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Newsletter

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Insights & Ideas

MOFCOM Released Interim Provisions on the Implementation of the Security Review System for Mergers and Acquisitions of Domestic Enterprises by Foreign Investors (Author: Minyu SUN; Xu LIU)

The Notice of the General Office of the State Council regarding the Establishment of the Security Review System for Mergers and Acquisitions of Domestic Enterprises by Foreign Investors (the “Notice”) has taken effect as of March 5, 2011. The Notice, for the first time, requires for a national security review by a ministerial panel (the “Ministerial Panel”) for any merger or acquisition of a domestic enterprise by a foreign investor (an “M&A”) that may have potential impact on China’s national security. Under the guidance of the State Council, the Ministry Panel is consisted of the National Development and Reform Commission, the Ministry of Commerce(or “the MOFCOM”), and other concerned departments based on the specific industries or fields of the transaction. The foreign investors (applicants for national security review) mainly communicate with the MOFCOM, which accepts the application for national security review and informs the applicants of the national security review results. On March 4, 2011 (the previous day of the effective date of the Notice),the MOFCOM issued the *Interim Provisions on Issues Related to the Implementation of the Security Review System for Mergers and Acquisitions of Domestic Enterprises by Foreign Investors* (“Interim Provisions”) to specify what is not detailed in the Notice. It should be noted that the Interim Provisions expires on August 31, 2011, and may be further revised by the MOFCOM upon expiry based on public comments and MOFCOM’s experience in implementing them.

The Interim Provisions specify, supplement and detail the Notice in the following items:

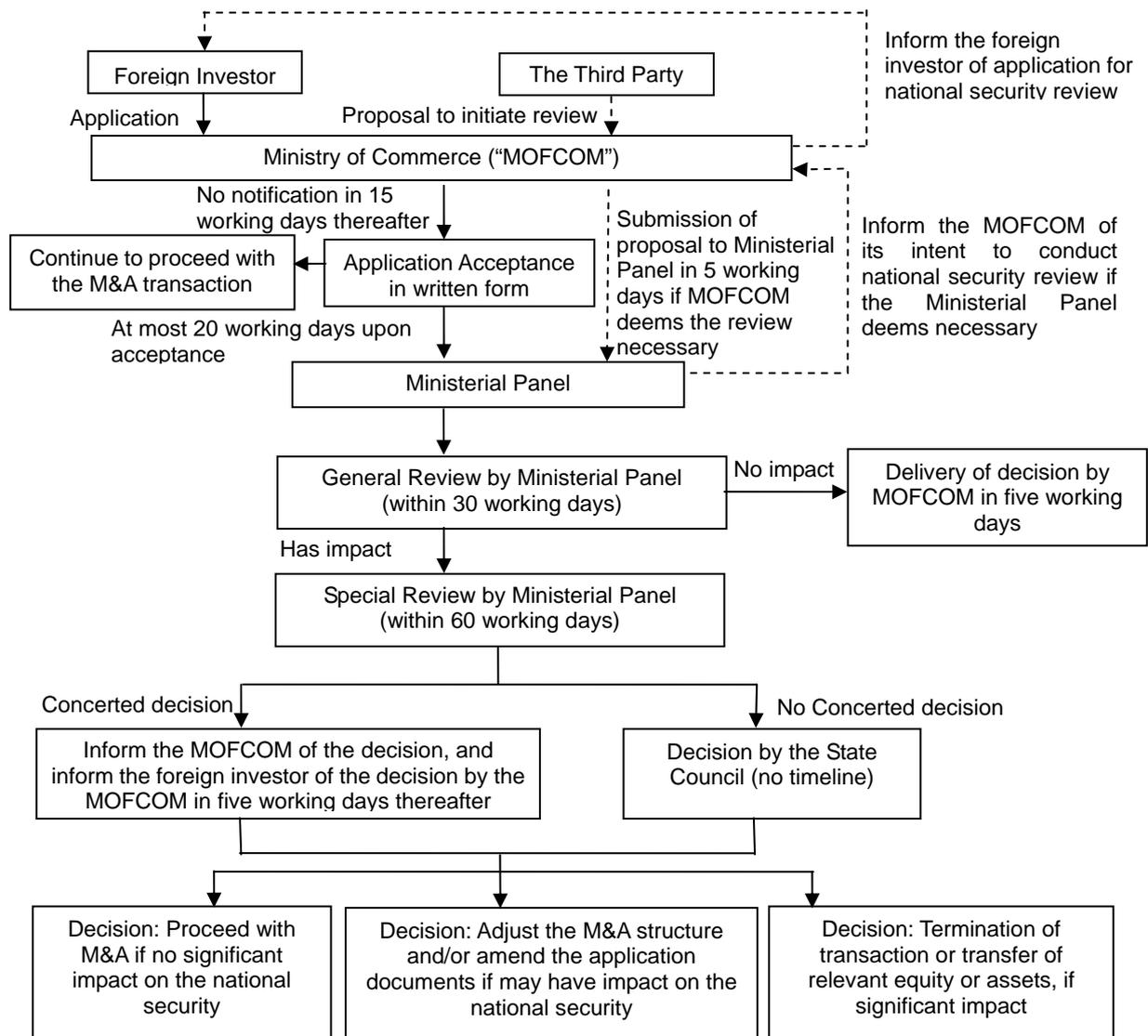
- a) Local commerce departments are entitled to decide whether an M&A transaction falls into the scope of the national security review. The local commerce department may refuse to accept the application, if it finds that the pending M&A transaction is subject to the security review while the foreign investor fails to file the same with the MOFCOM for national security review.
- b) The foreign investor/applicant may consult with the MOFCOM before officially filing an application for review on the procedural matters of proposed mergers and acquisitions.
- c) The applicant is required to submit an application to the MOFCOM for a security review at any time during the process of merger and acquisition if such merger and acquisition meets the threshold for national security review.
- d) The Interim Provisions clarify the application documents that should be submitted by foreign investor while filing for security review, which include:

- i. Written application for M&A security review and a statement describing the concerned M&A transaction, to which the signature of the legal representative of the applicant or authorized representative shall be affixed;
- ii. Identity certification or registration certification, and credibility letter of the foreign investor which have been notarized and certified; identity certification of the legal representative, or the power of attorney issued by the foreign investor and identity certification of the authorized representative thereof;
- iii. Statement on the information pertaining to the foreign investor and its affiliates (including its actual controller or parties acting in concert), and a statement on its relationship with the government of relevant countries;
- iv. Statement on situations of the target domestic enterprise, its articles of association, business license (photocopy), audited financial statements for the previous year, structure chart prior to and after the M&A, and a statement on the situations of enterprises invested by the target enterprise, and business licenses (photocopy) of such enterprises;
- v. Contract, articles of association, and partnership agreement of the foreign-invested enterprise to be established after the M&A, and the name list of members of the board of directors thereof appointed by the shareholders, and senior executives to be engaged such as the general manager, partners, etc.;
- vi. In case of equity acquisition, the equity transfer agreement or the agreement on subscription by the foreign investor for the increased capital of the domestic enterprise, resolution of the shareholders' meeting or general meeting of shareholders of the target domestic enterprise, and the relevant asset evaluation report shall be submitted;
- vii. In case of assets acquisition, the resolution of the authority or property right owner of the concerned domestic enterprise approving the sale of the assets, assets purchase agreement (including the checklist and status of the assets to be purchased), statement on the information of each party to the agreement, and the relevant asset evaluation report shall be submitted;
- viii. Statement on the impact of the voting rights enjoyed by the foreign investor after the M&A on the resolution of the shareholders' meeting, general meeting of shareholders, or the board of directors, or on the execution of partnership affairs, a statement on other situations that may result in the transfer of actual controlling rights related to business decision-making, financial matters, human resources, technologies, etc., to the foreign investor or affiliates inside and outside of China, and the agreement or documents relevant to the aforementioned situations; and

The MOFCOM reserves the right to require the applicant to submit other documents as it deems necessary.

- e) The proposal of the third party (namely, relevant departments of the State council, national industrial associations, enterprise in the same trade, and upstream and downstream enterprise) to initiate national security review should be accompanied with a statement on the relevant merger and acquisition, including the basic information of the merger and acquisition and its impact on the national security, based on which the MOFCOM and the Ministerial Panel will decide whether to require the foreign investor to file for national security review. However, what information should be included and to what extent that the statement would be deemed as sufficient by the MOFCOM or the Ministerial Panel remains unknown according to the Interim Provisions.
- f) The applicant could expect the timeline to be followed by the MOFCOM's acceptance of the application and the review by Ministerial Panel. The Interim Provisions clearly specify that upon its acceptance of a foreign investor's application, the MOFCOM will have fifteen (15) working days to make a decision on whether the concerned M&A transaction is subject to national security review. Where the MOFCOM decides that the transaction is covered by security review, it shall notify the applicant in writing with the 15-day period, and submit the application to the Ministerial Panel for review within five (5) working days upon the notification. Also, the MOFCOM is expected to inform the applicant of the review results in five (5) working days after it receives such results from the Ministerial Panel. If the MOFCOM does not inform the applicant otherwise within that fifteen (15) working days' period, the applicant can proceed with the proposed M&A transaction.
- g) The impact on the national security review of the proposed M&A transaction is subject to the review of the Ministerial Panel/State Council. According to the Notice, the proposed M&A is to be determined as either having no impact on the national security or having significant impact on the national security. The Interim Provisions further prescribe that the Ministerial/State Council may determine that the proposed transaction may have impact on the national security, and the applicant could eliminate such impact by adjusting the transaction structure, amending the application documents and re-applying with the MOFCOM for the review.

The below chart sets forth the basic procedures that national security review shall follow according to the Notice and the Interim Provisions:



Legal Updates

1. MOFCOM Issued Notice on Issues Concerning Foreign Investment Administration (Author: Kaiying WU; Yeting CAI)

In order to facilitate related work of delegating its approval authorities over certain foreign investment items to its counterparts at the provincial level (“**Provincial Authority**”) and canceling the examination and approval over certain foreign investment items, on February 25, 2011, the Ministry of Commerce (“**MOFCOM**”) promulgated *the Notice of the Ministry of Commerce on Issues Concerning the Administration of Foreign Investment* (the “**Notice**”). The Notice took immediate effect following its release. Upon the Notice coming into force, part of the items listed below will be no longer subject to approval by commerce departments, approval power over certain items originally subject to MOFCOM’s examination and approval will be delegated to the Provincial Authority, and some items will be under even stricter administration.

Cancelation of Examination and Approval

The Notice states that with respect to the establishment of the domestic branch office of a foreign-invested enterprise for which there are no special requirements and the list of equipment imported as capital contribution, the competent commerce department shall not conduct examination and approval any more, and the foreign-invested enterprise may directly go through the formalities with the relevant departments. Likewise, with respect to the change in the legal address (except for the cases which are under the jurisdiction of other examining and approving authorities), name, or name of investors, of a foreign-invested enterprise, the enterprise may only need to file the change with the competent commerce department by presenting the application, resolution made by the governing body of the enterprise, amendment to the contract/Articles of Association, the document showing the changed items, and photocopies of the original foreign-invested enterprise approval certificate and renewed business license, within 30 days after completing the change registration formalities with the concerned industrial and commercial administration. The competent commerce department shall renew the foreign-invested enterprise approval certificate for the enterprise upon receipt of all the above documents.

Delegation of Authority

Besides, MOFCOM delegates part of its approval authorities to its counterparts at the provincial level. Under the Notice, foreign capital merger and acquisition projects with the turnover of less than 300 million U.S. dollars shall be examined and verified by the Provincial

Authority, but the items required to be examined and verified by MOFCOM in accordance with *the Provisions on the Merger and Acquisition of Domestic Enterprises by Foreign Investors* are not subject to the above quota restrictions and shall still be examined and verified by MOFCOM.

As to issues on handling the confirmation of foreign-invested projects encouraged by the State, in accordance with the principles for adjusting the power of examining and approving foreign-invested enterprises, the project confirmation of foreign-invested enterprises encouraged by the State with the total investment of less than USD 300 million shall be handled by the Provincial Authority in accordance with the relevant laws and regulations.

Strict Administration

The Notice further clarifies that, administration over foreign-invested joint-stock companies (listed companies), investments in RMB made by overseas investors, domestic investments made by foreign-invested partnerships and foreign investments in service sectors will be strengthened. The approval certificate of a domestically listed foreign-invested joint-stock company shall state the foreign investors and their shares and, if the accumulative amount of reduced shares held by such foreign investors exceeds 5% of the total share capital, the company shall apply for the renewal of the approval certificate with the competent commerce department. Where an overseas investor applies to use the income from cross-border trade settlement or lawfully obtained overseas in RMB to invest in China, the Provincial Authority shall report the application to MOFCOM (Department of Foreign Investment Administration) and then the investor may go through the relevant formalities.

It is worth noting that the Notice indicates, in particular, that a foreign-invested partnership enterprise whose primary business is investing (RMB funds) shall be treated as an overseas investor, and the competent commerce departments at all levels shall, in accordance with the relevant regulations, improve the administration on examination and verification of such enterprises. For finance lease, international express, advertising, auction, value-added telecommunication and others involving special stipulated management of provinces, municipalities and autonomous regions, microfinance, market research, credit rating, security service and other sensitive industries, venture capital investment, equity investment and management, and other industries involving large capital inflows, the Provincial Authority shall strictly examine and approve foreign investments.

2. NDRC Released Notice on Delegating Approval Authority on Outbound Investment Projects to Lower-Level Counterparts (Author: Kaiying WU; Taoran WANG)

The National Development and Reform Commission (the “**NDRC**”) issued the *Notification on Delegating Approval Authority on Outbound Investment Projects to Lower-level Counterparts* (the “**Notification**”) on February 14, 2011, which came into force on the same day. For the purpose of accommodating the demand for the development of outbound investment under the new situation, the Notification has amended some previous provisions regarding the approval authority on outbound investment projects and record filing, establish a project registration system and narrow the scope of projects that require information report.

Clarification on the Scope of Application

The Notification is applicable to the approval of outbound investment projects (including investment projects in Hong Kong Special Administrative Region and Macaw Special Administrative Region) made by domestic entities or their subsidiary companies or institutions abroad.

Investment projects in Taiwan should apply the *Notification on Issuing the Measures for the Administration of Investment in Taiwan by Mainland Enterprises* rather than the Notification.

Delegation of Authority to Approve Projects

According to the *Temporary Administrative Measures for Approval of Overseas Investment Projects* issued by the NDRC in 2004, the provincial national development and reform departments (the “**Provincial NDRC**”) shall approve those outbound investment projects concerning resource development, in which the Chinese party invests less than 30 million US dollars or those projects in which the amount of foreign exchange invested by the Chinese party is below 10 million US dollars. The NDRC shall approve those outbound investment projects concerning resource development in which the investment made by the Chinese party reaches 30 million US dollars or above or those projects in which the amount of foreign exchange invested by the Chinese party reaches 10 million US dollars or above. For those outbound investment projects concerning resource development in which the investment made by the Chinese party reaches 200 million US dollars or above or those projects in which the amount of foreign exchange invested by the Chinese party reaches 50 million US dollars or above, they are subject to the examination of the NDRC and the approval of the State Council. The outbound investment projects which are subject to the approval of the Provincial NDRC, if conducted by the centrally-administered enterprises, may be decided by the enterprises themselves and then filed with the NDRC.

The Notification made certain adjustment to the foregoing approval authority by delegating part of the approval authority originally exercised by the NDRC to the Provincial NDRC.

Pursuant to the Notification, those outbound investment projects concerning resource development with an investment of less than 300 million US dollars by the Chinese party and the non-resource development projects with an investment of less than 100 million US dollars by the Chinese party (excluding special projects) conducted by local enterprises shall be subject to the approval by the Provincial NDRC. Such outbound investment projects conducted by centrally-administered enterprises may be decided by the enterprises themselves and filed with the NDRC. For those outbound investment projects concerning resource development with an investment of more than 300 million US dollars or those non-resource development outbound investment projects with an investment of more than 100 million US dollars by the Chinese party, then shall be subject to the approval of the NDRC.

Establishment of Project Registration System

With respect to those projects that are subject to the approval of the Provincial NDRC, the Notification creates a system of project registration. It is provided in the Notification that, for those outbound investment projects concerning resource development with an investment of more than 30 million US dollars and less than 300 million US dollars by the Chinese party, and those non-resource development outbound investment projects with an investment of more than 10 million US dollars and less than 100 million US dollars by the Chinese party, the Provincial NDRC, before its issuance of approval documents, shall report to the NDRC for registration. The registered approval documents shall be the basis for completing relevant procedures and enjoying relevant policies.

Improve Record-filing Measures

The Notification provides that the record filing of outbound investment projects carried out by the centrally-administered enterprises shall be implemented in compliance with the *Notification of the General Office of National Development and Reform Commission on the Record Filing Certification of Outbound Investment Projects*, where the amount of investment contributed by the Chinese party reaches 30 million dollars but below 3 billion dollars in projects concerning resource development or the amount of investment contributed by the Chinese party reaches 10 million dollars but below 1 billion dollars in projects concerning non-resource development.

The following diagram illustrates the specific approval authority and process of different types of outbound investment projects following the Notice coming into force:

Amount of Capital Contributed by the Chinese Party	Centrally-administered Enterprises	Local Enterprises
when the amount of capital contributed in a project concerning resource development is above 3 billion dollars or the amount of capital contributed in a project concerning non-resource development is above 1 billion dollars	subject to the approval of the NDRC	subject to the approval of the NDRC
when the amount of capital contributed in a project concerning resource development reaches 30 million dollars but below 3 billion dollars, or the amount of capital contributed in a project concerning non-resource development reaches 10 million dollars but below 1 billion dollars	decide on its own and then submit to the NDRC for record filing pursuant to the <i>Notification on Further Improving the Administration of Outbound Investment Projects</i> issued by the NDRC	subject to the approval of Provincial NDRC with prior registration by the NDRC
when the amount of capital contributed in a project concerning resource development is below 30 million dollars or the amount of capital contributed in a project concerning non-resource development is below 10 million dollars		subject to the approval of the Provincial NDRC

Adjust the Scope of Projects that Require Submission of Information Reports

Pursuant to the *Notification on Further Improving the Administration of Outbound Investment Projects* issued by the NDRC in 2009, before launching the substantial work of any overseas acquisition projects and overseas bid projects, the enterprise in concern shall submit an information report to the NDRC and courtesy copied to the State Council.

The Notification narrows down the scope of projects that require submission of information reports, and provides that an information report is only required to be submitted and courtesy copied in those overseas acquisition projects and overseas bid projects, where the amount of investment contributed by Chinese party reaches 1 billion dollars or above.

Approval of Special Projects

The Notification provides that the following investment projects, regardless of amounts, shall be submitted to the Provincial NDRC or the state-owned administrative enterprises for a preliminary review and then be submitted to the NDRC for a final approval, OR be first examined by the NDRC and then be submitted to the State Council for final approval:

- a) investment projects in nations or regions which have no diplomatic relationship with China or are subject to international sanctions or are undergoing wars, riots, etc.;
- b) outbound investments projects involving sensitive industries such as basis telecom trade, cross-boarder water resource development and exploitation, land development on large scale, main power grids and mass media.

3. MOC Promulgated New Interim Provisions on the Administration of Internet Culture (Author: Rong CHEN; Yeting CAI; Feng YAN)

On March 18, 2011, the Minister of Culture (“**MOC**”) promulgated a newly amended *Interim Provisions on the Administration of Internet Culture* (hereinafter referred to as the “**New Provisions**”) which came into effect on April 1, 2011, the *Interim Provisions on the Administration of Internet Culture* promulgated on May 10, 2003 and revised on July 1, 2004 (hereinafter referred to as the “**Old Provisions**”) was abrogated simultaneously.

The changes made by the New Provisions to the previous version are mainly set forth below:

Lower the Levels of the Internet Cultural Entity Approving and the Comprehensive Law Enforcement Authorities

The New Provisions clarify that MOC shall only take charge of formulating the guidelines, policies and plans related to the Internet culture development and administration, and supervising the nationwide Internet cultural activities. According to the New Provisions, the commercial/non-commercial entities which conduct Internet cultural activities, shall file to provincial level authorities, namely the culture administrative departments under people's governments of provinces, autonomous regions, or municipalities directly under the Central Government for examination and approval/record. Moreover, the culture administrative departments under people's governments at or above the county level shall be in charge of monitoring and supervising Internet cultural activities within their administrative areas and the county level or above culture administrative departments or cultural market comprehensive law enforcement agencies under people's governments may punish any violation of the relevant regulations.

Specify the Application Conditions, Operating Norms and Penalties for Violations of the Internet Cultural Entities

The New Provisions state that the Internet cultural entity which engages in online game business shall possess a registered capital of no less than RMB 10 million, and the Internet Cultural Operating Permit shall be valid for a period of three years, if the holder wishes to continue conducting the Internet cultural business, it shall apply for renewal thirty days prior to the expiration of the said permit. Compared with the Old Provisions, the New Provisions also specify that the commercial internet cultural entity that offers domestically produced Internet cultural products shall file for records with the cultural administrative departments at or above the provincial level within 30 days after their operations officially begin, and the specific measures for the same shall be provided separately. In addition, the New Provisions specify more detailed penalties in connection with different kinds of illegal Internet cultural operating activities. If the Internet cultural entity violates relevant laws and regulations, the competent government agencies may choose to order the entity to rectify the violation within a stipulated period, impose a fine ranging from RMB500 to RMB30,000, order to cease its business for rectification or to temporarily shut down its website, or revoke its Network Cultural Business Permit according the severity of such violation, and if the violation constitutes a crime, the entity shall be investigated for criminal responsibility.

Furthermore, the New Provision also made fine-adjustments in respect of the content of the Internet cultural products and the Internet cultural activities.

4. The “Regulations on Publication Administration” and the “Regulations on Administration of Audio and Video Products” Amended (Author: Dong LIU; Guanglei ZHANG; Bingning LI)

On March 19, 2011, the State Council promulgated the Decision on Amending the “Regulations on Publication Administration” and the Decision on Amending the “Regulations on Administration of Audio and Video Products”, which came into force on the date of issuance. The amendment of the above two major administrative regulations about administration of publishing activities, was made to meet the needs of reform of publishing industry and development of new media forms.

Amendments on the “Regulations on Publication Administration”

The amended “Regulations on Publication Administration” has specified the application and approval procedures for publishing activities, expanded the application areas and scope, strengthened duties of supervision and administration of press administrative authorities, further improved measures of supervision and administration, and clarified legal responsibilities. The amendments mainly include:

- a) clarifying the authorities approving publishing activities. The wording of approving authorities has been changed from "administrative departments of publication" to "competent publication administrative departments".
- b) clarifying the starting point of the approving time limit. The time limit for approving authorities to make decisions has been changed from within 60 days as of receipt of the application letter to within 60 days as of acceptance of the application.
- c) classifying the "publishing entities" into the "institution as legal person" and the "enterprise as legal person". The former needs to process the registration, change and cancellation procedures with the institution registration authorities, and the latter needs to process the above procedures with the administrative departments for industry and commerce.
- d) based on the original rules allowing the establishment of the Sino-foreign equity joint ventures, Sino-foreign contractual joint ventures and WFOE of books, newspaper, periodical distribution business, further allowing the establishment of the foreign invested enterprises of electronic publication distribution in the above three forms, and canceling the restrictions on foreign invested periodical business.
- e) adding provisions on publication and distribution through network. Under the new rules, any of the entities or individual businesses who engaged in distribution business through Internet should obtain a Publication Business Permit. Operators providing network trade platform service should review the identity of entities and individuals applying for carrying out publication distribution business through the network trade platform, and check their Publication Business Permits.
- f) adding rules on the procedures of change and cancellation registration of the entities or individual businesses carrying out publication distribution business. Under the new rules, in the case that the entities or individual businesses carrying out publication distribution business change the registered items of publication business licenses or conduct merger, consolidation and division, they should process approval procedures, and then competent registration procedures with the administrative department for industry and commerce after approved. To terminate operation activities, they should process cancellation registration with the administrative departments for industry and commerce, and record with the original competent publication administrative departments.
- g) adding restrictions on the activities of publishing entities. In accordance with the new rules, publishing entities shall be warned, ordered to correct and punished under the following situations: unauthorized ceasing publishing activities for more than 180 days, publication import entities' incompliance with the rules on the approval procedures of change, and quality of publications' inconsistency with relevant rules and standards.

Amendments on the “Regulations on Administration of Audio and Video Products”

The amended “Regulations on Administration of Audio and Video Products” has adjusted the rules of importing and distributing audio and video products and regulatory authorities, clarified duties of press and publication administration departments, and simplified requirements of procedures of reproducing entities accepting to be entrusted to reproduce audio and video products, which specifically includes:

- a) clarifying the authorities approving audio and video products publishing activities. The wording of approving authority has been changed from “administrative departments of publication” to “competent publication administrative departments”.
- b) clarifying the starting point of the approving time limit. The time limit for approving authorities to make decisions has been changed from within 60 days as of receipt of the application letter to within 60 days as of acceptance of the application.
- c) amending the requirements and procedures about reproducing audio and video products. Under the new rules, entities reproducing audio and video products who accept a commission to reproduce audio and video products shall, in accordance with relevant provisions of the state, execute entrustment agreements with entrusted publishing entities, and check the Audio and Video Products Publishing Permit, duplicates of Business Licenses, sealed authorization letters of reproducing audio and video products, as well as power of attorney obtained by publishing entities. In case that the audio and video products are not for sale, they shall check certificates of identity of the entrusting entities and authorization letters of reproducing products not for sale issued by entrusting entities.
- d) changing the wording of persons carrying out the retail and rental business of audio and video products, from the “individual” to the “individual businesses”.
- e) adding relevant provisions on electronic publications. The new rules have broadened the application scope to the publication production, reproduction, import, wholesale, retail and other activities of electronic publications.

The amendments to these two regulations are of significant importance to clarifying the approval and processing procedures of press publication and audio and video products industry, and will be helpful to improving the efficiency of the approving authorities, and providing the industry with effective reference and guidelines.

Important Announcement

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