

China

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China Issues Amended Foreign Investment Catalogue for Public Comment

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*On November 4, 2014, the National Development and Reform Commission (NDRC) issued an announcement to seek public comments on a draft amending the **Catalogue for the Guidance of Foreign Investment Industries**. The deadline for submission of comments is December 3, 2014.*

Under PRC law, foreign investment projects are divided into four categories: (1) “permitted,” (2) “encouraged,” (3) “restricted,” and (4) “prohibited.” Foreign investment projects under the “encouraged,” “restricted” and “prohibited” categories are listed in the Catalogue, which is subject to renewals and amendments by the NDRC and the Ministry of Commerce (**MOFCOM**) from time to time. Foreign investment in industries that are not listed in the “encouraged,” “restricted” and “prohibited” categories under the Catalogue are “permitted” investment. The Chinese government started to publish the Catalogue in 1995, and the latest version was issued by NDRC and MOFCOM on December 24, 2011. The Catalogue is an important official policy to guide foreign investment in China.

Compared with the 2011 Catalogue, the 2014 Draft Catalogue has made a considerable number of changes to reduce restrictions on foreign investment in China. For example, the number of restricted items has been reduced from 79 to 35, the number of items that must involve Chinese domestic stakeholders in the forms of equity joint ventures or cooperative joint ventures has been reduced from 43 to 11, and the number of items requiring the Chinese investor(s) to be the controlling shareholder(s) has been reduced from 44 to 32. Therefore, the number of categories prohibiting the form of wholly foreign-owned enterprise (**WFOE**) is reduced from 87 to 43. However, there are notable exceptions, including continued restrictions on foreign ownership in automobile manufacturing, hospitals and certain sectors of the education sector.

We highlight below some noteworthy changes proposed by the 2014 Draft Catalogue for your attention.

Significant Opening-Up in Manufacturing Sector

It is notable that the 2014 Draft Catalogue opens up the manufacturing sector. Many restrictions in the manufacturing sector in the 2011 Catalogue have been lifted in the 2014 Draft Catalogue, such as the beverage manufacturing industry, tobacco industry, petroleum processing and coking industry,

manufacturing of medicine and pharmaceuticals, special equipment manufacturing industry, common equipment manufacturing industry, etc.

Restrictions on Financial Sector Liberalized

Foreign investment in finance companies, trust companies and currency brokerages has been removed from the restricted industries in the 2014 Draft Catalogue. Requirements on foreign investment in banks are specifically addressed in the 2014 Draft Catalogue, which provide that no single foreign financial institution, together with an affiliate under its control or under common control, shall hold over 20% of the equity interest of a bank, and the foreign financial institutions described above shall, in aggregate, hold no more than 25% of the equity interest of a bank.

Automobile Manufacturing

Under the 2011 Catalogue, the manufacturing of complete motor vehicles, special purpose motor vehicles and motorcycles (**Auto Manufacturing**) was categorized as a permitted industry. However, under the 2014 Draft Catalogue, Auto Manufacturing is added to the restricted category. The 2014 Draft Catalogue also reaffirms the existing restrictions on foreign ownership in an Auto Manufacturing joint venture (i.e. not exceeding 50%) and the number of joint ventures for manufacturing complete vehicles (i.e. passenger vehicles, commercial vehicles and motorcycles) a foreign investor is allowed to establish in China (no more than two). Such changes reflect a trend of the Chinese government to tighten up the approval of any Auto Manufacturing joint ventures in the future. Although the foreign auto industry has hoped that the limitations on foreign ownership (i.e. not exceeding 50%) in manufacturing joint ventures and on the number of foreign-invested Auto Manufacturing joint ventures by one foreign investor would be lifted, the 2014 Draft Catalogue does not change such limitations.

Real Estate and Infrastructure

The 2014 Draft Catalogue lifts certain restrictions on the real estate sector (such as development of tracts of land, high-class hotels, office buildings and international exhibition centers, of real estate secondary market transactions, and of real estate intermediary or brokerage companies), which were in the restricted category in the 2011 Catalogue. Also, foreign investment in the construction and operation of golf courses and villas is removed from the prohibited category. In addition, the requirement that the Chinese investor(s) must have majority shareholding in the construction and operation of municipal metros and light railways under the 2011 Catalogue has been removed under the 2014 Draft Catalogue.

Other Noteworthy Restrictions

Restrictions have also been extended to a number of industries, such as health care, education, etc.

For medical institutions (such as hospitals), the 2014 Draft Catalogue clearly lists it as a restricted industry, and the form of foreign investment is limited to a cooperative joint venture.

In the education sector, new restrictions have been introduced to tertiary education and pre-school education, which require a cooperative joint venture for engaging in and a dominant position by the Chinese investor(s). The Chinese investor(s)'s dominant position is also required for common high school education, which only required a cooperative joint venture under the 2011 Catalogue.

New Prohibited Industries

The 2014 Draft Catalogue also adds several new prohibitions on foreign investment, in, among others, the production of nuclear fuel, wholesale and retail of tobacco, production of genetically modified plant seeds, Chinese legal consulting (restraints on non-Chinese legal consulting, however, have been removed), Internet publishing services and the operation of antique stores and auction houses selling cultural relics.

It is reported that the 2014 Draft Catalogue is expected to be submitted to the State Council for approval by the end of 2014, and will be implemented as soon as it is approved by the State Council. We will monitor any developments in the 2014 Draft Catalogue and keep our clients advised. We understand that both the American Chamber of Commerce and the European Chamber of Commerce in China are submitting detailed comments on any proposed changes in the 2014 Draft Catalogue that may impact their member companies, so there may be changes in any final draft.

If you have any questions about the content of this alert, please contact the Pillsbury attorney with whom you regularly work, or the authors below.

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