

A horizontal banner image with a grid overlay. It contains various legal symbols: a scale of justice on the left, a judge's gavel on the right, and a close-up of a person's face wearing glasses in the center. The text "JONES DAY COMMENTARY" is overlaid in white, bold, sans-serif font.

JONES DAY
COMMENTARY

CHINA ISSUES NEW POLICIES TO ATTRACT FOREIGN INVESTMENT

On April 6, 2010, the State Council of China issued Several Opinions on Further Improving the Work of Utilizing Foreign Investment (the "Opinions").

BACKGROUND

The global economic and financial crisis has been affecting foreign direct investment in China since 2008. The amount of foreign investment into China during the first half of 2009 dropped 17.9 percent, and between 2008 and July 2009, foreign investment decreased for 10 consecutive months. Furthermore, the foreign press has reported that China no longer welcomes foreign investment in the manner it was welcomed before and has cited the cancellation of previous forms of preferential treatment for foreign investors and the central government's rejection of several major foreign acquisitions. The Opinions thus aim to refute the notion that China no longer welcomes foreign investment. Although the full impact of the Opinions remains to be seen, the Opinions express the following overall goals: to optimize the

structure of foreign investment; to attract more foreign investment to central and western undeveloped regions; to diversify the use of foreign investment; to further reform and simplify the foreign investment administrative system; and to create a favorable investment environment for foreign investors.

We summarize below some key features of the Opinions that are likely to have an impact on foreign investors and their future or existing investments in China.

AMENDMENT OF THE FOREIGN INVESTMENT CATALOGUE

The Catalogue of Industries for Guiding Foreign Investment (the "Foreign Investment Catalogue") was issued by China's National Development and Reform Commission ("NDRC") and the Ministry of Commerce ("MOFCOM"). The Foreign Investment Catalogue has been amended four times since its issuance, and the most recent revision was made in October 2007. The Foreign Investment Catalogue sets out "encouraged,"

“restricted,” and “prohibited” categories for all foreign investment projects in China. Any foreign investment project not included in the Foreign Investment Catalogue is deemed to be permitted. Generally speaking, encouraged foreign investment projects will be entitled to certain preferential treatment, while the restricted projects are subject to more restrictive approval requirements.

The Foreign Investment Catalogue is supplemented by a Central and Western China Foreign Investment Catalogue, which lists additional encouraged activities and sectors for projects in central and western regions.

The Opinions indicate that the Foreign Investment Catalogue and Central and Western China Foreign Investment Catalogue will be amended to: (i) facilitate the general planning of major industry adjustment and restructuring; (ii) cultivate and develop emerging industries, *i.e.*, renewable energies, biological and pharmaceutical industries, and the information industry; (iii) promote the development of the service industry; (iv) support technical innovation; and (v) emphasize environmental protection, energy saving, and decreasing emissions. The Central and Western China Foreign Investment Catalogue will also add labor-intensive projects into the encouraged category, which is to encourage environmentally friendly but labor-intensive projects.

The Opinions also set forth certain preferential policies benefiting qualified foreign investment. For example, by the end of 2010, qualified foreign-invested research and development centers are entitled to exemptions from China customs duty and value-added tax for the import of necessary goods related to the research, and some qualified projects falling under the encouraged category are entitled to discounted land prices at 70 percent of the statutory minimum price. Additional details are expected to be specified in subsequent rules that are yet to be promulgated.

ENCOURAGING FOREIGN INVESTMENT IN CENTRAL AND WESTERN CHINA

The economy and infrastructure of central and western China are not as well-developed as in eastern China. In order to implement the Strategies of Western Development set forth by the central government, the Opinions extend certain preferential tax policies to foreign-invested enterprises in China’s central and western regions.

The new income tax law that became effective in January 2008 unifies the income tax rates of both domestic enterprises and foreign-invested enterprises to 25 percent, and the original preferential tax treatment applied to all foreign-invested enterprises was cancelled. However, foreign-invested enterprises in central and western China that fall under the encouraged investment category may still enjoy a preferential tax rate of 15 percent until the end of 2010. The Opinions indicate that such preferential tax policies for foreign-invested enterprises in central and western China might be further extended. In addition, new incentives will be issued to encourage the relocation of the foreign-invested enterprises from eastern regions to central and western regions.

PROMOTING DIVERSIFIED USES OF FOREIGN INVESTMENT

The Opinions also aim to: (i) encourage foreign investors to participate in the restructuring of domestic enterprises through mergers and acquisitions; (ii) encourage foreign investors to invest in China’s public companies as strategic investors; and (iii) support the listing of qualified domestic enterprises in overseas capital markets. Most importantly, the Opinions confirm that China is looking to have more foreign-invested enterprises listed on China’s domestic stock exchange.

Moreover, the Shanghai Stock Exchange has completed draft rules governing the listing and trading of overseas-based companies and plans to launch an international board that would allow foreign companies to sell shares denominated in Chinese currency for the first time. It is expected that the international board of the China stock market will be launched at the end of this year.

SIMPLIFYING THE APPROVAL PROCESS FOR FOREIGN INVESTMENT

To make the regulatory approval process more efficient, the Opinions have adjusted the approval process by reallocating approval authority governing foreign investment, giving more delegation to respective local governments. Originally, encouraged and permitted projects with a total investment amount exceeding US\$100 million needed to be approved by NDRC and MOFCOM at the central government level in Beijing. Upon the issuance of the Opinions, only encouraged and permitted projects with a total investment amount exceeding US\$300 million must be approved by NDRC and MOFCOM. Any foreign investment project below US\$300 million may be approved at the respective local government levels. However, the approval structure for projects falling under the restricted category remains unchanged. The Opinions also indicate that the government will continue to improve the administration of and legislation for antitrust review and national security review for foreign acquisitions.

OTHER OBSERVATIONS

Although the Opinions highlight the overall direction that China's foreign investment policies are intended to take in the future, the Opinions lack detail in many areas. It is still not very clear what amendments to the Foreign Investment Catalogue will be made, what preferential policies will be issued to promote foreign investment in central and western China, what regulations will govern national security review of foreign investors' acquisitions, and when the international board of the China stock market will be formally launched.

It also remains to be seen whether a set of effective well-reasoned and well-coordinated implementation rules will be adopted to implement and reach the goals that are expressed in the Opinions.

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