

# Legal Commentary

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## Insights into the New Strategic Investment Management Measures

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On November 1, 2024, the Ministry of Commerce of the PRC (“**MOFCOM**”) and five other administrative authorities issued revisions to the *Measures for the Administration of Strategic Investment in Listed Companies by Foreign Investors* (the “**Measures**”), which make significant changes to the original version promulgated in 2005. As revised, the Measures lower the thresholds for foreign investment with respect to the scope of investors, asset requirements, investment methods, payment methods for consideration, shareholding ratios, and lock-up periods. The Measures are conducive to further expanding the channels for foreign investment in the securities market, unleashing the potential for attracting investment through strategic investment channels, encouraging foreign investment to conduct long-term and valued investments, and facilitating A-share listed companies to issue shares to foreign investors for mergers and acquisitions. The revisions to the Measures will come into effect on December 2, 2024. In this article, we present our insights into significant aspects of these revisions.

### Scope of Strategic Investments subject to the Measures

The Measures apply to foreign investors’ acquisition and medium- to long-term holding of A-shares of listed companies through the new shares issuance to specific investors, shares transfer by agreements, tender offers, and other methods stipulated by national laws and regulations (collectively, “**Strategic Investments**”). Compared with the original Measures, the revisions further expressly allow foreign investors to make Strategic Investments by tender offers.

The Measures do not apply to the following situations:

1. QFII and RQFII investments in listed companies;
2. investments in listed companies by stock connect schemes, such as Shanghai-Hong Kong Stock Connect, Shenzhen-Hong Kong Stock Connect, and Shanghai-London Stock Connect to purchase shares or depositary receipts;
3. acquiring A-shares of listed companies due in the IPO of the invested enterprise;
4. foreign natural persons who meet the relevant requirements buy and sell shares of listed companies in the secondary market or acquire shares of listed companies through equity incentives. For example, foreign natural persons who work in mainland China and whose securities regulatory

authorities of the country (region) to which they belong have established a regulatory cooperation mechanism with China Securities Regulatory Commission, acquire shares of listed companies in the secondary market, or foreign employees of domestic listed companies who work overseas may participate in equity incentives of listed companies.

Foreign investors who engage in Strategic Investments in companies listed on the National Equities Exchange and Quotations should refer to the Measures.

### Expanding the scope of foreign investors

Consistent with the *Foreign Investment Law of the PRC*, the scope of foreign investors in the revised Measures includes foreign natural persons, allowing foreign natural persons to make Strategic Investments in listed companies. The scope of foreign investors includes foreign natural persons, enterprises, or other organizations. The Strategic Investments in listed companies by the investors from the Hong Kong Special Administrative Region, Macao Special Administrative Region, and Taiwan Province, as well as the Chinese citizens residing abroad, should refer to and comply with the Measures.

### Specific requirements of foreign investors

Foreign investors who intend to make Strategic Investments should meet the following three requirements.

	Specific requirements in the revisions	Comparison
<b>Requirement one</b>	<ul style="list-style-type: none"> <li>■ Foreign enterprises or other organizations shall be established and operated in accordance with the law, with steady and stable financial condition, good credit, mature management experience, completed governance structure, good internal control system, and standardized business behavior.</li> <li>■ Foreign natural persons shall have the corresponding ability to identify and bear risks.</li> </ul>	The requirements for foreign enterprises or other organizations are consistent with the original Measures. New requirements for foreign natural persons are added.
<b>Requirement two</b>	<ul style="list-style-type: none"> <li>■ The total actual assets shall be no less than US \$50 million or the total actual assets under management shall be no less than US \$300 million.</li> <li>■ If the foreign investors become the controlling shareholder of a listed company, the total actual assets shall be no less than US \$100 million or the total actual assets under management shall be no less than US \$500 million.</li> <li>■ If the total actual assets or the total actual assets under management of foreign enterprises or other organizations do not comply with the above-mentioned assets requirement, but their wholly-owned investor (referring to foreign natural</li> </ul>	<p>This revision reduces the asset requirement for foreign investors which make Strategic Investments as non-controlling shareholders, while the assets requirement for Strategic Investors who become controlling shareholders are consistent with the original Measures.</p> <p>Foreign investors who meet the asset requirement will continue to be allowed to make Strategic Investments</p>

	Specific requirements in the revisions	Comparison
	persons, enterprises or other organizations wholly owning the aforementioned entities) applies with the above-mentioned assets requirement, then the foreign investors can conduct Strategic Investment, but at the same time, the wholly-owned investor shall make a commitment or agree with the foreign enterprise or other organization to jointly bear responsibility for the relevant investment activities.	through overseas subsidiaries on the premise of jointly bearing responsibility.
<b>Requirement three</b>	<ul style="list-style-type: none"> <li>■ In the past three years, foreign investors have not been subject to any domestic or foreign criminal penalties or serious penalties by regulatory agencies. If the enterprise or other organization has been established for less than three years, it shall be counted from the date of establishment.</li> </ul>	Compared with the original Measures, there is added a new requirement of not being subject to any criminal penalties domestically and internationally.

### Cross-border share exchanges – consideration and requirements

The original Measures do not contain relevant provisions on cross-border share exchanges. In principle, mergers and acquisitions of domestic enterprises through cross-border share exchanges were required to be the equity of overseas listed companies, according to the *Provisions on Merger and Acquisition of Domestic Enterprises by Foreign Investors*. As revised, the Measures broaden the consideration eligible for cross-border share exchanges to attract foreign investors to make Strategic Investments in listed companies through cash, equity, and other means and also to facilitate the acquisition of overseas assets by A-share listed companies through cross-border share exchanges. Meanwhile, taking into account the existing regulatory rules for issuance to specific investors and tender offers to ensure the fairness of the transaction, foreign investors are allowed to use the shares of either overseas listed companies or non-listed companies as the payment consideration for Strategic Investments implemented through the issuance to specific investors of new shares and tender offers. However, only the shares of overseas listed companies can be used as payment consideration for Strategic Investments executed through shares transfer by agreements.

Referring to the relevant conditions for cross-border share exchanges according to the *Provisions on Merger and Acquisition of Domestic Enterprises by Foreign Investors*, the revised Measures stipulate that foreign investors who make Strategic Investments in listed companies by means of cross-border share exchanges should further comply with the following requirements:

1. the overseas company shall be legally established, the place of registration has a consummate corporate legal system, and the overseas company and its management have not been seriously punished by domestic or foreign regulatory authorities in the past three years; if the Strategic Investment is conducted through shares transfer by agreements, the overseas company must be a listed company;
2. the foreign investors legally hold the equity of the overseas company and can be transferred according

to laws and regulations, or the new shares legally issued by foreign investors;

3. comply with the *Securities Law of the PRC*, the *Company Law of the PRC* and the relevant regulations of the State Council, the securities regulatory authority of the State Council, the stock exchanges and securities registration and clearing institutions;
4. comply with the relevant regulations of the state on overseas investment management and complete relevant procedures.

Under the above circumstances, when the foreign investors conduct the registration formalities for the acquired shares of the A-share listed company, the foreign investors shall submit the certification materials that the relevant formalities for the domestic investors' overseas investment have been completed, which means, the overseas investment formalities for the domestic investors to acquire the shares of the overseas company in the cross-border share exchanges payment shall be completed before the foreign investors acquire the shares of the A-share listed company.

The use of unlisted overseas company shares as transaction consideration is subject to certain rules to ensure fairness in the transaction. According to relevant provisions of the *Company Law of the PRC*, and the relevant provisions of listed companies refinancing and asset acquisition, the shares of overseas companies used as consideration for the subscription of new shares issued by A-share listed companies shall be appraised, and the listed companies and their intermediaries are required to fully verify and disclose the assets, financial situation, and basis for valuing the overseas companies whose shares are to be used as consideration. As for tender offers, according to the relevant provisions of the *Measures for the Administration of Acquisition of Listed Companies*, foreign investors shall provide audited financial accounting reports for the past three years and share a valuation report of the overseas company to which the consideration shares belong, cooperate with the due diligence work of the independent financial consultant hired by the listed company, and at the same time provide cash options to shareholders of the listed company participating in the tender offers.

## Shareholding ratio

The original Measures stipulated the first Strategic Investment involving a foreign investor should involve more than 10% of the listed company's equity.

The revised Measures do not set up additional shareholding ratio requirements for foreign investors that make Strategic Investments, but retain the shareholding ratio consistent with the requirements for such transactions, namely:

1. there is no shareholding ratio requirement for issuance to specific investors, but if foreign investors participate as strategic investors in the issuance of a listed company, the foreign investors should still comply with the requirements of *Opinions No. 18 on the Application of Securities and Futures Laws*, which require that strategic investors hold a relatively large proportion shares of the listed companies (the exact amount is unstated);
2. for shares transfer by agreements, the proportion of shares acquired may be no less than 5%;

3. for tender offers, the scheduled acquisition may be no less than 5%.

### **Lock-up period**

The revised Measures reduce the lock-up period from 3 years to 12 months for foreign investors who make Strategic Investments. This shortened lock-up period will not apply to foreign investors whose Strategic Investments were completed before the revisions take effect. The Measures have no special restrictions on the disposition of A-shares acquired by Strategic Investment, and foreign investors will still need to comply with the relevant regulations on disposing of A-shares.

Foreign investors may make public commitments in accordance with the requirements of intermediaries, listed companies, or related parties. If a Strategic Investment does not comply with the Measures, is made through false statements, or by other unlawful means, the foreign investor is barred for 12 months following rectification of the non-compliance from transferring, donating or pledging the shares of the listed company involved, participating in dividends, exercising voting rights, or influencing the voting of the shares of the listed company.

The 12-month lock-up period notwithstanding, a foreign investor may still be subject to a longer lock-up period in accordance with other laws or regulations. For example:

1. an 18-month lock-up period applies if the foreign investor's Strategic Investment constitutes the acquisition of control of a listed company;
2. an 18-month lock-up period applies if the Strategic Investment of foreign investors, as controlling shareholders, actual controllers or their controlled affiliates of listed companies, or will be controlling shareholders of listed companies by subscribing for the shares issued this time, or as "strategic investors" by "a locked-price issuance";
3. a three-year lock-up period applies for foreign investors who acquire new shares issued by a listed company which result in the shares owned by the foreign investors in the listed company exceeding 30% and the shareholders meeting agrees to exempt the tender offers obligation.

In addition, the wholly-owned investor of an overseas company shall be subject to all the above-mentioned lock-up period where it meets the asset requirements (see Requirement 2 of "Specific Requirements of Foreign Investors" above) but makes a Strategic Investment through an overseas company that does not meet this requirement after the Strategic Investment is completed, and under this circumstance, if the wholly-owned investor transfers the equity of the overseas company, the new transferee should still comply with the foreign investor's requirements stipulated in the Measures, assume the rights and obligations of the wholly-owned investor and the foreign investor in the listed company, and perform information disclosure obligations and other obligations in accordance with the laws and regulations.

### **Strategic Investments not to require MOFCOM approval or filing**

In general, there are no substantive differences between administrative procedures for foreign and non-foreign investors that engage in Strategic Investments with listed companies, whether by issuance to specific investors, shares transfer by agreements, or tender offers.

The revisions to the Measures conform to the *Foreign Investment Law of the PRC*, which entered into effect in 2020 and abolished blanket approval and filing requirements for unique to foreign investors, such as establishing and altering foreign-invested enterprises and Strategic Investments in A-share listed companies. The Measures clarify that foreign investors or listed companies that implement Strategic Investment should submit investment information to the relevant MOFCOM department after the listed company completes the issuance, the shares transfer by agreements, or the tender offers, and when the shareholding ratio of foreign investors changes by more than 5% or the foreign holding or relative holding position changes after the Strategic Investment is completed, which are consistent with the requirements of the *Foreign Investment Law of the PRC* and the *Measures for Reporting Foreign Investment Information*.

### **Compliance with other domestic regulatory requirements**

In addition to the above-mentioned requirements, shareholding ratio, lock-up periods, and other provisions, foreign investors who make Strategic Investments in A-share listed companies also need to comply with the laws and regulations regarding foreign investment, state-owned assets management, concentrations of undertakings, foreign exchange, taxation, national security review, financial supervision, fulfillment of information disclosure obligations, foreign investment information reporting, and other domestic legal regulatory requirements.

### **Verification opinions of Third-party Consultants**

When making a Strategic Investment, the foreign investors and listed companies should engage financial advisory institutions, sponsors, or law firms (“**Third-party Consultants**”), registered in mainland China comply with provisions of the *Securities Law of the PRC* to conduct a due diligence investigation into the Strategic Investment with respect to the following requirements of the Measures, express clear opinions, and respectively state the number of shares and shareholding ratio of the listed companies acquired and held by the foreign investors and the persons acting in concert with them.

1. compliance with foreign investor requirements;
2. whether the transaction constitutes a cross-border share exchange, and whether it complies with the applicable requirements;
3. whether the investor has made a public commitment to extend the share lock-up period and to restrict share rights with respect to non-compliant Strategic Investments;
4. whether the transaction affects or may affect the national security; and
5. whether the transaction involves the negative list and complies with the relevant requirements for foreign investment.

If a Strategic Investment is conducted through shares transfer by agreements or tender offers, the foreign investor should engage Third-party Consultants to issue a report which verifies these particulars. If the Strategic Investment is conducted through the issuance to specific investors by a listed company, the foreign investor should engage Third-party Consultants to issue a report on 1 to 3, above, and the listed company should engage Third-party Consultants to issue a report on 4 and 5, above.

**Conclusion**

Foreign investors have made more than 600 Strategic Investments in listed companies since the Measures were first promulgated in 2005, according to a press briefing held by MOFCOM and the five other administrative authorities. In our view, this revision to the Measures will continue to promote China's high-level opening up and make greater efforts to attract and utilize foreign capital to invest in listed companies, which will contribute to the healthy and stable development of Chinese capital market.

## ***Important Announcement***

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