清华-布鲁金斯公共政策研究中心
BROOKINGS-TSINGHUA CENTER FOR PUBLIC POLICY

A Study on the External Environment for the Investment of Chinese Enterprises in the United States

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Contents

Introduction

[Abstract] In recent years, direct investment of Chinese enterprises into the United States has received extensive attention. Through a systematic analysis of the external environment for the investment of Chinese enterprises in the United States in such areas as legal review, political environment and business operation as well as their associated risks, this report seeks to explore the institutional factors affecting Chinese investment in the United States and offer investment advice for Chinese enterprises.

[Key words] direct investment of Chinese enterprises in the United States, legal review environment, political haggling environment, business operation environment

Preface

China is now entering the fast track of foreign direct investment (FDI). In 2010, China's outward FDI totaled $68 billion, ranking first among developing countries and fifth worldwide[1]. However, most of China's outward FDI is flowing into developing countries in Asia, Africa and South America, while investment in developed countries in Europe and the United States is still very limited. By the end of 2009, China had invested a total of $18.17 billion in developed countries, accounting for only 7.4% of China's outward FDI stock, and China's FDI outflow to the United States, $3.34 billion in total, only represents 1.4% of its existing FDI stock[2]. In a sharp contrast to the fact that China and the United States are each other's second largest trading partner, only 0.1% of the FDI flowing into the United States comes from China. The size of China's FDI is far smaller than that of Mexico, Saudi Arabia, ROK, Brazil and India, and about equivalent to that of New

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1UNCTAD ,World Investment Report 2011, http://www.unctad-docs.org/UNCTAD-WIR2011-Full-en.pdf

2Statistics of China's Outward Direct Investment in 2009, http://www.fdi.gov.cn/pub/FDI/wztj/jwtztj/t20100920_126763.htm

Zealand and Austria[3]. According to the estimate of the Asia Society, China will invest over $1 trillion globally by 2020, and a considerable part of this new investment will flow into the United States and other developed countries[4].

US society has both expectations and concerns about Chinese investment. Chinese investment can be a positive factor in driving local economic growth and creating jobs. Many state governments are now setting up special agencies in China to attract business investment. According to data from the Council of American States in China, more than half of the states in the US have set up representative offices in China to facilitate bilateral trade and Chinese investment in their states[5]. However, due to differences in political systems and cultural traditions, the United States is still worried that China may use its investment to seek control of certain sectors of the US economy and threaten US national security. The political disruptions and setbacks experienced by Chinese investors in recent years have much to do with this mindset. Several acquisition deals initiated by Chinese investors, including the CNOOC bid for Unocal in 2005, the Huawei-BainCapital bid for 3Com in 2007, the NWII bid for Firstgold in 2009, and

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3According to the statistics of the US Bureau of Economic Analysis (BEA), by the end of 2009, China's cumulative direct investment in the United States totaled US$2.3 billion, while the total US FDI inflow for the same period stood at US$2.3 trillion. Source: BEA, http://www.bea.gov/international/index.htm

4An American Open Door? Maximizing the Benefits of Chinese Foreign Direct Investment,
http://asiasociety.org/policy-politics/center-us-china-relations/american-open-door

5The Council of American States in China, http://www.casic.us/chinese/member/memberlest.asp?cd=104, accessed on 15 May, 2011.

Huawei's bid for the assets of 3LeafSystems in 2011, all failed due to intervention from various groups in the United States on the grounds of national security. [6]

Given this background, it is even more imperative to study the external environment for Chinese investment in the United States. When analyzing the investment environment facing Chinese enterprises in the United States, one should not just consider risks such as natural disasters, accidents and the commercial risks caused by market changes, poor management and exchange rate volatility, but also gain a deeper understanding of the external environment for investment in the United States and those non-commercial risks – the risks of political environment and business environment. The risk of political environment refers to the passive risk Chinese enterprises face when entering the US market due to lack of knowledge of the relevant US laws concerning foreign direct investment, and the active risks in the process of investment review or regulation caused by the interference of political forces in the United States. The business environment risk refers to possible lawsuits and economic losses that Chinese enterprises may experience after entering the US market due to the substantial differences between the two countries in terms of legislation on environmental protection, product responsibility, intellectual property, labor and employment and taxation.

6The Dawn of China's Rise: A New Chapter in Chinese Overseas M&A, http://www.deloitte.com/view/zh_CN/cn/services-cn/csg-cn/e574184fa7f9c210VgnVCM2000001b56f00aRCRD.htm.

I. Literature Review

In the 1980s, British economist J.H. Dunning (Dunning, 1980) put forth the Eclectic Theory of International Production, which suggests that only companies with advantages in ownership, internalization and regional location are capable of outward direct investment[7]. Based on the analysis of the FDI flows and economic development levels of 67 developing countries between 1967-1978, Dunning offered an explanation of the dynamic relationship between a country's level of economic development and its position in international FDI distribution, which is known as the Investment Development Path (IDP) theory. He pointed out that only when a country reaches a certain stage of economic development, will it have more FDI outflow than inflow, thus becoming a net FDI exporter.[8] According to UNCTAD (2000), there are five main reasons for companies to engage in outward direct investment, specifically cross-border M&A: maximizing synergistic effect, lowering hurdles for entering foreign markets, gaining access

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to foreign markets and control of strategic assets, enabling swift transfer of assets, and expanding market presence and boosting competitiveness. The report also suggests that the emerging trend of globalization is also a major factor driving cross-border investment.[9] Chunlai Chen and Christopher Findlay (2003) believe that most of the cross-border M&A deals are initiated for the purpose of acquiring strategic assets, such as R&D centers, brands, local sales and networks. In certain situations, M&A deals are also used by multinational corporations as a means to seek advantage and control in new markets as well as to achieve such goals as economy of scale, business diversification and collaborative management. Chen and Findlay note that when gaining advantage in the market is vitally important for the company, M&A is not only cheaper than building new factories, but also faster in raising competitiveness

In his analysis of the advantage and motivation behind China's outward investment, Sun Jianzhong (2000) proposes the theory of comprehensive advantage. He believes that diversified investment incentives, differentiated advantages and multi-dimensional investment space complement and reinforce each other, together building China's strength in outward direct investment, and delivering investment benefits for China. Deng Ping (2007) concludes from a study on China's experience in outward direct investment in recent years that acquiring strategic resources (e.g. technology, managerial expertise and brands, etc.) and increasing business competitiveness are the primary reasons for Chinese

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investment in developed countries.

Karl Sauvant and Clarence Kwan (2008) believe that whether Chinese companies can resolve the non-commercial risks they face when investing in the United States depends mainly on whether all the stakeholders can take action to help them mitigate these challenges. Chinese enterprises will only be able to control the political risks associated with their investment by improving their capability for executing cross-border M&A and familiarizing themselves with the legal and institutional environment of the United States.. Ni Quansheng (2011) believes that the traditional theory of direct investment only partly explains the direct investment of Chinese enterprises in the United States. Despite their advantage in capital access and policy preference, Chinese enterprises lack competitiveness in technology and management, which is why their direct investment in the United States has failed to yield a high return. Daniel Rosen and Thilo Hanemann (2011) pointed out that the political interference experienced by Chinese investors in the United States mainly includes the obstruction of commercial interest groups, the China-threat rhetoric used by politicians to fish for political capital and the squeezing of Chinese companies by US "hawks". The US government should send a positive and clear signal to Chinese investors, understand the true intentions of Chinese enterprises, and strengthen communication with China in order to maintain policy flexibility, and avoid escalating and politicizing disputes. It should adopt a systemic approach in managing foreign direct investment, reduce the political influence in national security review, and ensure the growth and openness of the

US economy. Fang Zhiyin (2011) analyzed the Committee on Foreign Investment in the United States (CFIUS) reviews and congressional intervention concerning Chinese companies' bids for US assets over recent years, and suggested that seeking the maximum protection within the existing legal framework is the rational way for Chinese companies to deal with the situation.

A few articles have attempted to examine the legal review, political games and business operation environments for Chinese enterprises investing in the United States from the perspective of the differences between the two countries in terms of legal systems, political systems and business environments. The above-mentioned studies have provided a diversified perspective and an important source of knowledge for exploring the non-commercial risks facing Chinese companies in the United States and lay the foundation for further analysis of the logic behind the factors affecting Chinese investment in the United States.

II. Legal review environment and passive risks

When investing in the United States, Chinese enterprises first face a completely different legal review environment, a so-called passive risk. This risk chiefly arises if their direct investment runs against current US regulations concerning foreign investment, or if they file for review to the authorities as required. The US features a high degree of openness to foreign investment and usually does not discriminate between countries, giving equal treatment to foreign and domestic enterprises. However, as the US attaches great importance to political and economic security, foreign capital is still subject to various restrictionst. Foreign direct investments are limited and regulated by federal, state and special laws for industry access, M&A and national security.

1. Legislation limiting access to industries

Out of considerations for national security and public services, foreign capital is subject to legislative restrictions in the US, whether a greenfield investment or direct investment in a certain industry through M&A. Unlike in China, where the Ministry of Commerce and other departments regularly release a Guiding Catalogue of Industries for Foreign Investment, the US does not have a dedicated authority to give administrative opinions that encourage, restrict or prohibit FDI in certain industries, but exercises such regulation through legislation governing the industries themselves. Fields sensitive to foreign investment include transport, communication and media, financial services, national defense, energy and mining. US laws control the entry of foreign capital into specific industries in the following ways:

First, requirements for US citizenship. The US limits the entry of foreign capital by requiring a certain ratio of US citizens among the directors and management of the company, and a ratio of of voting shares to be held by US citizens. This approach to foreign capital administration, focusing on substantial ownership and effective control, was first used in keeping foreign capital out of the US aviation industry. After World War I, Congress feared that foreign control over US airlines might endanger national security and the economy.

II. Legal review environment and passive risks

The Air Commerce Act of 1926 states that for an air transport enterprise, a US company controlled by US citizens should hold at least 51% of the voting shares, and the chairman of the board and at least two thirds of the directors should be US citizens. After revisions in the form of the Civil Aeronautics Act of 1938 and the Federal Aviation Act of 1958, restrictions on foreign capital into the aviation market were tightened rather than loosened, with the proportion of voting shares to be held by US citizens raised to 75%. Similarly, for sea transport, US law only allows foreign vessels in its ports that are engaged in international business and arriving from a foreign port, but does not allow them to conduct business between US ports. The still-effective Merchant Marine Act of 1920 (or Jones Act), states that only a vessel built and registered in the US, owned by a US company, and having at least 75% of its crew being US citizens is allowed to engage in cargo transport directly between two ports within the borders of the US (including territories and possessions) or via a foreign port.

Second, nature of capital sources. The US decides whether a foreign investor can obtain a license for a certain business by examining its sources of capital and investment method. This is most common in fields closely related to national security such as telecommunication, energy and national defense. According to the Communications Act of 1934 (1996 Amendment), a foreign investor can obtain a US communications license but only depending on its capital channels and method of investment. First, any foreign government, company or organization controlled by a foreign government, foreign political party, foreigner or any company established under foreign law is prohibited from entering the US communications market and licenses for broadcast and common carrier are denied, regardless of whether a direct or indirect investment. . Second, for direct investment in a US company holding licenses for broadcast and common carrier, the total investment of all foreigners shall not exceed 20% of the company's total shares, and foreigners are prohibited from acting as directors or managers. Lastly, for indirect investment in such companies or its parent company (i.e. a holding company that holds more than 50% of its shares and controls its operations), foreign investors shall not hold more than 25% of the shares of the holding company.

The US exercises even stricter control over such fields as energy, mining and national defense, where foreign capital is almost entirely prohibited. The Atomic Energy Act of 1954 states that, to prevent potential harm to national defense, public security or public health, no license for nuclear facility operation may be granted to a foreigner, nor any company controlled by a foreigner, foreign company or foreign government. Similarly, the Mineral Leasing Act of 1920 only allows the federal government to sell mining rights to such resources as coal, oil, oil shale and natural gas to US citizens, US companies or other US entities. Such rights may not be sublet or re-let to a foreigner , unless approved by the Secretary of the Interior,. In the field of science and technology for national defense industries, foreign capital is also prohibited, unless approved by the Department of Defense or other relevant authorities. It is far from easy to obtain such approval. and Foreign investment in this field shall also not exceed 5%. These restrictions are tougher than those requiring a proportion of US citizens or licensing system, , as any capital deemed as foreign investment is restricted from or entirely prohibited from entry into these industries.

Third, the principle of reciprocity. The US restricts the entry of foreign capital through case-by-case review by regulatory authorities. Compared with other restrictions, this method involves more factors and gives more power to the authorities. In the telecommunications industry, as mentioned above, the Federal Communication Committee (FCC) has the right to allow for more than 25% of shares to held by any foreign investor in a company through case-by-case review, provided that such ownership does not contravene public interest, . According to the principle of reciprocity, this rule only applies when the investor's home country does not impose restrictions on US investment. Similarly, in the air transport industry, according to the Open Skies Agreements, a foreign investor may come to own as much as 49% of the shares of a US airline through case-by-case review, including a minimum of 25% of non-voting shares, provided that the company remains in the substantial control of US citizens and a bilateral agreement on aviation exists between the US and the home country of the foreign shareholder.

Case-by-case review is occasionally used in such fields as telecommunication, national defense and aviation, but is a necessary procedure for foreign capital to enter the US banking industry. The International Banking Act of 1978 established national treatment for foreign banks, stating that a branch or agency set up in the US by a foreign-funded bank has the same rights, obligations and restrictions as US banks in the same locality. The Fair Trade in Financial Services Act of 1995, however, increased obstacles for foreign banks to enter the US market by adding reciprocity requirements. It states that, if the home country of a foreign-funded bank refuses to grant national treatment to US banks, the Federal Reserve has the right to limit the foreign-funded bank's access to the US market. Furthermore, according to the Foreign Bank Supervision Enhancement Act of 1991, for a foreign-funded bank wishing to set up a branch, agency, commercial loan company or subsidiary in the US, the bank must be under the overall regulation of finance authorities of its home country and the meet requirements of consolidated financial statement supervision, before it is allowed into the US market by the Federal Reserve. Lastly, any foreign investor wishing to control a US bank through a bank holding company must comply with the Bank Holding Company Act of 1956, and can only proceed upon approval of the Federal Reserve. In short, reciprocity-based regulation through case-by-case review by authorities not only adds uncertainty to foreign investment in the US, but provides grounds for the US government to impose sanctions and threats under Section 301 on countries not granting equal opportunities for entry to US companies .

2. M&A regulatory regime

Apart from putting restrictions on foreign capital in certain sectors through legislation, the United States also regulates US local M&A activities of foreign enterprises through antitrust agencies and securities regulatory authorities. Unlike access restrictions, the M&A law regime does not specifically target FDI, but is equally applicable to all M&A activities by both local and foreign enterprises. The comparable law regime in China was put in place later than in the US and is being enforced in a much different environment. Specific information on US laws and regulations related to M&A and foreign capital is as follows:.

First, M&A control by antitrust agencies. As a fundamental law regime to uphold competition and order in the US market, antitrust laws are mainly formulated to regulate activities that aim to undermine market competition, form business monopolies or hinder, sabotage or halt competition. Major M&A laws include the Sherman Act and the Clayton Act, while the Hart-Scott-Rodino Antitrust Improvements Act of 1976 (HSR Act) and its rules mainly stipulate tM&A procedures, such as filing, review and investigation. Foreign investments are also subject to regulation of their M&A activities in accordance with the above laws.

, Parties involved in M&A activities, including tender offers, mergers and consolidations, and investors of joint ventures must file the transaction with the Federal Trade Commission (FTC), the US antitrust authority, and the Antitrust Division of the Department of Justice for review, if filing requirements are met. Both parties to the M&A must be the ultimate parent entities with each of the involved entities under their direct or indirect control. According to the HSR Act, investors engaged in business activities in the United States or any activities that may affect the US commerce will have to make a filing regarding the M&A activity prior to the completion of the M&A transaction if the size of the parties and the value of the transaction both exceed certain thresholds, and can only proceed after a 30-day waiting period, as . The HSR Act also provides that M&A activities involving foreign capital that qualified for the lowest filing threshold but are not heavily involved in US commerce shall be exempted from the filing obligation. Such activities include acquiring non-voting securities of US companies, voting securities of non-US companies and foreign companies acquiring foreign assets. However, if the companies are to be acquired by foreign government entities and are engaged in interstate commercial activities, exempted filing must be made. Meanwhile, actual review of M&A activities is done mainly in accordance with the Clayton Act and the Sherman Act. The Clayton Act unequivocally prohibits assets or equity mergers and acquisitions that “may substantially lessen competition or tend to create a monopoly”, while the Sherman Act considers “unreasonable restraint of trade” resulting from M&A,

anticompetitive conspiracy or attempts to monopolize illegal. The regulatory authorities also provide guidance for enterprise M&A by the jointly released Horizontal Mergers Guidelines. The Guidelines are not legally binding, but the analytical framework has been accepted by most courts, so Chinese investors should carefully study these provisions . To increase the clarity and transparency of the law enforcement process, the regulatory authorities released new Horizontal Mergers Guidelines in 2010, eliminating the five-step analytical process of defining the relevant market, calculating market concentration, determining whether mergers have adverse competitive effects, assessing factors such as new market entry, customer efficiency gains and failing company defense and finally determining whether to prevent the mergers or not. Instead, the new Guidelines stress that merger analysis does not consist of uniform application of a single methodology, due to the different features of different sectors, products and markets. Finally, if mergers involve restricted sectors, the transactions need to be reviewed by both the authorities in charge of the specific sectors and the antitrust agencies. The results of these foreign-funded mergers may become more unpredictable as a result of overlapping and conflicting reviewing powers of different authorities, as well as political factors.

Therefore, when the parties and the transaction meet the filing threshold requirements of the HSR Act, Chinese investors need make a filing with the authorities and provide all required information, including disclosing the ultimate parent entity of the buyer. Given the confidentiality of the information submitted and that the information will only be used to review the merger itself, Chinese investors should not be overly concerned, especially when Chinese government entities or state-owned enterprises are involved. The parties will be fined if the required filing is not made. Once an enterprise is considered to have proceeded with illegal mergers, it will be forced to divest, dissolve or split and may also face civil and criminal litigations by the authorities and civil compensation ligation for compensation of up to three times the losses of the affected enterprises or ordinary customers.

Secondly, M&A reviews by securities regulatory agencies. The major provisions in US securities law involving acquisition of listed companies are found in Article 13 and 14 of the Securities Exchange Act of 1934 (commonly known as the Williams Act of 1968). While the Securities & Exchange Commission (SEC) is not authorized by law to approve or reject a transaction, it can adversely affect the transaction or even force the related parties to give up by pushing out the closing date of the transaction with a prolonged review process. Hostile bids or cash tender offers, especially when Chinese government entities or state-owned enterprises are involved, may lead to even stricter review of the relevant documents filed. In addition, unlike Chinese securities law, the Public Company Accounting Reform and Investor Protection Act of 2002, more commonly known as the Sarbanes–Oxley Act of 2002, provides that the management must assume a larger responsibility in the internal control of the company upon completion of acquisition.

If Chinese investors wish to acquire securities of a company listed on the American Stock Exchange or OTC markets, they need to abide by US federal and state securities laws in addition to SEC rules and regulations. The Williams Act provides that when a purchaser attains a certain proportion of a publicly listed company's equity, the purchaser must fulfill certain disclosure obligations in accordance with the required procedures, so that shareholders of the target company can get a thorough understanding of purchaser's background, the purpose of the offer and its possible impact on the company, so to arrive at a correct decision. At the toehold acquisition stage, i.e. through joint actions the purchaser holds or attains over 5% of a listed company's shares, the purchaser should complete a Form 13d to register with the SEC, the stock exchange and the target company within ten days of becoming a 5% plus shareholder. Apart from basic information on the purchaser and the target company, the purchaser is required to disclose the source of funds used in the offer, a list of lenders, the purpose for which securities are acquired, the plans the purchaser might have for the target company, the total amount of such securities the purchaser holds and any agreement or understanding regarding purchase and sales of such securities in the past 60 days. Following, whenever the shareholder buys or sells 1% of such shares or has any change in shareholding intentions, it should file an amendment to the form with the aforementioned three parties within one day. At the tender offer stage, i.e. the purchaser extends an invitation to multiple potential investors to purchase the target company shares at a price lower than the market price, the investor should complete Form 14d-1 to make an additional statement to the aforementioned three parties. Apart from information included in Form 13d, the purchaser must also disclose the quantity, price, tender offer time limit and method of payment. The tender offers should remain valid for no less than 20 working days, and committed shareholders are entitled to withdraw at any time after 60 days from the date of the original tender offer or request or invitation, even if the tender offer has expired, as long as the tendering party has not yet made its purchase. After the acquisition is completed, another major risk faced by Chinese enterprises on the US securities market is the mandatory disclosure of internal governance information as prescribed by the relevant laws. Following the financial frauds and scandals of Enron, WorldCom and other listed companies, the US government rolled out the Sarbanes–Oxley Act to increase the accuracy and reliability of company disclosures and uphold the trading order of the securities market. Since its implementation on July 15, 2006, the Act has been noted for its wide coverage and strict punitive measures. President George W. Bush called it the most far-reaching reform of American business practice since the time of Franklin D. Roosevelt in the 1930s and 1940s. The Act strictly defines the responsibilities and obligations the management of listed companies must bear in internal control, including the requirement of the management to produce an internal control report as part of each annual report submitted to the SEC, which will hold the entire management accountable, and assess the effectiveness of the internal control structure and procedures on financial reporting.

If Chinese enterprises fail to fulfill their obligations in accordance with the aforementioned laws, they will face various administrative regulations or judicial litigation. For those who violate securities trade laws and provisions, the SEC can enforce various punitive measures through judicial or administrative procedures, such as civil fines, return of illegal proceeds, prohibition of employment, condemning and restricting activities or business, suspending or revoking registration qualifications and other sector-specific punitive measures. As for violations of the Sarbanes–Oxley Act, if financial reporst do not conform with all requirements, the violator shall be fined not more than $1,000,000 or imprisoned not more than 10 years or both. Anyone who willfully certifies any financial report with the knowledge that it does not conform with all requirements shall be fined not more than $5,000,000 or imprisoned not more than 25 years or both.

3. National Security Review Mechanism

The US has adopted much industry-specific legislation restricting or prohibiting foreign investments as matters of national security. Mergers and acquisitions of existing US companies undertaken with foreign capital, are subject to review or regulation. Furthermore, cross-border mergers and acquisitions in the US are also often affected by national security considerations, especially after the September 11 attacks. Perhaps in response to the risks posed to US national security by the large number of Japanese acquisitions of American companies in the 1980s, the US Congress passed the Exon-Florio Amendment in 1988, which established the national security review mechanism for foreign mergers and acquisitions. Afterwards, a series of additional laws and regulations, including the Byrd Amendment in 1993, the Foreign Investment and National Security Act (FINSA) in 2007 and the Regulations Pertaining to Mergers, Acquisitions and Takeovers by Foreign Persons (RPMATFP) , were enacted to form the country's current national security review system for foreign mergers and acquisitions, featuring a combination of the power of the Committee on Foreign Investment in the United States (CFIUS) to review transactions, the President's power to veto a transaction, and the authority of Congress to supervise the entire process.

FINSA gives CFIUS, which originally exercised its power to conduct national security reviews upon authorization of the President, the status of a statutory agency to increase its authority. It also increases the number of CFIUS members. As a result, the scope and authority of government review have been expanded. The basic logical assumption underlying the setup of CFIUS for national security review of foreign investments is that in certain cases, the control of US businesses by foreign capital may pose threats to US national security, while the same threats are not present if businesses are controlled by Americans.

The purpose of CFIUS and its regulations is to give the President the authority to suspend or ban any acquisition, merger or takeover if the President has convincing evidence that any foreign person who has actual control of the business engaged in interstate commerce in such transactions may (emphasis added) take actions that may threaten US national security. CFIUS and its regulations are applicable to covered transactions, i.e., any contemplated or pending merger, acquisition or takeover that could result in a business engaging in interstate commerce to be controlled by a foreign person. FINSA of 2007 also has a new definition of national security that, in addition to the traditional national security considerations, also looks at the potential national security implications of any transaction involving tangible or intangible systems or assets critical to the US (such as banks, water supply, critical technology and critical infrastructure). Therefore, the scope of the definition of national security is expanding. Any CFIUS member or the President may initiate a review and interpret national security from their own individual perspective. "The US government departments responsible for national security generally call for a more stringent regime on foreign investments, with particular emphasis on restricting investments from China, because China is regarded as a strategic rival, not an ally, of the US. In fact, confidential intelligence is playing an increasingly important role in the review of CFIUS."

FINSA, by authorizing Congress to perform a national security review of any attempted merger, acquisition or takeover of US assets by a foreign person that may threaten US "national security", has the effect of preventing or significantly delaying certain foreign investments in the US. As FINSA does not offer an explicit definition of "national security", many transactions in many industries may be subject to CFIUS review. Upon notification of a contemplated transaction, CFIUS will have a 30-day review of the transaction on behalf of the President and determine whether a 45-day investigation will follow to determine the impact of the transaction on US national security. During the review process, CFIUS will appoint a lead agency to monitor and implement any agreement that may be entered into between the parties to the transaction and the relevant government agency to mitigate specific national security concerns. The execution of one or more mitigation agreements may be imposed as a pre-condition for CFIUS to approve the transaction in question. FINSA authorizes CFIUS to reopen a review when a party to a transaction is found to have materially breached a mitigation agreement. Therefore, Chinese investors, when entering into such mitigation agreements, must keep this risk in sight and take sound internal control measures to ensure compliance with the agreements.. Furthermore, even if a transaction is not filed for national security review, a government official or department with proper authority may still request a CFIUS review and CFIUS must initiate an investigation if the transaction involves the acquisition of any US assets by an entity controlled by a foreign government. Other actions that the US government may take include not taking any action against the transaction, seeking to suspend or ban the transaction, entering into an agreement to mitigate the specific national security concerns, or ordering divestment within three years after the completion of the transaction (subject to certain exceptions). For the parties to a transaction, a main benefit of filing a notification with CFIUS is that if the transaction is not hindered, the government may not order divestment after the completion of the transaction.

The US government rarely exercises its rights under the law to stop a transaction. “China’s investment activities in the United States have been smooth by and large, with most projects not subject to the national security review, and the few that were indeed subject to the review had almost all received fair hearings. However, the signals that come from Washington are somewhat mixed and confusing, and these not just from CFIUS.” Nevertheless, even in the absence of any formal intervention by the US government, many contemplated transactions may still end up failing. Strong public opinion and political pressure may be enough to prevent transactions – CNOOC’s failed bid for Unocal is a prime example. Therefore, the acquiring party needs to engage experienced lawyers and government relations advisors to make an assessment on issues related to national security concerns under FINSA, as well as an assessment of the political climate and public opinion concerning the contemplated transaction.

III. Political Environment and Active Risks

In addition to the aforementioned legal review risks and passive risks, Chinese investors in the United States also face various active risks in their intial entry stage related to political issues. These types of risks are not isolated, but interrelated. With political stability and a sound legal system, the US generally does not face typical political risks of regime change, coup d'état and social disturbance, but the dynamic political environment on which the US public governance is based tends to make Chinese investors unfamiliar with such an external environment vulnerable to active risks. In other words, political opposition from various interest groups, or political considerations, may lead to the introduction of additional legal requirements that bring unpredictable risks to foreign investments.

1. Constitutional Basis for Foreign Investment Review

The US system is based on the separation of powers, with checks and balances between the legislative, executive and judicial branches of government. Many government policies have to be reviewed and passed in Congress to become law. The US constitution grants the power to regulate foreign trade to Congress, which later "delegates" some of the power to negotiate and enter into agreements with foreign governments to the government in the Foreign-Trade Zones Act of 1934. Therefore, Chinese enterprises intending to invest in the US must take the role of Congress into full account in their investment activities.

The Federal Constitution of 1787, which established the three branches of government, i.e. the executive, the legislative and the judicial, represented by the President, Congress and the federal court, respectively, marked the establishment of the US as a true sovereign state. Congress and the President are elected by voters in relatively independent electoral districts. The power balance, contention and competition between the President and Congress under the mechanism of separation of powers have been a main thread running through the evolution of modern US democratic politics. In a sense, a good understanding of the legal basis and political rationale underlying the functioning of Congress is a prerequisite for a comprehensive understanding of US foreign policymaking.

Section 1 of Article I of the US Constitution reads: "All legislative Powers herein granted shall be vested in a Congress of the United States, which shall consist of a Senate and House of Representatives." The legislative power belongs to Congress, but any bill adopted at Congress has to be signed by the President to become law. The President has veto power over Congress, which in turn may override a Presidential veto by a two-thirds majority vote. The unique arrangement of the US political system makes the two parallel government branches of executive and legislation jointly responsible for US economic activities with foreign countries. This is a consensus-building process between the President and Congress. The legislative process of the US Congress features a five-layer deliberation structure comprising Congress members, sub-committees, committees, standing committees and joint committees. The committees generally dominate the process and outcome of legislation. The large number of proposals submitted by Congress members are subject to the screening and selection of the corresponding committees, with only a small number of them being eventually submitted to Congress for deliberation. The committees, with their well-defined division of responsibilities, enable Congress to handle the great number of proposals by category and specialty and improve the efficiency of legislation.

There are many ways in which Congress takes part in and influences the legislation governing foreign economic activities: Congress can enact laws governing foreign-related economic activities in accordance with the Constitution; it can authorize legislative agencies to participate in international economic negotiations and vote on international treaties; it can directly influence the executive agencies' foreign-related economic activities through its power on foreign-related government budgets; it has the power of appointment and is able to endorse or approve senior officials for economic affairs; it has the power to supervise, advise and investigate the executive agencies in implementing foreign-related economic policies by, for example, requiring the executive agencies to submit reports and executive officials to attend hearings and provide testimonies; and it can also leverage its power over economic legislation and policymaking through the media.

2. Political Environment behind Government Policymaking

The characteristics of US society and the pluralism underlying the US political system further increase the uncertainty of its policymaking process and outcome. The decentralized power system characterized by the sharing of diplomatic power between Congress and the President, the multi-party system and interest group politics has always made US foreign policies full of uncertainty. Each administration tries to win the support of more interest groups. US foreign policies are actually often the result of bargaining and compromise among interest groups. In the formulation of foreign-related laws and policies, Congress is inevitably subject to the influence of the congressional system, industrial and regional politics, and various interest groups. The US congressional system is a geographically-based (electorates and states) system of representation, providing conditions for the industries to directly influence the representatives from their electorates and, ultimately, congressional politics. Industries build their power base in Congress on the basis of their geographic location, scope of distribution and degree of concentration to influence the decision-making on economic and trade issues in the House of Representatives and the Senate.

The primary motive of almost all Congress members is to get reelected. To a large extent, they are also easily motivated by competing local interests and thus pay particular attention to the concerns of the industries or companies in their home states or electorates. Although not all foreign-related economic laws and policies concern the immediate interest of their states or electorates, the geographical distribution of domestic industries constitutes the micro-basis of the US Congress's foreign-related economic policymaking. The US is a country with highly active interest groups. Interest groups are also known as pressure groups, advocacy groups or lobby groups. On the one hand, interest groups exist in the US because in the context of the country's unique political philosophy and constitutional framework, the prevailing institutional structure as conceived by the so-called political elites is one of “small-government”, one that leaves rights and liberty in the hands of the people. Interest groups serve as a bridge of communication between the government and society. These interest groups can be divided into Wall Street financial interest groups, business interest groups, trade union interest groups, agricultural interest groups and religion and human rights groups, etc. On the other hand, these interest groups often influence the government's foreign economic policymaking through lobbying, voting, influencing the public opinion, recommending potential appointees or staff and providing information.

The US media also influence the country's foreign economic policymaking in various ways, including by providing sources of information for government policymaking, shaping the public opinion, publishing think-tank views, and influencing the activities of interest groups. The enactment or revision of laws in the US Congress is often triggered by specific events or changes in the environment. The dissemination and even exaggerated interpretation of these events in the media soon make them focal topics among the public. In comparison with government officials, lawmakers have a greater reliance on media information when considering economic policies. A Senate aide once commented that "90 percent of what they [Congress] react to comes from the front pages of the New York Times and the Washington Post." In a sense, these characteristics of Congress members are more prominently reflected in the way they handle issues related to China. James Dull notes, "Over 60 percent of the members of Congress have never travelled to foreign countries. When China is seen in a negative light in the media, they find it effective to take a stance against China and support human rights. Essentially, they neither know much about China nor really care about China nor really oppose China. They react as part of a behavioral pattern, a political gesture. Yet this mindset and behavior, when covered in the media, will foster a policymaking environment that is even more unfriendly to China." Hao Yufan comments that "Congress may reject a transaction for reasons not confined to real national security concerns. In an age with widespread worries about a rising China, this tendency of politicizing an otherwise pure economic issue poses a serious threat to the normal operation of the direct foreign investment review process."

3. Analysis of Chinese Investment Cases

The majority of active risks in the review process generally impact enterprises by way of laws and regulations. The host government uses laws and regulations to translate political issues into legal issues mainly in the following two ways:

First, the administrative authority uses existing laws to reject or impose special regulatory control on foreign mergers and acquisitions. The Exon-Florio Amendment specifically concerning foreign mergers and acquisitions passed in 1988 (and made permanent through the President's signature of another bill in 1991), for example, grants the President the power to suspend or ban those acquisitions, mergers or takeovers considered to pose threats to US national security. As the Amendment does not have a clear definition of the all-important "national security", the President has full discretion as to whether a transaction threatens national security, thus leading to the possibility that the President could abuse power for political purposes. In fact, there have been indeed such cases. The Amendment was originally introduced in response to Japan's aggressive investments in the US. However, after it took effect, it has been only applied to Chinese attempts at mergers or acquisitions, which were often ultimately abandoned by the investors because of the rejection or pressure of the review authority. In 1990, China National Aero-Technology Import & Export Corporation (CATIC), a manufacturer of civil aircraft parts rarely used for military purposes, acquired MAMCO (a US company), but was ordered by the President under the Exon-Florio Amendment to relinquish its ownership in MAMCO; the acquisition was eventually rejected. In 1999, after an extended review, CFIUS, the implementer of the Exon-Florio Amendment, rejected the request of Hughes Aircraft Company to sell a satellite to the Hong Kong-based China Asia-Pacific Mobile Telecommunications Satellite Co., Ltd. In 2003, the Hong Kong-based Hutchison Whampoa Limited and Singapore Telecommunications Limited launched a joint bid to acquire World-Link Communications Inc. but were forced to give up the bid after CFIUS refused to accept its revised proposal and initiated a 45-day comprehensive investigation. In September 2007, the American alternative asset management and financial services company Bain Capital joined hands with the private Chinese firm Huawei Technologies Co. Ltd. to acquire the digital electronics manufacturer 3Com for $2.2 billion. According to the documents submitted to the SEC, Bain Capital would have a 83.5% stake in the target company, with the remaining 16.5% owned by Huawei Technologies. In order to dispel the US government's potential national security concerns, 3Com stated that Huawei Technologies would not receive critical technology or secure sales contracts from the US government or have control of the company's operations by virtue of the transaction. However, the acquisition still met with opposition from various US parties. The Republican and Democratic leaders of the Energy and Commerce Committee sent a joint letter to then Treasury Secretary Henry Paulson, demanding the relevant information the Treasury Department had obtained from the investigation of the acquisition. They were concerned that the alleged military background of Huawei Technologies might impact national security and held that the transaction should not be approved. Due to the pressure, Bain Capital and Huawei Technologies eventually withdrew their application from CFIUS and in effect shelved the project.

Second, laws and regulations can be made or revised to impose special requirements on foreign mergers and acquisitions. Where the existing laws are inadequate to prevent a foreign merger or acquisition, the host state may revise existing laws to strengthen regulation of the transaction. On June 23, 2005, CNOOC, a state-owned company and largest offshore oil and gas producer in China, made an all-cash acquisition offer for the California-based oil company Unocal, the ninth-largest oil company in the US, for $67 per share, totaling $18.5 billion. Before this offer, Chevron Corporation had made an offer for Unocal at a total price that was $1.5 billion less than CNOOC's. What made Unocal so attractive to CNOOC was that 70% of

Unocal's current proven oil and natural gas reserves were in Asia and the Caspian region. The combination of Unocal's resources and CNOOC's market potential would create huge economic value. The acquisition was a pure commercial action with the aim of expanding the sources of oil supply and ensuring the stability of oil imports to China. However, this transaction caused a big stir in the US. Many Congress members wrote letters to the President demanding a strict review of the CNOOC bid for Unocal, and the media, political circles and even the public also voiced strong opposition. On June 30, 2005, the House of Representatives ordered the US government to put a halt to the acquisition plan by an overwhelming vote of 333 to 92 and to investigate the acquisition itself by an even greater majority vote of 398 to 15. As a result, the transaction would have to wait for another four months and three weeks to obtain the outcome of the review. This obviously would cause CNOOC lose the opportunity to compete with Chevron Corporation. Fu Chengyu, General Manager of CNOOC, said that the US revision of the American Power Act was the main reason why CNOOC gave up the acquisition. After eight months of investigation, the US authorities ordered CNOOC to withdraw its bid for Unocal.

In spite of the failed bid of CNOOC for Unocal in 2005, major changes have taken place since, with a number of Chinese energy companies having successfully entered the US market. For example, CNOOC did succeed in acquiring the shale gas assets of Chesapeake Energy Corp. in Texas, Colorado and Wyoming in 2010 and 2011, and CNPC established a joint venture with Devon Energy Corp. in January 2012 to develop oil and gas in the western region of the US and acquired a gas field of Chesapeake in Oklahoma. An important reason for these changes is that adjustments to the US energy structure since 2000 have substantially reduced not only the US's reliance on oil imports but also the energy intensity of its economy. In addition, the transformation of the US energy sector requires a huge amount of investment and this process can be accelerated by foreign investments.

In summary, with its legislative power, the US Congress plays an important role in foreign mergers and acquisitions. Meanwhile, the President's administrative orders have equal validity with the law. The President has the power to veto any bill passed in Congress, which in turn can override the President's veto by a two-thirds majority vote and make the bill a law. In addition, there are many kinds of monopoly groups, community and interest groups, such as trade unions and farmers' organizations, which also exert a certain influence. Out of the consideration of economic interests or support of voters, both the President and Congress members may be motivated to pass laws or policies that are unfavorable to multinational corporations. The state maintains a holistic perspective in determining national strategies and there are considerations not only of an economic nature but also of a political, national security or military nature. In the event of any deviation of the intentions of multinational corporations from the state's strategic goals, it is often the multinational corporations that will get hurt.

IV. Business Operation Environment and Related Risks

In addition to the legal review environment and political environment during the entry stage of investments in the US, Chinese enterprises also face a different business operation environment and related noncommercial risks after they have made their investments. The US federal and state laws and regulations related to business operation are far stricter and more rigid than those in China. The Worker Adjustment and Retraining Notification Act (WARN Act), the Occupational Safety and Health Act (OSHA), the Anti-Discrimination Act, and laws related to protection of intellectual property rights and the environment, in particular, must be strictly complied with and any violation will lead to serious consequences.

1. External Environment of Business Operation Management

The first aspect is environmental protection. The US, at the federal, state and local levels, has numerous, often overlapping and detailed environmental laws, including the Comprehensive Environmental Response, Compensation and Liability Act (CERCLA). Some of these are based on strict liability rather than a fault-based system. Some laws pertain to hazardous substances and companies that use them in the operation of a business, while others apply to the production and emission of wastes and pollutants. In the case of contaminated properties, cleanup is often required. Due to the extensive nature of environmental laws, in many cases, extensive involvement of environmental legal counsel and other advisers is necessary. The US Supreme Court, the highest judicial body in the US, has established the basis under which a parent corporation may or may not be liable for a violation of CERCLA by its subsidiary in the United States v. Bestfoods, 524 U.S. 51 (1998). In brief, the Supreme Court ruled that a parent corporation is liable under CERCLA for the acts of its subsidiary only to the extent that a) the commonality of identity between the parent and the subsidiary is such that the subsidiary's corporate veil is removed by the state law under which the subsidiary is organized, and b) the parent actively participates in and exercises control over the operations of the subsidiary's facility. With respect to the parent's direct liability, the court concluded that the parent "must manage, direct, or conduct the operations specifically related to the contamination, that is, operations associated with the leakage or disposal of hazardous wastes or decisions about compliance with environmental regulations" in order to be held liable. As a result, this case provides guidance as to the procedures and practices that a parent corporation can observe so as to free itself from the liabilities under CERCLA.

The Exxon Valdez oil spill that occurred in Alaska in March 1989 led to the reform of laws governing oil pollution and the adoption of the Oil Pollution Act the following year. As the accident was caused by collision with a reef, the Act emphasizes the prevention of oil tanker spills, requiring, for example, all oil tankers operating in the US waters to come with a double hull. However, it has little effect on oil spills in deep-water drilling sites. In fact, the Act sets a limit of compensation of $75 million, provided that the spill is not caused by negligence. The BP oil spill in 2010, which caused the death of 11 workers and huge environmental damage to the Gulf of Mexico, was the largest accidental marine oil spill in the history of the US. According to the estimate of Goldman Sachs, BP will need to pay a total amount of $20-400 billion for the cleaning and compensation related to the oil spill. In fact, BP has already been mired in thousands of litigations concerning compensation for environmental damage, property damage and personal injuries in the US and beyond as a result of its violation of US environmental laws. Up to now, BP has already paid $4 billion for post-oil disaster clean-up. But the eventual liability it will bear may be even higher. According to the size of the oil spill, BP may face more than $2 billion in civil penalties since the law calculates the fine for oil spills at $1,100 per barrel and, if it is caused by gross negligence, at $4,300 per barrel, and there is evidence indicating that there has indeed been negligence on the part of BP. In the summer of 2010, BP established a $20 billion fund for compensation related to the oil spill as required by the US government. The fund was established to reduce the number of lawsuits filed directly against BP and the resulting legal costs, and to compensate the plaintiffs as soon as possible. According to the plan, BP will inject $3 billion and $2 billion into the fund in the third and fourth quarters of 2010, respectively, and inject $1.25 billion into it on a quarterly basis thereafter until the total amount reaches $20 billion. This compensation fund will be mainly sourced from BP's future oil drilling income, with the scope of compensation covering the companies and individuals suffering losses from the oil spill and plaintiffs filing personal injury lawsuits against BP. However, the fines imposed by the federal and state governments are outside the scope of compensation of the fund.

The second aspect is product liability. A foreign company that manufactures or sells defective products into the US can be held liable under the US law for damages resulting from product liability claims. The product liability law has two main objectives: providing a mechanism for compensating the affected plaintiffs and encouraging producers and distributors to take measures to keep defective products from the market. It is established in the Restatement (Second) of Torts Section 402A that the producer of defective products shall be liable for tort claims. The strict liability in tort law established in the Restatement, where the plaintiff has no obligation to demonstrate the strict liability of the defendant, has become a principle of US product liability law. However, it soon became evident that 402A, created to handle liability for manufacturing defects, could not appropriately be applied to cases of design defects or defects based on inadequate instructions or warnings. In the Restatement (Third) of Torts Section 402A, the product liability takes the place of the rule of 402A and product defects are divided into three types, i.e., manufacturing defects, design defects and instruction/warning defects, with the strict liability only applying to manufacturing defects and the defendant only assuming negligence liability for design and instruction/warning defects.

The Toyota recall of 2009 was due to faulty pedals and unintended acceleration. The US, known as a "country on wheels", was the world's first country to establish an automobile recall system. It adopted the National Traffic and Motor Vehicle Safety Act as early as in 1966; and in this context, the US Department of Transportation set up a new agency – the National Highway Traffic Safety Administration (NHTSA). Over the recent years, the US has improved its automobile recall system. The new Traffic Safety Act passed at the two Houses of Congress and promulgated on October 11, 2000 imposes even stricter rules. For example, the fine for manufacturer's civil liability is increased from $925,000 to $15 million, and the maximum term of imprisonment for any automobile manufacturer that conceals defects and causes personal injuries or deaths is increased from five years to 15 years. In addition, there are a series of supporting regulations that provide for motor vehicle safety recall, including Motor Vehicle Safety in the United States Code and the Defect and Nonconformity Reporting, Tire Confirmation and Information Record, Notice of Defect and Nonconformity, Civil Penalty and Criminal Penalty, and Liability for Defect and Nonconformity in the Code of Federal Regulations. The Toyota recall covered the North America, Europe and China markets and reached its peak in January 2010. In the US, it is estimated that Toyota will recall more than six million cars. Toyota plans to agree to pay a fine at the statutory limit of nearly $16.4 million, the highest fine ever issued by the US government to an automaker. In addition, at least six US insurers are setting about claiming compensation from Toyota. By contrast, the manufacture and sale in the US of defective products by a US subsidiary should, under appropriate circumstances, not expose the foreign parent to liability. Although product liability area is one in which US courts are more prone to hold a parent corporation liable for its subsidiary's actions, various conditions must be met before it will generally do so and the foreign company parent is in a better defensive position than if it had manufactured or sold the goods itself.

2. Internal Links of Business Operation Management

The first is labor and employment. There are a myriad of US federal, state and local laws governing the hiring, employment, treatment, benefits and termination of employment of employees in the United States. In general, these laws apply on a uniform basis to all US businesses, although some do not apply at all or have less stringent requirements in the case of smaller businesses, or as a practical matter have proven irrelevant. For example, there are various laws regarding the formation, recognition and rights of trade unions and their members, but the overall number of union employees has been declining and the existence of unions in certain industries, in particular high technology and service-type businesses, is much less common than in others. Other laws prohibit not hiring employees based on race, gender (including pregnancy), age, religion or national origin, as well as handicapped persons under certain circumstances. Other laws establish minimum wages, maximum number of hours to be worked (generally by non-salaried and certain salaried employees), compensation for injured employees, and payments into unemployment insurance funds for the benefit of employees terminated involuntarily. However, the terms of these laws do not apply to the non-US activities of a foreign company. One federal law of particular potential importance to foreign buyers is the Worker Adjustment and Retraining Notification Act ("WARN"). WARN requires employers with 100 or more full-time employees to provide a 60-day written notice to employees in the event of a "plant" closing or mass layoffs at a single site. Some states have laws based on similar principles, but with lower thresholds. WARN and its state counterparts may be particularly important to foreign companies acquiring a US business if the buyer is planning to relocate significant portions of the acquired business to outside of the United States. Moreover, while WARN does not apply to the conduct of a foreign entity outside of the United States, the regulations under WARN make clear that the parent corporation of an entity engaging in layoffs covered by WARN can be liable for its subsidiary's failure to comply with WARN "depending on the degree of [the subsidiary's] independence from the parent."

The US does not have separate laws regarding sexual harassment. However, the provisions of the Civil Rights Act of 1964 concerning the prohibition of gender discrimination in employment provide a legal basis for taking a legal action against the harasser. In judicial practice, the definition of sexual harassment has been gradually deepened and its application has also been gradually expanded. According to the Policy Guidance on Sexual Harassment adopted by the Equal Employment Opportunity Commission (EEOC) in 1980, "Unwelcome sexual advances, requests for sexual favors, and other verbal or physical conduct of a sexual nature constitute sexual harassment when (1) submission to such conduct is made either explicitly or implicitly a term or condition of an individual's employment, (2) submission to or rejection of such conduct by an individual is used as the basis for employment decisions affecting such individual, or (3) such conduct has the purpose or effect of unreasonably interfering with an individual's work performance or creating an intimidating, hostile, or offensive working environment." In addition, the US has relevant laws requiring large companies to establish anti-sexual harassment rules, covering rule formation, training system, who handles complaints and complaint procedures. In the event of any sexual harassment in the company, the company will hold joint liability since it fails to create a fair and safe environment. Under the EEOC's guidance, an employer is responsible for the acts of non-employees, with respect to sexual harassment of employees in the workplace, where the employer (or its agents or supervisory employees) knows or should have known of the conduct and fails to take immediate and appropriate corrective action. In reviewing these cases, the EEOC will consider the extent of the employer's control and any other legal responsibility that the employer may have with respect to the conduct of such non-employees. In the 1986 case where the management and employees of Mitsubishi's Illinois plant were involved in the sexual harassment of more than 400 female workers, the US District Court ordered Mitsubishi to pay over $34 million to the more than 400 female workers.

The second is intellectual property rights. The US was one of the first countries to establish a system of intellectual property rights and has put in place a complete legal system governing intellectual property rights, including the Patent Act, Trademark Law, Copyright Law and Unfair Competition Act. To fully perform its duties under the World Trade Organization (WTO) Agreement on Trade-Related Aspects of Intellectual Property Rights (TRIPS), the US government enacted the Uruguay Round Agreements Act on December 8, 1994 to revise the existing intellectual property rights laws. The intellectual property rights protection in the US is mainly judicial protection. In law enforcement, the US has established a multi-layer judicial system. The first instance of cases of infringement of copyrights, registered trademarks, patents, plant varieties and IC layout designs is governed by the US federal district courts. Cases concerning intellectual property rights disputes are generally heard by state courts before, if any party has objection to the judgment of a district court, being appealed to the Federal Circuit Court for final judgment. Intellectual property rights cases concerning patent disputes are generally heard by the Federal Circuit Court and appealed to the Supreme Court of Appeal. The Federal Circuit Court was established to reduce conflict of jurisdiction before hearings and make the patent system more stable. In addition to the above cases, the Federal Circuit Court also has jurisdiction over the first instance of cases involving unfair competition and abuse of trade secrets related to the above rights. The state courts generally have jurisdiction over cases involving registered trademarks, infringement of trademarks obtained under the common law, abuse of trade secrets and unfair competition.

On March 7, 2006, the US House of Representatives passed the Stop Counterfeiting in Manufactured Goods Act and Protecting American Goods and Services Act of 2005, which revised the Trademark Counterfeiting Act to include acts of selling counterfeit marks (labels, stickers, packaging, badges, emblems, charms, engravings, cases, boxes, or documentation), expand “trafficking” to imports and exports, and increase the penalty on counterfeiting acts (the counterfeited goods are forfeited, destroyed or otherwise disposed according to the law). Moreover, the court will also order the convicted to compensate the victims for their losses. That is to say, any actual or attempted counterfeiting act constitutes a felony, with the severity of punishment depending on the quantity and value of the counterfeit trademarks involved. In addition, according to the relevant provisions of the Copyright Law, it is a criminal offense to reproduce or distribute more than one copy of copyrighted work with retail value exceeding $1,000 for commercial benefit or personal gain, or within a period of 180 days, thus constituting copyright infringement. The offense can be divided into three classes: base felony (1-3 years of imprisonment), felony with enhancing element (3-5 years of imprisonment) and misdemeanor (less than one year of imprisonment). There are two "thresholds" in convicting the copyright infringer - the quantity reproduced or distributed and the retail value, where the retail value is the retail value of the work that is infringed upon, of which the provisions are different from those applicable to acts of trafficking counterfeit goods or services. In addition, it can be seen from the above provisions that an act may constitute an offense even if it is not for profit-making purposes. The court will order forfeiture, destruction or disposal in other ways of the counterfeit works and the tools and equipment used to make them. It merits mentioning that although a work is copyright-protected as of the date of its creation, the prerequisite for the filing of an infringement lawsuit is that the work in question has been registered at the US Copyright Office.

Furthermore, Chinese enterprises operating in the US must comply with the federal and state laws on taxation; otherwise they will face legal sanctions under the corresponding laws. The US tax jurisdiction is distributed between the federal government and local governments (50 states, District of Columbia and county governments). All US citizens and foreign enterprises and individuals doing business in the US are subject to the US tax laws. Any company's tax obligations depend on its operating activities and the place where it operates. The US has the most complicated and rigorous tax regulations in the world. The taxes are collected by the federal government, state governments and local governments. The federal government mainly collects federal income tax, property taxes and gift taxes. The state governments and local governments mainly collect state income tax, franchise taxes, goods and services taxes, occupancy taxes and property taxes.

Conclusion

Expanding China's direct investments in the US may reduce the trade imbalance between China and the US and the pressure of the USD/RMB exchange rate on China, prevent liquidity risk caused by capital surplus, reduce the shrinking value of China's foreign exchange reserve and promote the deepening of the international division of labor and the adjustment of China's industrial structure. It will also benefit Chinese enterprises in their effort to learn and draw on advanced foreign management experience and technology and further improve their international competitiveness. However, at present, Chinese enterprises have little experience in investing in the US, and academic circles have done very limited research on the legal review environment, political environment and business operation environment in the US.

This research report holds that the passive investment risks arising from the legal review environment in the US are primarily caused by the investors' unfamiliarity with the existing US foreign direct investment system and the lack of understanding of US laws, regulations and implementation mechanisms concerning industry policy restrictions, anti-trust regulation on mergers and acquisitions, information disclosure requirements for listed companies and national security review mechanisms. Likewise, the active investment risks arising from the political environment are mainly the result of the huge political differences between China and the US that make it hard for Chinese investors to truly appreciate the political background embedded in the government decision-making process under the system of checks and balances. In many cases, investments fail because the investors are unable to properly handle their relationships with Congress, the Administration, the public and the media when facing opposition from various fronts.

The business operation environment and related risks are an issue concerning how Chinese enterprises can adapt to US regulations on business operation management after a successful merger or acquisition. While they have handled domestic laws and regulations effectively, Chinese enterprises must realize that the relevant US laws and regulations, especially those governing environmental protection, product quality, labor and employment, and intellectual property rights, and their enforcement, are hugely different, and the penalties for violations are harsher and more stringent. Chinese enterprises investing in the US must attach the utmost importance to this issue, otherwise they risk huge losses resulting from these various potential legal actions. It is hoped that these issues will draw the attention of the academic community and lead to more in-depth studies on the external environment and related risks faced by Chinese enterprises in their investment activities in the US that would ultimately offer insight into how to effectively avoid and tackle the issues involved.

Conclusion

Expanding China's direct investments in the US may not only reduce the trade imbalance between China and the US and the pressure of the USD/RMB exchange rate on China, prevent the liquidity risk caused by capital surplus, reduce the shrinking value of China's foreign exchange reserve and promote the deepening of the international division of labor and the adjustment of China's industrial structure, but also bring benefits to Chinese enterprises in their effort to learn and draw on advanced foreign management experience and technologies and further improve their international competitiveness. However, at present, Chinese enterprises have little experience in investing in the US, and even the academic circle has done very limited research on the legal review environment, political haggling environment and business operation environment in the US.

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