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# China News Alert Issue 271

## Capital Markets

### Money supply to be raised to boost liquidity

The country's top policymakers have announced a series of measures to boost the supply of money and stabilize the capital market to arrest the slowing down of the economy.

The State Council, the country's Cabinet, has raised the money supply growth target from 16 percent in 2008 to 17 percent, which will be "3 to 4 percentage points above the total growth of economic output and consumer prices" next year.

The measure, announced recently, is one of the 30 designed to "strengthen the financial sector's support" to the economy to ensure a stable and relatively fast growth.

The measures came three days after the Central Economic Work Conference, which reiterated the government's decision to boost domestic demand to tackle the global economic slowdown.

Analysts said the 30 measures would help act as a booster for the government's $586-billion stimulus package, which extends up to 2010.

"Policy at the moment is generally being focused on boosting liquidity in the banking sector and making sure that it is used to fund investment in infrastructure projects," Glenn Maguire, chief Asia-Pacific economist at Societe Generale SA in Hong Kong, said recently.

Other steps announced over the weekend to tackle the downturn include:

Aiming to achieve a loan growth of 4 trillion yuan ($586 billion) for all financial institutions and increasing the loan quota for policy banks by 100 billion yuan this year;

Suspending sales of three-year central bank notes and reducing sales of one-year and three-month bank notes;

Supporting enterprises to conduct mergers and acquisitions through the capital market, and allowing overseas banks to provide loans to domestic firms for the purpose;

Setting up futures for other commodities such as steel and grains; and

Asking insurers to expand insurance coverage to areas such as agriculture, cars, house purchase and short-term export credit.

The growth of money in the country shrank from 16 percent in August to 15 percent in November as businesses and consumers cut their spending owing to the global financial crisis.

Spooked banks grew more cautious, approving new loans very cautiously because of worries over corporate profitability.

The latest steps are expected to help the government implement its proactive fiscal and relatively loose monetary polices to boost growth.

As part of the policies, the central bank has cut the benchmark-lending rate from 7.47 percent to 5.58 percent since September. It has lowered lenders' reserve requirement ratio and scrapped curbs on local banks' monthly loans, too.

#### Call to lend more

A top banking official urged lenders to provide more loans to ensure a relatively fast economic growth, even though it could mean an increase in bad loans.

"Bad loans will certainly increase this year, posing a real challenge for banks," Liu Mingkang, chairman of China Banking Regulatory Commission, said at a conference.

But "we encourage banks to offer a helping hand to enterprises with good fundamentals," Liu said, because "it would be costlier to let them go under".

Some banks have responded to the call. China Merchants Bank, for instance, pledged to offer at least 5 billion yuan to smaller firms next year compared with less than 10 billion yuan over the past two decades.

[Source: China Daily](http://www.chinadaily.com.cn/bizchina/2008-12/15/content_7303363.htm) ([see archive](Money_supply_to_be_raised_to_boost_liquidity.pdf))

### M&A Lending Exits Banking Gray Zone

Responding to Beijing's initiative to encourage the financial sector and support economic growth, the China Banking Regulatory Commission (CBRC) for the first time has given legal status to merger and acquisition lending.

Guidelines for the commercial banks that will be allowed to offer M&A loans were issued by the CBRC on December 9.

The new policy lets strong commercial banks -- defined as those with at least 10 percent capital adequacy ratios -- write the loans.

The policy change was not expected to lead to wave of leveraged buyouts. But it should give banks and their clients a legal route for M&A loans, which until now were issued cautiously inside a gray legal zone.

The move also parallels a series of government measures and initiatives aimed at encouraging state-owned enterprises to pursue overseas, cross-region and cross-industry consolidations, CBRC said.

In addition, as the number of overseas M&A transactions by Chinese enterprises grows, CBRC said, M&A lending services would support international expansions.

“M&A loans will promote corporate consolidation,” said Arthur Cai, computer maker Lenovo Group's head of corporate development for the Asia Pacific region.

Moreover, Cai thinks state-owned companies will be in a better position than private firms, particularly small- to medium-sized enterprises, to benefit from the new policy as they try to finance expansions.

Risk management is a focal point for regulators. CBRC said its principle is “to allow qualified commercial banks to offer M&A lending, provided that they adroitly balance market needs and risk control.” The policy also stipulates that buyers and target companies “have relatively high industry or strategic connections.”

“Commercial banks involved in M&A lending that concern cross-border transactions also must evaluate country risks, foreign-exchange risks and transit-of-capital risks,” CBRC said.

Borrowers should provide guarantees such as assets and equity, or third-party guarantees. Loans are limited to 50 percent of a bank's net core capital, and a loan to a single borrower cannot exceed 5 percent of net core capital. Payback terms cannot exceed five years.

“Banks are responsible for eliminating risks when lending for M&A,” said Cong Feng, a senior M&A manager with Citic Securities. “Credit examiners should look at whether projects make sense or not, and whether there is solid security to back up the loan.”

Permitting M&A loans will benefit state-owned banks such as Industrial and Commercial Bank of China, said a senior executive at ICBC's investment banking division. “It will clear up difficulties that investment banks have previously encountered,” the executive said. “ICBC once fought strenuously to have this new policy carried out.”

Until now, the ICBC executive said, some bankers were tempted to mask M&A lending as standard credit to bypass regulators.

The policy also applies to the more than 30 foreign banks incorporated in China, a CBRC official who participated in drafting the guidelines told.

But foreign banks are cool toward the policy. “I have not yet heard any internal discussion on M&A lending,” said Lisa Liang, a public relations manager at JP Morgan Chase Bank (China) Ltd.

“Foreign banks so far have had relatively little involvement in the merger and acquisition market in China,” said Ashley Jing, a senior executive at South Korea's Woori Bank.

Foreign banks hold about 2 percent of the total assets in China's banks. With limited yuan deposits, they rely on the interbank market to maintain liquidity.

“Moreover, foreign banks' knowledge about Chinese companies is relatively limited compared to local Chinese banks,” Jing said. “M&A projects are extremely risky.”

Banks qualified under CBRC's guidelines include China's four, major state-owned banks as well as China Merchants, Citic Bank, and Industrial Bank. Each has reported a 10 percent capital adequacy level, according to third quarter financial statement.

Most commercial banks, including Shenzhen Development Bank and Pudong Development Bank, currently would not be qualified because they failed to reach the 10 percent threshold in the third quarter.

“CBRC has set the principle for M&A lending,” said Citic's Cong. “We will wait and see how commercial banks respond.”

[Source: Caijing](http://english.caijing.com.cn/2008-12-11/110037495.html) ([see archive](M_and_A_Lending_Exits_Banking_Gray_Zone.pdf))

### Real estate investment trusts to come soon

The properties in Tianjin Binhai New Area and Shanghai Pudong New Area may be packaged into the first pilot units of the long-awaited real estate investment trusts (REITs) and listed on the bourses in Shenzhen and Shanghai respectively, reported recently.

According to the report, regulators, including the central bank, the China Securities Regulatory Commission (CSRC), and the Ministry of Housing and Urban-Rural Development are still developing related regulations.

An executive meeting of the State Council, China's cabinet, held on Dec 3, released nine measures to boost the role of the financial sector in the economy, including legitimizing REITs to provide an alternative for developers to raise money in the market.

In mid 2008, Shanghai Pudong New Area was reported to have finished preparatory work on funds related to infrastructure properties, which targeted some office buildings and retail spaces with good performance and lease contracts.

The Tianjin Binhai New Area has also released its plan for pilot units for REITs. "Tianjin targeted the high-end industrial and commercial properties to develop REITs. Through financing in the capital market, the rent revenue and investment income can contribute to the shareholders' dividends," Zheng Jinqiao, chairman of Richlink International Capital Co, was cited by the newspaper as saying.

"Raising capital will be the most urgent task for the real estate industry in the Asia Pacific region in 2009," said a report jointly released by PricewaterhouseCoopers (PwC) and the Urban Land Institute on Dec 9.

So far, mainland regulators have not worked out how to cope with controversial issues such as double taxation - taxes imposed on both property assets and dividend payment of REITs.

"Taxation is the main hurdle," said Zheng, "REITs can come out as long as the tax problem is resolved."

[Source: China Daily](http://www.chinadaily.com.cn/bizchina/2008-12/15/content_7305858.htm) ([see archive](Real_estate_investment_trusts_to_come_soon.pdf))

### Profits from Equity Incentives to be Based on Performance

China's State-owned Assets Supervision and Administration Commission (SASAC) and Ministry of Finance specified that listed companies must decide the proportion of equities to be granted and exercised by the incentive objects based on the assessment results of their performance.

Under the Circular on Issues Concerning the Implementation of Equity Incentive Systems by State-owned Controlling Listed Companies released by the said departments on December 11, during the validity term of the right exercising, for the top proportion of the profits from equity incentives of the incentive objects in the total remunerations (including incomes from the equity incentives) when the equity options are granted, in principle, that of domestically listed firms and overseas H share companies shall not exceed 40%, and that of overseas red-chip companies may not exceed 50%.

The requirements shall be indicated in the companies' equity incentive management or equity granting agreements.

[Source: Lexis Nexis](http://hk.lexiscn.com/latest_message.php?id=5133) ([see archive](Profits_from_Equity_Incentives_to_be_Based_on_Performance.pdf))

## Real Estate

### Real estate sector gets policy props

The government recenetly waived business tax on real estate sales and relaxed mortgage policies for second-home buyers in the latest attempt to buoy the sluggish property market.

The policies were among those unveiled at an executive meeting of the State Council, or the Cabinet, presided over by Premier Wen Jiabao.

The 5.5 percent sales tax will be waived if the property is sold two years after purchase. Previously, owners had to wait at least five years before selling their house tax-free.

And if owners now want to sell their houses in less than two years, they only have to pay taxes on the profit, not the sale price.

"This move is expected to boost the market, but may drag down prices in new residential buildings (because of a possible increase in transactions of pre-owned homes)," said Qin Xiaomei, research chief at CB Richard Ellis' Beijing branch.

The floor space of residential properties sold in the first 11 months fell 18.8 percent from a year earlier, while real estate investment growth slowed to 22.7 percent in the January-November period, down from 24.6 percent in the first 10 months, according to the National Bureau of Statistics.

Falling transactions are squeezing an economy already hurt by the global turmoil, as the property sector is one of the biggest drivers of China's domestic consumption, contributing a quarter of fixed-asset investment and employing 77 million people.

Experts have said reviving the property sector is vital to the government's efforts to counter the current downturn, which has worsened in the past month.

"The latest package will definitely help boost market confidence, but we should not expect an instant rebound in the market, since more detailed regulations are believed to be in the pipeline," said Gu Wei, spokesman for Longfor Property.

"However, it is really a big move, reflecting the government's resolve to rejuvenate the property market," he added.

The State Council also said it would allow people with "smaller-than-average" apartments to buy a second home on preferential terms till now reserved for first-time buyers, such as lower down payment requirements and interest rates.

"This policy relaxation has really made us excited and could help in speeding up the recovery of the market," said a sales manger of Beijing Capital Land.

However, Zheng Fei, a 30-year-old company executive, said he would adopt a wait-and-watch attitude, betting property prices will continue to fall and the government may announce more favorable policies.

The government also said it would support developers' "reasonable" financing needs, and increase credit help for developers of low-price units catering to low-income groups. It also pledged to provide housing for 9.9 million low-income families in the next three years.

Rural homes in dangerous condition will also be renovated.

The People's Bank of China, the central bank, said recently that developers building low-rent public housing could enjoy a 10 percent discount on lending rates, effective next month.

And the National Development and Reform Commission, the nation's top economic planner, recently announced 10 billion yuan in subsidies for affordable housing.

[Source: China Daily](http://www.chinadaily.com.cn/cndy/2008-12/18/content_7316013.htm) ([see archive](Real_estate_sector_gets_policy_props.pdf))

## Corporate & Commercial

### China to inject 30 billion yuan into major economic development district

The Guangzhou Development District (GDD), the largest of its kind in China in terms of GDP, will spend 30 billion yuan (4.38 billion U.S. dollars) in the coming three years to help thousands of enterprises cope with the global financial crisis.

Xue Xiaofeng, director of the GDD administrative commission, said recently the government spending would trigger another 70-billion-yuan investment from the private sector.

"We are kind of placing orders of 100 billion yuan for enterprises in the district. We hope to give them timely assistance when the global financial crisis is still worsening," Xue said.

Among the GDD's massive investment, 25 billion yuan will be used to improve infrastructure, 2.3 billion yuan for innovation fostering, one billion yuan for high-tech development and the rest for human resources, social security and other fields.

Th GDD was established in 2002 in Guangzhou, capital of the southern economic powerhouse Guangdong Province, and has now 2,600enterprises with foreign investment and 3,800 domestic enterprises.

Last year the district's GDP grew by 20.18 percent to 94.8 billion yuan, becoming the country's largest economic development district in terms of GDP for the fourth straight year.

As a result of the global financial crisis, some enterprises in the GDD have fewer orders from overseas and those engaged in metal metallurgy, one of the district's six leading industries, made cutbacks, said Xue.

However, Xue said none of the enterprises in the districted has gone bankrupt because of the international crisis.

[Source: China Securities Journal](http://www.cs.com.cn/english/ei/200812/t20081217_1685501.html) ([see archive](China_to_inject_30_billion_yuan_into_major_economic_development_district.pdf))

### Central government investments to focus on five areas

Investments from central government will focus on five major areas next year, reporters recently learned from the National Development and Reform Work Conference.

These issues include; agriculture, rural areas and farmers; welfare housing projects; infrastructure construction in areas including transportation; energy conservation and emissions reduction; and social undertakings.

Several principles must be upheld when expanding investments next year. The investment projects must integrate well with one another and must be able to effectively trigger social investment. Well-organized specialized planning with precise execution of the preliminary stages of work is required. At the same time, the goods orders must be placed and payments made as quickly as possible in order to strictly control capital and quality.

[Source: China Securities Journal](http://www.cs.com.cn/english/ei/200812/t20081215_1683490.html) ([see archive](Central_government_investments_to_focus_on_five_areas.pdf))

## Taxation

### China to keep general tariff level at 9.8% in 2009

China would keep the country's general tariff level at 9.8 percent next year, the same as in 2008 and in 2007, the Ministry of Finance (MOF) announced recently.

The nation will lower import tariffs on five commodities, including fresh strawberries, from Jan 1, the ministry said in a statement, adding the limited scope and margin of lower tariffs was the reason why the general tariff level was left unchanged from that in 2008.

The tariff level for farm produce will be maintained at 15.2 percent and that for industrial products at 8.9 percent, according to the statement.

#### Macro control leverage

The ministry said tariffs on specific items would also be adjusted to support four sectors -- agriculture and rural development, technologies that will benefit industrial upgrading and equipment manufacturing, energy and environment conservation, and the industries of textile, steel and fertilizer that are in difficulties.

The nation would impose temporary import tariffs on animal feedstuff and some large farming equipment as well as spare parts, the MOF stated, without providing further details.

It also said the country may cancel the temporary import tariffs on pork, among others, and resume most-favored nation rates based on market demands.

However, the country will continue to impose seasonal export tariffs on fertilizers like carbamide and impose special export tariffs on some compound fertilizers, in order to meet domestic demands first.

While speaking of support for the troubled textile, steel, and fertilizer industries, the ministry said the nation would levy lower import tariffs on "raw materials that have huge demand in domestic production" in the form of lower temporary tariffs, without giving further details.

The ministry said the nation would impose lower import tariffs on some technology products, such as ion exchange membrane, and key equipment and spare parts that are essential in promoting new technologies.

The country would also continue to levy lower temporary tariffs on equipment, as well as spare parts, that are useful in conserving the environment, while keeping in place temporary export tariffs on energy- and resource-consuming products, such as coke and wood pulp, and those on energy products, such as coal and crude.

The ministry also announced lower tariffs next year with a number of countries, including Pakistan, New Zealand, and Singapore, a move aimed to to boost bilateral and multilateral trade with other countries to fight falling exports amid the ongoing global crisis.

MOF official Bai Jingming said the country had been increasingly employing tariff policies to adjust macro control policies over the past few years.

#### WTO commitments fulfilled

The ministry also said that China was almost at the finish line in respect to honoring the commitments of cutting tariffs it made upon joining the World Trade Organization (WTO) in 2001.

China's general tariff level has been lowered by more than 35 percent since the country's accession to the WTO, down from 15.3 percent in 2001 to the present 9.8 percent.

The tariff level had been substantially lowered in the five years since 2001, to reach 9.9 percent as early as in 2005.

"It is very important for Chinese exporters at such a time of crisis, if overseas countries could fulfill their commitments of market access for Chinese products, which should be effective at the same time when China fulfilled its promise to reduce tariffs and non-tariff barriers," Mei Xinyu, a trade expert with the Ministry of Commerce.

[Source: China Daily](http://www.chinadaily.com.cn/bizchina/2008-12/18/content_7317990.htm) ([see archive](China_to_keep_general_tariff_level_at_98_in_2009.pdf))

### China VAT Reform to Help Firms Cope with Financial Turmoil: Official

A senior Chinese official said recently that the country's value-added tax (VAT) reform would help domestic enterprises to tide over the adverse effects of the financial crisis.

Zheng Jianxin, deputy director general of the taxation department of China's Ministry of Finance, said Chinese exports were hit by the financial turmoil, which started in the United States, and the government was weighing measures to reduce the impact.

"The VAT reform would encourage investment and technological upgrading at Chinese companies, boost domestic demand, improve companies' competitive strength and play a positive role in helping companies to tackle the financial crisis," Zheng said during an online interview with netizens on the website www.gov.cn.

China announced last month to extend its value-added tax (VAT) reform to all industries nationwide from Jan. 1, 2009, as part of the 4 trillion yuan (584 billion U.S. dollars) stimulus package in the next two years to buttress economic growth.

The reform was aimed at shifting from the existing production-based to a consumption-based VAT regime, which would enable companies to get tax deductions on spending on fixed assets, Zheng said, adding that this would reduce the tax burden on companies by more than 123 billion yuan next year.

The reform would also scrap policies that exempted imported equipment from VAT, and removed foreign-funded companies from eligibility for tax rebates on domestic equipment purchases and put them on an equal footing with domestic companies, he said.

"The VAT rate for small businesses and the self-employed who fall into the small-scale taxpayers category was reduced to a universal 3 percent from 6 percent for industrial firms and from 4 percent for commercial companies, while the VAT rate for mineral products rose back to 17 percent from 13 percent," he added.

Zheng said the raising of the VAT rate for mineral products was to support resource conservation in the country.

Wang Jide, a senior official from the State Administration of Taxation, said tax burdens on companies would not only be reduced, but would also become more rational, as the administration would strengthen the check-up of taxpayers' information and intensify invoice management.

Wang added that the reform would aid the development of the country's small and medium-sized companies, many of which were suffering from the effects of the financial crisis.

[Source: China Securities Journal](http://www.cs.com.cn/english/ei/200812/t20081210_1678977.html) ([see archive](China_VAT_Reform_to_Help_Firms_Cope_with_Financial_Turmoil_Official.pdf))

### Exemption of Vehicles Purchase Tax Suggested

A proposal suggesting a possible tax reduction or exemption for purchasing cars with engines of less than 1.6 litres was filed recently as reported.

The suggestion is part of a series of effort aimed at boosting China's auto market. It was filed by the National Association for Passenger Car Information Exchange over to the National Development and Reform Commission, the Ministry of Finance, the Ministry of Industry and Information Technology, and the Ministry of Commerce.

The proposal gives two options for the reduction or exemption of vehicles purchasing tax.

Scheme A suggests imposing on vehicle purchasing tax in accordance with the auto's engine size. It ranges from 2 percent for a car with an engine of less than 1 litre, to 10 percent for those of more than 4 litres.

Scheme B calls for the exemption of vehicle purchasing tax for cars with an engine size of less than 1.6 litres, often categorized as low-emission vehicles.

Sources say the proposal, aimed at stimulating domestic consumption and at the same time conserving energy and cutting emissions, is being considered by China's top decision makers. And the second option is their favoured plan.

"The central government is mulling over plans to stimulate the domestic auto market," said Dong Jianping, deputy secretary general of the China Association of Automobile Manufacturers, "and the fuel price and tax reform would be the most efficient way to achieve this goal, while reform on vehicle purchase tax being the second best option."

China now imposes a 10 percent vehicle purchase tax to car buyers. Currently, cars with an engine size of between 1.0 and 1.6 litres took up about one third of sedan sales from January to October.

[Source: China Securities Journal](http://www.cs.com.cn/english/ei/200812/t20081217_1685510.html) ([see archive](Exemption_of_Vehicles_Purchase_Tax_Suggested.pdf))

## Other

### Supreme Court Specified Execution Procedure for Litigation Law

Beginning on 1 January 2009, if applicants for execution apply for the execution of property to the people's courts where the property to be executed is located, they shall provide the certification documents from the administration of the courts on the property executable.

According to the interpretation of the Supreme People's Court on application of the execution procedures of the Civil Litigation Law of the People's Republic of China released on November 10, after accepting the application for the execution, if parties involved hold dissidence against the jurisdiction, they shall make the dissidence within 10 days upon the receipt of the execution notice. During the examination and review of the jurisdiction dissidence, the execution will not be suspended.

[Source: Lexis Nexis](http://hk.lexiscn.com/latest_message.php?id=5136) ([see archive](Supreme_Court_Specified_Execution_Procedure_for_Litigation_Law.pdf))

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