Charltons - China News Alerts Newsletter - 20 May 2004

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# China News Alert Issue 55

## Headlines

### State Council released circular requesting full reform of fixed assets investment projects

The State Council recently issued a circular requesting regional government departments to conduct full-scale reform with respect to fixed assets investment projects that are either currently being undertaken, or that are in the planning stage.

According to the circular, local government departments shall classify projects within their respective jurisdictions into different categories. Those projects that are expressly prohibited by national laws and regulations or that violate the relevant laws and policies must be stopped; those projects that violate environmental regulations, urban planning regulations, or credit and loan policies etc. should be stopped; and relevant government departments shall ensure a reasonable completion schedule for those projects that are in accordance with relevant law, regulation and national policies.

In particular, in principle no new projects in the iron and steel, electrolyte aluminum and the cement industries will be approved this year, and any exception in this regard must be approved by the Central Government.

### "Measures for the administration of port-related services" implemented

On May 10, 2004, the Ministry of Communications issued "Regulations for the administration of port-related services". The Regulations will come into force on June 1, 2004. The Regulations purport to regulate port operations, which include activities undertaken by port operators to provide port facilities or services to ships, passengers, or merchandise within the port area. According to the Regulations, a port business license must be obtained in order to provide port related services. The Regulations also set out the conditions for engaging in port-related services, as well as the rules with respect to the application process for obtaining the port business license.

### Franchising business to expand into commercial service sector and other new sectors

After more than a decade of development, the franchising business in China is gradually expanding into new sectors in addition to the existing food and beverage and retail sectors. These new sectors include sports and fitness facilities, medical and health check-up centres, outdoor sports equipment, budget travel accomodation, and tourism services entities.

## Capital Markets

### CSRC changing IPO rules

On May 11, 2004, the CSRC issued the "Stocks Issue Examination and Approval Standards Memorandum No. 17 ¨C Criteria relating to the examination and approval of company financing by way of IPO", which sets out the following criteria on funds raised under IPOs:

1. The amount to be raised in an IPO may not exceed twice the unaudited net assets of the company one year prior to the submission of the IPO application. The amount of the promoters' share of accumulated undistributed profits is to be deducted in the calculation of the unaudited net assets.
2. Before the company distributes dividends to promoters, the relevant administrative procedures and the registration process with the Administration for Industry and Commerce must be completed before the IPO.
3. On the first page of the prospectus, there must be a special notice relating to the promoters' share of the company's accumulated undistributed earnings; and any post-listing plans with respect to these earnings must be disclosed in the chapter of "Issue Pricing and Dividend Distribution Policy".

### First list of approved sponsor institutions and sponsor representatives released

China's first list of approved sponsor institutions and sponsor representatives has recently been released. The list contains 67 registered securities firms and 609 registered sponsor representatives. This signals that the sponsorship system is to be fully implemented, and according to the CSRC, securities firms and professionals engaged in the profession must in the near future change their business management models consistent with the new system.

The CSRC also emphasized that registered sponsor representative status is not for life, and that registered sponsor representatives must meet the requirement of being a sponsor representative to at least one completed domestic or overseas IPO within two years, subject to being delisted from the registered sponsor representatives list.

### China to control credit and loan risks by issuing catalogue on curbing low-quality mass production industries

The State Development and Reform Commission, the People's Bank of China and the CBRC recently jointly issued a "Circular on further strengthening the coordination between industry policies and credit and loan policies, and to control credit and loan risks", and a "Construction catalogue on curbing low-quality mass production industries in certain industries", which restricts or prohibits low-quality mass production, to guide the direction of credit and loans, and to control credit and loan risk.

According to a State Development and Reform Commission spokesperson, the catalogue is divided into two sections, a section on prohibited industries and a section on restricted industries. The catalogue encompasses industries such as iron and steel, nonferrous metals, machinery, construction materials, petrochemicals, light industries, textiles, pharmaceuticals and printing.

The criteria used to categorise certain construction projects in the prohibited category are as follows: those that seriously affect production safety, or those that seriously pollute the environment, quality at below national standards, high consumption level of raw materials and energy, and investment projects prohibited by law and regulation. The various factors used in putting certain construction projects in the restricted category are as follows: those with seriously excessive production capacity, those that do not improve upon the existing industry structure, use outdated techniques or technology which have already been replaced by more advanced and mature techniques or technologies, those that are detrimental to the preservation of resources and of the environment, and investment projects restricted by law and regulation.

## Foreign Investment

### China to further open up its logistics market to foreign invested enterprises

On May 12, 2004, Vice-Director of the State Development and Reform Commission Li Shenglin stated that China will continue to firmly support the opening up of the Chinese logistics market.

During the Sino-American discussion session on logistics, Li went further to compare the Chinese logistics market with that in the U.S. and stated that China will continue to make significant improvements in this sector, which includes industries such as distribution, transportation and storage of goods.

### Ministry of Construction issues "Provisional regulations with respect to construction engineering design activities undertaken by foreign enterprises in the PRC"

On May 10, 2004, the Ministry of Construction issued "Provisional regulations with respect to construction engineering design activities undertaken by foreign enterprises in the PRC" ("Provisional Regulations").

According to the Provisional Regulations, foreign enterprises that purport to engage in construction engineering design in the PRC must enter into a joint venture with at least one Chinese design enterprise with a valid construction engineering design qualification certificate issued by the relevant administrative authority. According to the Provisional Regulations, the administrative authority responsible for construction shall review whether the foreign party to the joint venture has the requisite design capability, and only approved foreign enterprises may enter into joint ventures with domestic enterprises to undertake construction engineering design. Foreign enterprises undertaking construction engineering design in the PRC must meet the requirements of the compulsory engineering construction standards, and regulations govering the formulation of engineering designs. Foreign enterprises are prohibited from participating in the design of security engineering projects, search and rescue engineering projects and other projects which China is not open to foreign investment.

The Provisional Regulations will come into effect 30 days after the date of promulgation (30 days after May 10, 2004).

## Real Estate

### Measures for the administration of subsidized housing" formally implemented

In order to strengthen the construction and administration of subsidized housing, the Ministry of Construction, State Development and Reform Commission, Ministry of Land Resources and the People's Bank of China jointly issued the "Measures for the administration of subsidized housing" on May 13, 2004. The Measures took effect on the same day. The Measures set out the target market, as well as the construction standards and the pricing standards for subsidized housing. Subsidized commercial housing is, in principle, commercial housing that is subject to protective governmental policies.

## Corporate & Commercial

### SASAC implements a "Circular with respect to printing the answers to the questions relating to asset clearance and capital verification work III"

On April 29, 2004, SASAC under the State Council issued a "Circular with respect to printing the answers to the questions relating to asset clearance and capital verification work III", with answers to issues relating to asset clearance and capital verification work including:

* The issue of a certificate with respect to the loss of assets before the restructuring;
* The standards for loss forecasting;
* The treatment of applications for doubtful debts;
* Cancellation after verification of the reserve for reduction in the value of the assets for enterprises which have implemented the "Accounting System for Enterprises";
* The validity period for asset clearance and capital verification results; and
* Various other accounting treatments with respect to asset clearance and capital verification work.

### Reform of publishing, only one publisher to remain a non-profit organization

According to sources, all 568 publishers in China are faced with full-scale reform to transform themselves into for-profit enterprises with the exception of the provincial level branches of the People's Publishing House. Aside from the People's Publishing House at the Central Government level, each province, autonomous region and municipality directly under the control of the Central Government may retain a branch of the People's Publishing House or an alternative policy-type publishing house as a non-profit publisher. Within 5 to 7 years, the remaining Chinese publishing houses over 530 will be restructured into for-profit enterprises, and in an effort to support the restructuring, these enterprises will be exempt from paying enterprise income taxes for a period of 5 years after the restructuring.

### Iron prices have dropped significantly, State Development and Reform Commission predicts fall in prices to continue

The State Development and Reform Commission recently announced that since mid March, the prices of domestic iron materials in particular iron construction materials have dropped sharply. The Commission predicts that the price of iron materials will continue to decline in the near future. The drop in price for iron materials could in part be explained by the recent government policies to tighten controls on investments in the sector to prevent investment overheating.

### State Administration of Quality Control and Quarantine calls for halt of import of used Japanese plastic materials

Recently the State Administration of Quality Control and Quarantine issued a public announcement to halt the processing of all quality inspections and quarantining with respect to used plastics originating in Japan, in the light of a recent fraud case uncovered by the customs authority in Shandong province and the local state administration of quality control and quarantine involving the import of substandard used plastics from Japan in gross violation of the "Basel Convention" and of Chinese environmental protection standards. This is the first time that China has imposed a full-scale temporary ban on used raw materials originating in another country.

### 20 state owned enterprises under the control of SASAC's Beijing office to implement new remuneration system

The Beijing branch of SASAC will conduct a pilot project to implement new "Provisional measures for the administration of remuneration for the directors of state owned enterprises or state controlled enterprises in the City of Beijing" ("Provisional Measures") in a selected 20 enterprises among the 92 enterprises under its control. The Provisional Measures apply to CEOs, general directors and company secretaries. The Provisional Measures allow for the determination of remuneration based on basic indices and differential indices. The basic annual indices include the amount of net profit realized by the enterprise, and the net rate of return on assets. The differential indices in general reflect the characteristics and differences within the industries. The Provisional Measures also divide the remuneration of directors into two parts: basic remuneration (not tied to the performance of the enterprise) and performance based remuneration.

## Insurance

### China aims to expand medical insurance coverage in four areas

The Ministry of Labour and Social Security recently announced that China will aim to expand the scope of the country's basic medical insurance coverage in the following segments of the population: retired employees and employees in difficulty from bankrupt state owned enterprises; hourly rate and free-lance workers; personnel of mixed state owned and privately owned enterprises, personal business and other non-state owned economic organizations; and relocated farmers working in urban areas.

## WTO

### Russia to increase import duty on goods originating from China

Import duties imposed by Russia on commercial goods originating in China have recently increased by up to seven fold. In early April, the Russian customs authority advised their port authorities to strengthen controls on commercial goods originating from China. In particular, in addition to restricting the entry of Chinese commercial goods, the Russian customs authorities have also imposed an additional 30% import duty on Chinese consumer goods or USD3.50 per 1,000g, compared with the USD0.2 to USD1.4 per 1,000g charged more than half the time previously.

Prior to the increase in import duties, Russia did not issue any official documents and did not advise the Chinese authorities in this regard. The Chinese Embassy in Russia is currently negotiating with their Russian counterparts to resolve this issue.

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