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China Reaffirms Its Openness to Foreign Investment

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On April 13, 2010, the State Council of the People's Republic of China ("China") published a circular, "Certain Opinions on Strengthening Deployment of Foreign Investment" ("Opinion No. 9"),¹ that outlines new policies governing inbound foreign investment. These new policies include guidelines to (i) encourage foreign investment in China's high-end manufacturing, high-tech and eco-friendly industries;² (ii) encourage foreign investment in China's central and western regions;² (iii) promote diversified methods for foreign investment; (iv) further reform the regulatory regime to streamline and simplify the foreign investment regulatory approval process; and (v) create a favorable investment climate. The publication of *Opinion No. 9* signifies the Chinese government's commitment to optimize the use of, and upgrading the industrial landscape for, foreign investment.

Opinion No. 9 may be seen as an official response to recent criticism alleging that China has been deliberately slowing down the pace of inbound foreign investment.³ *The China Daily* – China's official English newspaper – described *Opinion No. 9* as a message that "the Chinese market can be a better place for all kinds of investors only if they brace for intensifying competition."⁴

Opinion No. 9 requires government at the local, provincial and central levels to improve the utilization of foreign investment via the following five means:

Increase Number of Encouraged Industries for Foreign Investment

Opinion No. 9 requires the *Foreign Investment Industrial Guidance Catalogue* (the "Foreign Investment Catalogue") to be amended to reflect the new state policy of encouraging foreign investments in high-end manufacturing, high-tech businesses (including R&D centers), advanced service businesses (including permitting multinationals to establish headquarters, procurement centers, accounting centers, settlement centers and profit centers within China, as well as engage in outsourcing services), new energy and energy-saving businesses and environmentally-friendly businesses. There are notably two specific incentive measures provided in *Opinion No. 9*:

- land to be used by "encouraged" foreign investment projects⁵ with an "intensive pattern of land use"⁶ is to be prioritized and local government is authorized to lower land premiums by a discount of up to 30% of the statutory minimum transfer price (as determined under the *National Standards on the Minimum Transfer Price for Industrial Land*);⁷ and

- qualified foreign-invested R&D centers are to be exempted from import duties, value-added taxes and consumption taxes for imported items used for scientific and technological development purposes until the end of 2010.

Encourage Foreign Investment into the Central and Western Regions

For the first time since China began its market reforms in 1979, labor-intensive foreign investment projects are officially encouraged in the central and western regions so long as such projects comply with applicable regional environmental protection regulations. Specific incentives include: (i) preferential enterprise income tax rates applicable to certain foreign-invested enterprises (“FIEs”) doing business in the regions and (ii) encouraging foreign invested commercial banks to open branches and otherwise operate in the regions.

Diversify Foreign Investment Methods

The methods of foreign investment that are expressly encouraged include direct investment and mergers and acquisitions in relation to domestic enterprises; strategic investment in domestically-listed companies; and fundraising on overseas stock exchanges. The central government expressly states that foreign investment in form of venture capital shall be encouraged, while those in form of private equity be actively utilized. To encourage the foregoing, *Opinion No. 9* also contemplates that the exit mechanisms for such venture capital or private equity investments will be improved.

Reform the Foreign Investment Approval Regime

The State Counsel has increased the approval threshold for projects catego-

rized as “encouraged” and “permitted” by the *Foreign Investment Catalogue* (except for projects requiring central government approval according to the *Government Verification and Approval Investment Project Catalogue*).⁹ Previously, any project with a total investment amount of USD100 million or more required central approval whereas the new reforms raise such threshold to USD300 million. *Opinion No. 9* further permits central government ministries and commissions to delegate certain of their approval powers to their local branches. For example, *Opinion No. 9* provides that local governments are now permitted to approve foreign-invested service projects (other than financial and telecom service projects). Further, *Opinion No. 9* calls for a review of the current list of projects requiring governmental verification and approval to reduce, to the extent possible, the scope of the list. It also calls for increasing the transparency of the approval process, simplifying approval procedures and shortening the approval time for foreign investment projects.

Create and Maintain a Favorable Investment Environment

Opinion No. 9 reflects the central government’s determination and support for furthering the development of economic zones as a investment administration model by permitting qualified state-level and provincial level economic development zones to increase and adjust the sites of their industrial parks. Other directions aimed at improving the investment environment include (i) simplifying the foreign exchange settlement procedures for the capital accounts of FIEs; (ii) allowing postponement of capital contributions by foreign investors facing temporary financial distress; and

(iii) promoting bi-literal or multi-lateral investment opportunities.

In sum, *Opinion No. 9* demonstrates that the Chinese government is moving forward with its policy to open up the Chinese market to foreign investment. However, *Opinion No. 9* only expresses high-level principles. The real effect of *Opinion No. 9* will depend on the implementing rules expected to be released in the future by the various governmental agencies under the State Council, in particular the Ministry of Commerce and the NDRC (these two being the primary forces shaping the regulatory regime for foreign investments in China). Even *Opinion No. 9*’s requirement that the *Foreign Investment Catalogue* be amended has no clear timeline. Until these implementing rules and amendments are released, precisely how far the Chinese government is resolved to go to encourage foreign investment will remain unclear.

1 The full text is available at http://www.gov.cn/zwqk/2010-04/13/content_1579732.htm (last visited Apr. 21, 2010).

2 The central and western regions in China include Chongqing city, all five of China’s autonomous regions and 12 provinces apart from the eastern and southern coastal cities and provinces.

3 According to a recent American Chambers of Commerce in China survey, 38% of its members felt unwelcome in China, representing an increase from 26% last quarter. The list of concerns included inconsistent regulations and judicial treatment, and discrimination against foreign-invested enterprises in government procurement. See “US business feeling unwelcome in China, says survey,” available at <http://news.bbc.co.uk/2/hi/8579528.stm> (last visited Apr. 21, 2010).

4 “Chinese market heaven for all investors,” available at http://news.xinhuanet.com/english2010/indepth/2010-04/15/c_13252152.htm (last visited Apr. 21, 2010).

5 Foreign investment projects are classified into four categories, “permitted,” “encouraged,” “restricted” and “prohibited,” and each category is subject to different regulatory and approval controls. The *Foreign Investment Catalogue* provides details on the categorization scheme and applicable regulatory and approval requirements.

- 6 The current regulatory framework does not define “intensive pattern of land use” and it therefore remains uncertain which entities will qualify for such land premium policy.
- 7 Beginning in 2006, the Chinese central government has issued a series of orders regulating land pricing. One approach has been to mandate that auction, bidding or listing procedures be used in transfers of industrial land by local government to ensure market prices apply. The central government simultaneously established national standards to fix minimum prices for transfers of industrial land that must be achieved even if the land is sold through auction, bidding or listing procedures.
- 8 Certain FIEs in central and western China may qualify for a lower enterprise income tax rate of 15%, compared to the standard rate of 25%. Currently, an FIE qualifies if its business falls within the “encouraged” category of the *Foreign Investment Catalogue* or if at least 70% of its revenues are generated from business activities listed in the *Catalogue of Priority Industries for Foreign Investment in Central and Western China*.
- 9 The *Catalogue of Investment Projects for Government Verification and Approval* was promulgated by the State Council in 2004, along with its Decision on Reforming the Investment System. An official from the National Development and Reform Commission (“NDRC”) has stated publicly that the central government has been considering amending the catalogue to shrink the current list of projects requiring central government approval by almost half. See “发改委：新《政府核准的投资项目目录》或将减半” (NDRC: The Projects under the new *Catalogue of Investment Projects for Government Verification and Approval* may be reduced by half), available at <http://money.163.com/09/0326/18/55BNV53C00252G50.html> (last visited Apr. 21, 2010).

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