

Strengthening the facilitation and protection of foreign investment, the <Foreign Investment Law> provides support to a high-level opening-up

News Flash
China Tax and Business Advisory
March 2019
Issue 12

In brief

On 15 March 2019, the 2nd session of the 13th National People's Congress (NPC) approved the <Foreign Investment Law of the People's Republic of China (PRC)>¹ (hereinafter referred to as the "<Foreign Investment Law>"). On the same day, President Xi Jinping signed the President Order No.26, announcing that the <Foreign Investment Law> will come into force from 1 January 2020. On 23 December 2018, the Standing Committee of the 7th session of the 13th NPC reviewed the <Foreign Investment Law (1st Draft)> for the first time and on 26 December 2018, the <Foreign Investment Law (1st Draft)> was released on the website of the NPC of the PRC for public opinions. Then, on 29 January 2019, the Standing Committee of the 8th session of the 13th NPC took the 2nd review of the <Foreign Investment Law (2nd Draft)>. The whole legislation progress of the <Foreign Investment Law> is beyond expectation.

Since the commencement of the Reform and Opening-up 40 years ago, China has established a legal system for foreign investment mainly consisting of the <Law on the Sino-Foreign Equity Joint Venture>, <Law on the Sino-Foreign Cooperative Joint Venture> and <Law on Wholly Foreign-owned Enterprises> (hereinafter referred to as the "Three Foreign-invested Enterprise (FIE) Laws". With the change in situation relating to China's opening up and utilization of foreign investments, the "Three FIE Laws" cannot cope with the need of building an open economic system. As such, a fundamental law to replace the prevailing "Three FIE Laws" is urgently needed in the area of foreign investment. In recent years, the Chinese government has put forward a series of strategic decisions to expand the opening-up as well as to facilitate foreign investment, setting forth clear requirements for unifying domestic and foreign investment laws and refining the legal system of foreign laws and regulations. Formulating a fundamental law on foreign investment was included in the legislation work plan of the Standing Committee of the NPC in 2018.

The newly promulgated <Foreign Investment Law> establishes the basic framework of China's new legal system for foreign investment and sets forth uniform regulations on the access, facilitation and protection, etc., of foreign investment, which provides a stronger legal protection for China to further expand its opening-up, and to utilize foreign investment effectively. In this issue of China Tax and Business News Flash, we will provide you with our detailed interpretations on the main points of the <Foreign Investment Law> and share with you our observations.

In detail

The <Foreign Investment Law> is comprised of six chapters and 42 articles, including: general principles, investment facilitation, investment protection, investment administration, legal liabilities and supplementary provisions. Compared with the <Foreign Investment Law (Discussion Draft)> (consisting of eleven chapters and 170 articles) issued by the Ministry of Commerce (MOC) in 2015, the <Foreign Investment Law> has been greatly simplified in the number of chapters and provisions. The chapters on access administration, national security review and information reporting have been removed and replaced by more principle-based provisions. After the <Foreign Investment Law> becomes effective, it is expected that the State Council and the competent government authorities will sort out and revise the prevailing laws and regulations for foreign investment and issue additional implementation measures, to formulate a new legal system for foreign investment.

Clarify the legal status of the law

The <Foreign Investment Law> is positioned as the fundamental law on foreign investment. It will not regulate foreign investment based on the organizational form and framework of the enterprise. Instead, the organizational form, framework and activity guidelines of FIEs shall be subject to the Company Law and the Partnership Enterprise Law, etc.

Roll out the administration of the pre-establishment national treatment plus negative list mechanism for FIEs' access to China

Since 2013, China has successively released the negative list for foreign investment which is applicable to foreign investors and the negative list for market access which is applicable to both domestic and foreign investors. The latest negative lists for foreign investment issued in June 2018 include the <Special Administrative Measures for Foreign Investment (the Negative List) (2018 Version)>² (with 48 measures) which is applicable nationwide and the <Special Administrative Measures for Foreign Investment in the PFTZs (the Negative List) (2018 Version)>³ (with 45 measures) which is applicable in the PFTZs only. Foreign investors in sectors that are not on the negative lists for foreign investment would be subject to the <Negative List for Market Access (2018 Version)>⁴ issued in December 2018 similar to Chinese investors (such as state-owned enterprises and private enterprises) and enjoy equal treatment in market access.

The <Foreign Investment Law> clearly stipulates that foreign investment would be subject to the pre-establishment national treatment plus negative list administration system and provides specific definition for the terms "pre-establishment national treatment" and "negative list", which signifies that China has abolished the case-by-case approval system in foreign investment administration. This significant change indicates that China's reform of foreign investment legal system is moving towards a more open and flexible direction, adapting to the changes of economic globalization and international investment rules. The negative lists for foreign investment are expected to be further shortened in 2019, which will provide more opportunities for foreign investors.

Ensure equal treatment of domestic enterprises and FIEs

Enjoying equal treatment has always been one of the major requests of foreign investors and FIEs. The <Foreign Investment Law> sets forth certain principle-based provisions of equal treatment for FIEs in the chapter of "Investment Facilitation", which mainly include:

- All national policies on supporting the development of enterprises shall equally apply to FIEs in accordance with the laws;
- The state ensures that FIEs can equally participate in formulating standards in accordance with the laws, and strengthen information disclosure and social supervision on the standard formulation; and the mandatory standards formulated by the state shall equally apply to FIEs;
- The state guarantees FIEs can participate in government procurement activities through fair competition; and products manufactured and services provided by FIEs within the territory of China shall be treated equally in a government procurement and
- FIEs can conduct financing through public offering of shares, corporate bonds and securities or by other means.

In January 2017, the State Council issued the <Notice Regarding Measures on the further Opening-up and the Use of Foreign Capital> (Guofa [2017] No.5, hereinafter referred to as "Guofa No.5"), proposing to further create a fair competition environment for FIEs, which put forward certain measures such as fair competition review, promotion of fair competition among domestic enterprises and FIEs, fair participation in standardization work and fair participation in government procurement biddings, etc. The above-mentioned measures have been formulated in the <Foreign Investment Law> through legislation to provide legal protection to FIEs in enjoying equal treatment in China. It not only helps create a stable, fair, transparent and predictable business environment, but also boosts foreign investors' confidence to make investments in China.

Strengthen the protection of foreign investment

The <Foreign Investment Law> adopted the investment protection system in the <Foreign Investment Law (Discussion Draft)> and revised certain clauses, including:

- Strictly restricting the conditions of expropriating FIEs in China;
- Foreign investors can, in accordance with the laws, freely transfer into and outside China their contributions, profits, capital gains, income from asset disposal, royalties of intellectual property rights (IPR), legitimate compensation or indemnity derived from liquidation, etc., within the territory of China in CNY or foreign currency;
- Protecting the intellectual property rights (IPR) of foreign investors and FIEs as well as the legitimate rights and interests of the relevant stakeholders and strengthening the liability investigation of IPR infringement; the conditions for technology cooperation during the process of foreign investment, shall be determined based on negotiation following the principle of fairness and any administrative measures to force the transfer of technology are not allowed;
- Adding a new provision of confidentiality obligation for administrative authorities and their staff to keep the business secrets of foreign investors and FIEs obtained during their duties;
- Restricting the power of administrative authorities in formulating regulatory documents of foreign investment. Where

relevant laws or regulations are not available, the relevant authorities are not allowed to impair the legitimate rights and interests of FIEs or impose any additional obligations on FIEs, or set any conditions for market access and exit as well as intervene with their normal production and operation activities;

- Establishing a complaint mechanism for FIEs to allow them or their investors to apply for administrative review or file administrative lawsuits when their rights and interests are infringed; and
- FIEs can voluntarily establish and join any chambers of commerce or associations to protect their own legitimate rights and interests.

Regarding the issue of mandatory technology transfer which foreign investors are very concerned about, the prevailing *<Contract Law of the PRC>* and *<Patent Law of the PRC>* both stipulated the prohibition of mandatory technology transfer and the IPR protection. Guofa No.5, the *<Notice Regarding Measures on Promoting the Growth of Foreign Capital in China>* (Guofa [2017] No.39) and the *<Notice on Several Measures for Utilizing Foreign Capital Positively and Effectively to Promote High-quality Economic Development>* (Guofa [2018] No.19) issued by the State Council from 2017 to 2018 also repeatedly stressed that “strengthening and improving the IPR protection of FIEs and prohibiting the mandatory technology transfer through administrative measures”. The *<Foreign Investment Law>* provides a specific clause for this issue to respond to what foreign investors are very concerned about. It helps dispel foreign investors’ doubts by giving FIEs a “reassurance”.

Reflect the requirements of “Streamlined Administration, Delegated Powers, Improved Regulation and Services” and simplify administration on foreign investment

In addition to implementing the negative-list administration system for foreign investment, the *<Foreign Investment Law>* also embodies the requirements of “Streamlined Administration, Delegated Powers, Improved Regulation and Services” and further simplifies the procedures on administering foreign investment, for instance:

- All levels of governments and competent departments are required to simplify the procedures, improve the efficiency, optimize public services to improve their services for foreign investment;
- Unless otherwise stipulated in the laws and regulations, the competent departments shall review the applications of foreign investors in accordance with the same conditions and procedures provided for domestic investors;
- If the investment information to be submitted to the competent departments of commerce by foreign investors or FIEs is available through information sharing among different departments, the requirement of duplicated information reporting is not allowed.

Pushing forward the reform of “Streamlined Administration, Delegated Powers, Improved Regulation and Services” in the foreign investment sector helps to create an efficient and convenient investment environment and attract more foreign investors to make investments in China. The reporting of foreign investment information via a unified system for both domestic and foreign investments can avoid duplicated reporting and reduce FIEs’ compliance burdens to facilitate foreign investment.

The takeaway

By the end of 2018, the total number of FIEs established in China under the “Three FIE Laws” was nearly 960,000, with accumulated total amount of foreign capital actually used in China of over US\$2.1 trillion. Foreign investment has become an important driver in China’s economic and social development. The enactment of the *<Foreign Investment Law>* demonstrates China’s determination and confidence to further expand the opening-up and to facilitate foreign investment, which can help protect foreign investors’ legitimate rights and interests, promote a new pattern of comprehensive opening-up to achieve the goal of high-quality economic development with a high-level of opening-up by creating a rule of law, internationalized and convenient business environment.

We notice that the relevant provisions of “contractual control relationship (VIE structure)” in the *<Foreign Investment Law (Discussion Draft)>* had been removed from the *<Foreign Investment Law (1st Draft)>* that had been submitted for review. The *<Foreign Investment Law>* adopts this revision but retains a miscellaneous clause of “other approaches of investment stipulated in the laws, administrative regulations or circulars of the State Council”. The *<Foreign Investment Law>* no longer provides specific regulations on such issues like the VIE structure arrangement, leaving room to issue technical provisions on the VIE structure arrangement in separate laws or administrative regulations in the future. It still remains to be seen how the VIE structure arrangement and practical issues will be addressed in the future.

The *<Foreign Investment Law>* will come into effect from 1 January 2020 and the “Three FIE Laws” will be abolished at the same time. For FIEs established in accordance with the “Three FIE Laws”, the *<Foreign Investment Law>* grants the existing enterprises a five-year transitional period to maintain their original organizational structures. As the prevailing foreign-invested administrative regime, under the complicated administrative regulations, has been implemented for quite a long time, while the *<Foreign Investment Law>* only provides principle-based provisions. Therefore, we have to wait for the State Council to issue specific implementation regulations to provide clarification on how to enforce the *<Foreign Investment Law>*. As the organizational form and framework as well as activity guidelines of FIEs will be subject to the Company Law and the Partnership Enterprise Law, foreign investors of existing Sino-foreign equity joint ventures or Sino-foreign cooperative joint ventures may need to start negotiating with the Chinese investors to revise the equity or cooperative joint venture agreements or the articles of association.

In terms of Hong Kong, Macao and Taiwan investors, Premier Li Keqiang met the press on 15 March 2019, clearly pointing out that Hong Kong, Macao and Taiwan investments can follow the <Foreign Investment Law> and those existing effective arrangements and practices would continue to be adopted⁵. As companies, enterprises and other economic entities of Hong Kong, Macao and Taiwan investors are treated as FIEs according to the prevailing <Detailed Implementation Rules (DIRs) for the Law on Wholly Foreign-owned Enterprises>, it is anticipated that after the <Foreign Investment Law> takes effect, the treatment of Hong Kong, Macao and Taiwan investments by reference to foreign investment may be clarified in the DIRs to be issued in the future.

Endnote

1. For the <Foreign Investment Law of the PRC>, please refer to the official link:
http://www.npc.gov.cn/npc/xinwen/2019-03/15/content_2083532.htm
2. For the <Special Administrative Measures for Foreign Investment (the Negative List)> (2018 Version), please refer to [China Tax & Business News Flash \[2018\] Issue 23](#) for more details.
3. For the <Special Administrative Measures for Foreign Investment in the PFTZs (the Negative List)> (2018 Version), please refer to [China Tax & Business News Flash \[2018\] Issue 23](#) for more details.
4. For the <Notice Jointly Issued by the NDRC and the MOC Releasing the Negative List for Market Access (2018 Version)>, please refer to [China Tax & Business News Flash \[2019\] Issue 2](#) for more details.
5. For the details of Premier Li Keqiang meeting the press, please refer to the official link:
http://www.gov.cn/premier/2019-03/15/content_5374033.htm#allContent

Let's talk

For a deeper discussion of how this issue might affect your business, please contact:

PwC's China Business & Investment Advisory Team

Bo Yu Partner +86 (10) 6533 3206 bo.yu@cn.pwc.com	Linjun Shen Partner +86 (21) 2323 3060 linjun.shen@cn.pwc.com
--	--

PwC's China Business & Investment Advisory Team specializes in China regulatory advisory and implementation work, ranging from market entry solutions, structure set-up, foreign exchange solutions, to restructuring solutions, e.g., equity transfer, merger and liquidation, etc. The team maintains close dialogues with various Chinese approval and registration authorities as well as industry bureaus at central and local levels. It also has extensive involvement and experience in advising clients on business cases from both the regulatory and practical perspectives.

To further discuss on China related legal issues, please contact:

Rui Bai legal team

Jing Wang Rui Bai Law Firm* Senior Counsel +86 10 8540 4630 jing.wang@ruibailaw.com	Penny Zhao Rui Bai Law Firm* Counsel +86 10 8540 4623 penny.zhao@ruibailaw.com
---	--

Xin Bai legal team

Jamie Yang Xin Bai Law Firm** Partner +86 21 5368 4177 jamie.y.yang@xinbailaw.com	Liang Jiang Xin Bai Law Firm** Counsel +86 21 5368 4024 liang.jiang@xinbailaw.com
---	---

To further discuss on Hong Kong related legal issues, please contact:

Tiang & Partners legal team

Rebecca Silli Tiang & Partners*** Partner +852 2833 4988 rebecca.silli@tiangandpartners.com	Martyn Huckerby Tiang & Partners*** Registered Foreign Lawyer +852 2833 4918 martyn.huckerby@tiangandpartners.com
---	---

*Rui Bai Law Firm is an independent law firm and a member of the PwC global network of firms

**Xin Bai Law Firm is an independent law firm and a member of the PwC global network of firms

***Tiang & Partners is an independent Hong Kong law firm. It is associated with PwC Legal International Pte. Ltd. (a licensed Foreign Law Practice) in Singapore.

Neither Tiang & Partners nor PwC Legal International Pte. Ltd. has any control over, or acts as an agent of, or assumes any liability for the acts or omissions of, the other.

About us:

Rui Bai Law Firm and Xin Bai Law Firm are independent China law firms and members of the PwC global network of firms, dedicated to providing clients with integrated solutions and high-quality legal advice in Mainland China, across Asia and globally. The lawyers are governed by Chinese regulatory standards and they provide legal opinions and advice to clients on matters under Chinese law. Principally based in Beijing and Shanghai, our teams operate across China and very often on global projects.

Tiang & Partners is an independent Hong Kong law firm. It is associated with PwC Legal International Pte. Ltd. (a licensed Foreign Law Practice) in Singapore. We also collaborate closely with Rui Bai Law Firm in Beijing and Xin Bai Law Firm in Shanghai to provide seamless legal services to our clients in China.



One-stop tax information platform of Shui Jie 2.0 version

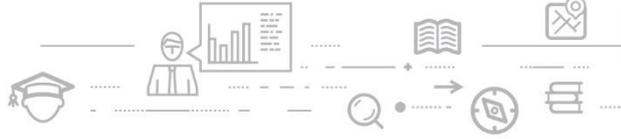
Your exclusive tax think tank



iPhone
(iOS 10 or above)



Android
(Android 6.0 or above)



- For Android users, please scan the QR code to access to Tencent App store.
- Shui Jie web portal - <https://taxnews.pwchk.com>.



In the context of this News Flash, China, Mainland China or the PRC refers to the People's Republic of China but excludes Hong Kong Special Administrative Region, Macao Special Administrative Region and Taiwan Region.

The information contained in this publication is for general guidance on matters of interest only and is not meant to be comprehensive. The application and impact of laws can vary widely based on the specific facts involved. Before taking any action, please ensure that you obtain advice specific to your circumstances from your usual PwC's client service team or your other tax advisers. The materials contained in this publication were assembled on 18 March 2019 and were based on the law enforceable and information available at that time.

This China Tax and Business News Flash is issued by the **PwC's National Tax Policy Services** in China and Hong Kong, which comprises of a team of experienced professionals dedicated to monitoring, studying and analysing the existing and evolving policies in taxation and other business regulations in China, Hong Kong, Singapore and Taiwan. They support the PwC's partners and staff in their provision of quality professional services to businesses and maintain thought-leadership by sharing knowledge with the relevant tax and other regulatory authorities, academics, business communities, professionals and other interested parties.

For more information, please contact:

Matthew Mui
+86 (10) 6533 3028
matthew.mui@cn.pwc.com

Please visit PwC's websites at <http://www.pwccn.com> (China Home) or <http://www.pwchk.com> (Hong Kong Home) for practical insights and professional solutions to current and emerging business issues.

www.pwccn.com