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Legal Updates

1. Highlights of the 2022 Amendment to the Provisions on Administration of Foreign-invested Telecommunications Enterprises
2. Overseas IPOs: Key Issues in the Draft Archives Rules

1. Highlights of the 2022 Amendment to the Provisions on Administration of Foreign-invested Telecommunications Enterprises

Author: Group II of Transaction Division

On April 7, 2022, the State Council announced its *Decision on Amending and Annulling Certain Administrative Regulations* (State Council Decree No. 752; the "**Decision**"), which will take effect on May 1, 2022. The Decision primarily aims to promote the separation of operating permits and business licenses, to deepen reforms of "streamlining administration, delegating powers, improving regulation, and strengthening services", and to stimulate the development vitality of market players. The Decision amends 14 and annuls 6 regulations, of which the first item is the third amendment of the *Provisions on Administration of Foreign-invested Telecommunications Enterprises* (the "**Foreign-funded Telecom Provisions**"; and such third-amended version shall be hereinafter called the "**Foreign-funded Telecom Provisions 2022**").

Promulgated on December 11, 2001, the Foreign-funded Telecom Provisions were first amended on September 10, 2008 by the State Council's *Decision on Amending the Provisions on Administration of Foreign-invested Telecommunications Enterprises* (State Council Decree No. 534), which mainly changed department names to conform to the State Council's institutional reform. The State Council promulgated a second amendment to the Foreign-funded Telecom Provisions on February 6, 2016 (the "**Foreign-funded Telecom Provisions 2016**") via its *Decision on Amending Certain Administrative Regulations* (State Council Decree No. 666). The second amendment sought to implement the "issuing business license before operating permit" reform, placing in Article 16 the application for a telecom operating permit no longer a prerequisite to applying for a business license. The third amendment was promulgated on April 7, 2022, making breakthroughs in many respects compared to the current 2016 version. For example, the Foreign-funded Telecom Provisions 2022 conform to the current *Foreign Investment Law of the People's Republic of China* ("**Foreign Investment Law**"), specify an exception where the shareholding limits on foreign investors can be exceeded, relax requirements on foreign investors of having a good track record and operational experience, and simplify the telecom operating permit application procedures and shorten the statutory time limits on review and approval of applications. This commentary gives a summary analysis of relevant changes found in the Foreign-funded Telecom Provisions 2022 and is for reference only. For a comparison between the Foreign-funded Telecom Provisions 2022 and the Foreign-funded Telecom Provisions 2016, please see our commentary dated April 9, 2022.

Comprehensive conformity with the Foreign Investment Law

Compared to the Foreign-funded Telecom Provisions 2016, the 2022 amendment modifies the definition of a foreign-invested telecommunications enterprise to conform to the Foreign Investment Law and removes contents related to the Approval Certificate for Foreign-invested Enterprises, etc. that became obsolete since the Foreign Investment Law entered into force.

On January 1, 2020, the Foreign Investment Law and the *Regulations for the Implementation of the Foreign*

Investment Law of the People's Republic of China (collectively, the "**New Foreign Investment Rules**") officially came into force, which simultaneously repealed the *Law of the People's Republic of China on Joint Ventures with Chinese and Foreign Investment*, the *Law of the People's Republic of China on Foreign-Capital Enterprises*, and the *Law of the People's Republic of China on Chinese-Foreign Contractual Joint Ventures* (collectively, the "**Old Foreign Investment Laws**").

Pursuant to the Foreign Investment Law, a foreign-invested/foreign-funded enterprise refers to an enterprise established under PRC law within mainland China and with all or part of its investment from foreign investors. The organizational form, institutional framework, and operating principles of foreign-invested enterprises are regulated by the *Company Law of the People's Republic of China* and the *Law of the People's Republic of China on Partnership Enterprises*, among others. Accordingly, in Article 2 of the Foreign-funded Telecom Provisions 2022, where a foreign-invested telecommunications enterprise is defined, expressions are removed such as "with Chinese investors", "in the form of a joint venture with Chinese and foreign investment", and "jointly invest", and a foreign-invested telecommunications enterprise is defined as "an enterprise lawfully established by foreign investors within the territory of the People's Republic of China to operate telecommunications businesses." These changes are made to conform the Foreign-funded Telecom Provisions 2022 to its enabling law, and to ensure that both foreign-funded telecom enterprises incorporated under the Old Foreign Investment Laws (i.e., those undergoing the five-year transitional period) and those established under the Foreign Investment Law fall under the umbrella of the Foreign-funded Telecom Provisions 2022.

The Foreign-funded Telecom Provisions 2022 also remove contents related to the Approval Certificate for Foreign-invested Enterprises, in conformity with the Foreign Investment Law, which abolished case-by-case review and approval of foreign investment. These changes achieve comprehensive conformity between the Foreign-funded Telecom Provisions 2022 and the New Foreign Investment Rules.

Exception specified for foreign ownership restrictions on telecom business

The Foreign-funded Telecom Provisions 2022 retain the 49% and 50% mandatory limits set forth in the ratio of capital contributions from foreign investors of telecom enterprises operating basic telecommunications services and value-added telecommunications services, but conclude with the exception "unless otherwise prescribed by the State".

The above change echoes existing national and local regulations to further relax restrictions on the proportion of foreign ownership in the telecommunications field. For example:

- On January 6, 2014, the Ministry of Industry and Information Technology ("**MIIT**") and the Shanghai Municipal People's Government jointly issued the *Opinions on Further Opening up Value-added Telecommunications Business to Foreign Investments in the China (Shanghai) Pilot Free Trade Zone* (MIIT Lian Tong [2013] No. 410), whereby the foreign investment ratio of certain types of value-added telecommunications business in the China (Shanghai) Pilot Free Trade Zone ("**Shanghai Pilot FTZ**") is allowed to exceed 50% on a pilot basis.
- On June 19, 2015, the MIIT issued the *Circular on Lifting Restrictions on the Proportion of Foreign Equity in Online Data Processing and Transaction Processing Business (For-profit E-commerce)*

(MIIT Tong [2015] No. 196), a decision to lift nationally restrictions on the proportion of foreign equity in online data processing and transaction processing businesses (for-profit e-commerce), starting from pilot practice in the Shanghai Pilot FTZ, with the maximum ratio being 100%. When applying for an online data processing and transaction processing operating (for-profit e-commerce) permit, the foreign equity proportion requirement imposed on foreign-invested enterprises is in accordance with the circular and other requirements and corresponding approval procedures are subject to the then-effective Foreign-funded Telecom Provisions.

- On June 30, 2016, the MIIT issued the *Notice on Issues Relating to Hong Kong and Macao Service Providers Engaging in Telecommunications Business in Mainland China* (MIIT Tong Xin [2016] No. 222), allowing Hong Kong and Macao service providers to set up joint ventures or wholly-owned enterprises in mainland China to provide six types of value-added telecom services, including online data processing and transactions handling (restricted to for-profit e-commerce), domestic multi-party communication services, and storage-and-forward services, with no limitation on the proportion of Hong Kong and Macao investment.
- In addition, according to the *Special Administrative Measures (Negative List) for the Access of Foreign Investment in Pilot Free Trade Zones (2021)* (Decree of the National Development and Reform Commission and the Ministry of Commerce, No. 48), effective January 1, 2022, with respect to telecommunications companies, the pilot policy schemes for the initial areas of the Shanghai Pilot FTZ (11.1 square miles) have been implemented in all parts of the pilot free trade zone, and e-commerce, domestic multi-party communications, storage-and-forward, and call center services are exempt from the 50% foreign share restriction on value-added telecom services.

Apart from the above regulations, the Hainan Free Trade Port and other areas have also introduced policies to ease foreign share restrictions in specific telecommunications fields. These policies and changes create ample space for continuous stimulation of foreign investment vitality in the telecommunications field and enhance its level of opening-up.

Foreign investors no longer required to have a good track record and operational experience in telecoms business

According to the Foreign-funded Telecom Provisions 2016, the principal foreign investors of foreign-funded telecom enterprises operating basic and value-added telecom businesses should have "a good track record and operational experience" in their corresponding telecom businesses. The Foreign Telecom Provisions 2022 remove this requirement for the principal foreign investors of foreign-funded enterprises operating value-added telecom businesses, which offers substantial qualification relief to foreign investors in this category. However, while the 2022 amendment lifts this requirement for the principal foreign investors of foreign-funded basic telecom business operators, the removal will have limited substantive effect, given that the Foreign Telecom Provisions 2022 still require foreign investors to obtain a basic telecom operating permit in their country or region of registration. Therefore, the following analysis mainly focuses on principal foreign investors of foreign-funded telecom enterprises operating value-added telecom services.

The MIIT states in the form-filling guidance notes under its current Service Guidelines for Reviewing and Approving Telecom Operating Permit Applications that, to prove telecom business experience, a principal foreign investor should give written details of its (or its first-tier parent/subsidiary's) earlier provision of value-added telecom services, accompanied by documentary evidence; the foreign investor (or its first-tier parent/subsidiary) should also provide written description and screenshots/relevant documents if it has acquired any permit, filing-record, or experience in operating any well-known website or apps prior to making the application. Since there are no further rules to clarify the foregoing requirements, a foreign-invested applicant for a value-added telecom operating permit normally needs to communicate its specific situation with the regulator, who then decides at its discretion whether the principal foreign investor can be deemed as "having a good track record and operational experience in operating value-added telecom business", which lays a certain level of uncertainty on this issue. Moreover, many foreign-funded telecom business operators only have foreign investors who purely engage in financial investments and have no experience in operating non-financial, substantive businesses, let alone any track record or past in value-added telecom business. As a result, in practice, such enterprises are quite likely to fail the test for obtaining a value-added telecom operating permit under the Foreign-funded Telecom Provisions 2016.

The Foreign-funded Telecom Provisions 2022 no longer require principal foreign investors to have "a good track record and experience in operating value-added telecom business", making it easier for foreign-invested enterprises to apply for a value-added telecom operating permit and allowing those enterprises more predictability in being granted the permit. This is materially favorable news for foreign-invested enterprises engaging in value-added telecom business, and for foreign institutions choosing to invest in value-added telecom business operation in China.

In particular, the relaxation of approval requirements may affect enterprises seeking a listing in Hong Kong through a variable interest entity, or VIE structure, in terms of the reasonableness of their use of a VIE structure to avoid foreign ownership limits on the basis that a joint venture "can hardly satisfy the requirement that foreign investors have a good track record and operational experience in value-added telecom business". The Stock Exchange of Hong Kong ("**HKEX**") currently adopts the "narrowly tailored" principle for issuers applying for an IPO in Hong Kong under a VIE structure. Specifically, the VIE structure may be used to address limits on foreign ownership only if the relevant operating entity engages in activities that involve foreign investment restrictions. The issuer must otherwise directly hold the maximum permitted interest in the relevant operating entity. Given that, in practice, applicant issuers and their agent teams normally, through statutory analysis, regulatory interviews and other means, justify their VIE structure (with a wholly PRC-invested operating entity) under the "narrowly tailored" principle by demonstrating that, in reality, a Sino-foreign joint venture can rarely obtain a value-added telecom operating permit. However, after the Foreign-funded Telecom Provisions 2022 come into force, it will be difficult for an issuer to argue from a statutory perspective that a Sino-foreign structure cannot satisfy the granting conditions of relevant permits; furthermore, it may be unlikely for issuers seeking an IPO in Hong Kong to demonstrate extreme practical difficulty in obtaining relevant value-added telecom operating permits if the MIIT grants a certain number of value-added telecom operating permits to foreign-invested enterprises after the Foreign-funded Telecom Provisions 2022 take effect. As a result, issuers seeking an IPO in Hong Kong may adjust the shareholding structure of their operating entities based on these new circumstances.

Simplified permit application process, shortened statutory time limit for examination

The Foreign-Funded Telecom Provisions 2022 significantly modify Articles 11 to 16 of its 2016 predecessor, mainly in the following two aspects: first, it abolishes the Approval Certificate for Foreign-invested Enterprises and the Decision on Approving Foreign Investment in Telecommunication Business ("**Approval Decision**"), which currently serves as the condition precedent to the application for a telecom operating permit; also, it substantially reduces the statutory time limit for examining telecom operating permit applications.

According to the MIIT's *Circular on Strengthening Interim and Ex-post Supervision over Foreign-invested Telecommunications Enterprises* (MIIT Tong Xin Han [2020] No.248) issued on October 15, 2020, the MIIT will cease to issue Approval Decisions from the promulgation date of the State Council's *Decision on Canceling and Devolving a Batch of Items Subject to Administrative Examination and Approval* (Guo Fa [2020] No.13), namely September 21, 2020, and the corresponding foreign investment examination procedure is integrated into the telecom operating permit approval process. Pursuant to the foregoing provisions, after cancellation of the Approval Decision procedure, the MIIT and provincial telecom administrations should take measures to step up interim and ex-post supervision over foreign-invested telecom enterprises. For example, while handling telecom operating permit applications, the relevant authorities should strictly oversee the applicants' actual compliance with foreign shareholding limits; regulators should intensify monitoring of day-to-day operations of foreign-funded telecom enterprises by urging them to report relevant information as requested; oversight methods such as the "random inspection and public release" model (note: this model comprises inspections of randomly selected entities by randomly selected inspectors and the public release of inspection results) should be adopted to enhance supervision, and illegal activities found during supervision should be investigated and treated in accordance with law, with relevant information disclosed to the public; regulators should carry out credit supervision by truthfully recording illegal and dishonest practices, adopting differential regulatory approaches, etc. The Foreign-funded Telecom Provisions 2022 remove all Approval Decision-related contents in the 2016 version to be consistent with the above provisions.

Furthermore, according to the Foreign-funded Telecom Provisions 2016, in order to apply to the MIIT for a telecom operating permit, foreign-invested enterprises should complete the following steps first: 1) obtain a Decision on Approving Foreign Investment in Telecommunication Business issued by the MIIT; 2) obtain an Approval Certificate for Foreign-invested Enterprises granted by the competent commerce authority; and 3) complete registration formalities with the administration for industry and commerce. By contrast, in combination with the abovesaid New Foreign Investment Rules, the "issuing business license before operating permit" reform, etc., the Foreign-funded Telecom Provisions 2022 streamline the above procedures down to the following: upon completion of market entity registration formalities with the competent administration for market regulation, a foreign-invested enterprise may apply with the MIIT for a telecom operating permit by submitting materials required in the Foreign-funded Telecom Provisions 2022. The 2022 amendment also merges application for a basic telecom operating permit and a value-added telecom operating permit into one same process, with a mere difference in the examination time limit. The Foreign-funded Telecom Provisions 2016 require the MIIT to make a decision on whether to grant the Approval Decision within 180 days after receiving an application, and the Foreign-funded Telecom

Provisions 2022 require the MIIT to make a decision on whether to grant a basic telecom operating permit within 180 days upon receipt of an application. The streamlined process actually shortens the overall statutory time limit for examining a basic telecom operating permit application by cutting off formalities such as the commerce authority's review process (with a 90-day time limit). On the other hand, the statutory time limit for examining a value-added telecom operating permit application is shortened not only by the above streamlined process but also through an express statutory reduction to "60 days upon receipt of the application" (from 90 days in the 2016 version).

The above changes made by the Foreign-funded Telecom Provisions 2022 will establish a more efficient process for foreign-invested telecom enterprises to apply for a telecom operating permit and would reduce uncertainties imposed on the applicants' business operations due to a prolonged examination process.

Conclusion

Although the Foreign-funded Telecom Provisions 2022 is freshly released and awaits more specific practice guidelines, this amendment is launched as part of the government's endeavor to promote the separation of operating permits and business licenses, to deepen reforms to "streamline administration, delegate powers, improve regulation, and strengthen services", and to stimulate the development vitality of market players. It reveals the affirmative attitude of China towards foreign investments in the telecommunications field, and we are optimistic about how it will work out.

2. Overseas IPOs: Key Issues in the Draft Archives Rules

Author: Transaction Group

On April 2, 2022, the China Securities Regulatory Commission (the "**CSRC**") published the revised *Provisions on Strengthening Confidentiality and Archives Administration of Overseas Securities Offering and Listing by Domestic Companies (Draft for Comments)* (the "**Draft Archives Rules**"). The *Draft Archives Rules* is now open for public consultations until April 17, 2022.

This newsletter summarises the key content in the Draft Archives Rules that are relevant for overseas securities offerings and listings of domestic companies.

Background to the revision of the confidentiality and archives administration rules

The Draft Archives Rules updates and revises the *Provisions on Strengthening Confidentiality and Archives Administration for Overseas Securities Offering and Listing* (Announcement No. 29 [2009] of the CSRC, "**Current Provisions**") jointly issued by the CSRC, the Ministry of Finance of the PRC, the National Administration of State Secrets Protection, and the National Archives Administration of the PRC.

The Draft Archives Rules are intertwined with and echo at the legislative level two key documents[1] in relation to the reform of the overseas listings record-filing system, which are still in draft form:

- *Provisions of the State Council on the Administration of Overseas Securities Offerings and Listings by Domestic Companies (Draft for Comment)* (the "**Administration Provisions on Overseas Offerings and Listings**");
- *Administrative Measures for the Record-Filing of Overseas Securities Offerings and Listings by Domestic Companies (Draft for Comments)* (the "**Filing Measures for Overseas Offerings and Listings**").

Analysis of the key constructs of the rules for the administration of confidentiality and archives

I Explicit expansion of the scope of application

Under the Current Provisions, the confidentiality and archives administration rules are applicable to an "overseas securities offering and listing", including companies to be listed, as well as securities companies and securities service institutions that provide relevant securities services. The term "overseas listed company" under the Current Provisions refers to a domestic joint stock limited company that issues overseas-listed shares abroad. In other words, the Current Provisions mainly apply to "H-shares" projects where the listed entity is incorporated in the PRC.

In light of the Administration Provisions on Overseas Offerings and Listings and the Filing Measures

[1] The Administration Provisions on Overseas Offerings and Listings and the Filing Measures for Overseas Offerings and Listings are still in the legislative process and have not yet come into effect.

for Overseas Offerings and Listings, the scope for the application of the Draft Archives Rules has been adjusted to be consistent with the overseas listing record-filing system that is currently underling the legislative process. In other words, the Draft Archives Rules includes both overseas direct offerings (i.e. where the listed entity is incorporated in the PRC) and overseas indirect offerings (i.e. where the listed entity is not incorporated in the PRC, but where the PRC operating company is part of the group).

II Further clarification of regulatory aims

As a result of the above expansion of scope, the Draft Archives Rules adjusts its scope from "overseas listed companies (including proposed listed companies") under the Current Provisions to "domestic enterprises" covering both domestic joint stock companies directly listing overseas and domestic operating entities that indirectly list overseas through non-PRC incorporated listing vehicles.

At the same time, the Draft Archives Rules also clearly define "securities companies" and "securities service institutions", both of which are subject to its supervision, to include **domestic and overseas** securities companies, securities service institutions, as well as their domestic member institutions, representative institutions, affiliated institutions, and cooperative institutions, etc. This builds on the Current Provisions, by accounting for the complexities of overseas listings (i.e. subjecting indirect listings to its jurisdiction to account for the creation of overseas structures), and by refining and filling in regulatory gaps.

In addition, the Draft Archives Rules explicitly include within the scope of its supervision overseas accounting firms that engage in auditing business related to overseas issuances and listings of domestic enterprises. Overseas accounting firms that engage in auditing business related to overseas issuances and listings of domestic enterprises are required to abide by corresponding procedures in accordance with relevant state regulations. At present, according to the *Interim Provisions on the Audits Conducted by Accounting Firms Concerning the Overseas Listings of Domestic Companies* (effective July 1, 2015) issued by the Ministry of Finance, if a PRC company retains an overseas accounting firm, such overseas accounting firm should carry out business cooperation with a PRC accounting firm and fulfil its regulatory procedures, such as making a report to the provincial finance department where the PRC company is located, with a copy to the Ministry of Finance. After these Draft Archives Rules come into effect, whether new regulatory policies will be adjusted for the cross-border practices of overseas accounting firms will be further clarified by regulators.

III Confidentiality and management system implementation requirements

1. Confidentiality and archives system

The Draft Archives Rules require that, in relation to the overseas listing activities of domestic enterprises (which as stated above also includes indirect listings), such domestic enterprises, as well as securities companies and securities service institutions providing relevant securities services, are required to strictly comply with the relevant requirements on confidentiality and archives management, **establish a sound confidentiality and archives system**, and take necessary measures to implement their confidentiality and archives management responsibilities.

It should be noted that "whether a sound and complete, standardized confidentiality and archives management system has been established and put in place" is currently a key point of review by the CSRC in H-share listings (the listed entity is incorporated in the PRC), and legal advisors are required to comment on this when filing an H-share listing application with the CSRC.

We understand that in the context of the Administration Provisions on Overseas Offerings and Listings, which sets out clear requirements for the establishment of confidentiality and archives management, companies proposing to submit record-filing applications to the CSRC under the Administration Provisions on Overseas Offerings and Listings should have established and implemented the relevant confidentiality and archives management systems prior to the filing. This will apply after the Administration Provisions on Overseas Offerings and Listings and the Filing Measures for Overseas Offerings and Listings take effect.

2. Regulatory procedures for materials involving state secrets or archives with a sensitive impact

According to the Draft Archives Rules, if during the course of an overseas offering and listing (whether listed directly or indirectly), if a PRC company needs to publicly disclose or provide to securities companies, accounting firms or other securities service providers and overseas regulators, any materials that contain relevant state secrets or that have a sensitive impact (i.e. be detrimental to national security or the public interest if divulged), the PRC company should complete the relevant approval/filing and other regulatory procedures.

Compared to the Current Provisions, where materials containing "state secrets" are subject to approval from competent authorities and a filing with state secrecy departments, the Draft Archives Rules expand such scope to include materials containing "state secrets and government work secrets". Unlike state secrets, the definition of which is relatively clear (i.e. bearing the "state secret" mark by the holder), "government work secrets" are determined respectively by responsible government organs and units without any uniform standard or marking requirement. Accordingly, "government work secrets" may include (but are not limited to), government documents and materials marked as "internal document", "internal matter", "internal material", and the like. Therefore, prospective listed companies should closely monitor secrecy or sensitive impact issues when providing service institutions and overseas regulators with documents and materials obtained from government departments (including communications and correspondences with those departments).

The Draft Archives Rules also require a PRC company to complete relevant procedures stipulated by applicable national regulations if it plans to publicly disclose or provide documents and materials that, if divulged, would jeopardize national security or the public interest. This revision is consistent with the set of laws and regulations on national security, cybersecurity, and data security issued in recent years, stressing the need to stay compliant with relevant regulatory policies when disclosing listing-related documents and materials to service institutions and overseas regulators.

3. Divulgence reporting system

The Draft Archives Rules also require domestic companies, securities companies and securities service providers that discover the divulgence or possible divulgence of state secrets, to take

immediate remedial measures and timely report the same to relevant organs and departments.

4. Archives administration requirements

- The Draft Archives Rules retain the requirement in the Current Provisions that archives such as **working papers produced in the PRC** by securities companies and securities service institutions, which provide PRC companies with securities services during its overseas issuance and listing, **should be stored in the PRC**. Furthermore, under the Draft Archives Rules, **the transmission of all such working papers to recipients outside of the PRC is required to be approved by competent authorities of the PRC**. This approval requirement no longer just applies to state secrets, national security or the vital interests of the state as stipulated by the Current Provisions;
- Article 8 of the Draft Archives Rules states, "Domestic companies that provide securities companies, securities service providers and overseas regulators with accounting archives [including working papers] or copies thereof, which have important preservation value to the nation and the public shall complete due procedures in compliance with applicable national regulations";
- Article 9 of the Draft Archives Rules also states, "Where archives [including working papers] or copies of archives, which have important preservation value to the nation and the public needs to be transmitted to recipients outside the PRC, due approval procedures shall be followed in accordance with applicable national regulations". Although the term "important preservation value to the nation and the public" is consistent with the terminology in the Archives Law of the PRC, neither has elaborated on the specific meaning of such expression. Also, the Archives Law prohibits "selling or gifting" such archives "to non-PRC or non-PRC organizations", which does not appear to be consistent to this Article 9. The specific requirements still need to be clarified in subsequent implementation rules.

IV Regulatory coordination mechanisms

1. Domestic regulatory coordination mechanism

On the basis of the regulatory coordination mechanism established between PRC regulators under the Current Provisions, the Draft Archives Rules adds the Ministry of Finance as another PRC regulatory authority (being the primary regulator of accounting firms), which reflects the overall content of the Draft Archives Rules.

2. Cross-border regulatory cooperation mechanism

The Draft Archives Rules establishes a cross-border regulatory cooperation mechanism as prescribed in Article 177 of the PRC's Securities Law and strengthens cross-border regulatory cooperation under the principles of reciprocity and mutual benefit as prescribed in the Administrative Provisions Regarding Overseas Issuance and Listing. It shifts the overall direction of cross-border supervision of overseas listings from a "PRC dominant" approach under the Current Provisions to a "cross-border regulatory cooperation mechanism". Specifically,

(1) There is no differentiation between an "on-site inspection" and an "off-site inspection"

Under the Current Provisions, overseas securities regulators and other relevant bodies may conduct an on-site inspection or an off-site inspection on companies that have listed (or intend to list) overseas, as well as securities companies and institutions providing services for the overseas issuance and listing of securities (including accounting firms). An on-site inspection had to be conducted at the relevant site in the PRC, required prior approval from competent PRC authorities, and had to be carried out mainly by PRC regulators or had to have relied on the inspection results of PRC regulators. With respect to an off-site inspection, companies that have listed (or intend to list) overseas, securities companies and securities service providers (including accounting firms) had to obtain prior approval from competent PRC regulators only if the relevant case involved state secrets, archives (including working papers) administration and other matters subject to such prior approval.

In light of the extended jurisdiction under the Draft Archives Rules, regulating both direct and indirect overseas issuances and listings by domestic enterprises, and considering international cross-border audit supervision practices, the Draft Archives Rules no longer differentiate inspections by overseas bodies on geographical or methodological grounds, but rather places them under unified regulation of a common cross-border cooperation mechanism. This also addresses and consolidates Article 177 of the PRC's Securities Law, which provides that "overseas securities regulatory authorities shall not carry out investigation, evidence collection, etc. directly in the PRC", by enabling the cross-border cooperation mechanism to regulate investigations, inspections and evidence collection by overseas securities regulators and relevant authorities with respect to the overseas issuances and listings by domestic enterprises.

In addition, the Draft Archives Rules require relevant domestic enterprises, securities companies and securities service institutions to report to the CSRC or relevant authorities before cooperating with overseas regulators or relevant authorities in their investigations and inspections or providing materials to them. We tend to believe that this reporting obligation arises where those overseas regulators or authorities carry out an investigation or inspection under the cross-border regulatory cooperation mechanism, with the assistance from the CSRC or competent PRC authorities pursuant to relevant mechanisms. To some extent, it means the burden of obtaining the CSRC's prior approval for an investigation or inspection is shifted to overseas securities regulators or relevant overseas authorities pursuant to the cooperation mechanism. It is also consistent with Article 177 of the PRC's Securities Law, the enabling law of the Draft Archives Rules, in terms of the principle that "no organization or individual is allowed to provide the documents and materials relating to securities business activities to overseas parties without the consent of the securities regulatory authority of the State Council and the relevant State Council department(s)." Where a cross-border regulatory cooperation mechanism is not established between the PRC and certain countries and organizations, Article 177 of the Securities Law will directly apply.

(2) Submission of the overseas listing application is separate from the provision of materials under the cross-border regulatory cooperation mechanism

After the promulgation of the PRC's Securities Law, the question of whether prior consent from the

CSRC and relevant State Council department(s) was required prior to submitting overseas listing applications to securities exchanges and regulators outside of the PRC was a hotly debated and constantly inquired issue. As Article 177 is under Chapter 12 (Securities Regulatory Authorities) of the PRC's Securities Law, Paragraph 1 of Article 177 focuses on establishing a cross-border regulatory cooperation mechanism, and the first sentence of Paragraph 2 stresses that overseas securities regulators should not carry out evidence collection for an investigation directly in the PRC, the common belief in practice was that the provision of securities business related documents and materials under Paragraph 2 of Article 177 tended to exclude the submission of listing applications to overseas securities exchanges and regulators.

The Administrative Provisions Regarding Overseas Issuance and Listing of Securities and the Measures for the Overseas Issuance of Securities and Listing Record-Filings set forth record-filing requirements for domestic enterprises that intend to list and issue securities overseas, while the Draft Archives Rules establish a reporting system for relevant investigations, inspections and the provision of materials under a cross-border regulatory cooperation mechanism. These rules and regulations viewed together form the basis for regulating the overseas issuance and listing of securities by domestic enterprises.

We hope the above policy adjustments will positively promote a consensus to be reached soon between PRC regulators and overseas regulators on cross-border audit supervision, which will create a favourable regulatory environment for the development of PRC issuers listed overseas.

Important Announcement

This Newsletter has been prepared for clients and professional associates of Han Kun Law Offices. Whilst every effort has been made to ensure accuracy, no responsibility can be accepted for errors and omissions, however caused. The information contained in this publication should not be relied on as legal advice and should not be regarded as a substitute for detailed advice in individual cases.

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