

China alert

Tax and regulatory developments

TAX

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Rules eased further as China continues to attract foreign investment

In brief

- Two new sets of regulations issued recently significantly relaxed rules governing foreign investment – both for major investments in listed companies, and for second-tier investments
- This issue of China alert explores the regulations and their implications for foreign investors

Relevant regulations discussed in this issue:

Administrative Measures for foreign investors making strategic investments in Listed Companies, Order (2005) No.28, issued on 31 December 2005 by five government bodies, effective from 31 January 2006 (Order 28)

Supplementary Regulation for Foreign-invested Holding Companies, Order (2006) No. 3, issued on 26 May 2006 by the Ministry of Commerce, effective from 1 July 2006 (Order 3)

Notice on Implementation of the Regulation Clarifying the Application of Laws and Regulations in Respect of the Approval and Registration of Foreign Invested Enterprises, Gong Shang Wai Qi Zhi (2006) No. 102, issued on 26 May 2006 by the State Administration of Industry and Commerce (Notice 102)

New rules, new structures

Foreign investors with strategic investments in PRC-listed companies are currently regulated by *Order 28*.

Under *Order 28*, a foreign investor which takes a stake in a PRC-listed company is required to acquire the A-shares of at least 10% of the total issued shares of the listed company for a minimum period of three years. In addition, the foreign investor (or its parent company) has to:

- Hold overseas assets of not less than USD100 million in total; or
- Manage overseas assets of not less than USD500 million in total

However, these rules are set to change. May 2006 saw the release of *Order 3*, which – when taken together with rules governing the establishment of holding companies by foreign investors – marks a significant reduction in the investment requirements.

Order 3, which took effect on 1 July, allows foreign-invested holding companies to invest in China-listed companies. A holding company established under these rules will be regarded as an 'overseas shareholder' of the listed company.

According to the pre-existing regulations contained in *Shangwubuling (2004) Notice 22*, the minimum registered capital of a holding company established by a foreign investor is USD30 million. Therefore, with the release of *Order 3*, foreign investors are now effectively allowed to invest in PRC-listed companies via a holding company with a registered capital requirement of only USD30 million – significantly lower than the requirements under *Order 28*.

Contact us

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Second-tier investment restrictions also relaxed

Since 1 September 2000, a foreign-invested enterprise investing in the PRC either by setting up or acquiring a share in a PRC has been subject to a 50% threshold under *Order 6*, issued by the Ministry of Foreign Trade and Economic Cooperation (now known as MOC) and the State Administration of Industry and Commerce (SAIC). That is, the level of investment made by the FIE should not be more than 50 percent of the net asset value of the investor FIE.

This all changed in May 2006, when the SAIC announced, in *Notice 102*, that this 50 percent threshold would be dropped.

Although *Notice 102* does not explicitly specify an implementation date, it is generally interpreted that the notice took effect from the date of issuance (i.e. 26 May 2006).

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