

Chapter 1

Overview of progress and policy challenges

Abstract. *China has made progress in providing a business environment conducive to foreign direct investment (FDI). The challenge now is to move towards a more rules-based policy framework that will attract high-quality FDI from OECD countries. The OECD proposes a number of policy options for the Chinese government to consider in further developing such a framework. These include additional streamlining of the investment project approval process, reconsideration of unnecessary sectoral restrictions on foreign investment, and measures to increase transparency and strengthen the rule of law.*

A. OVERVIEW

China has been highly successful in attracting foreign direct investment (FDI) and significant progress has been made in improving the FDI policy framework. However, there remains an unexploited potential to attract FDI from OECD countries. Continuing efforts need to be made both in bringing laws and regulations into conformity with internationally recognised standards and in ensuring their implementation at local level. Policy options are available to enable China to develop a more rules-based system.

1. China has made significant progress in providing a business environment conducive to FDI

China has made significant progress in providing a business environment conducive to FDI since the major shift to economic reform in 1978, as evidenced in this study. A closed economic system has been rapidly opened to trade and investment. Major economic institutions have been replaced or transformed. Others, like the state-owned enterprises (SOEs) and the financial system, are undergoing lengthy reform that will bear fruit in the future.

FDI has played an important role in China's economic development for nearly a quarter of a century. It has enabled China to establish new branches of industry and Chinese consumers to experience a far wider range of goods and services. It has brought in new technology in many fields. Foreign-invested enterprises (FIEs) have provided employment, much of it embodying training and experience in both technological and managerial skills which are transferable to domestic enterprises. FDI has played a major role in expanding China's international trade, which has developed to half of GDP. FIEs now account for half of China's two-way merchandise trade. They provide employment directly and indirectly to many millions of employees.

At the same time, it is worth bearing in mind that China receives far less FDI per head than many developing as well as developed countries and that much FDI in China still takes the form of short-term, labour-intensive manufacturing, while investment in high-tech activities, particularly in services sectors, lags behind. There is therefore still much scope for raising the quality of FDI as well as continuing to increase its quantity.

2. Following WTO accession, the challenge is to attract high-quality FDI

The challenge now is to attract more long-term, capital-intensive, high-tech, high-value-added projects in more sectors of the economy. China also needs to adopt policy frameworks designed to ensure that spillovers from the foreign corporate presence to the domestic economy are optimised.

China's accession to the WTO has already brought about major advances in FDI policy. In addition to the removal of trade-related investment measures (TRIMs), China is also opening its services sectors, including the financial sector. Existing FIEs may now distribute their products in China and engage in foreign trade. These changes will provide opportunities for OECD members to play a bigger role in making direct investments in China.

Multinational enterprises in OECD countries have the capital and the technology to be able to provide longer-term projects embodying advanced production methods. However, OECD members have between them provided a disproportionately small amount of FDI to China, especially by comparison with their relatively large share of China's merchandise trade.

3. Towards a rules-based FDI attraction strategy

FDI has in the past been attracted to China partly by incentives such as lowered taxes. Such incentives were effective in the early period of reform and opening up in the early 1980s to the extent that they were perceived as compensating in part for the lack of a pre-existing business and infrastructure capable of accommodating foreign investment. They also drew attention to the attraction of China as an investment destination at a time when it was not yet widely perceived as such. It is not clear that such a rich set of incentives is necessary for attracting FDI now that China is now well on the global investment map. As pointed out later in this study, recent surveys show that foreign investors are much more concerned about the overall regulatory regime than about incentives.

Financial incentives for foreign investors can best be reconsidered when this process is part of a broader effort to make the overall national tax system fairer, simpler, more transparent and more conducive to private investment, whether foreign or domestic. Such enhancement may reasonably be rated a greater priority than abolishing fiscal incentives before the deficiencies for which they are perceived as providing some compensation have been rectified.

A recent OECD report on FDI for Development confirms that foreign investors prefer to locate investments – especially large, long-term investments – in countries and territories that have predictable policy regimes. Major changes in policy and legislation require sufficient preparation

and consultation time, and it is highly advisable that foreign investors be given an opportunity to express their views before changes are implemented.

In addition to fiscal incentives, the Chinese government has worked hard to attract FDI by making investment in China more convenient. Measures to accomplish this aim include the reduction of delays in approving FDI projects and the expansion and improvement of the physical infrastructure. These measures enhance the investment environment for FDI and may also benefit domestic enterprises. Such convenience-based attraction measures can be used by local authorities to compete with each other to attract FDI. Such competition is healthy because it improves the overall national business environment without the risk of exhausting fiscal resources.

A sound legal system is a major pillar of the rules-based investment environment that is beginning to take shape in China, where the government has, in a remarkably short period of time, established a wide-ranging body of FDI-related legislation. It is also striving to develop an impartial and effective court system, but, for institutional and manpower reasons, this work will take years, rather than months, to achieve its objective.

Effective implementation of law matters because investors, whether foreign or domestic, need to have guaranteed property rights, including intellectual property rights (IPR). Many countries, including some of China's neighbours, have gone through a stage of copying the products of their competitors. But, as the history of world technology shows, Chinese people are themselves highly inventive when the institutional framework allows them to be so. The sharply rising number of domestic patents is testimony that this is still true. Much stronger implementation of China's IPR protection legislation and its international commitments in this regard is needed, not just to attract FDI but also to stimulate domestic creativity.

Transparency requires the establishment of a legislative and regulatory regime that is stable, internally consistent and publicly available in an understandable form. Coherence between national and local legislation and regulation is required by WTO, OECD and other internationally recognised standards. The existence of internal, undisclosed rules governing investment project approval, for instance, is not compatible with the principle of transparency.

Consultation with the foreign investor community on new FDI-related legislation and regulations does now take place, but it still tends to be selective, so that some major foreign investors who consider themselves to be the key players in a specific sector complain about being left out. In OECD countries, the free climate of discussion and debate facilitates the formulation of new laws by allowing the public, including all interested parties, to raise objections and make suggestions before laws are passed. Waiting until after the laws are

promulgated to find out what are the problems in implementing them complicates the situation by obliging the government to issue, in addition to the original law, sets of implementing regulations and revised laws.

In moving towards a rules-based FDI attraction strategy, there is a concomitant move to competition based on raising standards in areas such as environmental protection and labour management. An important aspect of this change of strategy is a move from lax to strong implementation of environmental standards. A country or locality that does this could deter investment by polluting industries, but will more certainly attract FDI from companies in services sectors and in high-technology manufacturing, because these will be seeking locations capable of attracting and retaining staff who are highly mobile and who do not wish to live in unpleasant environments.

Even where a dominant state-owned enterprise has been partly privatised, there is no guarantee that it will cease to exercise monopoly power not justified by the nature of the market concerned. Competition policy needs to be strengthened to make it easier for new companies, whether domestic or foreign-invested, to enter the market. Competition policy is particularly important as state-owned enterprise reform reaches a new stage in which foreign corporations play an increasing role in privatisations, allowing them to contribute positively to industrial restructuring that will greatly increase industrial productivity.

The increasing part played by mergers and acquisitions in FDI will necessitate more effective prudential regulation of China's capital markets and a visible improvement in the general standard of corporate governance. Bank reform will also have to be completed if the financial system is to be strong enough to fulfil its function in this process.

4. Improving the operating environment for FDI will benefit domestic enterprises

The experience of OECD countries is that a regulatory environment that is conducive to competition and in which foreign-owned enterprises are generally treated no differently from domestically-owned enterprises provides the best basis for the development of home-grown enterprises. China's own experience is also instructive in this regard. The enabling environment established for foreign business in the Special Economic Zones (SEZs) and other open areas has proved fruitful for the emergence of thriving domestic private enterprises, which represent a larger share of output there than in hinterland provinces. Most of the cases heard by the IPR courts, which were established partly in order to respond to problems faced by foreign investors, have been brought by domestic plaintiffs. Those industrial sectors that have been opened wide to FDI are already characterised by more

successful domestic firms, while protected sectors have generally remained dominated by state monopolies that are often inefficient and provide customer service that is not always satisfactory. Fears that liberalisation of these sectors would lead to domination by FIEs are largely unfounded, provided such liberalisation is accompanied by the development of vigorous anti-monopoly and competition legislation applied in non-discriminatory fashion to both domestic and foreign firms. Improving consistency will require improved co-ordination and strengthening of administrative structures which will benefit public governance. Steps in this direction could include:

- The appointment of a single agency, for example MOFCOM, to play a co-ordinating role in developing China's FDI policy, including co-operation with the OECD.
- The establishment of an inter-ministerial group to examine, develop and implement FDI policies.

B. POLICY OPTIONS

1. Consolidating gains from WTO accession

The commitments that China entered into when it acceded to the WTO represent a major step forward in the liberalisation of its investment regime, in particular in relation to trade-related investment measures (TRIMs) and intellectual property rights (IPRs) covered by WTO requirements. A major effort is being made to fulfil these commitments, supported by other WTO members.

Local protectionism

While there is no doubt that the central government is determined to live up to these expectations arising from WTO accession, it appears that protectionist opposition survives at local, enterprise and, in some instances, ministerial level. Local authorities are prohibited from engaging in local protectionism, according to a government regulation adopted in April 2001, but it is not yet clear to what extent this prohibition has been effective. To ensure that foreign investors and other observers understand that all possible efforts are being made to ensure compliance with WTO obligations relating to FDI at local level, steps to be taken by the Chinese authorities could include:

- Preparing an annual report on local compliance with regard to investment-related commitments, listing the problems that have been encountered and the measures taken to deal with them.
- Ensuring that the Provisions on Guiding Foreign Investment Direction remain in conformity with agreed practices relating to performance requirements, including Article 10 on export sales requirements.

Transparency and regulations governing the approval process

The existence of internal (*neibu*) regulations governing the process by which FDI projects are approved alongside public (*gongkai*) regulations is not transparent. It is reported that some local *neibu* regulations persist, and that they are generally more restrictive than national legislation and regulations. The existence of unpublished regulations permits the existence of rules that would not be acceptable if they were published. However, unless such unpublished regulations are made public, it is not possible to judge whether or not they are acceptable.

The Chinese government is already familiar with this problem and is committed to solving it following WTO accession. The rational solution involves a two-step procedure:

- It may be considered advisable that all local-level *neibu* rules and regulations should be disclosed, that is, converted to *gongkai* rules and regulations, initially by the local authorities that administer them to MOFCOM at national level, then by MOFCOM to the public, including foreign investors, along with any *neibu* rules still operating at national level.
- After full disclosure, it may be considered advisable that such rules, where they are inconsistent with national law or with other regulations or are in breach of China's international obligations, be abolished. Otherwise, if they are considered worthy of retention and are both compliant with China's international obligations and consistent with domestic legislation, they may be incorporated into existing *gongkai* regulations or promulgated separately.

2. Other measures for attracting and maximising the benefits of FDI

China's existing international commitments are a milestone on the road to liberalisation, not full liberalisation itself. In moving towards a fully rules-based FDI attraction regime further investment liberalisation measures could enhance the operating environment for FDI.

Further liberalisation of the approval process

Streamlining the approval process

The approval process could be amended to obviate unnecessary delays and obstacles in the approval process. Possible solutions may include:

- Raising the FDI project value limit above which approval has to be submitted to central government departments at national level and increasing the approval powers of local governments accordingly.
- Reclassifying projects from restricted to permitted or from permitted to encouraged, as appropriate, in accordance with a set timetable, to ensure

that they are submitted for approval at local, not national, level. (Unless and until the catalogues for guidance of foreign investment industries are replaced by an alternative guidance framework, as recommended below.)

- Reducing the number of steps in the approval process by merging and elimination to produce a genuine “one-stop shop” procedure.
- Fast-tracking the national-level approval process by allocating more resources, including staff, to it and reorganising the process to make it more efficient.
- Providing an acceptable time limit for approval or non-approval of a project by the examining and approving authority or authorities.
- Eventually introducing automatic approval within a reasonable time limit for all projects meeting the published approval criteria in full.

Separating FDI approval from other operations

It is inappropriate to maintain the FDI project approval process as part of administrative procedures that are the legacy of a central Reform system that has long ago fallen into disuse.

The separation could be made clearer by:

- Separating FDI approval by the State Development and Reform Commission (SDRC) from the SDRC’s function of approving investment plans by domestic state-owned enterprises (SOEs).

It is confusing and inappropriate for authorities concerned with FDI approval to be also engaged in local FDI promotion/attraction activities. Although specialised bodies have been set up for FDI promotion in many localities, in others the activities are still located in the same body.

Remaining confusion could be obviated by:

- Establishing separate bodies for FDI approval and FDI promotion at all levels where this has not already been done.

Regional incentives

To the extent that the investment incentives available to FIEs are the same as those on offer to domestic enterprises, the policy of attracting capital investment to the Western and Central regions is consistent with the principle of national treatment. However, such incentives do not constitute a sufficient condition for increased investment in those regions. If the Chinese government wishes to redirect investment westward, it may prefer to put the main emphasis on improvements in the business environment there.

The current policy of allocating state funds to infrastructure construction in the Western and Central regions is already an important part of this effort.

Institutional development is also necessary. Steps to ensure such development could include:

- Raising the standard of investment promotion and investment approval in these regions to that prevailing in the open coastal zones, where the authorities are generally much more flexible in their interpretation of FDI laws and regulations.
- Organising visits by officials in the Western and Central regions to their counterparts in SEZs and other open zones in the Eastern Region to share experience and gain a deeper understanding of procedures that have been successful in attracting investment.

Such measures would be relatively cost-effective and would retain their relevance even if the “invest in the West” policy were to be modified.

Reconsidering remaining ownership restrictions

As detailed in Chapter 3 of this study, market-access commitments in both industrial and services sectors already allow full foreign ownership of individual enterprises in a range of sectors within a reasonable time frame varying in most cases from 3 to 5 years (in reinsurance, wholly foreign-owned enterprises were allowed on accession, management consultancies will only be permitted wholly foreign ownership after 6 years). But not all sectors will be so fully opened up. There will still be restrictions within sectors that are scheduled for greater market access.

In view of the positive experience to date of sectors that have been opened to 100 per cent foreign ownership, the next steps in opening up could include:

- Publishing a consolidated list of all foreign ownership restrictions in all sectors.
- Explaining the reasons for each of these ownership restrictions.
- Progressively removing remaining foreign ownership restrictions.
- Phasing in full foreign ownership in the remaining sectors over a period similar to that prevailing in other sectors under existing commitments where no such case can plausibly be made.

The catalogues for guiding foreign investment

Following China’s accession to the WTO, three revised catalogues for guiding foreign investment (respectively: encouraged, restricted and prohibited) took effect in April 2002. These catalogues represent a major step forward in FDI regime liberalisation. The Chinese authorities are to be commended for this step and encouraged in their efforts to achieve further liberalisation by removing more categories of project from the catalogue of

prohibited foreign investment industries. The inclusion of sectors where national control is considered desirable, such as projects that endanger the safety and performance of military facilities, is understandable; where not self-evident, an explanation of the reasoning involved would be helpful.

It is not clear that there is any benefit in maintaining an extensive catalogue of restricted industries that effectively raises the approval hurdle higher for a wide range of industries and services, including, it is important to note, most of the services sectors that are being opened as a result of WTO accession. The existence of the restricted catalogue necessitates the reference of a project approval decision to a national authority (usually the State Development and Reform Commission, SDRC). The national authority then decides on approval on the basis of criteria regarding national economic policy or other considerations which are opaque because they are not precisely specified in such a way that a foreign investor can make a reasonable effort to comply with them.

- Abolition of the restricted catalogue in its entirety could be considered, at a time when the Chinese authorities judge further opening to foreign investment to be appropriate to the stage of development of the Chinese economy, as part of the next phase of liberalising the FDI catalogue regime.

Unlike the other two published catalogues, the encouraged catalogue does not restrict FDI in any way. The future of this catalogue will be largely determined by the Chinese government's policy regarding FDI-attracting incentives.

One reason for questioning the need for the continued existence of the encouraged catalogue is the increasing length and complexity that has resulted from successive liberalisations and that will undoubtedly be exacerbated by further liberalisation. The list is now so detailed that many of the items are likely to become rapidly obsolete as a result of technological progress.

The so-called "catalogue" of permitted investment projects – far larger in practice than the other three – is not published, but consists of all projects not listed in the three published FDI guidance catalogues.

A clearer presentation of the permitted range of foreign investment activities could be achieved by:

- Replacing the catalogue regime with a single short list of sectors that are barred to foreign participation, supplemented by a clear explanation of the grounds for selection. All projects not on the list would then be permitted.

As a transitional step towards wholesale reform of the catalogues, it would be good practice to reconsider the prohibition of foreign investment where the intention of controlling specific activities may be more effectively achieved in

other ways, such as prudential regulation. The result would be the publication of a smaller prohibited catalogue containing only items which it is international practice to restrict or which China has a special and understandable reason for restricting.

China currently prohibits FDI in a few traditional crafts such as the production of green tea, traditional Chinese medicines, bodiless lacquer ware, rice paper and ink tablets. The intention of this prohibition is presumably to ensure the continued existence of these activities because they are considered to be part of the national heritage. If this is the case, then the prohibition of inward financial flows supporting such activities would appear to be an inappropriate means of achieving such an aim, which might more effectively be pursued by other measures, for example by increasing the resources available for education and training in these fields.

Another category of prohibited FDI is in the establishment of futures companies. There appears to be no advantage to be gained from banning FDI from entering this financial sector that could not be more effectively obtained by imposing appropriate prudential regulation covering both domestic and foreign-owned enterprises.

PBC licensing criteria for foreign banks

China has committed itself to a major opening of the banking sector to foreign participation (see Chapter 1 of this study). However, the resulting regulations promulgated by the People's Bank of China (PBC) in February 2002 require such high capital requirements for setting up branches in China that only the largest foreign banks will be able to take advantage of the new market access opportunities. While the requirements for opening a representative office are relatively modest, those for establishment are much more strict: the parent bank must have US\$20 billion in total assets to open a branch and US\$10 billion to open a subsidiary. There are six levels of bank offices, with corresponding minima for operating funds in the case of branches and capital in the case of subsidiaries, in each case varying from Rmb 100 million to Rmb 600 million, or foreign currency equivalent. Considering that the regulations also include reasonable stipulations requiring foreign banks to be governed by adequate supervisory systems in their home countries and to possess adequate internal control systems, such high capital requirements appear disproportionate to guarantee stability and are interpreted by some representatives of foreign banking institutions as protectionism.

According to the Code of Liberalisation of Current Invisible Operations agreed by OECD countries, the total amount of any financial requirements imposed for the establishment of a branch or agency of a non-resident enterprise engaged in banking or financial services shall be no more than that

required of a domestic enterprise to engage in similar activities. Furthermore, the total of the financial requirements to be furnished by all the branches and agencies of the same non-resident enterprise shall be no more than that required of a domestic enterprise to engage in similar activities. The minimum capital requirements in the foregoing paragraph apply only to foreign, not domestic, banks. Assessing the extent to which this might be considered as discriminating against the establishment of foreign banks in China is complicated by the lack of a firm basis for comparison, since there are no private banks in China and state-owned domestic banks are the subject of a different set of regulations.

Greater opening of the banking sector to foreign participation could be achieved by:

- Lowering the capital requirements for branches and subsidiaries of overseas banks to less discouraging levels, in accordance with OECD and other internationally recognised standards.

Capital market opening

Portfolio FDI inflows are restricted by the largely closed nature of China's capital markets. At the same time, the expansion of FIEs is limited by restrictions on capital-raising measures such as corporate bond issuance. Steps towards allowing portfolio inflows to play a more effective role in enhancing inward FDI would include:

- Allowing more FIEs to list on domestic stock markets.
- Allowing FIEs to issue corporate bonds on the Chinese market.

3. Transparency-enhancing measures

Web sites dealing with FDI issues in China

Governments are increasingly using the World Wide Web to communicate information to their citizens and those of other countries, and also as a transparent, cost-effective, efficient and speedy method of supplying government services. All OECD member countries are taking steps to implement e-government initiatives at national, regional and local levels. China has itself made great progress in establishing web sites for government departments which in many cases are readable in English as well as Chinese (see list at the end of the Bibliography section). The quality of official web sites varies widely. Some are user-friendly, easily navigable, rich in content and frequently updated; others bear the hallmarks of neglect, with obsolete and irrelevant content, dead links, navigation problems and no pages in non-Chinese languages.

Those sites that deal with issues of interest to foreign investors have until recently displayed a similar quality variability (although the best of them are

actually much better than those of most other developing – and some developed – countries) and in addition have often suffered from excessive dispersion. Many localities have web sites that have selective content. There were until 2003 several national-level sites, with no clear indication for the uninitiated as to which was predominant. One of the best sites is actually a local one (Shanghai Foreign Investment Service Centre), which presents the most important information in English and is easy to navigate. However, this site may not be easy to find if the user is seeking a national information source. There has therefore not hitherto been a single easy or reliable method of finding an authoritative source of information on China's FDI policies, laws and application procedures on the World Wide Web.

This problem is one that is relatively easy to remedy. Doing so will constitute a step towards greater transparency of the FDI policy and legislative framework and will also provide a model for any other government departments that may eventually be required to comply with e-government standards.

- The OECD welcomes the inauguration of MOFCOM's FDI-related web site, Invest in China, www.fdi.gov.cn, on 1 January 2003 and offers its assistance in helping to ensure that the site is up to date, contains appropriate content in both Chinese and English, and is easily navigable.

Transparency of taxation legislation and regulations

It would be good practice to ensure that

- Authoritative versions of all tax regulations promulgated by the Ministry of Finance (MoF) and the State Administration of Taxation (SAT) relating to a foreign investment project, including all implementing rules, local rules and regionally-specific incentives, be made available on a regularly updated basis in English to foreign investors and members of the public requesting them. This may be done in print (for example, by upgrading the existing the SAT's journal of taxation) or on a web site, or (preferably) both.

Competition policy

Competition policy could be further enhanced by combining and developing the various fragmentary and dispersed policy initiatives of different ministries and departments into a coherent policy that provides a sound, transparent and non-discriminatory framework for competition.

This policy may well be made concrete in specific laws, formulated in a transparent manner to ensure consultation of all stakeholders, including foreign investors.

Transparency of labour compensation rules

The obligations of FIEs towards their employees in regard to the payment of social benefits remains inconsistent and unclear. This situation could be remedied by:

- Developing and implementing a consistent national body of regulations governing the entitlement of employees to social and pension benefits and clearly specifying the contributions to be made by employers to such benefits.
- Establishing mechanisms whereby both employers and employees can ascertain their individual pension and other entitlements in a fully transparent manner.

Accuracy and international comparability of China's FDI statistics

Accurate and internationally comparable FDI statistics constitute an important component of the transparency of a country's FDI policy framework, providing a realistic basis on which to judge the requirements for, and the success of, such a framework.

As explained in Annex I, current methods of compiling China's FDI statistics are inconsistent with international practice and in particular with those in use in OECD countries. The result is that there is a lack of clarity and occasional confusion regarding such statistics as the geographical distribution of investment sources and the existing stock of FDI. The continuation of co-operation between the Chinese government and the OECD to standardise and improve FDI statistics will contribute to greater transparency and a better understanding of actual trends in China's FDI inflows and outflows. This work is consistent with the statistical transparency commitments inherent in China's April 2002 participation in the IMF's General Data Dissemination System (GDDS).

Steps to improve transparency with regard to FDI statistics could include:

- Aligning the Chinese government's concepts, definitions and data collection with OECD and IMF recommended standards.
- Announcing the dates for regular public release of a set of FDI statistics revised in line with standards agreed with the OECD.
- Where the relevant data are available, revising back series of FDI statistics and publishing these in the same tables as statistics for the most recent year to allow comparisons over time using the latest available data.

4. Rule of law

Judicial independence and competence

Current efforts to improve the functioning and independence of the legal system could be intensified by:

- Training and appointing legally-qualified judges to all courts.
- Raising the pay of judges and other key legal personnel to reduce their vulnerability to offers of bribery.
- Enhancing the status of judges *vis-à-vis* local government and party officials.
- Establishing at national and regional level mechanisms to guarantee the execution of court judgments.

An accountable and transparent legislative process

Current efforts to establish a more transparent and accountable process of formulating legislation and regulations could be expanded to include:

- Publishing all legislation and regulations on a single, comprehensive, up-to-date and easily-navigable web site in both Chinese and English.
- Exploring the possibility of establishing a mechanism similar to that of the US Federal Register or equivalent systems in other OECD countries to publish draft laws and regulations and obtain public feedback on them as early as possible before promulgation.
- Increasing the scope of stakeholder consultation with regard to FDI-related legislation.
 - ❖ As a first step in this direction, a study might well be undertaken of existing forms of consultation with the intention of designing a more consistent and comprehensive method of organising such consultation involving all major players in an industry in both public and closed fora.
 - ❖ A full consultative process would in addition include an open public debate on proposed legislation, using all print and electronic media. Such a process has already been adopted in non-economic legislation (*e.g.* the new marriage law). This would be particularly helpful in the case of complex legislation on which maximum public discussion would help elucidate the main issues and facilitate the examination and evaluation of a wide variety of options. Such a procedure might be adopted on a trial basis in the case of proposed business legislation, such as that on mergers and acquisitions.

IPR protection

China has made progress in protecting intellectual property rights (IPR), but this remains an area in which multinational enterprises from OECD

countries still have serious concerns. Addressing IPR issues more effectively will enable China to attract more long-term investment, especially in high-tech areas where technology transfer is more likely to occur in an environment in which IPRs are well protected. It will also encourage domestic creativity.

Further measures to improve IPR protection could include:

- Continuing to educate citizens in the principles of IPR protection and its value for the promotion of discovery and invention in the modern world.
- Allowing all holders of copyright, patent rights and trademark rights, both foreign and domestic, to seek enforcement of those rights.
- Establishing minimum penalties for all categories of IPR violation.
- Providing means of sharing experience of best practice in IPR courts nationwide to enable upgrading of courts in hinterland areas to the advanced standards that have already been set in major cities such as Beijing.
- Establishing an effective mechanism to implement existing copyright law, in particular to detect, punish and deter software piracy on the part of manufacturers, wholesalers, retailers, the general public and other end-users, including both businesses and government departments.
- Closing down wholesale markets in which counterfeit goods are predominant.

Corruption

China has made some progress in tackling corruption and has also made a positive contribution to the ADB-OECD Anti-Corruption Initiative for Asia-Pacific. Further progress will be greatly enhanced by implementing the recommendations of this report regarding increased transparency and rule of law, in particular reducing regulatory ambiguity and the scope of official discretion, and raising the pay of state officials.

Further progress will also be supported by deepening the co-operation between China and the OECD in dealing with corruption issues.