review, it was high time to have in place a new national system for security review.

This is why the Chinese legislature adopted a foreign investment regime with a formal national security review system after 5 years of testing the FTZ security review system. Article 35 of the FIL mandated the State Council to establish a nationwide system for foreign investment security review.

14 From 1990 to 2017, four M&A transactions of US companies by Chinese companies were cancelled by the US presidents as a result of US national security review. In 2018, up to September 24, at least 5 cases of M&A of US companies with Chinese investment were withdrawn as a result of the national security review. See the State Council, The Facts and China's Position on China-US Trade Friction, https://english.www.gov.cn/archive/white_paper/2018/09/26/content_281476319220196.htm (Last Visited on July 16, 2025).

15 The Chinese MOFCOM spokesman made the following remarks at a regular press conference on August 30, 2018: "Recently, a few countries have introduced laws, regulations or measures to tighten foreign investment review, affecting some of China's ODI projects. China expressed its concern and will follow the developments closely to assess the impact of these measures on China's outbound investment. We've noted that the tightening of foreign investment security review is likely to cause concern among global investors about the investment environment, in particular about the potential abuse of national security review, of related countries". See MOFCOM, Regular Press Conference of the Ministry of Commerce (August 30, 2018), https://english.mofcom.gov.cn/News/PressConference/art/2018/art_afabd5d1e1db4e96afa73aa12b478364.html (Last Visited on July 16, 2025).

B. Codification of the New Security Review System

Just a few months after the promulgation of the FIL and before the entry into force of the FIL, a real national security review case, i.e., the 2019 acquisition of Zhongbai Holdings Group Co., Ltd. (hereinafter referred to as Zhongbai Group) by Yonghui Supermarket Co., Ltd. (hereinafter referred to as Yonghui Supermarket),¹⁶ added a further spur to the legislation of the new foreign investment security review system.

On March 28, 2019, Yonghui Supermarket notified Zhongbai Group that it would increase its direct and indirect combined shareholding in Zhongbai Group from 29.86% to a maximum of 40%. On August 21, 2019, the proposed transaction passed the anti-monopoly review. When Yonghui Supermarket was about to wrap up the transaction, it received a notice from the National Development and Reform Commission (NDRC) on November 11, 2019, which required the recipient to submit an application and supporting documents for foreign investment security review. Yonghui Supermarket is a foreign-invested listed company, the largest shareholder of which is the Dairy Farm Company (Hong Kong) Limited. The acquisition of Zhongbai Group by Yonghui Supermarket belongs to the reinvestment of a foreign-invested enterprise in China. Meanwhile, the acquisition proposal of Yonghui Supermarket, if fully implemented, would result in the shift of the actual control power of Zhongbai Group to Yonghui Supermarket. Since Zhongbai Group's business scope involves the retail industry, the logistics industry, agricultural products processing, and other fields, they seem to fall within the scope of the national security review set forth by the State Council Notice. Accordingly, the NDRC initiated a national security review against Yonghui Supermarket. From a legal point of view, it is reasonable that the acquisition of a retail company, which is involved in agricultural products processing, by a foreign-invested enterprise mandates a security review. However, there were some controversies emerging among foreign investors and scholars concerning the necessity for security reviews. Nevertheless, it can be seen that the reinvestment behavior of foreign-invested enterprises in China may still affect China's national security, at least

¹⁶ Scott Yu et al., *National Security Review in China: Ready to Embrace a Change?* <http://www.zhonglun.com/Content/2019/09-04/1647363311.html> (Last Visited on July 16, 2025).

from the perspective of the authorities, and therefore is subject to security reviews.

The year when the FIL was promulgated witnessed that China overtook the US as the largest recipient of foreign direct investment. Against this backdrop, it seems urgent to have in place a formalized national security review system needed to regulate foreign investment against possible national security risk. It is generally believed that the Yonghui case prompted an earlier promulgation of the formal security review system.

After a few months of deliberation, the NDRC and MOFCOM finally adopted the Measures for the Security Review of Foreign Investment¹⁷ (hereinafter referred to as “SRM”) on November 27, 2020. With the approval of the State Council, the SRM entered into force on January 18, 2021.

IV. FRAMEWORK OF THE NEW NATIONAL SECURITY REVIEW SYSTEM

Under the new pattern of comprehensive opening-up, the security review would become the most important part of the regulatory system for foreign investment. The new SRM drew on the experience of the initial national security review system and the FTZ security review system. As a result, it is a refined version of the foreign investment security review system. The SRM, which consists of 23 articles, provides for the authority in charge, the scope of matters subject to security review, and the procedure for security review, as well as legal liabilities for non-compliance of the SRM. The SRM is expected to strengthen risk prevention associated with foreign investment.

A. The Designated Department in Charge

According to Article 3 of the SRM, “the state shall establish a foreign investment security review working mechanism (hereinafter referred to as “working mechanism”) responsible for organizing, coordinating, and guiding the foreign investment security review work”. This article makes it clear that

¹⁷ The Measures for the Security Review of Foreign Investment was deliberated and adopted at the 13th executive meeting of the NDRC on November 27, 2020.

“under the the leadership of the NDRC and the MOFCOM and located in the NDRC, the office of the working mechanism shall be responsible for the routine work in relation to the security review of foreign investment”.

Under the original national security review system, a joint meeting mechanism was responsible for the security review of M&A by foreign investors. Both the NDRC and the MOFCOM were involved in carrying out a security review. It is therefore unclear which department should take the main responsibility in this regard, which might, for example, affect efficiency due to coordination between the two departments.

In the SMR, where a Working Mechanism replaced the previous joint meeting mechanism, it is clarified that the NDRC is the responsible department for foreign investment security review. Such a clear designation is conducive to making the security review procedure work more efficiently and smoothly.

B. Subject of Review

The SRM is basically in accordance with the FTZ Notice in terms of the scope of security review. While the first national security review system applied only to M&A of domestic enterprises by foreign investors, the SRM no longer limits itself to M&A. Just like the FTZ security review system that applies to both M&A and greenfield investment, the new security review system provides that security review shall be conducted for foreign investment which affects or may affect national security and the capabilities to ensure national security, or involves sensitive investors, sensitive targets of M&A, sensitive industries, sensitive technologies, and sensitive areas. The new SRM, pursuant to Article 2, covers the investing activities conducted by a foreign investor directly or indirectly in the territory of the People’s Republic of China.

There are three issues to be further discussed regarding the scope of SRM, that is, the definition of “foreign investment”, the meaning of “national security” and the identification of “important and key fields”.

1. Definition of “Foreign Investment”

There is no doubt that foreign investors and other relevant parties must identify which foreign investment is subject to security review. Paragraph 2 of Article 2

of the FIL tends to define foreign investment. It is noted that it does not adopt the asset-based definition commonly used in international investment treaties; instead, it follows the intuitive definition method adopted in foreign investment legislation.¹⁸

Consistent with the FIL, the new SRM defines “foreign investment” as the investing activities conducted by a foreign investor directly or indirectly in China, including the following circumstances: (i) A foreign investor, alone or together with another investor, invests in a new project or invests in the formation of an enterprise in China; (ii) A foreign investor acquires any equity or asset of an enterprise in China by means of M&A; and (iii) A foreign investor invests in China by any other means.

While the definition covers both greenfield investment and M&A, it grants the regulator plenty of room for interpretation, making it likely that investments via variable interest vehicle (VIE) fall within its ambit.

In addition, there is also a further discussion on whether investments from Hong Kong, Macao and Taiwan should be the subject of security review. From an administrative perspective, the investment from Hong Kong, Macao and Taiwan is included in foreign investment when the administrative authorities deal with foreign investment statistical data. In practice, about 70% of the foreign investment is from Hong Kong, Macao and Taiwan.¹⁹ There is no reason to exclude investments from Hong Kong, Macao and Taiwan from the security review. The case of Yonghui Supermarket’s acquisition of Zhongbai Group already showed that the authorities are taking this approach.²⁰ Legally speaking, Hong Kong and Macao are special administrative regions, while Taiwan is a province of China, and all three are separate customs territories. Thus, the investments from Hong Kong, Macao and Taiwan, which cannot be directly identified as FDI, may be treated as FDI. Article 21 of the SRM stipulates clearly that “where an investor from the Hong Kong Special Administrative

18 Qingjiang Kong, *An Interpretation of the Foreign Investment Law of the People’s Republic of China*, The Law Press, 2019, p. 26.

19 MOFCOM, Report on Foreign Investment in China (2024), https://wzs.mofcom.gov.cn/ztxx/art/2025/art_a5f52f7bf1e7467cb87bfb0b2f10c3c0.html (Last Visited on July 16, 2025).

20 As mentioned above, the largest shareholder of Yonghui Supermarket is a Hong Kong company, i.e., Dairy Farm International Holdings Co., Ltd.

Region, the Macao Special Administrative Region, or the Taiwan region makes any investment that affects or may affect national security, these measures shall apply *mutatis mutandis*".

2. Meaning of "National Security"

Article 2 also clearly states that the national security review aims to find out whether a foreign investment activity affects or may affect China's national security. It is crucial to determine what national security is and whether a foreign investment activity may affect China's national security.

As stated above, both the NSL and FIL are the legal bases of the SRM, and the rules of these two laws are therefore governed. According to the NSL, which is based on "a holistic view of national security",²¹ national security refers to "the regime, sovereignty, unity and territorial integrity, welfare of the people, sustainable economic and social development, and other major interests of the state are relatively not faced with any danger and not threatened internally and externally, and the capability to maintain a sustained security status".²² It is defined so broadly as to cover people's security, political security, economic security, military security, cultural security, and social security, etc.²³ It is intriguing that no clear definition has been given to national security in Chinese laws and regulations. Neither the State Council Notice nor the FTZ Notice did so. While the 2011 security review system merely listed four items subject to security review, namely, national defense, the stable operation of the national economy, the order of basic social life, and the capacity of research and development of key technologies involving national security,²⁴ the 2015 FTZ Notice added national cultural security, public morality, and national cyber security as factors of consideration for security review.²⁵ It is only certain

21 A holistic view of national security is a term coined by Chinese President Xi Jinping. In April 2014, while presiding over the first meeting of the National Security Commission of the CPC Central Committee, Xi Jinping emphasized the need to take a holistic view of national security. Through such an approach, a full spectrum of security issues are assessed, ranging from human security, political security, economic security to military security, cultural security and social security, as well as international security.

22 The NSL, Article 2.

23 *Ibid.*, Article 3.

24 The State Council Notice, Article 2.

25 The FTZ Notice, Article 2.

to infer that the concept of national security is constantly changing, making it difficult to encapsulate. The broad definition is also conducive to enabling the government to take flexible responses to changes in foreign investment activities.

In this regard, it should be pointed out that the new national security review system embodies a preventive mechanism as well as an evaluation mechanism for whether foreign investment has or may have an impact on the national security of China. This is arguably in line with Article 9 of the NSL, which prioritizes the prevention of national security risks in maintaining national security. In this context, it leaves a question whether foreign investors' intention and capability shall be taken into account in determining whether their investment activity may affect national security. Some scholars advise taking these factors into consideration on a case-by-case basis.

3. Identification of "Important and Key Fields"

Article 4 of the SRM further stipulates that foreign investors or the relevant parties in China shall proactively report to the Office of the Working Mechanism any foreign investment in important agricultural products, important energy and resources, critical equipment manufacturing, important infrastructure, important transportation services, important cultural products and services, important information technology and Internet products and services, important financial services, key technology, or any other important field related to national security that may result in the foreign investor's acquisition of actual control over the invested enterprises.²⁶ This lengthy illustration aims to ensure that all foreign investment activities that affect or may affect national security are included within the scope of the new national security review system.

The terms "important" and "key" are also too vague for foreign investors to figure out whether their investment matches the scope of the security review or whether they should report their investment proactively. Therefore, substantial discretion is left to the authorities as to the interpretation of these terms.

²⁶ The SRM, Article 4.

In this regard, a further issue arises as to the relationship between the scope of the security review and the negative list. It seems that foreign investors may first refer their ongoing investment to the negative list to deal with this problem. In general, there is no need to make a security review of foreign investment in the fields prohibited by the negative list, because none will be allowed to make such investment. Most of the fields restricted to the negative list are identified as important and sensitive investment, which are likely to be covered by a security review. However, it could still not solve the problem in the following cases. Under the national security review system, even if foreign investment is not restricted by the negative list, it could still be subject to security review. The security review system is an independent system; that is to say, if foreign investment matches the situations listed in paragraphs 1 and 2 of Article 4 of the SRM, even if foreign investment is not subject to the negative list, it may still face the possibility of being subjected to a security review.

Some scholars also point out that the national security review system can be incorporated into the negative list framework. This is due to the fact that foreign investment may enter sectors only if certain conditions are met. If a particular foreign investment is not included on the negative list, the investment is believed not to have a significant negative impact on national security. Therefore, there is no point in subjecting such investments to security reviews. By combining a security review system with a negative list framework, the predictability and certainty of security reviews could be improved.²⁷ However, in the author's opinion, the negative list system and the national security review system are developed for different purposes. The negative list system is designed as a means to liberalize investment for the purpose of promoting foreign investment, so it has been shortened continuously. However, the national security review system is the last resort in preventing unwanted foreign investment that poses national security risks, which may arise in the course of inward foreign investment. Governments should stay cautious against foreign investments that may lead to an adverse impact on national security. As a matter of fact, as the negative list is supposed to provide an environment friendly to

²⁷ Yunpeng Wang and Ding Ding, Targeting the National Security Review by Negative List, *Business and Economic Law Review*, Vol. 4, No. 11, 2020, pp. 13–14.

foreign investment and help attract more inward foreign investment, security review is more needed to screen out potentially harmful investments. Hence, the national security review system subjects a broad scope of investment to a security review to this end. It is designed to provide potential investors with very clear procedures to make the review more effective so as not to cause the security review system to be a burdensome one for investors.

C. Review Procedures

The security review under the SRM is divided into three stages, namely, pre-review, general review and special review. At the pre-review stage, the office of the working mechanism shall decide whether a security review of the reported foreign investment is required and notify the party in writing within 15 working days. Before the office of the working mechanism makes a decision, the party may not make the investment.²⁸ “If the office of the working mechanism decides to conduct a security review of a reported foreign investment, it shall complete the general review within 30 working days of the decision. During the review period, the party may not make the investment”.²⁹

After the general review, the Office of the Working Mechanism shall decide whether the security review is passed or not. If it is deemed that the reported foreign investment does not affect national security, the security review is over in favor of the investor. If it deems that national security is affected or may be affected, then the Office of the Working Mechanism shall decide to initiate a special review.³⁰

The special review lasts for at most 60 working days, and under exceptional circumstances, the review period may be extended.³¹ Upon special review, if the reported foreign investment does not affect national security, the office shall decide that the security review is passed. If the reported foreign investment affects national security, it shall decide to prohibit the investment; provided that the imposition of conditions is sufficient to eliminate the effect on national security and the party agrees to accept the imposed conditions in

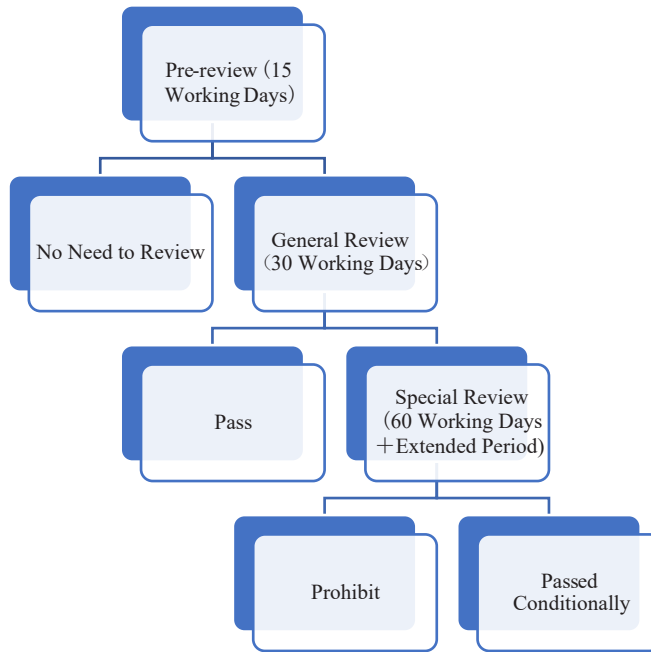
²⁸ The SRM, Article 7.

²⁹ *Ibid.*, Article 8.

³⁰ *Ibid.*

³¹ *Ibid.*, Article 9.

writing, the security review may be passed conditionally.



Source: Based on authors' compilation.

Figure 1: Procedures of National Security Review

D. Finality of Review Decision

The SRM did not mention the effectiveness of review decisions made by the Office of the Working Mechanism. However, according to Article 35 of the FIL, “the security review decision made in accordance with the law is final”. In other words, foreign investment national security review decisions are generally not subject to judicial review; that is, if investors disagree with the national security review decision, they are not allowed to file a lawsuit.

E. Sanction Measures

The SRM spells out new provisions on sanction measures against foreign investors and relevant parties that violate relevant provisions. If false materials are provided to the Office of the Working Mechanism or relevant information

is concealed, or if foreign investment has been conditionally approved through security review but the investment is not made in accordance with the specified conditions, the Office of the Working Mechanism shall order the entity to rectify the situation. Where security review is passed fraudulently by providing any false material or concealing any relevant information, the Office of the Working Mechanism shall revoke the relevant decision; and if the investment has been made, or if the party refuses to take corrective action, the Office of the Working Mechanism may order the party to dispose of its resultant equities or assets within a specified period and take other necessary measures to restore to the state before the investment was made and eliminate the effect on national security.³²

In addition, the violating party will incur further liabilities, i.e., a negative credit record shall be included in the relevant credit information system of the state, and joint sanctions shall be imposed on the party in accordance with the relevant provisions issued by the state.³³

The SRM also provides for the liabilities for concerned government employees who engage in misconduct. Article 20 of the SRM reads: “where in the foreign investment security review work, a state agency’s employee abuses his or her power, neglects his or her duties, practices favoritism, makes falsification, divulges a state secret, or divulges a trade secret to which he or she has access, the employee shall be subjected to disciplinary action in accordance with the law; and if the act is criminally punishable, be held criminally liable in accordance with the law”.

V. FEATURES OF THE NEW SECURITY REVIEW SYSTEM

A. Commendable Features

Compared with the previous security review system, the new national security review system are characterized by a few innovations, mainly reflected in the

³² *Ibid.*, Articles 17–18.

³³ *Ibid.*, Article 19.

following five aspects:

- (i) It expands the scope beyond M&A of domestic enterprises by foreign investors;³⁴
- (ii) It has a clear designation of the department in charge, thus avoiding the low efficiency arising out of coordination between the NDRC and MOFCOM;³⁵
- (iii) It introduces conditional approval choice in the decisions of security review;³⁶
- (iv) It simplifies the materials to be submitted for filing a security review from 8 files³⁷ to only 4 files;³⁸
- (v) It has in place disciplinary measures of the parties and government employees who violate the SRM.³⁹

B. Points to Be Further Clarified

The entry into force of the SRM also leaves a question to be answered: what is the relationship between the SRM and the FTZ Notice? In other words, will the FTZ Notice still apply to national security review of foreign investment in FTZs? The question must be answered in the first place.

If yes, two further questions are to be answered. One is whether the SRM could be quoted where the FTZ Notice is silent on a particular issue. For example, while the SRM mandates conditional approval⁴⁰ as to security review of foreign investment, the FTZ Notice is silent in this regard. Against the backdrop, clarification is needed as to whether conditional approval can be granted where national security review of certain foreign investment in FTZs is conducted pursuant to the FTZ Notice.

The other is which will prevail in the event of conflicts between the SRM and the FTZ Notice. For example, while the FTZ Notice focuses on security review of foreign investment involving sensitive investment entities, sensitive

³⁴ *Ibid.*, Articles 2 and 4.

³⁵ *Ibid.*, Article 3.

³⁶ *Ibid.*, Article 8.

³⁷ MOFCOM Provisions, Article 5.

³⁸ The SRM, Article 6.

³⁹ *Ibid.*, Articles 17–20.

⁴⁰ *Ibid.*, Article 9.2.

M&A targets, sensitive industries, sensitive technologies, and sensitive regions,⁴¹ the SRM refers to “important agricultural products, important energy and resources, major equipment manufacturing, important infrastructures, important transportation services, important cultural products and services, important information technology and Internet products and services, important financial services, key technologies, and other important fields”.⁴² It is important to clarify whether the two sets of norms refer to the same subject or not, as this determines their application to foreign investment in FTZs.

VI. A COMPARATIVE STUDY OF THE NEW SECURITY REVIEW SYSTEM

A. Emergence of a Wave of Strengthened National Security Review Worldwide

Global investment policies in 2020 and 2021 were found to be more restrictive than the previous year. According to the World Investment Report 2021, “a total of 152 policy measures or regulatory measures affecting foreign investment, which were reported by 67 economies in 2020, were restrictive, exhibiting an increase of 42% compared with 2019 and representing a 41% portion of total investment measures”.⁴³ The restrictive policies mainly took place in developed countries and emerging economies, which established or strengthened the national security review system in a variety of ways, such as establishing national security review legislation for foreign investment, amending the national security review system, expanding the scope of national security review for foreign investment, extending the national security review period, strengthening the national security review in specific fields and so on.⁴⁴ At present, 34 countries have already conducted foreign investment national security reviews.⁴⁵

⁴¹ The FTZ Notice, Article 1.1.

⁴² The SRM, Article 4.2.

⁴³ UNCTAD, World Investment Report 2021, p. 109, https://unctad.org/system/files/official-document/wir2021_en.pdf (Last Visited on July 16, 2025).

⁴⁴ *Ibid.*, pp. 111–114.

⁴⁵ *Ibid.*, p. 111.

Besides China, the US, UK, and the EU have all enacted new national security review laws or regulations.⁴⁶ Other countries have also strengthened their national security review systems for foreign investment, which is mainly reflected in the following ways. The first route is to extend the security review period. For example, Australia extended the security review period from 30 days to 90 days through the reform of the Foreign Acquisitions and Takeovers Act 1975 in December 2020. The second route is to expand the scope of the security review system by lowering the threshold of the security review system for foreign investment. For example, Germany revised its Regulations on Foreign Trade and Payments to lower the condition of the security review for different types of M&A for broadening the scope of security review system on the foreign M&A field; France cut their threshold for foreign takeovers from 25% to 10%; Japan increased the number of industries subject to security review system for expanding the scope of security review; and Italy included acquisitions from EU to expand the scope of security review. The third route is to strengthen the security review in specific fields. For example, Canada has paid attention to the fields which are critical to the COVID-19 pandemic, sensitive personal data, specific sensitive technology fields, key minerals fields, and investment fields for “state-owned or state-influenced” foreign investors; France added the field of biotechnology to the review list, etc.⁴⁷

Amid the general trend of strengthening restrictive measures against foreign investment, China established the foreign investment security review system to balance the investment regime which had been radically liberalized with the introduction of the modality of pre-establishment national treatment plus negative list.

B. A Comparison between the Chinese Security Review System and Its US Counterparts

The US has a long history of conducting security reviews of foreign investment, particularly foreign M&A of US companies. The CFIUS is the agency

⁴⁶ *Ibid.*, p. 113. The United States enacted the Modernization of Foreign Investment Risk Review Act in 2020. The United Kingdom ratified the National Security and Investment Act in April 2021. The European Union published the Regulation on Establishing a Framework for Screening of Foreign Direct Investments in 2019.

⁴⁷ *Ibid.*, pp. 111–114.

responsible for national security reviews. Understanding the CFIUS's development, history, and evolving role over time is essential in distinguishing between its parameters regarding "covered transactions". For all "covered transactions", or transactions that directly fall under the mandatory review of the CFIUS, the CFIUS must "determine whether a transaction threatens to impair national security, or the foreign entity is controlled by a foreign government, or it would result in control of any 'critical infrastructure that could impair national security'".

The CFIUS, established in 1975, is an interdepartmental agency mainly responsible for evaluating and monitoring the impact of foreign investment on the national security of the US. The CFIUS is chaired by the Secretary of the Treasury of the US, and the secretariat is located in the International Investment Bureau of the Department of Treasury, which takes the lead in the daily affairs of the committee.⁴⁸ The CFIUS has developed a complete set of measurement and evaluation systems in actual operation, and each member has a clear division of labor and cooperation with each other.

In 1988, in response to large-scale acquisitions by foreign companies, mainly Japanese companies, the US Congress passed the Exon-Florio Provisions as an amendment to the National Defense Production Act 1950. The amendment became the basic law of the US to regulate foreign M&A and protect national security, as well as to regulate foreign M&A of US assets. The Exon-Florio Act authorized the President and CFIUS to conduct a national security review of M&A of US companies by foreign investment. It stipulates that as long as there is sufficient evidence to prove that foreign M&A will endanger the national security of the US, the President has the power to suspend or cancel it. In the same year, the President of the US issued the Executive Order No. 12661, giving the CFIUS the mandate to implement Section 721. In 1992, Congress passed the Exon-Florio Amendment Act,

⁴⁸ Members of the CFIUS are composed of key officials from various departments, including the Department of State, Department of Defense, Department of Commerce, Department of Justice, Department of Energy, Office of Management and Budget, Office of the United States Trade Representative, Council of Economic Advisors, the Office of Science and Technology Policy, Office of Assistant to the President for National Security Affairs, National Economic Council and National Security Council. In 2003, the US Department of Homeland Security joined the CFIUS.

which added provisions for security review of M&A by foreign government-controlled companies in the US. The new act gave the President and CFIUS full authorization for security review and decision-making, but in fact, the review process is often disrupted by Congress and interest groups, causing endless delays and ultimately leading to the abortion of merger or acquisition. Of particular note is that on July 26, 2007, the then US President Bush signed the Foreign Investment and National Security Act 2007 (FISIA). The FISIA clearly requires national security reviews for foreign acquisitions of “critical infrastructure” and M&A by foreign state-owned enterprises.

After the September 11 attacks, the US became more sensitive to national security, and its identification of national security tended to expand. The CFIUS has raised the threshold for foreign M&A in the US, requiring foreign investors acquiring US companies to sign an “International Security Agreement” with the US. In 2003, the National Strategy for the Protection of Critical Infrastructure and Assets was issued, which identified 12 key economic sectors in the “critical infrastructure” category, including agriculture and food, water, public health, emergency service industry, national defense, telecommunications, energy, transportation, banking and finance, chemical/hazardous materials industry, postal and shipping, and information technology. Stricter security reviews of most M&A transactions by state-owned companies were required, and the review period was extended.

The most recent and arguably most revolutionary expansion to the CFIUS’s reviewing power and jurisdiction came from the FIRRMA. President Donald Trump signed the FIRRMA on August 13, 2018, becoming the first major overhaul of the CFIUS operations in over a decade and marking a new era in regulating foreign investment in the US. The new legislative move was taken in response to a shift in global powers. Greater emphasis and attention has been placed on Chinese investment and the potential national security threats that come along with such investment. In other words, behind the FIRRMA is the consensus to impose more restrictions specifically on Chinese direct investment into the US.⁴⁹

49 Farhad Jalinous et al., CFIUS Reform Becomes Law: What FIRRMA Means for Industry, *The M&A Journal*, November 2018, <https://themandajournal.com/articles/vol19/iss1/cfius-reform-implications-for-real-estate-transactions/> (Last Visited on July 16, 2025).

In the past, national security was mainly concerned with defense industrial bases and technology transfer, but after the FIRRMA, the US government offered more extensive interpretation of national security, and overseas investment in US critical infrastructure is subject to scrutiny of national security. Previously, the CFIUS's power to review certain foreign investment remained contingent on the level of control: if the investment did not result in the investor receiving sufficient control of the US entity or business, it had no authority to intervene in the proposed acquisition, merger, or takeover. The FIRRMA expands the scope of the CFIUS's regulatory review authority to cover both controlling and non-controlling investment, which involve "critical infrastructure",⁵⁰ "critical technologies",⁵¹ and the "sensitive personal data" of Americans.⁵²

VII. CONCLUDING REMARKS

At the outset, the Chinese foreign investment security review system was often compared with the US foreign investment security review system.⁵³ After

50 Under the FIRRMA, "critical infrastructure" refers to all "systems and assets, whether physical or virtual, so vital to the United States that the incapacity or destruction of such systems or assets would have a debilitating impact on national security".

51 "Critical technologies" is described in the FIRRMA with a broad coverage, which not only refers to defense articles or defense services included on the United States Munitions List set forth in the International Traffic in Arms Regulations, items included on the Commerce Control List set forth in the Export Administration Regulations, specially designed and prepared nuclear equipment, parts and components, materials, software, and technology, select agents and toxins, but to emerging and foundational technologies controlled pursuant to the Export Control Reform Act. On November 19, 2018, the Bureau of Industry and Security provided a proposed list of "representative technology categories" that would fall under the CFIUS as "critical technologies". The comprehensively defined list seems to cover all the cutting-edge scientific investment opportunities.

52 "Sensitive personal data" is defined to include ten categories of data maintained or collected by US businesses that (i) target or tailor products or services to sensitive populations, including US military members and employees of federal agencies involved in national security, (ii) collect or maintain such data on at least one million individuals, or (iii) have a demonstrated business objective to maintain or collect such data on greater than one million individuals and such data is an integrated part of the US business's primary products or services.

53 Allan Fels, Xiaoye Wang and Jessica Su, *The Chinese State Council Establishes a National Security Review System for Foreign Takeovers*, <https://www.concurrences.com/en/bulletin/news-issues/february-2011/the-chinese-state-council-establishes-a-national-security-review-system-for-en> (Last Visited on July 16, 2025); See *supra* n. 5.

the introduction of the FIL, which centers on the pre-establishment national treatment and negative list, the new national security review system was contemplated as a counterbalance to the most liberal foreign investment regime. In the meantime, the new national security review system was also considered as a countermeasure in response to prohibitive or restrictive US investment measures against China's overseas investment.

It seems that in order to catch up with the latter, which was upgraded by the FIRMA, the former underwent a formalization process. Upon careful examination of the foreign investment security review systems of China and the US, we find that China has introduced a system comparable to that of the US. In terms of jurisdiction, both systems are tailored to maximize foreign investment review; in terms of the ambiguity of key terms, both systems allow the government to exercise the greatest possible discretion. The only difference is that the Chinese foreign investment security review system is, to a greater or lesser extent, prepared as a toolkit for contingencies, while the US system is one of the legal toolkits ready to counter investment from China.

(Edited by Yunhan Wang)