# SIGNIFICANT CHANGES TO PRC FOREIGN INVESTMENT LAWS

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**Corporate/M&A Alert**

## LAW UPDATES

On September 3, 2016, the Standing Committee of the National People's Congress ("**NPC**") adopted the *Decision of the Standing Committee of the NPC on Revising Four Laws, Including the Law of the People's Republic of China on Wholly Foreign-Owned Enterprises* ("**Decision**"), which will come into effect October 1, 2016. The Decision focuses on the filing requirement for the establishment of and changes to foreign-investment enterprises ("**FIE**"), changing the previous "approval filing" to "record filing."

On the same day, the Ministry of Commerce ("**MOFCOM**") issued the *Interim Measures for Record-Filing Administration for Establishment of and Changes to Foreign-Investment Enterprises (Draft for Public Comment)* ("**Record-Filing Draft**") and intends to implement such measures together with the Decision as of October 1, 2016.

## BACKGROUND

Before being amended by the Decision, the four foreign investment laws (i.e., the *Wholly Foreign-Owned Enterprise Law*, the *Sino-Foreign Equity Joint Venture Enterprise Law*, the *Sino-Foreign Cooperative Joint Venture Enterprise Law* and the *Law on the Protection of Investment of Taiwan Compatriots*) provided that material corporate matters such as the incorporation of an FIE, change of equity ownership, change of business scope, consolidation and split, and extension of business term should fall within the jurisdiction of MOFCOM and trigger an approval filing, under which MOFCOM generally performs a substantial review of application documents in relation to the establishment of or changes to a corporation.

China applies a three-tier classification regulatory system on foreign investments (i.e., prohibited, restricted and permitted). From 2013 to 2014, China established four free trade zones—Shanghai, Guangdong, Tianjin and Fujian—where foreign companies are permitted to establish FIEs as long as the business of the FIE does not fall within the scope of the negative list ("**Negative List**"), which specifies the sectors in which foreign investors are prohibited or restricted from investing. In places other than free trade zones, the *Catalogue for Guidance of Industries for Foreign Investment* ("**Catalogue**") applies and the scope of the Catalogue is slightly different from that of the Negative List.

## MAIN PROVISIONS OF THE DECISION AND RECORD-FILING DRAFT

The Decision replaces the prior approval filing with a record filing if special restriction measures (i.e., Negative

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List) are not triggered. Thus, if the contemplated scope of the business of an FIE is not on the Negative List, MOFCOM approval will no longer be required and a record filing will suffice.

The main provisions of the Record-Filing Draft are as follows:

1. Filing Authority: MOFCOM at the provincial or sub-provincial level.
2. Application Scope: the Record-Filing Draft applies to the establishment of or changes to any FIE that does not fall under the Negative List.

> Articles 25 and 26 provide that if foreign investors conduct investment activities that are on the Negative List, MOFCOM may require such investors to cease operational activities. In other words, the record-filing regime does not apply to the prohibited/restricted businesses provided on the Negative List.
>
> Article 31 provides that investment companies, venture capital enterprises, and equity investment enterprises that have foreign investors will be deemed "foreign investors."
>
> Article 32 provides that investors from Hong Kong, Macau and Taiwan will be deemed "foreign investors" for purposes of the Record-Filing Draft, subject to the Negative List.

3. Timeline and Filing Matters:

> FIE establishment filing: after obtaining name pre-approval, an FIE's designated representative/agent can file for establishment either before obtaining a business license or within 30 days upon issue of a business license.
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> FIE amendment filing: an FIE should file within 30 days after any of the following changes:

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> basic information on the FIE, including name, registered address, enterprise type, business term, invested industry, business type, business scope, project nature, registered capital, total investment, organization structure and composition, legal representative, as well as information on the FIE's ultimate de facto controllers;
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> basic information on the investors of the FIE, including names, nationalities, addresses, types and numbers of certificates of incorporation, amounts of capital subscribed, modes of investment, investment period, territory source of funds, and investor types;
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> stock equity, cooperative rights and interests, including stock equity pledge;
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> merger and acquisition, split, and termination;

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> mortgage and transfer of property rights and interests;
>
> disinvestment of the foreign partners of a Sino-foreign cooperative joint venture; or
>
> entrusted operation management of a Sino-foreign cooperative joint venture.

4. Filing Method: the filing documents must be submitted online via the "Foreign Investment Comprehensive Management Information System" and the feedback and results of the filing will be provided online.
5. Penalties: MOFCOM may order an FIE or its investors to file amendments when an FIE or its investors fail to make a record filing in a timely manner. If no correction is made within the prescribed period, the FIE or its investors may be fined up to RMB 30,000.

## PRELIMINARY OBSERVATIONS

6. Nationwide Negative List
   The nationwide negative list has yet to be seen, but we expect that it will be published before October 1, 2016, so that the Record-Filing Draft and the Decision can be enforced as scheduled. It remains to be seen how different the nationwide list will be from the Catalogue and the current Negative List used in the free trade zones.
7. Draft Foreign Investment Law

In early 2015, a draft version of the Foreign Investment Law was released for public comment. The draft Foreign Investment Law contemplates an overhaul of China's foreign direct-investment regime. Given that the draft Foreign Investment Law is similar to the Record-Filing Draft in terms of the filing regime, e.g., it requires approval of any offshore change in the ultimate controller of an FIE (including variable interest entities) in sectors with market access restrictions, it remains to be seen whether the draft Foreign Investment Law will be enacted in the near future.

8. Existing Approval-Based Laws
   We expect that other relevant authorities (including the administration of industry and commerce, taxation, foreign exchange, etc.) will amend relevant regulations in related areas in order to accommodate the significant changes under the Decision. All of these positive changes to foreign investment laws will encourage more foreign investment and reduce uncertainty for foreign investors entering the Chinese market.

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