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New Regulations for Panda Bonds in China's Interbank Market

Financial and Investment Management Department

In recent years, with the development of China's economy and the internationalization of the renminbi, more and more overseas financial institutions and non-financial institutions have issued renminbi-denominated bonds in China¹ ("**Panda Bonds**"). The number and size of the Panda Bonds issued in 2018 have increased significantly. For the half year ended 30 June 2018, 23 Panda Bond issuances were offered in the China Interbank Bond Market ("**CIBM**") with a total amount of RMB 41.26 billion, accounting for 80.13% of total Panda Bond issuances by value². Eight Panda Bonds were issued in the Exchange Bond Market with a total amount of RMB 10.23 billion, accounting for 19.87% of the total Panda Bond issuances by value³.

Despite the relatively large size of Panda Bond issuances in China's markets, the relevant regulators had not issued specialized regulations for Panda Bonds, except for regulations on issuances of Panda Bonds by international development institutions. In practice, other overseas institutions that have issued Panda Bonds in the CIBM, such as foreign government agencies, overseas financial institutions and non-financial enterprises, have had to refer to relevant regulations and rules for domestic institutional bond issuances, which has led to some uncertainty.

On 25 September 2018, the People's Bank of China ("**PBOC**") and the Ministry of Finance ("**MOF**") officially issued the *Interim Measures for Administration of the Issuance of Bonds by*

¹ "China" and "Domestic" (for the purposes of this article only) refer to the territory of the People's Republic of China, excluding the Hong Kong Special Administrative Region, the Macao Special Administrative Region and Taiwan; "overseas" (for the purposes of this article only) refers to countries and regions outside of China.

² Please see <http://finance.sina.com.cn/money/bond/market/2018-08-10/doc-ihhnunsg9352799.shtml>, sourced from 联合资信.

³ Please see <http://finance.sina.com.cn/money/bond/market/2018-08-10/doc-ihhnunsg9352799.shtml>, sourced from 联合资信.

Overseas Institutions in the National Interbank Bond Market (《全国银行间债券市场境外机构债券发行管理暂行办法》) (the "**Interim Measures**") which officially abolished the *Interim Measures for Administration of Issuing Renminbi Bonds by International Development Institutions* (《国际开发机构人民币债券发行管理暂行办法》) (the "**IDI Measures**")⁴.

The Interim Measures aim to provide more systematic and specific guidelines for overseas institutions to issue Panda Bonds in the CIBM. The Shenzhen Stock Exchange also published a consultation draft of the rules for Panda Bonds in the corporate bond market this May⁵ and may issue the formal rules in the near future.

We intend to introduce the main contents of the Interim Measures in this article and analyze the changes to the regulatory rules for Panda Bonds in China.

I. The Issuers Regulated by the Interim Measures

Before the issuance of the Interim Measures, the IDI Measures were the only specialized regulation for CIBM Panda Bond issuances, which only applied to international development institutions. In practice, foreign government institutions, overseas financial institutions and non-financial enterprises largely had to refer to regulations and industry rules applicable to domestic institutions when issuing Panda Bonds. The Interim Measures expand the regulated issuers to foreign government agencies, overseas financial institutions and non-financial enterprises, and provide clearer guidelines for overseas institutions to issue Panda Bonds in the CIBM, which will thus further facilitate the development of the Panda Bond market in China.

II. Further Clarifying the Scope of Approved and Registered Issuances

Generally speaking, the Interim Measures simplify the administration of bonds issued by foreign institutions in China. According to the Interim Measures, the issuance of Panda Bonds by overseas financial institutions in the CIBM is subject to PBOC approval, and Panda Bond issuances by foreign government agencies, overseas non-financial institutions and international development institutions, etc. in the CIBM are registered with the National Association of Financial Market Institutional Investors ("**NAFMII**").

In addition, overseas financial institutions will submit to PBOC for recordkeeping a current prospectus, credit rating reports (if any), underwriting agreement and underwriting syndicate agreement, legal opinions and other final relevant documents.

III. Substantive Requirements for Overseas Financial Institutions to Issue Panda Bonds in the CIBM

The Interim Measures specify the specific requirements for overseas financial institutions to

⁴ Please see http://english.gov.cn/archive/state_council_gazette/2015/06/08/content_281475123345680.htm.

⁵ Please see http://www.szse.cn/lawrules/publicadvice/t20180525_536657.html.

issue Panda Bonds in the CIBM. These requirements are generally consistent with those requirements for domestic financial institutions (including PRC banking financial institutions and other non-banking financial institutions) to issue financial bonds in CIBM.

Below, we summarize the substantial requirements for different kinds of overseas issuers under the Interim Measures:

	Overseas Financial Institutions	Foreign Government Agencies and International Development Institutions	Overseas Non-financial Enterprises
Approval/Registration	PBOC approval	NAFMII registration	NAFMII registration
Substantive Requirements	<p>Paid-in capital of no less than RMB10 billion or its equivalent;</p> <p>the issuer has good corporate governance mechanisms and a sound risk management system;</p> <p>the issuer has stable financial conditions, good credit, and has been continuously profitable for the last three years;</p> <p>the issuer has bond issuance experience and is able to pay any of its debts;</p> <p>the issuer is under effective supervision by the financial regulatory authorities of the country or region in which it is located, and the main risk monitoring indicators are in compliance with the regulations of such financial regulatory authorities.</p>	Foreign government agencies and international development institutions shall have bond issuance experience and are in good credit standing.	The Interim Measures are silent on substantive requirements for overseas non-financial enterprises.

IV. Issuance Methods and Applicable Conditions for Installment Issuances

The Interim Measures stipulate that Panda Bonds may be issued in the CIBM either in full or in installments up to an approved or registered amount.

Foreign government agencies, international development institutions, and overseas financial institutions may apply to issue Panda Bonds in the CIBM in installments up to the approved or registered amount if they are experienced in issuing bonds abroad or have issued bonds within China and have maintained continuous information disclosures for more than one year.

Overseas non-financial enterprises may apply to issue Panda Bonds in the CIBM in installments in accordance with the relevant NAFMII rules. Under the *Rules for the Registration and Issuance of Debt Financing Instruments of Non-financial Enterprises in the Interbank Bond Market* (《银行间债券市场非金融企业债务融资工具发行注册规则》)⁶, non-financial enterprises are to complete issuances within two months of registration. In the case of installment issuances, each subsequent issuance is filed with NAFMII two business days in advance.

V. Registration and Custody

The Interim Measures only prescribe principled provisions for the registration and custody of CIBM Panda Bonds. The Interim Measures stipulate that CIBM Panda Bonds are to be placed under the custody of certain PBOC-approved depositories. Upon completion of an issuance, issuers will timely confirm the debtor-creditor relationship with the depository, which will promptly handle the bond registration.

The China Government Securities Depository Trust & Clearing Co., Ltd. and the Shanghai Clearing House are the current depositories designated by the PBOC. In practice, most Panda Bonds are under the custody of the Shanghai Clearing House. As of 30 September 2018, there were about 70 Panda Bonds registered with the Shanghai Clearing House, including the Panda Bonds issued by foreign government agencies, overseas financial institutions and overseas non-financial enterprises⁷; there were only five Panda Bonds issued by the international development institutions registered with the China Government Securities Depository Trust & Clearing Co., Ltd.⁸.

VI. Foreign Exchange Administration

According to the Interim Measures, overseas institutions that have been approved or registered to issue bonds in China go through foreign exchange registration formalities. Account opening, fund remittance, cross-border transfer, information reporting and other matters regarding fundraising must comply with the relevant regulations of PBOC and the State Administration of Foreign Exchange.

⁶ Please see http://www.nafmii.org.cn/english/lawsandregulations/selfregulatory_e/201706/t20170623_61901.html.

⁷ Based on our public search on the website of Shanghai Clearing House (<http://www.shclearing.com>).

⁸ Based on our public search on the website of China Government Securities Depository Trust & Clearing Co., Ltd. (<http://www.chinabond.com.cn>).

We understand that matters relating to Panda Bond issuance fundraising accounts and cross-border transfers of renminbi capital proceeds will continue to be subject to the relevant provisions in the *Notice on Issues Concerning the Cross-border RMB Settlement of RMB Bonds Issued by Overseas Institutions within China* (《关于境外机构境内发行人民币债券跨境人民币结算业务有关事宜的通知》) issued by PBOC in 2016.

In addition, according to the *Notice on Issues Concerning Full-coverage Macro-prudent Management of Cross-Border Financing* (《关于全口径跨境融资宏观审慎管理有关事宜的通知》) issued by PBOC in 2017, Panda Bonds for self-use, i.e. renminbi bonds issued within China by the offshore parent company of a domestic non-financial enterprise (other than government financial platforms and the real estate enterprises) and lent back to a domestic subsidiary, are not subject to foreign debt limits.

VII. Bond Ratings

Bond ratings are not mandatory for the issuance of Panda Bonds in the CIBM. The Interim Measures stipulate that if an overseas institution chooses to publicly disclose credit rating reports, such reports shall be issued by an accredited national interbank market credit rating agency.

The *Announcement on the Operation of Credit Rating Business in the Interbank Bond Market by Credit Rating Agencies* (《关于信用评级机构在银行间债券市场开展信用评级业务有关事宜的公告》) issued by PBOC in 2017 and the *Rules on Evaluation and Registration of Credit Rating Agencies in the Interbank Bond Market* (《银行间债券市场信用评级机构注册评价规则》) issued by NAFMII in 2018, specify the CIBM qualification requirements for credit rating agencies (including both the domestic and international credit rating agencies). The large international credit rating agencies (e.g. Standard & Poor's, Moody's and Fitch Group) will be able to provide credit rating services for CIBM Panda Bonds upon passing the registration assessment according to the regulations and rules above.

VIII. Information Disclosures

The Interim Measures provide detailed regulations on the information disclosures for Panda Bonds issued in the CIBM, especially on the relevant accounting standards. The main points include:

- i. The principle of authentic, complete and equivalent disclosure:** The information disclosed by the issuer is to be authentic, accurate, complete and timely, and must not contain false records, misleading representations or major omissions. Based on the principle of equivalent disclosure, the important information disclosed by the issuer in other markets must also be disclosed to the CIBM concurrently or within the shortest reasonable time.

- ii. Disclosure requirements for private issuances:** For CIBM Panda Bonds which are only issued to specific investors, the receivers of information disclosures are limited to the investors of such Panda Bonds, and the issuance documents such as prospectuses or financial reports must not be disclosed to the public.
- iii. Accounting standards:** Before the issuance of the Interim Measures, the financial reports of Panda Bond issuers were required to be prepared in accordance with China Accounting Standards ("**CAS**") or such equivalent accounting standards, which was costly and time consuming for prospective overseas issuers. However, the Interim Measures to some extent ease the financial report requirements for private issuances of CIBM Panda Bonds and also set different disclosure requirements for different kinds of issuers in the case of public issuances.
1. For CIBM Panda Bonds publicly issued by international development institutions, the Interim Measures require the issuer to declare the accounting standards used in its financial reports in a prominent position in the prospectus and financial reports. In addition, if the disclosed financial reports are not prepared in accordance with CAS or other accounting standards that are recognized by MOF to be equivalent to CAS according to principles of reciprocity, the issuer is required to disclose the material differences between the accounting standards adopted and CAS.
 2. For the CIBM Panda Bonds publicly issued by overseas financial institutions and non-financial enterprises, the Interim Measures require the issuer to declare the accounting standards used in the financial reports in a prominent position in the prospectus and financial reports. If the disclosed financial reports are not prepared in accordance with CAS or equivalent accounting standards, the issuer will also be required to provide the following supplementary information:
 - (1) material differences between the accounting standards adopted and CAS; and
 - (2) a reconciliation of differences based on CAS, and an explanation of the financial impact of the accounting standard differences on all important items in the financial reports.

If the issuer only discloses its financial reports to the qualified institutional investors with whom the issuer has entered into a written private subscription agreement, the issuer may negotiate with the qualified institutional investors to determine the accounting standards to be adopted in the financial reports, but the issuer is required to fully disclose relevant risks in a written private subscription agreement and have the investors confirm their undertaking of such risks.

- iv. Audit Requirements (expanding the scope of approved auditors):** The Interim Measures stipulate that if an issuer adopts CAS to prepare its financial reports, it is required to engage a PRC accounting firm with qualifications for securities and futures

business to audit the financial reports. Where other accounting standards are adopted, a PRC accounting firm with qualifications for securities and futures business or a foreign accounting firm may be engaged for the audit provided that it meets the following conditions:

1. it is legally registered and established in the country or region where it is located, and has obtained the practice qualification for auditing business and is in normal practice;
2. it has a good international reputation and market recognition;
3. it has engaged in publicly issued securities-related audits in the country or region where it is located, and has more than five years of experience in auditing publicly securities issuances; and
4. other conditions or regulatory requirements set by MOF.

The reconciliation information adjusted in accordance with CAS provided by overseas institutions is required to be certified by a PRC accounting firm with qualifications for securities and futures business.

If the issuer engages a foreign accounting firm to audit the financial reports related to the CIBM Panda Bonds, the foreign accounting firm is required to file with MOF within 20 business days before submission of the Panda Bond issuance application, and such report filings will be annually updated with MOF during the term of the bond issue.

IX. Language Requirement

Under the Interim Measures, if the issuer publicly discloses the issuance documents, such documents are required to be in simplified Chinese or otherwise provided with a simplified Chinese translation.

X. Applicable Law

Prior to the issuance of the Interim Measures, the IDI Measures explicitly stipulated that any breach of contract or other disputes arising out of or in connection with the issuance of renminbi-denominated bonds within China by an international development institution was to be governed by PRC law. In practice, CIBM Panda Bonds issued by foreign government agencies, overseas financial institutions and overseas non-financial enterprises were also subject to PRC law by reference to this regulation. The Interim Measures do not set any compulsory requirement as to the application of law, and provide some flexibility for CIBM Panda Bond issuances by overseas institutions. This trend is in consistent with the general principle of choice of laws for cross-border bond issuances in other countries.

The Interim Measures respond to the calls of investors in the CIBM as well as of foreign institutions to issue specialized regulations relating to CIBM Panda Bonds. Most provisions of

the Interim Measures agree and are consistent with the currently applicable rules and practices relating to Panda Bonds. On the other hand, the Interim Measures provide more detailed and flexible operating rules (such as the rules on accounting standards and financial reports) for overseas institutions to issue Panda Bonds in the CIBM. However, some of the provisions are still too general for specific transactions. NAFMII may issue specific guidelines soon and we will continue to pay attention to relevant rules and guidelines and keep you updated.

The above is a preliminary introduction to the main points of the Interim Measures. If you need further information on the above matters, please contact:

Yang TieCheng (+86 10 8516 4286/+86 139 1089 5267; tiecheng.yang@hankunlaw.com);

Zhu Jun (+86 10 8525 4690/+86 135 8187 7026; jun.zhu@hankunlaw.com);

Wang Shu (+86 10 8525 5526/+86 139 1009 1821; shu.wang@hankunlaw.com);

Ge Yin (+86 21 6080 0966/+86 186 0175 1666; yin.ge@hankunlaw.com);

Wan Jun (+86 21 6080 0995/+86 139 1657 3412; jun.wan@hankunlaw.com).

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