Charltons - China News Alerts Newsletter - 12 July 2011

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# China News Alert Issue 357

## Law

### Cost of employing foreigners to rise

New social insurance laws will make the hiring of foreign employees significantly more expensive for companies in China.

Draft measures based on thePRC Social Insurance Law set to come into effect on July 1st will make it so foreign workers in China will 'shall participate in social insurance analogically in accordance with this Law'. This has caused some concern that foreign workers and their companies could be hit with extra taxes. The main worry is that if foreign workers' new insurance contributions match those of local employees, the cost could be quite considerable, particularly in the case of younger foreigners.

The counter-argument follows that foreign workers' salaries are comparatively high so the cost of the social insurance policy will be relatively low. But many young workers come to China to begin their careers and now prospective employers will have to assess whether or not to take on the additional insurance burden or not pay it resulting in potentially hefty fines. The other option facing foreign workers is to take a pay cut to work in China.

Another aspect of the new social insurance laws that is causing consternation is that foreigners, upon written application, can get the social insurance agency to pay money back into his/her account in cancellation of the basic pension relationship with the PRC. This is in direct contrast with the law as it pertains to PRC citizens, who are expressly forbidden from any early withdrawals from their basic pension accounts.

The Ministry of Human Resources and Social Security released the draft on June 10th and the comment solicitation period ended June 17th.

China's new Social Insurance Law will come into effect on July 1st.

[Source: China Law and Practice，Global Times](http://www.chinalawandpractice.com/Article.aspx?ArticleID=2852271&LS=EMS539307) ([see archive](Cost_of_employing_foreigners_to_rise.pdf))

## M&A

### New MOFCOM draft regulations to toughen up on merger control

On June 13th the Ministry of Commerce solicited public comments on a draft regulations designed to address speculation that many large transactions that should have been notified for clearance have not been properly notified.

Proposals set out in the new Preliminary Regulations on the Investigation & Treatment of Failure to Report Concentration of Undertakings (Opinion Solicitation Draft) would give Mofcom the power to investigate, fine and order divestiture of mergers and acquisitions that have failed to be notified and cleared when they should have been.

In particular, Article 14 would give Mofcom the authority to step in and order the 'immediate suspension of a transaction or the proper disposal of the shares or assets involved in a timely manner.' Mofcom may also move to delegate to provincial level commerce departments the power to 'investigate a failure to report a notifiable concentration of undertakings.'

Fines of anything up to RMB 500,000 may also be levied with a RMB 1 million fine for any entity who try to obstruct or an investigation by concealing or destroying documents etc.

Details on confidentiality were also outlined in the draft regulations. If an orgnaisation is suspected of any wrongdoing, Mofcom will keep secret the names and details of concerned parties until decisions have been made. Those suspected with have a total of 15 business days to show they have not breached the duty to notify prior to implementation. If a failure to notify is confirmed, the parties to the transaction will have 30 days to provide relevant documents and to suspend the transaction in question.

The draft regulations also take care to point out any potential whistleblowers will be protected but it is unclear whether or not Mofcom will accept anonymous whistleblowers. Article 4 requires a whistleblower to provide information on the organisations in question and the whistleblower as well.

The draft regulations are the latest addition to China' 2008 Anti-Monopoly Law. As of June 23rd Mofcom are no longer accepting public comments on the proposals.

[Source: McDermott Will and Emery](http://www.mwechinalaw.com/news/2011/chinalawalert0611b.htm) ([see archive](Chinas_MOFCOM_Gets_Tough_on_Merger_Control.pdf))

[Draft regulations - unofficial translation](http://www.mwe.com/info/pubs/Chinas_MOFCOM_Gets_Tough_on_Merger_Control_Unofficial_Translation.pdf) ([see archive](Chinas_MOFCOM_Gets_Tough_on_Merger_Control_Unofficial_Translation.pdf))

## Investment

### New rules for cross-border RMB capital account related transactions

The PRC government continued to promote Renminbi in international transactions by issuing Circular 38 of 2011 entitled Notice on the Issues relating to the Regulation of the Practice of Cross-border RMB Capital Account Related Business.

These new regulations allow for RMB to be used in a much wider range of transactions involving the inflow and outflow of debt or equity.

The new rules fit into four major categories:

#### Outbound Foreign Investment

Subject to the appropriate filing and registration with the State Administration of Foreign Exchange (SAFE), institutions can go about outbound investment using RMB directly. The same institutions can now remit proceeds generated in RMB directly back to the PRC, provided they have been generated from either liquidation, reduction in capital or share transfer to a foreign assignee relating to offshore investments.

#### Foreign Direct Investment

Capital contribution to a PRC company can now be made by a foreign investor using RMB either inside or outside of the PRC. Previously, with few exceptions, no RMB funds were allowed to be used for such purposes.

RMB proceeds of foreign investors can also be remitted outside of the PRC directly, subject to filing with SAFE and provided they meet SAFE's standards.

#### Outbound Lending

Domestic enterprises can lend RMB direct to their offshore subsidiaries. On top of this RMB proceeds generated from such loans can be remitted straight back to the onshore lender.

#### Foreign Debt

Offshore lenders will now be able to deal out loans to domestic institutions (including financial institutions). SAFE will regulate these loans as if they were a foreign currency debt. The big difference is that unlike debt generated in a foreign currency, there is no need for an institution to open up a foreign debt account.

Domestic institutions providing security denominated in RMB for RMB foreign debts should be registered with SAFE for approval. Therefore the existing rules concerning the provision of foreign security by domestic institutions will be applicable.

This circular represents a significant step forward for full convertibility of RMB. Previously the PRC government has been very careful in its managing of RMB relating transactions. The Notice can be seen as a follow on from trial measures introduced in 2009 to use RMB in international trade settlement.

[Source: Mayer Brown](http://www.mayerbrown.com/publications/article.asp?id=11184&nid=6) ([see archive](SAFE_of_the_PRC_Issues_New_Rules_Regulating_Cross-Border_RMB_Capital_Account_Related_Transactions.pdf))

### CBRC to tighten regulations on investment products

The China Banking Regulatory Commission (CBRC) is looking to solicit opinions on wealth investment management, in an effort to better protect investors' interests.

The nation's banking regulator has ordered commercial banks to improve upon their information disclosure system so that clients will be more aware of the risks they will face when buying wealth investment products. The CBRC's planned tightening aims to further regulate one of the most profitable sectors in China's banking system. By the end of 2011's first quarter, commercial banks had sold 1.9 trillion yuan of wealth investment compared with last year's 1.7 trillion.

It has been suggested that the documents commercial banks supply to potential investors should include further information on the inherent risks investors will face. An assessment should also be carried out to determine a client's capacity to endure risks and ‘worst case scenarios' should be presented to them.

Other points the CBRC is recommending banks take into account include the investor's age, financial statements and investment experience.

[Source: Law Info China](http://www.lawinfochina.com/News/News_Detail.asp?Id=8623) ([see archive](Chinas_banking_regulator_set_to_tighten_regulations_over_investment_products.pdf))

### Government further clarifies registration requirements for Equity Investment Enterprises

Earlier this month the National Development and Reform Commission (NDRC) further clarified requirements issued in early 2011 for Equity Investment Enterprises (EIEs) in Noitce 253 (full title: Notice of Further Regulating the Development and Administration of Registration of Equity Investment Enterprises in Pilot Locations). The new Registration Guidance offers more detailed information on what the application process entails and which documents are required when registering an EIE.

Among the key clarifications the Registration Guidance offers is a closer look at the kind of EIEs are no longer required to register. Now EIEs that have a total capital of less than 500 million yuan (or foreign currency equivalent) will be exempt from having to register. Additionally, an enterprise with a total committed capital of over 500 million yuan but where the capital actually contributed is less than 100 million will also be exempt. This will likely reduce the amount and cost of administrative work for EIEs still in the early fund-raising stage.

Fund-raising itself is examined in further detail as well. In particular, three main points are clarified.

1. The number of investors in an EIE may not exceed 200 if the EIE is established as a joint stock limited company, and may not exceed 50 if in the form of a limited liability company or limited partnership;
2. The minimum capital subscription of each individual investor may not be less than 10 million; and
3. An investor may not invest in an EIE by entrusting other investors to hold the shares on its behalf.

Compliance requirements are also laid out in the Guidance, mainly to advise on what an EIE prospectus should include. Namely they must detail information on income, expenses, performance-based compensation and the income distribution method. Other aspects expected to be included are:

* Source of income and how the income is accounted for
* Management fees
* The principle and percentage of profit-sharing with respect to performance-based compensation
* Set up costs and expenses
* Methods of loss recovery
* Method and procedures for the distribution of profits to investors

As far as partnerships are concerned, the Registration Guidance offers a few points on the type of organisations that should not be allowed to be limited partners. Pursuant to PRC law, wholly state-owned companies or enterprises, listed companies or charitable organisations are not permitted to be general partners with an EIE. The Guidance also reiterates that not limited partners should be allowed to become involved in any part of the management of investment portfolios.

It is expected that all investment entities in the private equity industry will eventually fall under the rules of the new Regulation Guidance. The Guidance makes specific reference to foreign investment 'including offshore organisations' suggesting that China's PE industry stands to benefit a great deal from these new rules and regulations.

[Source: Deloitte](http://www.deloitte.com/assets/Dcom-China/Local%20Assets/Documents/Services/Tax/TaxanalysisEN2011/cn_tax_tap1412011eng_020611.pdf) ([see archive]

## Other

### CPI Higher in June than in May

China's Consumer Price Index (CPI) will be higher in June than it was a month previously according to Yao Jingyuan, former chief economist with the National Bureau of Statistics. In May the country's CPI rose to 5.5% year on year, well above the government's stated target of 4%.

CPI is often taken as a main gauge of inflation but despite this, Yao stated his confidence that China could achieve its 4% CPI target for the end of 2011. The difficulty of meeting this target will be eased by an expected fall in CPI during this year's final quarter.

According to China Daily, Yao's message was that China's economy showed a trait of stability with very minimal risks of sharp decline.

Yao laid a lot of the blame for the rise in prices on China's weak agricultural infrastructure as well as inflation pressures coming across from the US as a result of quantative easing.

[Source: China Daily](http://www.chinadaily.com.cn/china/2011-06/26/content_12779301.htm) ([see archive](Chinas_June_CPI_to_be_higher_than_May.pdf))

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