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# China News Alert Issue 286

## Capital Markets

### Banks get OK for insurance arms

China's big four State banks will be allowed to run their own insurance companies under a pilot program, an official from the country's banking regulator said.

"We have reached an agreement with the insurance regulator on allowing banks to set up their own insurance companies, and the big four banks will be the first to run it on a pilot basis," Lai Xiufu, an official from the China Banking Regulatory Commission (CBRC), said recently.

At a press conference in February, Li Kemu, vice-chairman of the China Insurance Regulatory Commission, indicated that there would be at least one approved insurance company floated by a bank this year.

"The two regulators have now reached a consensus on the regulatory framework, and most of the preparatory work is ready," said Li.

Besides the big four, a number of mid-sized banks, such as China Merchants Bank, have also submitted applications to the regulators, eyeing the business potential in the insurance sector - a sector growing at an annual average of 20 percent in the past decade.

However, the management risks arising from such an operation could pose a challenge, said Hao Yansu, an insurance professor from the Central University of Finance and Economics.

"To split the risks, it would be better for banks to set up an investment entity and initiate an insurance company through the investment arm," said Hao, adding the global financial crisis indicates that the more types of business an institution runs, the higher risks it will face.

Usually, it takes around seven or eight years for a new life insurer to reach the break-even point.

In 2008, China's banking sector realized a net profit after tax of 583.4 billion yuan, up 30.6 percent on a yearly basis.

[Source: China Daily](http://www.chinadaily.com.cn/bizchina/2009-04/14/content_7674649.htm) ([see archive](Banks_get_OK_for_insurance_arms.pdf))

### China banks cleared to buy insurer stakes

China's insurance regulator has given Bank of Communications and Bank of Bejing approval to buy into domestic insurers, the China Securities Journal reported recently.

The approvals mark an acceleration of the development of financial conglomerates in China, the paper quoted a source at a State-run commercial bank as saying.

The China Insurance Regulatory Commission has given Bank of Communications, China's fifth-largest lender, approval to buy a stake in Shanghai-based China Life-CMG Insurance Co, the paper said, citing sources.

The insurer is a joint venture between Commonwealth Bank of Australia and China Life Insurance.

The regulator has also approved the purchase by Bank of Beijing, which is 16 percent owned by ING Groep NV, of a stake in Pacific-Antai Life Insurance Co, the paper said.

The report did not specify the size of the stakes or the financial terms of the purchases.

China is relaxing its rules and allowing banks to enter the brokerage, fund management and insurance businesses to reduce their reliance on lending in a weakened economy, as well as to develop and deepen the country's financial services sector.

[Source: China Daily](http://www.chinadaily.com.cn/bizchina/2009-04/10/content_7666576.htm) ([see archive](China_banks_cleared_to_buy_insurer_stakes.pdf))

### CBRC will try to rein in risk

China's banking regulator said it will step up efforts to control risk management in Chinese banks as domestic lending continued to grow in March.

Chinese banks reportedly extended a whopping 1.87 trillion yuan worth of new loans in March, following record-setting lending growth in the first two month of this year.

The China Banking Regulatory Commission (CBRC) lifted annual lending quotas on domestic banks last November to boost economic growth amid the global financial crisis. Lending in Chinese banks has skyrocketed ever since.

The rise in March would bring the first-quarter figure for new loans to about 4 trillion yuan, close to the 5 trillion yuan lending target Premier Wen Jiabao announced at the National People's Congress.

World leaders vowed at the London G-20 Summit to regulate financial firms more strictly in the wake of the global financial crisis. Although Chinese banks have largely been left untouched compared to their western peers, it doesn't mean they're in a risk-free haven, analysts said.

This year's lending by Chinese banks has included a high proportion of discounted bill financing, generally used to meet companies' short-term cash needs, fuelling speculations that much of the surge in loans may be funding stock market speculation rather than business operations or investment.

Chinese media reported earlier that the CBRC had begun auditing lending growth in Chinese banks to learn where the new loans actually ended up.

Authorities have forbidden commercial banks from transferring funds raised from discounted bills into deposit accounts, China Securities Journal reported. The paper also quoted a regulatory official as saying that the current increase in credit basically reflected the demands of the real economy.

Liu Mingkang, chairman of the CBRC, said that capital adequacy ratio and provision coverage ratio in Chinese banks has to meet the latest regulatory requirement, when speaking at a meeting held at the Chinese Academy of Social Sciences.

According to latest regulations from the CBRC, capital adequacy ratio in major domestic banks has to be higher than 12 percent while provision coverage ratio in those banks need to be improved to 150 percent by the end of 2009.

As at the end of 2008, capital adequacy ratio in the country's top three State-controlled banks, Industrial and Commercial Bank of China (ICBC), China Construction Bank (CCB) and Bank of China (BOC), met the CBRC's 12 percent requirement. But both ICBC and CCB have to raise their provision coverage ratio by about 20 percentage points to keep in line with the CBRC's new regulation, while BOC's provision coverage ratio has to be boosted by about 30 percentage points.

In addition, China will ask foreign investors to commit to a lockup period of five years or more when they acquire stakes in Chinese banks, as an effort to shield domestic banks from the impact of stake sales by overseas investors.

CBRC chairman Liu mentioned the new policy for the first time last week without giving details on when it would be implemented. In recent months, several foreign banks have sold stakes in Chinese banks to raise cash amid the global financial crisis, causing share prices of Chinese banks to fluctuate.

[Source: Xinhua](http://news.xinhuanet.com/english/2009-04/13/content_11178602.htm) ([see archive](CBRC_to_try_to_rein_in_risk.pdf))

## Corporate & Commercial

### China regulates SOE share transfers

China's state asset watchdog said recently it will prohibit management staff of state-owned enterprises (SOEs) from transferring their shares in SOE affiliates and subsidiaries to their close relatives, its latest move to stop state assets ending up in private hands.

China issued a rule last October to forbid SOE middle and senior management officials to own shares in SOE affiliates, subsidiaries or other SOE-invested businesses, in order to curb state-asset losses. Those who already held such shares were ordered to transfer those interests.

The management staff are not allowed to sell the shares to their close relatives or the companies that the relatives control, said the State-owned Assets Supervision and Management Commission (SASAC) in a document, which made clear the details of the October rule.

Instead, the SOEs should be the first to buy those shares, whose prices should not exceed their audited net value in the previous fiscal year, said the SASAC.

Public discontent with state asset losses and privatization has been growing since share-holding reforms were launched three decades ago to introduce private ownership into SOEs.

SOE management ownership of equities in affiliates, subsidiaries and SOE-invested companies has led to problems, such as executives procuring products or services of those businesses at prices unreasonably higher than the market price, resulting in "state-owned assets losses in disguise," according to Zuo Daguang, director of the SASAC's Liaoning branch.

In order to contain insider-control and state-owned assets losses, the SASAC and the Ministry of Finance jointly issued a document in April 2005, forbidding management buyouts of large SOEs.

Thursday's document also specified the definition of the SOE senior and middle management staff, which include members of board of directors and supervisors. They were required to transfer shares in SOE affiliates within a year of the publication of the October rule or resign from their posts.

[Source: China Daily](http://www.chinadaily.com.cn/bizchina/2009-04/17/content_7686621.htm) ([see archive](China_regulates_SOE_share_transfers.pdf))

### CBEX to foster overseas M&As

The China Beijing Equity Exchange (CBEX) will act as the main catalyst in fostering domestic and cross-border mergers and acquisitions and also look to list itself in the near future, according to its chairman Xiong Yan.

"CBEX will play an active role in M&As and recently signed a cooperation agreement with Industrial and Commercial Bank of China (ICBC) and some other banks. As part of this, we facilitated the country's first M&A loan from ICBC in January," he said.

Xiong said the bourse intends to offer a broader platform for its clients through partnerships with global bourses. "We have set up joint-venture equity exchange bourses in Italy, the US and Japan, and will soon open one in Africa."

As a move to diversify its business, the CBEX recently established special platforms to trade in gold and environment investment. It is also working on bourses for forest resources, art works, residential housing and oil.

"Our plan is to build up a comprehensive equity exchange bourse and go public. This way we can make our operations more transparent," Xiong said.

Recently the exchange conducted the auction of the 2008 Beijing Olympics souvenirs and received an overwhelming response to it.

The drums and bamboo scrolls used for the opening ceremony was one of the favorites with prices going through the roof.

The 1,500 fous and bamboo scrolls sold for about 119 million yuan.

For fou, the traditional Chinese drum, the average price was around 60,000 yuan. The highest bid of 288,000 yuan was for a drum that had the lucky number 1890 printed on it.

China launched the Beijing Property Rights Trading Center in 1994 and renamed it CBEX 10 years later.

Following the reform of State-owned enterprises (SOEs) in the 1990s, a batch of regional equity exchange bourses was established to offer a fair and public environment for their assets and equity transactions.

"How to cut off the interest linkage? How to price these assets? These were the daunting problems that were facing us in those days," Xiong said.

By setting up equity exchange bourses, the problems more or less resolved themselves as they could offer a public platform to avoid insider trading and also introduce bidders to find the right market value, he said.

The CBEX along with its counterparts in Tianjin, Shanghai and Chongqing have today developed into the four leading equity exchange bourses in China that deal with the asset disposal of the SOEs that are directly overseen by the central government.

CBEX's total transaction amount last year surged 46 percent year-on-year to touch 94 billion yuan, with the added-value rate for the transacted State-owned assets reaching 29 percent.

For CBEX, the transaction of the financial assets was its second-largest business in 2008 and its total transaction amount reached 7.65 billion yuan.

"As of May 1, all the State-owned financial institutions will be required to enter the four big equity exchange bourses for assets transfer, and this will bring huge business opportunities for us," said Xiong.

[Source: Sina](http://english.sina.com/business/p/2009/0407/232140.html) ([see archive](CBEX_to_foster_overseas_M_and_As.pdf))

### Overseas investment norms released

The Ministry of Commerce (MOFCOM) recently released the guidelines for overseas investment and cooperation with 20 countries as part of its strategy to help Chinese enterprises seek overseas opportunities.

"Most of the Chinese investors lack in overseas experience and basic knowledge about the countries and the business environment. So we decided to come out with these guidelines," said Assistant Commerce Minister Wang Chao.

The country-by-country guidelines provide basic information on setting up an overseas enterprise. It also includes tips on how to foster local relations and where to seek help when in trouble.

The ministry said it expects to issue the guidelines for other countries and regions later this year.

China's overseas investment has been increasing rapidly in recent years. In 2008, the country's outbound investment in the non-financial sector soared by 63.5 percent to $40.65 billion. The contract value of projects in other countries and regions went up by 39.4 percent to $56.6 billion.

While many economic institutions have predicted that global investment activities would slow down this year due to the financial crisis, others said that it is the right time for Chinese firms to look at global investment opportunities.

"Many of the advanced sectors in developed countries are having cash flow problems now," said Xing Houyuan, a senior researcher on outbound investment with the commerce ministry.

"This is good news for Chinese firms who are keen on improving their own technologies," he said.

In addition, many firms from the developed countries have either cut or cancelled their investment in developing countries, and Chinese firms could utilize this opportunity to fill the gap, said Xing.

There has already been a flurry of activity on the investment front with other countries. Commerce Minister Chen Deming recently led a trade mission to Europe and it managed to clinch investment deals worth more than $13 billion.

The Ministry of Commerce is also sending a delegation to the United States later this month to explore trade and investment opportunities. According to some reports, the team is expected to visit Washington, Chicago and San Francisco.

But overseas investments could also be risky.

Liang Guining, a researcher with the ministry specialized in investment in Africa, said many developing countries are not transparent in decision making and do not have proper laws and regulations to protect foreign investors.

The risk can also turn out to be opportunities, according to Li. "For instance, the bad infrastructure in African countries could be a barrier for investors, but many countries also have favorable policies for investors in these sectors, which means plenty of opportunities for Chinese enterprises if they see it in the right way."

[Source: China.org](http://www.china.org.cn/business/news/2009-04/11/content_17587577.htm) ([see archive](Overseas_investment_norms_released.pdf))

### FDI norms look set to be tweaked

China will further streamline approval procedures for foreign direct investment (FDI) and channel more FDI into the underdeveloped western and central parts of the country, an official from the Ministry of Commerce (MOFCOM) said recently.

The move is part of the government's efforts to boost FDI inflow, which has been affected by the global financial crisis. China had authorized its provinces to approve FDI proposals worth up to $100 million last month.

MOFCOM spokesperson Yao Jian said the country would ensure a more convenient environment for examination and approval of FDI proposals and launch policies to spur foreign investment flow into China's central and western regions.

"FDI is of great significance in creating jobs and stimulating the economy," Yao said.

The ministry will also encourage investment in sectors such as hi-tech, services and environment protection, facilitate the establishment of more provincial-level economic and technological development areas, as well as mergers and acquisitions activity under the Chinese anti-monopoly law, Yao said.

MOFCOM statistics revealed that the value of FDI in March fell by 9.5 percent year-on-year, the sixth monthly drop in a row. FDI touched $8.4 billion in March, the largest ever in the past six months, but the monthly decline rate was far lower than that of the previous months; it had dropped by 32.7 percent in January and 15.8 percent in February.

In 2008, foreign investors in China, who accounted for 3 percent of the nation's total by number, contributed 30 percent to industrial output, 55 percent to its imports and exports, and created 11 percent of urban jobs.

In the first quarter, FDI in manufacturing and services dropped by 11.5 and 31.3 percent, among which, the real estate sector saw the biggest drop, of 38.3 percent.

Customs data also showed that in March, China's foreign trade decreased by double digits from a year earlier, the fifth monthly drop since last November.

But a positive indicator was that the contractions were getting smaller. Exports in March decreased by 17.1 percent, 0.4 and 8.6 percentage points lower than that of January and February. Moreover, exports of labor-intensive products including garments, bags, shoes and furniture were growing.

Experts have said China's foreign trade and FDI would witness mild growth in the last quarter of this year.

"The ease-off is encouraging, but the prospects are still tough and we cannot lower vigilance," Yao said.

With regard to foreign trade, Yao said the government would assist small and medium-sized enterprises in developing their overseas markets; offer them help in marketing, registration and branding; urge financial institutions to grant loans to the large-scale equipment providers for exports, and encourage the imports of products related to hi-tech and environment protection and primary products.

[Source: China Daily](http://www.chinadaily.com.cn/bizchina/2009-04/16/content_7682164.htm) ([see archive](FDI_norms_look_set_to_be_tweaked.pdf))

### Two Authorities Regulated Appraisal of Capital Contribution via Non-currency Properties

If investors make their capital contribution via capitalizing such non-currency properties as the objects, intellectual property, land use rights, they must entrust the asset appraisers which are established in line with law to conduct the asset appraisal.

Under the Circular on the Several Issues Concerning the Management of Appraisal of Capital Contribution via Non-currency Properties (Circular), which was jointly released by China's Ministry of Finance (MOF) and State Administration for Industry & Commerce (SAIC) on March 30, 2009, investors with capital contribution via capitalizing non-currency properties must be responsible for authenticity and validity of the non-currency properties they provide.

The Circular also stipulated that investors and other units or individuals must not interrupt the appraisal and appraisal conclusion of the capital contribution via non-currency properties.

[Source: Lexis Nexis](http://hk.lexiscn.com/latest_message.php?id=5623) ([see archive](Two_Authorities_Regulated_Appraisal_of_Capital_Contribution_via_Non-currency_Properties.pdf))

## Taxation

### Imported Equipments or be Entitled to Deduction of Value-added tax if Released from the Customs Supervision

If the customs supervision over the equipments which taxpayers imported in a tax-free manner for their self-use prior to December 31, 2008, and the taxpayers have acquired the special customs import value-added tax payment letter which the customs issue after January 1, 2009 due to the dismiss of customs supervision, they are eligible to deduct the value-added tax as specified in the letter from the output tax.

The aforementioned provisions were made by the Reply on Issues Concerning the Deduction of Import Value-added Tax on the Equipments which Are Imported in a Tax-free Manner and Are Released from the Customs Supervision, which was released by China's State Administration of Taxation on March 30, 2009. Under the Reply, taxpayers must pay the value-added tax for their selling of the aforementioned goods according to the applicable tax rates.

[Source: Lexis Nexis](http://hk.lexiscn.com/latest_message.php?id=5633) ([see archive](Imported_Equipments_or_be_Entitled_to_Deduction_of_Value-added_tax_if_Released_from_the_Customs_Supervision.pdf))

## Other

### Recall rule to cover all producers in China

Manufacturers who fail to recall or report substandard products face fines of up to 500,000 yuan (74,530 U.S. dollars), under a draft regulation released recently.

The proposal by the General Administration of Quality Supervision, Inspection and Quarantine was drafted after the tainted milk powder scandal, in which six infants died and a further 296,000 were made ill.

It stipulates that manufacturers immediately recall products if they are found to be unsafe. They must also stop producing and selling the product.

There is no timeframe given for a recall, but if the manufacturer fails to withdraw its products it can be ordered to comply and fined between 200,000 and 500,000 yuan ($29,260 and $74,530).

Experts said the proposal did not go far enough because it was confusing, did not give a deadline for the recall and punishment was weak.

"The fine for violators is far from enough," Dong Zhengwei, a Beijing-based lawyer, said.

"The manufacturers should be charged at least 10 or 20 times their commercial gains for their misconducts."

China has laws regulating the recall of the automotive, toy and pharmaceutical industries and there is a provision for recall in the newly implemented Food Safety Law.

However, a general regulation is absent and legislators have urged the government to strengthen product safety measures, including procedures for recall.

According to the proposal, manufacturers can still be charged if a consumer is harmed after the product has been recalled.

But it will be the responsibility of the manufacturers to investigate its own products once alerted to the product fault.

The regulation covers all China-made products, but does not include drug consumables and products produced and consumed by the Chinese army.

Members of the public are invited to comment on the proposal released by the State Council's Legislative Affairs Office.

Public hearings will be complete by May 26 and the Cabinet is expected to approve the regulation by the end of the year.

[Source: Xinhua](http://news.xinhuanet.com/english/2009-04/10/content_11160746.htm) ([see archive](Recall_rule_to_cover_all_producers_in_China.pdf))

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