



JONES DAY COMMENTARY

CHINA ALLOWS FOREIGN EXCHANGE CASH POOLING

On October 12, 2009, the State Administration of Foreign Exchange (“SAFE”) issued the Administrative Rules on Foreign Exchange Cash Pooling of Group Members of Enterprises in China, Hui Fa [2009] No. 49 (the “Rules”). The Rules provide guidelines for the establishment and operations of cash pooling in foreign exchange for enterprises and their affiliated members within China. The Rules came into effect on November 1, 2009.

ELIGIBLE PARTICIPATING MEMBERS

The Rules regulate only cash pooling in foreign exchange among enterprises or other organizations within China and do not apply to cross-border cash pooling. Members that can participate in cash pooling of a group include (1) the parent company, (2) a subsidiary of which the parent owns 51 percent or more, (3) a company of which the parent and subsidiaries separately or jointly own no less than 20 percent, (4) a company that does not satisfy the 20 percent ownership requirement, but the parent or subsidiary or both jointly are the largest shareholder

of the company, and (5) nonbusiness organizations under the parent or subsidiary. For foreign invested enterprises, Chinese companies that are controlled by the same foreign enterprise can also participate in a cash pooling for those Chinese companies.

SETTING UP CASH POOLING

Enterprises other than financial institutions normally cannot operate lending businesses because of the limitation of their business scope. A foreign exchange cash pooling is operated under an entrusted loan framework. A bank that is licensed to conduct a foreign exchange business will serve as the nominal lender (*i.e.*, the bank makes a loan to a borrowing member on behalf of the lending member). The enterprises determine the interest rate and other loan terms; the bank does not assume any credit risk and charges only a service fee. The principal enterprise setting up a cash pooling should select an authorized bank, and the participating members/lenders should open special foreign exchange accounts at the bank. The bank should apply for the establishment of

foreign exchange cash pooling with the SAFE branch at the location of the bank, which should make a determination on the application within 20 working days.

As an alternative to an entrusted loan arrangement, foreign exchange cash pooling can be implemented through a finance company of the enterprise group within China. In such situations, the finance company receives foreign exchange deposits from cash surplus members and makes foreign exchange loans to the members that need cash. As those activities are the normal business of a finance company, the approval of SAFE is not required.

RESTRICTIONS ON INTEREST RATES AND CURRENCY CONVERSION

The Rules require that interest charged in cash pooling should be determined in reference to interest rates on commercial loans for the same term on the international market. The interest rate cannot be abnormally high or low. One of the restrictions on foreign exchange cash pooling provided by the Rules is the conversion of foreign currency into Chinese currency, Renminbi. If a cash pooling is operated in an entrusted loan arrangement, a borrowing member is not permitted to purchase Renminbi using the foreign

currency obtained from the cash pooling or pledge the foreign exchange for a Renminbi loan. If the conversion into Renminbi is needed, the foreign exchange fund must be returned to the lending member, and the lending member can convert the foreign exchange into Renminbi according to applicable foreign exchange regulations.

If a foreign exchange cash pooling is operated through a group finance company, the finance company is allowed to convert foreign exchange into Renminbi for participating members. However, the finance company must satisfy certain requirements to conduct such business. Furthermore, the conversion must be approved by the SAFE branch at the location of the finance company.

LAWYER CONTACT

For further information, please contact your principal Firm representative or the lawyer listed below. General email messages may be sent using our "Contact Us" form, which can be found at www.jonesday.com.

Fuli Cao

+86 10 5866 1223

fcao@jonesday.com