

China Regulatory Updates

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1. Foreign Enterprises Allowed to Get Listed in Shanghai

On April 29, 2009, the PRC State Council promulgated the *Opinions of the State Council on Promoting Shanghai in Accelerating the Development of the Modern Service Industry and the Advanced Manufacturing Industry and the Construction of International Financial Center and International Shipping Center* (the “Opinions”), pursuant to which, as part of the efforts in transforming Shanghai into an international financial center, qualified foreign enterprises may be allowed to issue A shares on Shanghai Stock Exchange at an appropriate time in the future. In addition, the Opinions provide that (i) the proportion and scale of foreign investors’ participation in the Shanghai financial market will be gradually increased; (ii) the scale of international development institutions’ issuance of RMB-denominated bonds will be gradually expanded and foreign enterprises’ issuance of RMB-denominated bonds within China will be gradually promoted; and (iii) the Shanghai reinsurance market will be actively developed and the development of Chinese-funded as well as Sino-foreign joint venture reinsurance companies will be encouraged.

2. Draft GEM Board Matching Rules Circulated for Public Comments

In order to promote the implementation of the *Interim Measures on the Administration of Initial Public Offerings and Listings on the GEM Board* (the “GEM Board Measures”) (please refer to the April 2009 issue of *Han Yi China Regulatory Updates for brief introduction*), on April 17, 2009, China Securities Regulatory Commission (“CSRC”) made public requests for comments on the draft amendments to the *Measures on Issuance Examination and Approval Committee of CSRC* (the “Amended Committee Measures(Draft)”) and the *Measures on the Administration of the Sponsor Business for Securities Issuance and Listing* (the “Amended Sponsor Measures (Draft)”).

Pursuant to the Amended Committee Measures (Draft), CSRC is to establish a separate issuance examination and approval committee for the GEM board, which comprises thirty-five (35) members, ten (10) more than those for the main board. During the examination and approval process, each enterprise will be reviewed by a team of seven (7) members, and several teams may conduct work simultaneously to expedite the examination and approval process. In addition to accounting, legal and other professionals, the GEM board issuance examination and approval committee will further include industrial experts with technology and management expertise.

According to the Amended Sponsor Measures (Draft), the period of continuous supervision and guidance for the initially listed companies on the GEM board should be the remaining period of the year in which the companies are listed and the following three (3) full fiscal years, one (1) fiscal year longer than that of the main board. During the period of continuous supervision and guidance, the sponsor should, within fifteen (15) business days from the date on which the relevant listed company discloses its annual report or semi-annual report, disclose a follow-up report, analyzing and commenting independently on the items requiring continuous supervision and guidance in accordance with the Amended Sponsor Measures (Draft). In addition, the provision that the relevant sponsor representatives shall be subject to corresponding supervisory measures if the issuer's operating profit in the current year decreases by 50% or more compared with that of the previous year should only apply to the main board and is not applicable to the GEM board.

3. CIRC Sets New Rules for Investment by Insurance Companies

On April 7, 2009, China Insurance Regulatory Commission ("CIRC") issued five documents in connection with the adjustment of the investment channel of insurance funds, including the *Circular on Increasing Varieties of Bonds Investment for Insurance Institutions*, the *Circular on Regulating Stock Investment Business of Insurance Institutions*, the *Circular on Insurance Funds' Investment in Infrastructure Bonds Investment Plan*, the *Circular on Issuance of Guidance for the Establishment of Products of Infrastructure Bonds Investment Plan* and the *Circular on Strengthening the Capability of Asset Management* (collectively, the "Circulars").

Pursuant to such Circulars, (i) insurance companies with solvency ratio of above 150% are eligible to conduct stock investment business regularly in accordance with applicable rules, while those with solvency ratio of below 100% for two (2) consecutive quarters are prohibited from increasing their stock investment and should timely report their market risks and take effective counter-measures and controlling measures; (ii) CIRC has decided to adjust bond investment policies, expand the scope of investment and add new investment products, including local government bonds issued and cashed by the PRC Ministry of Finance (“MOF”) on behalf of the local governments, non-financial institutions’ debt financing instruments issued in the domestic capital market, such as mid-term notes, bonds and convertible bonds issued by large-scale state-owned enterprises (“SOEs”) in the Hong Kong capital market and other unsecured bonds; and (iii) insurance companies which intend to invest in infrastructure bonds investment plan sponsored by, among others, insurance asset management companies and trust companies, are subject to further requirements, including, among others, the solvency ratio requirement (of above 120% within the latest two (2) years), the board resolution requirement and the internal rule requirement.

4. Regulation on the Appraisal on Non-monetary Assets to Be Contributed to Companies Strengthened

MOF and the PRC State Administration for Industry and Commerce (“SAIC”) have recently jointly released the *Circular on Several Issues Related to Strengthening the Administration of the Appraisal with respect to Non-Monetary Assets to Be Contributed to Companies* (the “Appraisal Circular”). According to the Appraisal Circular, asset appraisal by qualified asset appraisal firms should be conducted if: (i) the investor invests with non-monetary assets, such as investment in kind, IP rights or land-use rights; (ii) at the time of capital verification or application for registration with SAIC or its local offices, there have been material changes of the non-monetary assets in terms of asset conditions, method of using or market environment compared with that at the base date of the asset appraisal, or the appraisal hypothesis has experienced material changes, which may render material changes in the value of the assets; or (iii) other circumstance which requires asset appraisal as provided under laws or administrative regulations occurs.

5. Pre-Tax Deduction of Enterprises' Asset Loss Regulated

On April 28, 2009, MOF and the PRC State Administration of Taxation ("SAT") jointly issued the *Circular on Pre-Tax Deduction Policy of Enterprises' Asset Loss* (the "Tax Circular"), further specifying the relevant policies applicable to the deduction of enterprises' asset loss from taxable income. The Tax Circular takes effect retrospectively as of January 1, 2008.

According to the Tax Circular, enterprises' asset loss refers to the asset loss actually occurs in the enterprises' operation and is in connection with the obtaining of taxable income, and such asset loss includes but is not limited to loss on cash, deposits, uncollectible accounts, loans, equity investment, loss on the shortage, damage, depletion, and pilferage of fixed assets and inventory, and loss caused by force majeure event such as natural disaster. However, loss caused by enterprises' overseas operation institutions resulting from asset loss, which should be calculated separately from the domestic institutions, should not be deducted from the relevant domestic taxable income.

The Tax Circular sets out the circumstances in which enterprises' asset loss may be deducted for the calculation of taxable income. For example, enterprises are entitled to pre-tax deduction of their loss on equity investment if any of the following circumstances occurs: (i) the investee is legally declared bankrupt, closed, dissolved, or legally cancelled or its business license is revoked; (ii) the investee suffers from seriously worsening financial status and aggregated huge loss and has suspended its operation for three (3) consecutive years with no reorganization plan to restore its operation; (iii) the relevant enterprise has no control over the investee, the investment term expires or is more than ten (10) years, and the investee has been insolvent due to loss on operation for three (3) consecutive years; (iv) the investee suffers from seriously worsening financial status and aggregated huge loss and has completed its liquidation procedure or has been in liquidation procedure for more than three (3) years; or (v) other circumstance stipulated by competent authorities of finance or tax occurs.

6. Minimum Lockup Period of Strategic Foreign Investors in Chinese Commercial Banks Increases to Five Years

Recently, Mr. Liu Mingkang, chairman of China Banking Regulatory Commission (“CBRC”) noted that CBRC had decided to extend the minimum lockup period of the shares held by the foreign strategic investors in Chinese commercial banks to five (5) years in the future, while the existing minimum lockup period required for foreign strategic investors has been three (3) years.

7. SASAC Further Strengthens Internal Control on SOEs

To further clarify and regulate employee stock ownership in SOEs, the State-Owned Assets Supervision and Administration Commission (“SASAC”) promulgated on April 16, 2009 the *Circular Concerning the Implementation of the Opinions on Regulating the Stock Ownership and Investment of State-Owned Enterprise Employees* (the “Implementation Circular”). Pursuant to the Implementation Circular, (i) the scope of SOEs and middle-level and above managerial personnel referred to in the *Opinions on Regulating the Stock Ownership and Investment of State-Owned Enterprise Employees* (please refer to the November 2008 issue of *Han Yi China Regulatory Updates* for more details) is clarified; (ii) the middle-level and above managerial personnel should not transfer the equity held by them to their close relatives or enterprises owned or actually controlled by their close relatives; and (iii) the price to be paid by state shareholders for the purchase of the equity held by such middle-level and above managerial personnel should in principle not be higher than the audited net-asset value of the invested SOEs in the latest fiscal year. The Implementation Circular also provides for the measures to deal with any violation of applicable laws and regulations in the process of restructuring of the SOEs.

8. Draft Supporting Rules of Anti-Monopoly Law Published for Public Comments

SAIC, as the authority responsible for the investigation and enforcement with respect to monopoly agreement and abuse of dominant market position other than price monopoly, published for comments on April 27, 2009 the draft *Relevant Provisions for Prohibiting Monopoly Agreement* (“Draft Provisions I”) and *Relevant Provisions for Prohibiting Abuse of Dominant Market Position* (“Draft Provisions II”).

Pursuant to the Draft Provisions I, the forms of monopoly agreements should include (i) written agreements or written decisions; (ii) oral agreements or oral decisions; and (iii) coordinated actions between operators, such as tacit agreements or concerted actions, though without express written or oral agreements or decisions. If the operators are in violation of the Draft Provisions I by entering into and implementing a monopoly agreement, in addition to cease of illegal activities and confiscation of all illegal incomes, they should be further subject to a fine in an amount between 1% and 10% of their respective sales income of the previous year. If the monopoly agreement has not been implemented, the operators should be subject to a fine in an amount of no more than RMB500,000.

In accordance with the Draft Provisions II, operators with market monopoly position should be prohibited from reducing, restricting or suspending current transactions or refusing new transactions with relevant parties without any warrant. The actions of refusing, reducing, restricting or suspending transactions with relevant parties under equal transaction conditions may be deemed as “without any warrant”. The operators will be subject to cease of illegal activities and confiscation of illegal incomes punishment, and will be further fined for an amount between 1% and 10% of their respective sales income of the previous year, if they have violated the provisions of the Draft Provisions II and have implemented the actions of abusing their market monopoly positions.

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