



September 16, 2011

China's Regulations on Implementation of the Security Review System for Mergers and Acquisitions of Domestic Enterprises by Foreign Investors Issued

Subsequent to *the Notice regarding the Establishment of the Security Review System for Mergers and Acquisitions of Domestic Enterprises by Foreign Investors* (“**Notice**”) issued by the General Office of the State Council on February 3, 2010 and *the Interim Regulations regarding the Implementation of the Security Review System for Mergers and Acquisitions of Domestic Enterprises* (“**Interim Regulations**”) issued by the Ministry of Commerce (“MOFCOM”) on March 4, 2010, the MOFCOM issued *the Regulations regarding the Implementation of the Security Review System for Mergers and Acquisitions of Domestic Enterprises by Foreign Investors* (“**Regulations**”) on August 25, 2011, which have taken effect and superseded the Interim Regulations as of September 1, 2011.

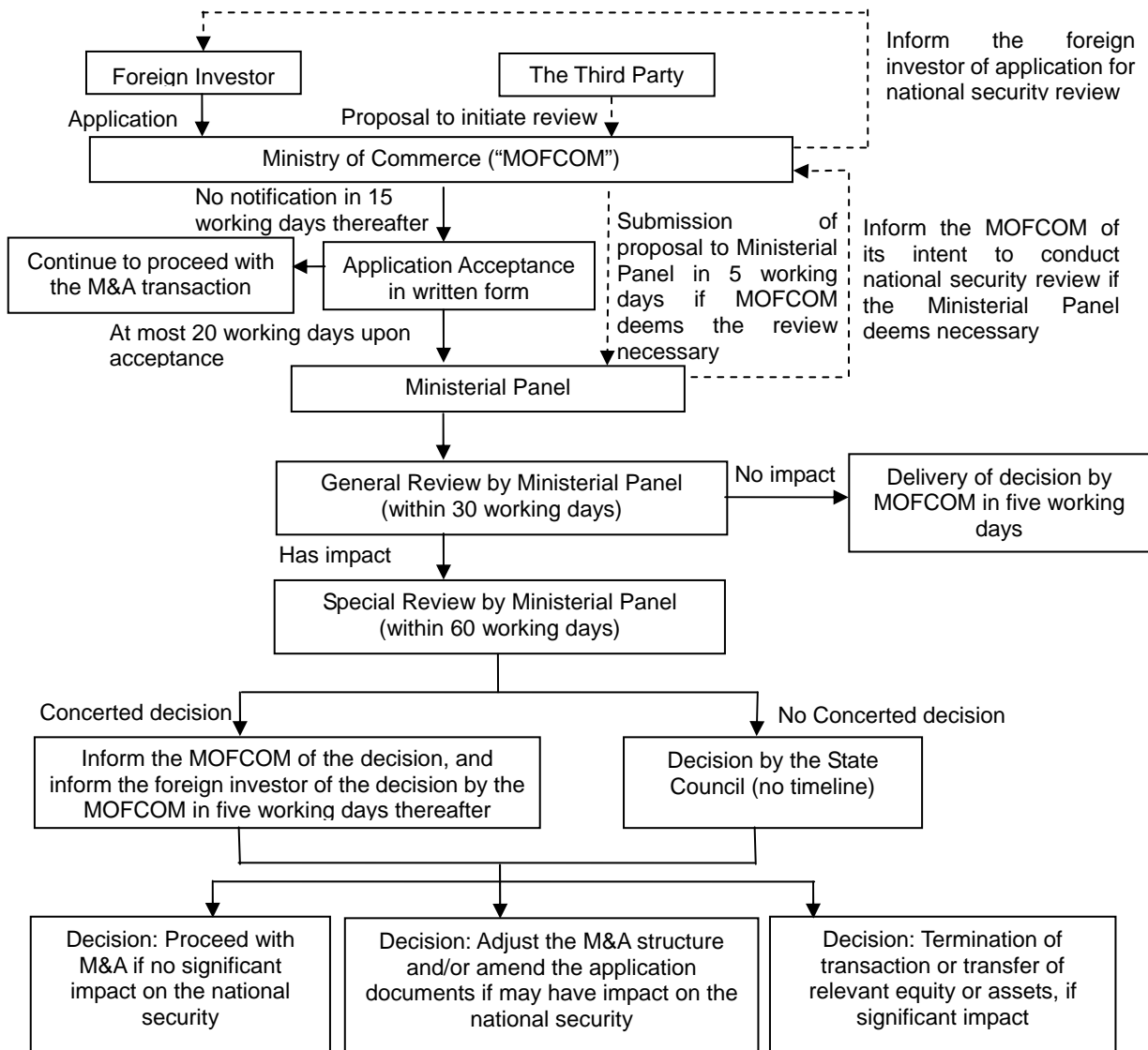
The Regulations highlight and specify the following issues:

1. Inbound investments made by a foreign-invested enterprise is subject to the national security review;
2. Failure to initiate the national security review application where applicable would result in the suspension of review and approval of the merger and acquisition (“**M&A**”) transaction by the local MOFCOM, which in turn shall report the situation to the central MOFCOM;
3. The Regulations explicitly state that foreign investors may not substantively circumvent the M&A security review by means including, but not limited to, nominee shareholders, trust, multi-level reinvestment, leases, loans, variable interest entities (“**VIE**”), or overseas transactions;
4. The consultation before national security review application is not compulsory. An applicant may directly initiate the national security review application without prior consultation with the MOFCOM.

With respect to the national security review procedures and the required application documents, the Regulations follow the provisions as prescribed by the Interim Regulations (for details, please refer to the *MOFCOM Released Interim Provisions on the Implementation of the Security Review System for Mergers and Acquisitions of Domestic Enterprises by Foreign Investors* published in the third edition of Han Kun Newsletter in 2011).

Although this is not the first time that VIE structures be subject to regulations issued by China's regulatory authorities, due to prior discussions over VIE structures raised by the issuance of the first batch of third-party payment licenses, inclusion by the Regulations of VIE structures into the scope of the national security review still draws great attention. However, it is worth noting that the purpose of the Regulations is to regulate national security review, not VIE structures. Theoretically, not all VIE structures are subject to the national security review; only those VIE structures which fall under the scope of the national security review are needed to be reported to the central MOFCOM for a review. Nevertheless, considering the ambiguity of the national security review scope as prescribed in the Notice, which industry being under the scope of the national security review remains unclear. Therefore, we would keep a close eye on the attitude and practice of the MOFCOM to see under which circumstances and industrial sectors VIE structures would trigger the national security review.

Below please find a chart illustrating procedures of the national security review.



Important Announcement

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If you have any questions regarding this publication, please contact or any of the following Han Kun lawyers:

Contact Us



Beijing Office

Tel.: +86-10-8525 5500
Suite 906, Office Tower C1, Oriental Plaza
NO. 1 East Chang An Ave.
Beijing 100738, P. R. China

Estella CHEN Attorney-at-law

Tel.: +86-10-8525 5541
Email: estella.chen@hankunlaw.com

Shanghai Office

Tel.: +86-21-6080 0919
Suite 5709, Tower 1, Plaza 66, 1266 Nanjing
West Road,
Shanghai 200040, P. R. China

Anita SUN Attorney-at-law

Tel.: +86-21-6080 0907
Email: anita.sun@hankunlaw.com

Shenzhen Office

Tel.: +86-755-3680 6500
Suite 4709, Excellence Times Plaza, 4068
Yitian Road, Futian District,
Shenzhen 518048, P. R. China

Jason WANG Attorney-at-law

Tel.: +86-755-3680 6518
Email: jason.wang@hankunlaw.com