



China Regulatory Updates

February 2010

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- › *Unique player in the PRC legal service market*
- › *Simplicity, but always with a focus on key points and attention to details*

Our Values

- › *Professionalism*
- › *Cost Efficiency and Effectiveness*
- › *Constant Self-Improvement Towards Perfection*



Foreign Investment

Rules on Registration of Foreign Invested Partnerships Released

Compliance Requirements for PRC Representative Offices of Foreign Enterprises Enhanced

State Council Issues New Measures to Encourage Foreign Investments

Securities

Experimental Margin Trading and Stock Index Futures Trading Soon to Be Launched

Insurance

Two New Rules on Insurance Companies Released

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Foreign Investment

Rules on Registration of Foreign Invested Partnerships Released

On February 2, 2010, PRC State Administration for Industry and Commerce (“SAIC”) released the *Provisions on the Administration of the Registration of Foreign Invested Partnership Enterprises* (the “Provisions”). As a supporting rule for the *Measures on the Administration of the Establishment of Partnership Enterprises by Foreign Enterprises or Individuals in China* issued in December 2009, the Provisions elaborate on the registration requirements and procedures of foreign invested partnerships (“FIPs”), but ambiguity still remains as certain issues are still not clearly addressed or specified. The key features of the Provisions are as follows:

(a) Market Entry Policies.

FIPs engaging in the following industries are prohibited to be registered: (i) industries where foreign investment is prohibited by the *Catalogue for the Guidance of Foreign Investment Industries*, or (ii) industries where foreign investment is not prohibited but is restricted by additional requirements such as “equity and/or cooperative joint venture only”, “controlling stakes or relative controlling stakes to be held by the Chinese investor”, or “limit on shareholding ratio of foreign investor” as set out in the *Catalogue for the Guidance of Foreign Investment Industries*.

Han Yi Observation: The scope of industries that FIPs can engage in is much smaller than that of foreign invested enterprises (“FIEs”). In other words, foreign investment in certain industries can only take the form of equity or contractual joint venture instead of FIP.

(b) Registration Procedures.

FIPs engaging in sectors that are encouraged or permitted for foreign investment can be directly registered with the local SAIC offices at the place where the FIPs are located. If a prior approval from the authority in charge of the business activities or projects to be engaged in by an FIP is required by applicable PRC law, such prior approval should be obtained before the FIP is registered with the competent SAIC office. If an FIP is proposed to be engaged in a business sector that is restricted for foreign investment but no prior government

approval is required, the relevant SAIC office should firstly consult with the authority in charge of such business sector with respect to the establishment and registration of the FIP. FIPs will be subject to administrative penalties if they engage in business activities that are restricted or prohibited for foreign investment without registration with the competent SAIC office in advance.

Han Yi Observation: The time period for the SAIC office's consulting process with the authority in charge of business sectors restricted for foreign investment with respect to the establishment of an FIP is not specified and such process may unpredictably prolong the whole registration process in practice. Furthermore, the Provisions do not address whether an FIP can make equity investment in other entities in China if “equity investment” is not clearly included in its business scope registered with the SAIC office.

(c) Capital Contribution.

The Provisions do not make any specific requirement on the minimum amount of registered capital and the term of capital contribution for the establishment of an FIP, which is quite different from those for FIEs. As to the forms of capital contribution to an FIP, in addition to foreign currency and lawfully obtained RMB cash, in-kind contributions are also permitted. It is noteworthy that for FIPs' general partners that are foreign citizens, personal services are also permitted as a form of contribution, subject to the rules issued by national-level authorities with respect to foreign employees in China.

Han Yi Observation: The above mentioned provisions are generally consistent with the currently effective PRC Partnership Law. As a partnership, FIPs do not need to comply with strict contribution schedules mandatorily required by law as FIEs do. Partners are free to determine the contribution amount and schedule in their partnership agreement.

(d) Investment FIPs.

FIPs with investment as their principal business (the

“Investment FIPs”) should register their establishment with the SAIC offices at provincial level. Any domestic investment made by such FIPs should be handled pursuant to applicable laws, regulations and rules applicable to foreign investment.

Han Yi Observation: Although the Provisions have made it clear that an Investment FIP may be duly registered in China, it is still unclear whether a prior approval should be obtained from the offices of PRC Ministry of Commerce (“MOFCOM”) or any other government department for registration of the Investment FIP. Please note that although the local governments of certain regions in China have

promulgated rules on Investment FIPs, there is no nation-level legal basis for the operation and administration of Investment FIPs so far. Furthermore, ambiguity still remains as to whether the equity investment made by Investment FIPs should be treated as foreign investment or FIEs’ investment and how the Investment FIPs can settle the foreign partners’ capital contributions in foreign exchange. As the Provisions only focus on the registration requirements and procedures of FIPs with SAIC offices, people will have to wait for other authorities (including without limitation, MOFCOM and PRC State Administration of Foreign Exchange) to issue separate rules to solve the aforesaid operational issues of FIPs.

Compliance Requirements for PRC Representative Offices of Foreign Enterprises Enhanced

On January 4, 2010, SAIC and PRC Ministry of Public Security jointly issued the *Notice on Further Strengthening the Administration of the Registration of Resident Representative Offices of Foreign Enterprises*(the “Notice”), in a bid to tighten up scrutiny on foreign rep. offices.

The Notice has included the following new compliance requirements: (i) any foreign company intending to establish a rep. office in China should have validly existed for at least 2 years and should submit its duly notarized and authenticated certificate of incorporation ; (ii) a rep. office should generally have no more than 4 representatives

(chief representative included). Representatives of existing rep. offices will be generally kept even if the number of such representatives is over 4, but no additional representative can be appointed; and (iii) the local offices of SAIC should do spot checks on newly established rep. offices within 3 months after issuance of the registration certificate to verify the relevant registered information. The Notice reiterates that the validity period of a rep. office’s registration certificate is one year, which period can be renewed in each year. Moreover, the SAIC offices may impose fines on rep. offices for their conduct of any profit-making business activities.

State Council Issues New Measures to Encourage Foreign Investments

The State Council has recently publicly declared to put forward new measures to boost foreign investment. In an effort to attract more foreign investment into China, the State Council will further relax restrictions on foreign investment. The highlights of the new measures are as follows:

(a) The *Catalogue for Guidance of Foreign Investment Industries* will undergo another round of amendments to lift certain existing restrictions on foreign investment. Foreign investors are encouraged to invest in sectors of high-end manufacture, hi-tech, modern service, new energy, and energy conservation and environment protection. Measures contained in the nationwide industrial adjustment and revitalization plans are also applicable to qualified FIEs. Priority to land supply will be

given to foreign invested projects of intensive land utilization in the encouraged industries.

(b) Foreign investors are encouraged to invest in labor intensive industries in central and western China in line with relevant environment protection requirements. FIEs will enjoy more governmental supports in terms of investment policies, technologies and funds.

(c) Foreign investors are encouraged to participate in the restructuring and reorganization of domestic companies by way of M&A. The experimental operation of foreign invested guarantee company for medium and small sized enterprises will follow a faster schedule.

(d) The number of government approvals related to

FIEs will be further reduced and the transparency of approval process will be improved.

- (e) The development of various industrial development zones will be further streamlined

and strengthened, and the establishment of border economic cooperative zones will be expedited. The forex settlement procedures of capital contributed by foreign investors will be simplified.

Securities

Experimental Margin Trading and Stock Index Futures Trading Soon to Be Launched

Recently, the State Council has approved in principle the launch of the experimental margin trading by selected securities firms as well as the operation of stock index futures (the “SIF”). This new move could help stabilize stock prices by allowing selling short on the A-share markets, and promote the development of the Chinese securities market.

The China Securities Regulatory Commission (“CSRC”) has recently promulgated the *Guidelines on Launch of Experimental Margin Trading Business by Selected Securities Firms* (the “Guidelines”). According to the Guidelines, selected securities firms should formulate their own thresholds for qualified clients, including the minimum capital amount, securities investment related experience and risk management capacity, and etc. The margin trading should only be open to such selected securities firms’ existing clients that have maintained their securities accounts for at least 18 months. It seems that, unless otherwise required by CSRC, QFIIs will be likely permitted to participate in margin trading, if (i) the securities

firms they open their accounts with are among the selected firms (*the list of selected firms is reportedly to be determined in March*); and (ii) they can satisfy the relevant requirements stipulated by such securities firms.

As for SIF trading, pursuant to the draft *Provisions on Establishment of Adequacy Rules for Investors Engaged in Stock Index Futures Trading* issued by CSRC, legal person investors and other types of economic organizations are all permitted to engage in SIF trading. However, according to the draft *Trial Implementing Measures on Adequacy of Investors Engaged in Stock Index Futures Trading* issued by the China Financial Futures Exchange, QFIIs, securities firms and fund management companies should secure CSRC’s approval before engaging in SIF trading. As there are no rules issued by CSRC on the approval of QFII’s participation in SIF trading so far, it can be concluded that QFIIs cannot engage in SIF trading at the current stage until CSRC further spells out the approval requirement and relevant procedures.

Insurance

Two New Rules on Insurance Companies Released

1. *Insurance companies permitted to invest in unsecured corporate bonds on domestic intra-bank market*

The China Insurance Regulatory Commission (“CIRC”) has lately issued the *Circular on Matters Related to Insurance Institutions’ Investment in Unsecured Corporate Bonds* (the “Circular”) and insurance capital is permitted for the first time to invest in unsecured corporate bonds with a

long-term credit standing rated as AAA (or its equivalent) that are issued on the domestic intra-bank market .

The Circular has however put various limits on the maximum investment amount of unsecured bonds: (i) to the extent permitted by existing rules, the balance of the amount of unsecured corporate bonds purchased with insurance funds should not exceed 20% of the net assets of the issuer; (ii) the

balance of the amount of unsecured corporate bonds purchased by an insurance company from its affiliated issuers should not exceed 10% of the net assets of such insurance company; (iii) with respect to any specific unsecured bond product, the amount purchased by insurance companies under the same insurance group in the same round of issuance should not exceed 60% of the total amount issued in this round. In practice, however, since currently most of the unsecured corporate bonds are not issued by way of public bidding as required by the Circular, insurance companies could not invest in unsecured corporate bonds now.

2. *Qualifications of directors, supervisors and senior executives of insurance companies further regulated*

On January 26, 2010, CIRC circulated the newly amended *Measures on Administration of Qualifications of Directors, Supervisors and Senior Executives of Insurance Companies*, which will come into force on April 1, 2010, to further supplement, and comply with, the *PRC Insurance Law* that took effect in 2009.

The major amendments include the following: (i) the thresholds on years of professional experience are raised and further emphasized for certain positions; (ii) compliance requirements for senior executives are expanded; and (iii) insurance companies are required to establish formal employment relationship with senior executives.

For further information, please write us at inquiry@hanyilaw.com.

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