

## New Rules to Further Relax China's Foreign Investment Registration Requirements

By Pingshan Li and Will Lu

On September 3, 2016, the Standing Committee of the National People's Congress of the People's Republic of China (PRC) adopted the *Decision to Amend the Four Laws Governing Foreign-Invested Enterprises* (Decision). The four laws include *The Law on Foreign-Invested Enterprises*, *The Law on Sino-Foreign Equity Joint Venture Enterprises*, *The Law on Sino-Foreign Cooperative Joint Venture Enterprises* and *The Law on the Protection of Investments by Taiwan Compatriots* (collectively, FIE Laws). The Decision represents a legislative step to further lessen the regulation of foreign direct investments in China. Following the adoption of the Decision, on September 30, the State Administration for Industry & Commerce (SAIC) issued the *Notice on Implementing Foreign-Invested Enterprises Registration Filing Requirements* (SAIC Notice). On October 8, the Ministry of Commerce (MOFCOM) issued the *Interim Administrative Measures on Record-Filing of Foreign-Invested Enterprises' Establishment and Amendment* (collectively, Record-Filing Measures) to replace the old rules with regard to the approval requirements for the establishment and amendment to registration of foreign-invested enterprises (FIEs) in China. The following is a summary of what is anticipated to change – and remain unchanged – under these new laws, rules and measures.

To clarify, FIEs include not only foreign-invested enterprises, but also Sino-foreign equity joint venture enterprises, Sino-foreign cooperative joint venture enterprises and enterprises invested by Hong Kong, Macau and/or Taiwan investors.

### One Change to China's Major Market Entry Control Regimes

#### **No Changes for Those in Restricted or Prohibited Industries**

MOFCOM and the National Development and Reform Commission promulgate the Foreign Investment Industry Guidance Catalogue (Catalogue) with regular updates; the most recent was published in 2015. Pursuant to the Catalogue, which is also the focal policy statement of China's market entry control, foreign investments into China are generally divided into four categories: (i) encouraged industries, (ii) permitted industries, (iii) restricted industries, and (iv) prohibited industries. As these names signify, the treatments of the four categories by the Chinese government are different in terms of the entry approval process.

According to the new Record-Filing Measures, which prescribe a simpler process compared with the previous regime, most investments in the encouraged or permitted industries pursuant to the

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Catalogue will be considered "Qualified Investments" that are eligible to follow the Record-Filing Measures and therefore enjoy a more straightforward process than before. It should be noted that pursuant to the Catalogue, certain encouraged or permitted industries have special requirements regarding controlling shareholders or senior management positions for policy reasons. In accordance with the Record-Filing Measures, investments in such industries would still be subject to the original "approval then registration" regime. For example, the industries involving commercial satellites, air transportation or power grids are encouraged industries but investments in these industries require Chinese controlling shareholders. Another example is accounting- or auditing-related businesses, which require Chinese chief partners. Foreign investments in these businesses would still have to follow the previous approval process and the Record-Filing Measures would not apply.

### ***The New Record-Filing Registration Regime***

Under the prior regime, the establishment of an FIE must be approved by MOFCOM or its designated local counterpart first. The specific industry the investment is to be in and the total amount of investment are the most important factors that dictate whether another approving authority (for example, the environmental protection agency) would be involved. Only after receiving approval from MOFCOM or its designated local counterpart will the FIE then be

allowed to register with SAIC and thus be legally established in China.

With the newly introduced regime, Qualified Investments will need to register in only one place: a national online filing system. In addition, this will be a "filing" process, not an approval process; the filing party will be required to file only an application form with supporting documents. The processing entity, generally a local counterpart of MOFCOM, will review the formality of the application but not its substance. It generally takes only three working days to process the filing and the filing results will be published on the online filing system.

Unlike the old approval-then-registration regime, where approval by MOFCOM is a prerequisite for the registration of an FIE with SAIC, in most instances under the new regime, the registration of an FIE can even proceed prior to the online MOFCOM record-filing as long as the FIE is a Qualified Investment.

For any investment that is not a Qualified Investment, the approval-then-registration regime remains unchanged.

### **Other Major Changes: From Approval-Based Regime to Record-Filing Regime**

#### ***Simplified Application Process***

In the old regime, the approving government authority was required to review the substance of the application documents and make a determination whether the proposed investment

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was in compliance with Chinese law and policy. The new record-filing system more closely resembles most business registration systems in the United States, where substantive review of the filing materials is not required. The new regime is supposed to be more streamlined and save money and time for foreign investors registering businesses in China. More importantly, the system will bring more certainty to the process of establishing FIEs in China.

### ***Wider Application of Record-Filing System with Certain Exceptions***

The new record-filing regime cannot be used in the following situations: (i) the proposed FIE is not a Qualified Investment; (ii) a foreign party proposes to acquire a domestic Chinese company that has no prior foreign shareholder or beneficial owner; and (iii) a foreign party proposes to acquire a publicly traded company in China. These types of application filings must still go through the original approval-then-registration regime.

### ***More Disclosure and More Information Sharing***

The Record-Filing Measures require the applicant to disclose its ultimate beneficial owner, which was not previously required. Under the original regime, only the State Administration of Foreign Exchange (SAFE) or its local counterpart would require an FIE to verify whether its beneficial owner includes PRC residents, and if not, no further information would be required. The new Record-Filing Measures seem to adopt a more stringent

approach and require broader disclosure on beneficial ownership information.

Besides the new disclosure requirement, it is worth noting that MOFCOM is planning to share the record-filing information of an FIE with other government authorities, including SAIC, SAFE, China Securities Regulatory Commission, Public Safety Bureau, Tax Authority and Customs. The official reason for such information sharing is to create a credit system that will be based on the information collected by MOFCOM and the aforementioned other authorities in the course of record-filings, investigations or government audits.

### **Uncertainties**

#### ***Negative List***

It is widely believed that the Catalogue will be replaced by a national "negative list," which has been implemented on a trial basis in the China (Shanghai) Pilot Free Trade Zone since 2013, and was later expanded to the Guangdong, Tianjin and Fujian free trade zones in 2015. Only those proposed FIEs that are not in the industries on the national negative list would be able to use the new record-filing system. However, it is not clear when a nationwide negative list will be promulgated by the State Council. There are reports that the Chinese government is "negotiating" the national negative list with the U.S. government as it is one of the most controversial pending topics under the draft Bilateral Investment Treaty between China and the United States.

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Although the exact scope of the national negative list remains unclear, it is expected to contain substantial changes from the Catalogue.

### **New Role of SAIC**

When applying under the new record-filing system, pre-approval by MOFCOM for the registration of an FIE by the SAIC will no longer be required. The SAIC will be expected to play a heightened “gate-keeper” role in screening FIE registrations or amendments to such registrations. The SAIC has urged its local counterparts to switch to the “new tasks” and “new challenges” in conjunction with the new record-filing system. At this very initial stage of implementing the Record-Filing Measures, it remains to be seen how SAIC will tackle its new responsibilities.

### **The Big Picture**

As practitioners of international business law involving China, we welcome the new developments because we believe they will streamline the processes for establishing FIEs in China. We believe it is part of a bigger trend as the Chinese government continues to reduce market entry restrictions on foreign investments. As we wait to see how these new rules and measures will be implemented, as well as what the final national negative list will look like, we are cautiously optimistic about the potential of this more open and welcoming business filing and registration system to benefit our clients.

### **FOR MORE INFORMATION**

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