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Newsletter

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Legal Updates

1. **General Overview of China's New Foreign Investment Catalogue (Authors: Wenyu JIN, Fanglu LIN, Yuanxin NIE)**

On March 13, 2015, China's National Development and Reform Commission (the "NDRC") and Ministry of Commerce ("MOFCOM"), promulgated the Catalogue on Guidance for Foreign Investment (the "2015 Catalogue"). The 2015 Catalogue replaces a prior version of the catalogue promulgated on December 24, 2011 (the "2011 Catalogue"). The 2015 Guidance Catalogue will become effective on April 10, 2015.

The 2015 Catalogue aims to i) relax market access for foreign investors; ii) change foreign investment administration, iii) reduce the number of industries foreign investment is restricted for the sake of adjusting and optimizing China's economy and iv) relax foreign capital percentage limitations in certain industries.

Below is a brief summary of the important amendments in the 2015 Catalogue.

The Internet, Information and Technology Industries

The 2015 Catalogue reflects China's general policy of encouraging more foreign investment in the Internet and information technology industries. Specifically, the 2015 Catalogue removes foreign capital percentage limitations in the e-commerce industry. Whereas in the 2011 Catalogue, foreign capital in value-added telecommunications services (such as e-commerce) could not exceed 50%, the 2015 Catalogue explicitly states that e-commerce is no longer subject to such limitation. Furthermore, the 2015 Catalogue adds "the development and application of technologies for the Internet" to the catalogue of "encouraged" industries (the "Encouraged Catalogue"). On the other hand, "internet publishing services" industries have now been placed in the catalogue of "prohibited" industries (the "Prohibited Catalogue"), where no foreign investment is allowed.

Commercial Services Industries

The 2015 Catalogue contains many adjustments to items relating to retail, finance, entertainment, and many other types of services industries. In particular, the 2015 Catalogue removes restrictions on the following industries: "audio-visual product distribution", "direct marketing, mail order, and online sales", "photography services", "entertainment management", and "financial companies, trust companies, currency brokerage companies, and insurance brokers". Accounting and auditing firms are no longer required to only be structured in the form of Sino-foreign equity or cooperative joint ventures, though the chief partner still has to be a Chinese national. Furthermore, the 2015 Catalogue adds the following industries to the Encouraged Catalogue: "elderly-care institutions", and "industrial design, architectural design, costume design, and other creative industries".

The 2015 Catalogue does not specify the qualifications for foreign investment banks and securities companies, though it does increase the foreign capital limit in securities companies from 33.3% to 49%. The 2015 Catalogue does set further foreign capital percentage limitations in banks, namely the following: i) a single overseas financial institution, as a sponsor or as a strategic investor, along with its controlled or joint-controlled affiliates, shall not hold more than 20% of the shares of a single Chinese-funded commercial bank, ii) overseas financial institutions, as sponsors or as strategic investors, along with their controlled or joint-controlled affiliates, shall not collectively hold more than 25% of the shares of a single Chinese-funded commercial bank, iii) amongst all overseas financial institutions, only banking institutions can invest in rural Chinese commercial banks.

The 2015 Catalogue moves “legal consultancy” (excluding the provision of information on an item’s impact on the Chinese legal environment) from the catalogue on “restricted” industries (the “Restricted Catalogue”), where foreign investment is permitted subject to conditions, to the Prohibited Catalogue, and modifies the phrasing of the industry to “consulting on Chinese legal affairs.”

Market research industries remain restricted to foreign investment, and are limited to Sino-foreign equity or cooperative joint venture. Specifically, Chinese parties shall be the controlling shareholders of television and radio program ratings industries. Also, auction houses and cultural relic shops engaged in the auctioning of cultural relics have been placed into the Prohibited Catalogue.

Education

The 2015 Catalogue only places “non-academic occupational training institutions” in the Encouraged Catalogue. “Institutions of higher learning” and “pre-school education institutions” are in the Restricted Catalogue, both limited to Sino-foreign cooperative joint ventures led by Chinese parties. Furthermore, “ordinary senior high schools” have to now be led by Chinese parties, in addition to being in the form of a cooperative joint venture as stated in the 2011 Catalogue. The 2015 Catalogue explicitly states that “led by Chinese parties” means that i) the principal or major persons in charge of administrative matters shall be Chinese nationals, and ii) Chinese nationals’ membership on councils, boards of directors or joint management committees of Sino-foreign cooperative education institutions shall not be less than half. These new items and clarifications, amplify to some extent the foreign investment restrictions in the education industry.

Manufacturing

The 2015 Catalogue removes many items from the Restricted Catalogue. Examples include the raw chemical materials and chemical products manufacturing industries, the chemical fiber manufacturing industry, the transportation equipment manufacturing industry, and the computer and other electronic equipment manufacturing industries. Furthermore, the 2015 Catalogue removes limitations for certain items in the transportation equipment manufacturing industry, the electric machinery manufacturing industry and other industries. For example, foreign investment in

industries relating to “the design and manufacturing of air-borne equipment for civil airplanes”, “the design and manufacturing of yachts”, “manufacturing of power transmitting and transforming equipment”, “manufacturing of air traffic control system equipment” and others, are no longer required to be made only in the form of Sino-foreign equity or cooperative joint ventures. Industries relating to “the construction and operation of urban subways and light rails”, and “the comprehensive maintenance of infrastructure for high-speed railway lines, passenger railway lines, and intercity railways”, are no longer subject to the requirement that the controlling shareholders have to be Chinese parties.

Real Estate and Other Infrastructure Construction Industries

Compared with the 2011 Catalogue, the 2015 Catalogue relaxes restrictions for foreign investment in infrastructure construction industries such as transportation and real estate. For example, foreign investment in industries relating to “the construction and operation of urban subways and light rails” are no longer subject to the requirement that the controlling shareholders have to be Chinese parties. The 2015 Catalogue removes restrictions on foreign investment in the real estate industry. Specific examples include the development of tracts of land, the construction and operation of high-grade hotels, high-end office buildings, and international exhibition centers, secondary market transactions in real estate, and real estate intermediary or brokerage companies.

Energy

The 2015 Catalogue reflects China’s general policy of encouraging foreign investment in industries relating to energy conservation, environmental protection, and alternative energy. For example, the “construction and operation of nuclear power stations” has been removed from the Restricted Catalogue to the Encouraged Catalogue, with a requirement that Chinese parties be the controlling shareholders. In addition, “clean coal power generation projects” and the “construction and operation of sewage treatment plants” have been added to the Encouraged Catalogue.

Medicine and Medical Care Services

The 2015 Catalogue removes foreign investment restrictions in industries relating to the production of many kinds of vitamins, vaccines, narcotic and psychoactive material drugs, and blood products. However, the 2015 Catalogue adds “medical institutions” to the Restriction Catalogue, and foreign investment in such medical institutions may only be in the form of a Sino-foreign equity or cooperative joint venture.

Summary

The 2015 Catalogue generally relaxes market access for foreign investors, changes the foreign investment administration, reduces the number of industries where foreign investment is restricted for the sake of adjusting and optimizing the China’s economy, and relaxes foreign capital percentage limitations in certain industries, with the aim to expand the amount of foreign investment. However,

the 2015 Catalogue does add some new industries into the Restricted Catalogue or Prohibited Catalogue. The 2015 Catalogue generally provides foreign investors with greater access to the China market. We will keep track of China's policies on foreign investment and share the latest trends with you in a timely manner.

2. SAFE Release New Circular to Simplify Direct Investments Foreign Exchange Policies (Authors: Gloria XU, Xi YAN)

On February, 28, 2015 the State Administration of Foreign Exchange (“**SAFE**”) released the *Circular of the State Administration of Foreign Exchange Further Simplifying and Improving Policies on the Administration of Foreign Exchange for Direct Investments* Hui Fa [2015] No. 13 (the “**Circular**”). As suggested by its title, the Circular aims to simplify the administration of foreign exchange for direct investments. The Circular will come into effect on June 1, 2015.

The main points of the Circular are as follows:

Administrative Registration and Approval of Foreign Exchange for Domestic and Offshore Direct Investments Cancelled

Domestic investors of domestic foreign-invested enterprises and offshore investment enterprises no longer need to apply to SAFE to conduct registration and approval of foreign exchange. Rather, they may register such foreign exchange for their direct investments with banks that have already obtained the relevant qualifications, and subsequently they may open direct investment accounts and handle the exchange of funds.

Simplifying the Administration of Confirmation Registration for a Foreign Investor's Direct Domestic Investments

According to the Circular, confirmation registration for the following two types of contributions by foreign investors is no longer required: (1) non-monetary contributions relating to direct domestic investments; (2) contributions relating to the acquisition of stock from Chinese shareholders. Monetary contributions by foreign investors still must be booked and registered as monetary contributions relating to their direct domestic investments.

Foreign Exchange Filing for Offshore Reinvestment Cancelled

Record keeping procedures for foreign exchange are no longer required when domestic investors who own or control offshore enterprises intend to establish or obtain control over new offshore enterprises by means of overseas reinvestment.

Annual Inspection of Foreign Exchange Direct Investments Cancelled

The Circular cancels the annual inspection of foreign exchange direct investments. Rather, domestic and offshore direct investments shall now be subject to stock equity registration. The Circular extends the time deadline for such registration and the channels through which such registration can be made. The deadline for registration is now September 30 each year. The channels through which such registration can be made include the enterprise itself, through accounting firms, or through banks, each using a common information system. Those enterprises that fail to make such registration will have their business supervised and controlled by SAFE through the common information system. Furthermore, banks are not permitted to handle foreign exchange business for non-complaint enterprises.

Supervision after Registration Strengthened

Since banks will directly process foreign exchange registrations, SAFE's will now supervise and manage enterprises following such registrations.

The Circular notes, however, that quarterly submissions of required data to SAFE's office at the place of registration is still required for foreign-invested enterprises that have participated in SAFE's stock equity direct investment sample survey. The Circular does not elaborate on how such sample survey will take place.

Supervision of Banks Strengthened

Since banks will now be responsible for foreign exchange registrations following the implementation of the Circular, there are express instructions in the Circular on enhanced training and guidance for relevant banks. There must be improved compliance at banks, and rule-breaking banks are subject to specified punishments.

Policies in Pilot Areas Reforming Capital Exchange Settlement by Foreign-Invested Enterprises Remain Unaffected.

The implementation of the Circular does not affect the discretionary settlement policy set forth by SAFE's *Circular on Several Issues with respect to the Establishment of Pilot Projects to Reform the Administration of Foreign Exchange Capital Exchange Settlement by Foreign-Invested Enterprises in Several Areas* Hui Fa [2014] No. 36.¹

¹ This circular 36 applies to the following areas: the Tianjin Binhai New Area, the Shenyang Economic Zone, the Suzhou Industrial Park, the East Lake National Innovation Zone, the Guangzhou Nansha District, the Hengqin New Area, the Chengdu Hi-Tech Industrial Development Zone, the Zhongguancun National Innovation Zone, the Chongqing Two Rivers Area, the Heilongjiang Pilot Areas for Foreign Exchange Management Reform for Development and Opening Along Border Areas, the Wenzhou Comprehensive Financial Reform Pilot Area, the Pingtan Comprehensive Experimental Zone, the China - Malaysia Qinzhou Industrial Park, the Guiyang Comprehensive Free Trade Zone, the Qianhai-Shenzhen-Hong Kong Modern Service Industry Cooperation Zone and the Qingdao Wealth Management and Finance Comprehensive Reform Pilot Area.



Important Announcement

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