



# China Regulatory Updates

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## FOREIGN INVESTMENT

## MOFCOM Solicits Public Comments on Draft Measures Concerning FIE Equity Contribution

According to the requirements of “promoting the diversified utilization of foreign investments” under Circular 9 issued by the State Council in 2010, on May 4, 2011, MOFCOM issued the *Measures for Administration of Equity Contribution to Foreign-Invested Enterprises* (Draft for Public Comments) (the “Draft”), which makes detailed and systematic stipulations on issues related to capital contribution made to foreign-invested enterprises (“FIE”) in the form of equity. Basically, MOFCOM offices would not approve application for equity contribution to an FIE due to lack of implementing details.

According to the Draft, if a domestic or foreign investor (the “Investor”) makes capital contribution with the equity held by it in a domestic enterprise (“Equity Enterprise”) and (i) establishes an FIE through green field investment, (ii) converts a domestic funded enterprise into an FIE through capital increase, (iii) causes equity change to an FIE through capital increase (such FIE, the “Investee Enterprise”), the following requirements should be met:

- (a) the equity to be contributed should have clear and complete title and can be legally transferred; the equity may not be contributed if (i) the registered capital of the Equity Enterprise has not been duly paid off, (ii) the equity has been pledged, (iii) the equity has been frozen according to law, (iv) the equity may not be transferred according to the articles of association or other provisions, or (v) the Equity Enterprise is a foreign invested investment enterprise or a foreign invested

venture capital (equity) investment enterprise;

- (b) the equity contribution will not cause cross equity holding between the Investee Enterprise and the Equity Enterprise;
- (c) the amount of equity contribution and other non-monetary contributions made by all shareholders of the Investee Enterprise should not exceed 70% of its registered capital; and
- (d) after the equity contribution is made, the business scope of the Equity Enterprise and the Investee Enterprise and their directly or indirectly held enterprises should comply with the *Catalogue for Guidance of Foreign Investment Industries* and other relevant regulations regarding foreign investments; in case of any noncompliance, the relevant assets or equity should be carved out before the application for equity contribution.

According to the Draft, the provincial MOFCOM or central MOFCOM should be responsible for approval of equity contribution based on their respective approval authority. The provincial MOFCOM at the place where the Investee Enterprise is located shall have approval authority over equity contribution (i) where the Investee Enterprise is an FIE, and the equity contribution will not cause a change of control from the Chinese party to the foreign party, and (ii) made in the service sectors except for those explicitly subject to central MOFCOM approval.

## SAFE Issues New Operating Rules on Foreign Exchange Registration of Round-Trip Investments by Domestic Residents

In order to further clarify the principles of administration and issues related to the application of the SAFE *Circular on Relevant Issues Regarding Foreign Exchange Control over Financing and Round-Trip Investments by Domestic Residents Through Offshore Special Purpose Vehicles* (HUI FA [2005] No. 75; “Circular 75”) and to simplify relevant operating procedures, on May 27, SAFE issued the *Operating Rules on Foreign Exchange*

*Control over Financing and Round-Trip Investments by Domestic Residents through Overseas Special Purpose Vehicles* (HUI FA [2011] No. 19; “Circular 19”), which will become effective as of July 1, 2011. Meanwhile, with respect to the current operating details of Circular 75 (i.e., HUI ZONG FA [2009] No. 77; “Circular 77”), if any provisions thereof related to foreign exchange registration of round-trip investments by domestic residents are inconsistent

with Circular 19, such provisions should be repealed.

Compared to Circular 77, Circular 19 has more detailed and explicit stipulations on issues such as the relevant foreign exchange registration of special purpose vehicles set up by domestic individuals, the foreign exchange registration of establishment and acquisition of domestic enterprises and approval for record of income from capital change.

For example, Circular 19 specifies the registration of round-trip investments by non-special purpose vehicles and clarifies once again the additional items required in foreign exchange registration of special purpose vehicles set up by domestic individuals. Circular 19 will deal with common issues related to foreign exchange registration of round-trip investments by domestic residents through offshore entities, and will facilitate SAFE offices to effectively monitor round-trip investments.

## SECURITIES/M&A

### CSRC to Revise Supporting Rules on Asset Restructuring Involving Listed Companies

CSRC issued the *Decision on Revising the Relevant Rules regarding Material Assets Restructuring and Supporting Financing of Listed Companies* (Drafts for Comments) (the "Draft") on May 13, 2011, with an aim to revise the *Measures for Administration of Material Assets Restructuring of Listed Companies* and other relevant regulations on assets restructuring and supporting financing of listed companies (the "Measures"), so as to further regulate back-door listing, improve the system of asset purchase by way of share issuance and provide policy support for M&A financing and restructuring.

(a) Requirements for Back-Door Listing Tend to Be Similar to IPO

The Draft makes explicit definition on back-door listing, which refers to the transaction where, from the date of change of control, the total assets purchased by a listed company from the acquirer account for at least 100% of the total assets of such listed company specified in the audited consolidated financial statements for the latest accounting period. Meanwhile, the Draft raises the regulatory requirements for back-door listing: (i) the acquiring company should have operated for at least three years consecutively, have aggregate profits exceeding RMB20 million for the latest two accounting years and have been profitable for each of these two accounting years, (ii) after the back-door listing, the listed company should be independent from its controlling shareholder, actual controlling party and other related parties in terms of business, assets, finance, staff and etc., and there should be no horizontal competition or other apparently unfair related-party transaction, and (iii) the back-door listing should comply with PRC

industrial policy, and specific industries such as finance, venture capital investment should be subject to CSRC separate rules. In addition, CSRC also strengthens the ongoing supervision of back-door listing companies by independent financial advisors, and requires that the period of ongoing supervision should be at least three accounting periods from the date of CSRC approval.

(b) Improve the System of Asset Purchase by Share Issuance

According to the Draft, in order to promote industrial integration and enhance synergy with existing principal business, to the extent there is no change of control, a listed company may purchase assets by share issuance to specific parties other than its controlling shareholder, actual controlling party or related parties controlled by it, provided that, for the sake of resource allocation efficiency, the following conditions should be met: (i) the number of shares to be issued should not be less than 5% of the total shares of the listed company after such issuance; or (ii) the transaction amount of the assets to be purchased by an enterprise listed on main board or SME board should not be less than RMB100 million, and the transaction amount of assets to be purchased by a ChiNext listed company should not be less than RMB50 million.

(c) Support Concurrent Operation of Material Assets Restructuring and Supporting Financing of Listed Companies

The Draft has lifted restrictions that the material assets restructuring and supporting financing of listed companies should be operated separately,

and explicitly provided that a listed company may raise some supporting funds when it purchases assets by share issuance, which are used to pay

part of the consideration and provide working capital to enhance the integrated performance of the material assets restructuring, and etc.

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