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New Regime for China Foreign Direct Investment

Legal Update

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On October 8, 2016, the Ministry of Commerce of China (MOFCOM) issued Interim Measures on the Administration of Record Filing for the Establishment of and Change to Foreign Invested Enterprises (Interim Measures). These Interim Measures implement reforms in the government approval process and filing system for most foreign invested enterprises (FIEs) that were announced last month by the Standing Committee of the People's Republic of China. On September 3, 2016, the Standing Committee amended four regulations on foreign direct investment and investment from Taiwan (FDI), which marks a new, more lenient FDI regulatory regime. These amended regulations took effect on October 1, 2016, and apply to FIEs, including wholly foreign owned enterprises (WFOEs), equity joint ventures (EJVs) and cooperative joint ventures (CJVs). The amendments removed the previously required case-by-case administrative approval process for FIE establishment and certain significant corporate changes. Under the new regime, instead, FIEs that do not fall under the limited category or prohibited category of the Foreign Investment Catalogue, and are not subject to any shareholder limitations under the Foreign Investment Catalogue would only need to submit a record filing to MOFCOM or its local counterparts. Furthermore, FIEs are allowed to file through an online system as late as 30 days after the establishment or change.

The new record filing process applies to the following matters that previously required approvals from MOFCOM or its local counterparts:

- FIE establishment;
- FIE significant corporate changes, such as:
 - WFOE spin-offs, mergers, extensions of duration of existence and other significant corporate changes;
 - EJV extension of duration of existence and winding up; and
 - Material changes to CJV contracts, assignment of obligations and rights under CJV contracts, delegation of operation and management of CJVs, and extension of CJVs duration of existence;

The Interim Measures further specify the scope of record filings, in particular, the scope of "significant corporate changes" as follows:

(1) Changes to basic information on an FIE, including name, registered address, type of enterprise, duration of existence, industry of investment, business type, business scope, whether the equipment for the FIE is eligible for tax reduction or exemption, registered capital, total investment, organizational structure, legal representative, ultimate actual controller of the FIE and contacts or contact details;

(2) Changes to basic information relating to the investors of an FIE, including name, nationality or address (registered place or address), ID card type and number, subscribed capital contribution, form of contribution, deadline for contribution, source of fund and type of investors;

(3) Changes to equity and cooperation rights and interests;

(4) Mergers, spin-offs and terminations;

(5) Mortgages and transfers of property rights and interests of FIEs;

(6) Advance exit of investment by foreign investors from CJVs; and

(7) Delegation of operation and management of CJs.

Note that it is not clear whether a pledge of equity would constitute a change to equity under the Interim Measures. It was included in the draft version as an example of changes to equity under the third category above, but is not in the final version of the Interim Measures.

Where mergers, spin-offs or reductions of investment shall be publicly announced under the law, the record filing should also include information about the public announcement. For listed companies or SMEs listed on the National Equity Exchange Quotations (NEEQ), record filing is not required for changes to basic information relating to the investors or changes to equity unless the changes to the shares owned by foreign shareholders are more than 5 percent in aggregate, or that there is a change of control or change of relative control.

FIEs shall submit the following documents for recording filings:

- Documentation for name verification or business license;
- An FIE Formation Record Filing Affidavit signed by all investors or all founders, or an FIE Change Record Filing Affidavit signed by the legal representative or authorized representative of the FIE;
- Documentation for representative or jointly entrusted agent designated by all investors, all founders, or the FIE, including power of attorney for and proof of identification of the representative or agent;
- Documentation for authorization for other person(s) to sign relevant documents by FIE investors or legal representative, including power of attorney and proof of identification of the representative or agent (not required if no such authorization);
- Proof of subject qualification of investors or proof of identification of natural person investors (not required if there is no change to basic information relating

to the investors); and

- Proof of natural person identification of the legal representative (not required if there is no change to the legal representative).

The Interim Measures also clarified the timeline for FIE record filings. As mentioned above, FIEs would have to submit record filings online within 30 days after their establishment or significant corporate changes. Within three working days after the submission, MOFCOM or its local counterparts would confirm completion of the record filing in the system. If MOFCOM or its local counterparts determines that the submission is incomplete, inaccurate or that the business scope needs to be further explained, then MOFCOM or its local counterparts would notify the FIEs and allow 15 days for supplemental filings. If an FIE fails to file sufficient supplemental filings, MOFCOM or its local counterparts would notify the FIE that the filing is incomplete. The FIE can resubmit the record filing afterwards. But in the case where the establishment or significant corporate change has already taken place, the resubmission shall be filed within five days after notice of incomplete filing.

Violation of the Interim Measures will be published by MOFCOM or its local counterparts. MOFCOM and its local counterparts will share records of such violations with other government agencies. Records of violations will only be removed if the FIE or its investors correct the violation, and do not commit another violation of the Interim Measures in three years after the violation on record. FIE or investors that violate the Interim Measures may be subject to fines smaller than RMB 30,000.

The Interim Measures apply to “investment-type FIEs”, including investment companies and venture capital firms. However, it is not clear whether equity investment companies are also governed by the Interim Measures, as it was included in the draft version but is not in the final version.

The Interim Measures would not apply to antitrust investigations or national security review. In addition, service providers from Hong Kong and Macau that only invest in mainland China under trade in service agreements between mainland China and Hong Kong and Macau would still be subject to relevant record filing regulation specifically governing such investment.

The Interim Measures came into effect on October 8, 2016. Any pending application for approvals relating to the establishment and corporate changes which would now be subject to record filing under the Interim Measures submitted and accepted by MOFCOM or its local counterparts before the implementation of the Interim Measures would be cancelled automatically and the relevant FIEs or their investors shall submit record filings under the Interim Measures instead.

These amendments to FIE regulations and the Interim Measures are expected to substantially ease government control of and involvement in FDI. Approval from MOFCOM or its local counterparts would no longer be a pre-requisite to establishment and certain corporate changes of FIEs not subject to restrictions and the administrative process would be simplified and streamlined. That said, there are

still issues to be clarified by authorities. We will continue to watch developments in the FDI regulatory regime and will issue follow-up alerts as appropriate.