

China Regulatory Updates

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1. MOFCOM Further Delegates Its Approval Authority to Lower Level Offices

In March 2009, the PRC Ministry of Commerce (“MOFCOM”) has consecutively effectuated 3 circulars (the “FIE Circulars”) to further delegate certain authority related to foreign invested enterprises (“FIEs”) to MOFCOM offices at provincial and municipal levels and the nation-level economic and technological development zone (“ETDZ”) administrations.

Highlights of the FIE Circulars include, among others:

- (a) Incorporation of an onshore branch by an FIE is only subject to the registration procedure with the competent local MOFCOM office where such FIE is incorporated (except for circumstances where approvals by local MOFCOM offices are explicitly required pursuant to applicable laws);
- (b) For FIEs that fall into encouraged category for foreign investments and do not need government balancing efforts on nationwide basis, the incorporation of and the subsequent changes with respect to such FIEs are only subject to approval by relevant provincial level MOFCOM offices or the ETDZ administrations regardless of their total investment amounts;
- (c) Establishment of an offshore branch or subsidiary by an FIE is subject to the approval from the relevant MOFCOM offices at provincial level (or municipal level if duly authorized by the provincial level government) and a written consent from the commercial section of the Chinese embassy/consulate office where such offshore setup will be located;
- (d) Except for projects that are subject to approval by the National Development and Reform Commission due to their size and nature and projects that will result in a change of control from the PRC side to the foreign side, all changes concerning an FIE originally examined and approved by the central MOFCOM office will generally be examined and approved by the relevant local MOFCOM offices;

- (e) On the foreign-invested investment companies (or holdcos), provincial level MOFCOM offices will generally have the authority to examine and approve (i) the setup and the subsequent changes and alterations so long as the holdco's registered capital does not exceed US\$100 million; and (ii) all changes and alterations of any holdco approved by the central MOFCOM office except where any single incremental capital increase exceeds US\$100 million or there occurs a change with the foreign parent's identity; and
- (f) On the foreign-invested venture capital investment enterprises ("FIVCIEs") and foreign-invested venture capital management enterprises ("FIVCMEs"), provincial MOFCOM offices and ETDZ administrations should generally have the authority to examine and approve (i) the incorporation and the subsequent changes of FIVCIEs and FIVCMEs with registered capital of no more than US\$100 million, and (ii) subsequent changes of FIVCIEs and FIVCMEs approved by the central MOFCOM office except where any single incremental capital increase exceeds US\$100 million or there occurs a change with the indispensable investor's identity.

2. Control Over PRC Enterprises' Outbound Investments Softened

Also in March 2009, the MOFCOM released the *Measures on Administration of Outbound Investments* (the "Outbound Measures"), which will become effective on May 1, 2009, in an effort to greatly reduce and simplify the approval procedures for outbound investments by domestic enterprises.

According to the Outbound Measures, domestic enterprises are required to submit application materials to and secure an approval from the central MOFCOM office only if the outbound investment: (i) will be made in countries that have no diplomatic relationship with China; (ii) will be made in other specific countries/areas (to be determined by MOFCOM, the PRC Ministry of Foreign Affairs and other relevant authorities); (iii) requires the PRC investor to invest an amount of US\$100 million or more; (iv) involves interests of multiple countries/areas; or (v) needs to establish offshore special purpose vehicles.

Local enterprises should submit application materials to and secure an approval from the competent provincial level MOFCOM office if the outbound investment: (i) requires the PRC investor to invest an amount between US\$10 million and US\$100 million; (ii) involves energy and mineral resource sectors; or (iii) is intended to attract funds from China.

For other outbound investments not included in the above provisions, investors will generally only need to fill in and submit application forms to MOFCOM (for companies directly administered by central government authorities) or the provincial level MOFCOM offices (for all other companies) for examination and approval. Decisions on whether or not to approve such applications will now need to be made by the MOFCOM offices within 3 working days.

3. Transfer of State-Owned Assets of Financial Enterprises Regulated

On March 17, 2009, the PRC Ministry of Finance (“MOF”) issued the *Measures on the Transfer of State-Owned Assets of Financial Enterprises* (the “Transfer Measures”) to regulate the transfer of PRC state-owned assets of qualified unlisted financial enterprises and the transfer of PRC state-owned shares of listed financial enterprises. The Transfer Measures will take effect on May 1, 2009.

According to the Transfer Measures, when a PRC state-owned or state-controlled unlisted financial enterprise intends to transfer its equity interests in its immediate subsidiaries, the approval from competent MOF offices should be obtained. As to the transfer of PRC state-owned shares of listed financial enterprises, the approval from the competent MOF office is required if: (i) the transferor is the controlling shareholder; or (ii) the transferor is not the controlling shareholder but has transferred, on a net and cumulative basis, at least 5% of the total shares of the listed financial enterprise within one year.

The Transfer Measures also provide that the transfer should be conducted through duly-established property right exchanges or securities trading systems. The Transfer Measures further provide that transfer by agreement is not permitted unless applicable laws have special qualification requirements for the transferee or under certain special circumstances (such as internal reorganization within a group company), in each case subject to approval by the State Council or the competent MOF office, as applicable.

4. Eligibility Requirements for Foreign Investors' Tax Treaty Treatment for Dividend Incomes Clarified

The PRC State Administration of Taxation (“SAT”) has recently issued the *Circular on Certain Relevant Issues Related to Implementation of Terms on Dividends under Tax Treaties* (the “Dividend Circular”), clarifying foreign investors’ entitlement to the income tax treatments provided under China’s tax treaties.

The Dividend Circular provides that, although according to relevant tax treaties by and between China and other countries/regions, tax residents of such countries/regions (the “Foreign Residents”) are entitled to the preferential income tax rate set forth in the relevant tax treaties for dividends they receive from PRC enterprises (the “PRC Entity”), so long as they own 25% (or 10%, as applicable) equity interests in such PRC Entity, the following requirements should also be satisfied, if any Foreign Resident intends to enjoy the treatment as set forth in the relevant tax treaty:

- (a) The Foreign Resident should be a corporate person as required by relevant tax treaty;
- (b) Among all owners’ equity and voting shares in the PRC Entity, the proportion directly held by such Foreign Resident should have reached the standard percentage as required by the relevant tax treaty; and
- (c) At any time during the 12 consecutive months before the Foreign Resident receives the dividends, the proportion directly held by such Foreign Resident in the PRC Entity’s registered capital should have complied with the standard percentage as required by the relevant tax treaty.

The Dividend Circular also provides that any transaction or arrangement structured or designed mainly for treaty-shopping purpose will not entitle the Foreign Resident to the preferential income tax rate as provided in the tax treaty. If the Foreign Resident has inappropriately enjoyed such preferential treatment, the competent tax authority is empowered to adjust the income tax payment obligation applicable to such Foreign Resident.

5. Statutory Minimum Taxable Gross Profit Margins for Real Estate Developers Lowered by 5 Percentage Points

On March 9, 2009, SAT issued the *Measures on the Treatment of Enterprise Income Tax on Real Estate Development and Operation* (the “EIT Measures”). According to the EIT Measures, real estate developers can see 5 percentage points drop in their statutory minimum taxable gross profit margins for their sales of the construction-in-process in three different categories of locations, i.e., the statutory minimum taxable gross profit margin shall not be lower than: (i) 15% if the project is located in provincial capital cities and cities with independent planning authority; (ii) 10% if the project is located in other cities; or (iii) 5% if the project is located in all other areas. The EIT Measures would have retrospective effect since January 1, 2008.

6. China to Launch GEM Board

On March 31, 2009, the China Securities Regulatory Committee (“CSRC”) issued the *Interim Measures on Administration of Initial Public Offerings and Listings on the GEM Board* (the “GEM Board Measures”), aiming to launch the second board for small and medium-sized companies to raise funds. The GEM Board Measures will take effect on May 1, 2009. It is reported that CSRC will soon start to accept applications for GEM board listings after all necessary preparatory works are completed and hopefully the GEM board will be in operation as early as the coming August.

According to the GEM Board Measures, candidates seeking IPO on the GEM board should satisfy various requirements, including among others: (i) being a joint-stock limited liability company with the operation history not shorter than 3 years on consecutive basis; (ii) consecutively posting profits in the latest 2 years with a aggregate net profit of at least RMB10 million with continuous increase momentum, or at least RMB5 million in the latest year with a business revenue of at least RMB50 million in the latest year and the business revenues in the latest 2 years having increased at least 30% respectively; (iii) at the end of the latest reporting period, having a net asset of no less than RMB20 million and having no loss that has not been made up; (iv) the total post-IPO capital stock amounting to no less than RMB30 million; and (v) mainly engaging in one single type of business in compliance with applicable PRC laws, regulations and policies.

7. Draft Operating Rules on State-Owned Property Right Transactions Published for Comments

On March 16, 2009, the PRC State-Owned Assets Supervision and Administration Commission (the “SASAC”) released the draft *Operating Rules on Transactions of State-Owned Property Rights Held by Enterprises* (the “Draft Rules”) for public comments.

According to the Draft Rules, the first public price quotation of the PRC state-owned property right under transfer should not be lower than its appraisal value duly filed with or approved by relevant government authorities. If no potential transferee responds to the first public price quotation, the transferor may lower the quotation (but no less than 90% of the appraisal value, unless prior approval has been obtained from the competent SASAC office) and issue a public notice again.

The Draft Rules also provide that in the case of installment payment arrangement for the purchase price, the initial installment should be no less than 30% of the total transfer price.

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

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