WILMERHALE

China’s State Council Announces Expanded Opening to Foreign Investment

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On January 17, China's State Council published the Notice on Several Measures on Increasing of Openness to Foreign Investment and Active Use of Foreign Investment (Guo Fa [2017] No. 5). The notice is intended to expand China's openness to foreign investment into China. The notice coincides with President Xi Jinping's speech in support of globalization at Davos but the details remain to be specified.

The notice consists of 20 measures divided among three chapters as follows:

1. Increased openness to foreign investment

The restrictions on market access by foreign investment in such sectors as services, manufacturing, and mining are to be lifted through amendment of the Catalogue for the Guidance of Foreign Investment Industries (the Catalogue) and other Chinese policies and regulations.

In particular, foreign investment restrictions in key service industries including banking-type financial institutions, securities companies, securities investment fund management companies, futures companies, insurance institutions and insurance intermediary institutions will be lifted. Restrictions on foreign investment in accounting and auditing, architecture and design, and credit ratings will also be lifted while the telecommunications, Internet service, culture, education and transportation industries will be opened in an orderly manner.

In the manufacturing sector, restrictions will be removed on railway transportation equipment, motor vehicles, ethanol fuel, and oil and fat processing. Foreign investors will be encouraged to invest in high-end, smart and environmentally-friendly manufacturing.

Foreign investors are also encouraged to take part in infrastructure construction through public-private partnerships, establish research and development centers in China, and cooperate with Chinese companies as well as technology and innovation institutions. To this end, China will facilitate the formalities for qualified foreign personnel to work in China.

We note, however, that the changes announced late last year in the draft revision of the Catalogue were quite modest. For example, in the financial services sector, the draft removes only credit ratings out of the restricted category and deletes nationality requirements on the managing partners of accounting and auditing firms, while financial services industries such as banking, insurance, and securities remain in the restricted category, with foreign investment in securities joint ventures limited to a minority equity interest. Thus, the extent to which the notice promises a reduction in foreign investment access barriers is unclear.

Moreover, the notice, like the revised draft Catalogue, also does not reduce restrictions on foreign investment in many critical sectors like information technology, while paradoxically welcoming foreign investment in sectors like railway transportation equipment where domestic competitors have already become dominant.

2. Maintain fair competition between foreign-invested and domestic companies

The notice emphasizes equal treatment of foreign-invested and domestic companies with respect to implementation of relevant policies and regulations, government procurement, intellectual property protection, formulation of industry standards, and equity and debt financing. Enforcement agencies are directed to refrain from imposing arbitrary restrictions on foreign investment. Such changes would be highly welcomed by foreign investors if implemented as a recent survey by the American Chamber of Commerce in China ranks "inconsistent regulatory interpretation and unclear laws," "increasing Chinese protectionism" and "difficulty obtaining required licenses" as principal challenges to doing business in China.

3. Attract more foreign investment

The notice provides that local governments are authorized to formulate their own policies to attract foreign investment. The notice encourages foreign investors to locate investments in China's northeastern and central regions by granting preferential tax, land and financing treatment. It is unclear how willing foreign investors will be to invest in regions that have not been attractive to domestic companies.

The notice directs the competent departments under the central government to formulate and implement the details for each measure.

In a news conference held on January 6 by the State Council Information Office, Vice Minister of Commerce Wang Shouwen maintained that China remains the world's second largest destination for foreign investment, and that the concern that China's investment environment has grown tougher for foreign capital to compete with homegrown companies is untrue. Mr. Wang assured that, through adoption of those measures, foreign investors will be welcome as always and will be respected and treated equally with domestic companies. Mr. Wang commented that remittances of foreign capital (such as dividends and decrease of registered capital reductions) would not be trapped in China under recent capital-control measures, which are intended to curb short-term speculative money outflows.

Foreign investors are unlikely to be reassured by such commitments in the near to medium term. China has recently taken a series of capital-control measures to fight an increasingly severe cycle of capital outflows that have weakened the yuan since last August. Last November, the State

Administration of Foreign Exchange instructed banks to sharply limit the threshold for approval by municipal-level foreign exchange regulators for capital remittances to $5 million, down from $50 million. Despite that, as reported by *The Wall Street Journal*, until now, few of China's capital control measures took obvious aim at foreign businesses. Foreign investors, especially non-strategic foreign investors in financial services sectors, are deeply concerned about the impact of China's clampdown on remitting their investment returns out of China.

Authors

Lester Ross

PARTNER

Partner-in-Charge, Beijing Office

lester.ross@wilmerhale.com

+86 10 5901 6588