

Legal Commentary

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Private Equity Law

Analysis of Beijing's New QFLP Scheme

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Beijing is one of China's first QFLP pilot zones—second only to Shanghai, which announced its own QFLP pilot scheme at the end of 2010 and heralded QFLP pilot work in other cities. Beijing announced its QFLP policies as early as February 2011, making Beijing a pioneer city and providing guiding significance. In recent years, a new era of QFLP investment has arrived, owing to China's continuous opening-up policies and expanding foreign exchange reforms, together with the increase of China assets allocation by foreign investors. Zhuhai, Suzhou, Xiamen, Hainan, and Shenzhen have each issued or updated new QFLP policies to further attract foreign investment in China. Beijing officially released the *Interim Measures on the Pilot Scheme of Qualified Foreign Limited Partners in Beijing* on 6th May, 2021 (hereinafter referred to as the “**New QFLP Measures**”), which improves Beijing's current QFLP policies. In this article, we introduce and analyze the provisions and specific requirements of the New QFLP Measures.

Supervisory mechanism

The New QFLP Measures call for a “pilot joint review mechanism,” which means the establishment and operation of QFLPs will be jointly supervised and examined by various regulatory authorities as follows:

1. The members of the pilot joint review work committee include the Municipal Financial Supervision Bureau, the Market Supervision Bureau, the Operations Department of the People's Bank of China, and the Beijing Branch of the State Administration of Foreign Exchange;
2. The pilot joint review office is established by the Municipal Financial Supervision Bureau;
3. The Municipal Financial Supervision Bureau, through the pilot joint review office, is responsible for daily affairs, and takes the lead in advancing pilot work, daily management and risk control, as well as accepting application materials and other relevant documents and coordinating relevant pilot joint review committee members in reviewing application materials. The Municipal Market Supervision Bureau is responsible for coordinating and guiding the registration of pilot enterprises. The Operations Department of the People's Bank of China and the Beijing Branch of the State Administration of Foreign Exchange are responsible for the supervision and control of foreign

exchange registration, account opening, capital exchange, cross-border RMB transactions, and other matters related to the New QFLP Measures.

Requirements for pilot fund management enterprises and pilot funds

Under the New QFLP Measures, in principle, **pilot fund management enterprises** and **pilot funds** (collectively referred to as “**Pilot Enterprises**”) should be registered and established in Beijing. The application requirements are as follows:

<p>Pilot fund management enterprises (corporations and partnerships are both acceptable)</p>	<p>Pilot fund management enterprises are categorized into domestic fund pilot fund management enterprises and foreign-invested pilot fund management enterprises.</p> <ol style="list-style-type: none"> 1. The controlling shareholder, actual controller, or executive partner of a private investment fund management enterprise shall be one of the following: a financial company (which is approved by the relevant national or regional regulator and holds a certificate issued by local regulators to engage in relevant financial services) or a management enterprise with fund AUM of not less than RMB 100 million or its foreign currency equivalent; 2. Private investment fund management enterprises or their shareholders operate normally, have sound governance structures and internal control systems, and have not been subject to disciplinary sanctions by judicial authorities or relevant regulatory agencies within the past three years; 3. At least two senior officers of a private investment fund management enterprises have at least three years’ experience in equity investment or equity investment management with good personal credit records; 4. Private investment fund management enterprises that continue to operate shall register with the Asset Management Association of China (“AMAC”) if they are so required in accordance with the current regulations; 5. Other terms required by pilot joint review members. <p>Han Kun Note: The New QFLP Measures allow for the domestic manager-foreign investor model, foreign manager-foreign investor model, and foreign manager-domestic investor model. Pilot fund management enterprises are required to have specified AUM and personnel headcounts, but not all are required to register with AMAC.</p>
<p>Pilot funds (may be incorporated or organized as a partnership, or formed as a contractual fund)</p>	<ol style="list-style-type: none"> 1. A single fund shall not in principle be less than RMB 100 million (or its foreign currency equivalent), and a private investment fund management enterprise may subscribe for a certain proportion of the fund interests; 2. Other terms required by pilot joint review members;

	<p>3. Newly-established pilot enterprises shall complete registration and filing formalities with AMAC in accordance with the prevailing provisions.</p> <p>Han Kun Note: Funds are subject to a minimum size threshold, i.e., RMB 100 million for each fund.</p>
<p>Qualified limited partners of pilot funds</p>	<ol style="list-style-type: none"> 1. Institutions or individuals that have corresponding risk identification and tolerance capabilities as well as relevant investment experience; 2. Institutional investors shall have sound governance structures and well-developed internal controls and not have been subject in the past three years to disciplinary sanctions by national or regional judicial authorities or relevant regulatory agencies. In the case of foreign institutional investors, each shall possess net assets of no less than USD 5 million or its equivalent and make single investments of no less than USD 1 million or its equivalent. In case of domestic institutional investors, each shall possess net assets of no less than RMB 10 million and make single investments of no less than RMB 1 million; 3. With respect to domestic and overseas individual investors, each shall possess net financial assets of not less than RMB 3 million and possess financial assets of not less than RMB 5 million or have average annual income of not less than RMB 500,000 over the past three years, and make single investments of not less than RMB 1 million; 4. Other terms required by pilot joint review members. <p>Han Kun Note: Domestic institutional investors are subject to the same requirements as domestic qualified investors of private investment funds. Foreign institutional investors are subject to stricter requirements than domestic institutional investors. Domestic and foreign individual investors are subject to higher asset requirements than domestic qualified individual investors of private investment funds.</p>
<p>Use of capital converted from foreign exchange settlement</p>	<ol style="list-style-type: none"> 1. Equities of non-listed companies; 2. Ordinary shares privately issued and traded by listed companies (including new private share issuances, block trades, negotiated transfers, etc.), preferred shares convertible to ordinary shares, shares converted from debt and convertible bonds, and participation as existing shareholders in private placements by listed companies; 3. Mezzanine investments, investments in private bond issuances, and non-performing assets; 4. Investments in domestic private investment funds; 5. Other business permitted by laws and regulations. <p>Without approval, pilot funds shall not use funds raised to make investments outside China.</p>

	<p>Han Kun Note: Permitted use of funds includes investments in primary and semi markets, mezzanine investments, investments in privately issued bonds, and non-performing assets. FOF investments and feeder vehicles are also permitted.</p>
<p>Use of foreign exchange settlement quotas</p>	<p>Where a pilot fund management enterprise initiates the establishment of pilot funds, the aggregate foreign exchange settlement quotas for all funds so established shall not exceed the foreign exchange settlement quota of the fund management enterprise as approved by the pilot joint review office. Unless otherwise provided, a pilot fund management enterprise may freely adjust the foreign exchange settlement quotas for each fund it establishes with the aggregated quotas for all funds capped by the foreign exchange settlement quota of the pilot fund management enterprise.</p> <p>Han Kun Note: Pilot fund management enterprises may initiate the establishment of several pilot funds, and there is flexibility such that foreign exchange settlement quotas for each fund may be adjusted with the aggregate quotas of all funds capped by the foreign exchange settlement quota of the pilot fund management enterprise.</p>

In terms of procedures, the New QFLP Measures provide that parties eligible to submit applications for pilot enterprises are private investment fund management enterprises, their controlling shareholders, actual controllers, or executive partners. Application materials are submitted to the pilot joint review office, which will then decide whether to approve the applicant’s application. If the pilot joint review office approves the application, it will issue to the applicant a review opinion with a stated pilot quota amount.

Information reporting and supervision during the term of the pilot enterprise

The New QFLP Measures stipulate rules for supervising pilot enterprises (particularly pilot funds) during their terms. The detailed rules are as follows:

<p>Pilot fund management enterprises</p>	<ol style="list-style-type: none"> 1. Periodically submit to the pilot joint review office business reports (including funds settlement and investment income), fund custody reports issued by a custodian bank, annual financial reports audited by certified public accountants, and quarterly reports of major events occurring with investment operations, and copy relevant authorities.
<p>Custodian bank</p>	<ol style="list-style-type: none"> 1. Keep complete information on the revenues and expenditures of pilot enterprise accounts for a period of 20 years for future inspection by the relevant authorities; 2. Supervise the use of funds in pilot enterprise escrow accounts, review the authenticity of the use of funds, and review the written opinions issued by the competent departments necessary for the investment. Reporting to the joint review

	<p>office and other member units without delay upon detection of any irregularities with respect to the accounts;</p> <p>3. Prepare a report on cross-border fund receipts and payments and foreign exchange settlement and sale of funds for the pilot enterprises each quarter, which shall be provided to the pilot joint review office and copied relevant authorities.</p>
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Conclusion

Beijing, among the pioneers of QFLP pilot cities, has always been a popular place for establishment of foreign equity investment enterprises. The city’s attractiveness will be further strengthened by the promulgation of the New QFLP Measures. The New QFLP Measures will create a favorable and convenient investment environment for overseas investors in Beijing by following the policy’s original regulatory logic while considering the actual needs of overseas investors and referring to QFLP policies in other regions. We will continue to watch the implementation of the New QFLP Measures and relevant implementation rules and hope it opens a path for more foreign investors to participate in the thriving Chinese private investment industry.

Important Announcement

This Legal Commentary 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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