COMMENTARY

AUGUST 2018

IN SHORT

The Situation: The Negative List is a list of industries for which foreign investment in China is either prohibited, or subject to greater scrutiny and restrictions.

The Development: Chinese authorities have issued a shortened Negative List, under which foreign ownership restrictions have been removed or relaxed in certain industries, including financial services, automotive, transportation, power, and resources.

Looking Ahead: Foreign investors should take advantage of the removal of restrictions in relevant industries, but be aware that other requirements could still be imposed.

China's National Development and Reform Commission ("NDRC") and Ministry of Commerce ("MOFCOM") released a shortened version of the "Foreign Investment Market Entry Special Administrative Measures" ("Negative List") on June 28, 2018. The shortened version of the Negative List took effect on July 28, 2018.

Background

China has been streamlining its administrative processes with respect to foreign investment since October 2016. Previously, all foreign investment proposals in China were subject to case-by-case examination and approval by the local branch of MOFCOM.

However, under the Negative List system, only those investments in the industry categories itemized in the Negative List are either prohibited for foreign investment or subject to approval by MOFCOM. (Additional restrictions are also imposed for some of the industries itemized in the Negative List, including foreign ownership caps, requiring a Sino-foreign joint venture and/or Chinese control of the joint venture, or requiring certain management personnel to be Chinese nationals.)

Foreign investment in any industry not referred to in the Negative List will receive national treatment, such that a mere record-filing with MOFCOM and the local Administration of Industry and Commerce will suffice (unless other laws prohibit or place restrictions on such projects for foreign and domestic investors alike).

Revised Negative List

The key changes under the revised Negative List are outlined below.

Financial Services. A foreign investor is no longer limited to a 20 percent shareholding (or aggregate shareholdings by foreign investors of 25 percent) in a domestic bank. Furthermore, beginning in 2018, foreign companies can hold a controlling 51 percent stake in joint ventures engaged in securities, fund management, futures, and life insurance business, and all foreign ownership caps will be removed for such ventures in 2021.

Automobile Manufacturing. Foreign ownership caps and limits on the number of manufacturing entities to be established in China will no longer apply for manufacturers of "new energy" vehicles (such as electric cars) and "special purpose vehicles" beginning in 2018. Foreign ownership caps will be removed for manufacturers of commercial vehicles in 2020 and for passenger vehicles in 2022. The limit of two manufacturing entities will be removed across the board in 2022.

> Only those investments in the industry categories itemized in the Negative List are either prohibited for foreign investment or subject to approval by MOFCOM.

Petrol Stations. Previously, any foreign-invested enterprise that operated more than 30 local petrol stations and sold different brands and types of petrol obtained from different suppliers would need to be majority Chinese owned. This restriction has been removed.

Railways. The requirements for Chinese control of foreign invested entities engaged in the construction and operation of railway trunk line networks, as well as rail passenger transportation, have been removed.

Ships and Aircraft. Requirements for majority Chinese control of foreign invested entities engaged in the design, construction, and maintenance of ships and certain types of aircraft (such as trunk aircraft, regional aircraft, certain helicopters, and drones), or in the case of general purpose aircraft, the requirement for a Sino-foreign joint venture, have been removed.

Shipping. An international ship freight company established in China is no longer required to be a Sino-foreign joint venture. In addition, international shipping agencies are no longer required to be Chinese controlled.

Power. The requirement for Chinese control of any foreign invested entity engaged in constructing and operating electricity networks has been removed.

Mining and Resources. Foreign ownership restrictions have been removed with respect to the exploration and mining of special and rare coal resources and graphite, the smelting and separation of rare earth, and the smelting of tungsten.

These changes come at a time when other countries are tightening foreign investment restrictions. For example, legislation that would, among other things, expand the jurisdiction of the Committee on Foreign Investment in the United States ("CFIUS") is expected to be signed into law very soon. For some time, CFIUS has been heavily scrutinizing Chinese investments in the United States. The new legislation would require mandatory declarations to CFIUS in certain transactions involving the Chinese government.

THREE KEY TAKEAWAYS

1. Although foreign investment in many industries in China remains prohibited or restricted, the recent revisions to the Negative List provide evidence of China's commitment to further open up its economy and present opportunities for foreign investors to have 100 percent ownership in certain industries where ownership caps previously applied.

2. Nonetheless, the possibility remains that state and/or local regulators may impose approval or other requirements when establishing such foreign invested enterprises, notwithstanding the more liberal policy under the revised Negative List.

3. Foreign investors should review all the relevant regulations and policies and consult with the responsible authorities when considering any investment in China.

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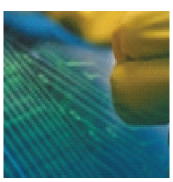

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