Year in review, Year to come
PRC Law

December 2019
Year in review
PRC Law in 2019

In 2019, mainland China continued on its path of attracting more inbound investment, whilst relaxing certain restrictions on capital flows and progressively liberalising its capital markets.

Prohibition on gender discrimination
On 18 February 2019, nine central government authorities jointly issued a circular promoting the employment of females and putting an express ban on gender discrimination during recruitment. Employers are not permitted to check marital or child rearing status during job interviews. Pregnancy tests in any pre-employment medical check are also now prohibited. A fine of RMB 10,000 to 50,000 may be imposed on employers whose job advertisements contain gender discrimination.

Clarifications around foreign debt registration
In February, the National Development and Reform Commission ("NDRC") released an official announcement regarding its requirement to register foreign debt (including debt incurred offshore by PRC-controlled entities) under NDRC Circular 2044. It observed that certain enterprises had been failing to comply with this requirement and reiterated the need to do so. It also clarified that local enterprises may register their foreign debt directly with central NDRC, rather than dealing with its regional branches. Previously, there had been some concerns that local NDRCs were taking differing approaches to registration, particularly in relation to offshore loans.

Shareholder protection enhanced
The Supreme People’s Court’s April judicial interpretation on the application of the Company Law (i) gives shareholders increased powers to obtain compensation for and take action against related party transactions, (ii) sets a 1-year time limit for profit distribution resolutions to be performed, and (iii) provides more flexibility to courts to refuse compensation to directors validly removed from office, and to uphold settlements between deadlocked shareholders aimed at avoiding company liquidations.

New market for the Shanghai Stock Exchange
In January, the Shanghai Stock Exchange launched the Sci-Tech innovation board ("STAR Market"). The STAR Market focuses on supporting enterprises in new and innovative industries, and allows businesses that are unprofitable, or with weighted voting rights structures, to go public. A widened price fluctuation range of 20% operates, with no limits on price fluctuation for the first five trading days. On 22 July 2019, trading commenced on this market, on which UBS was the first foreign underwriter to complete an offering.

More foreign participation in mainland China’s bond market
In September, the rules on foreign institutional investors trading on the interbank bond market were relaxed, allowing the transfer of bond investments and cash balances between an investor’s accounts opened under the qualified foreign institutional investor ("QFII") scheme and its RMB counterpart scheme as well as those directly opened in the interbank bond market. The record-filing procedures in the different markets were also streamlined.

Monopolistic behaviour sanctioned
The antitrust watchdog further toughened its stance against monopolistic conduct, by levying fines on the total turnover of the companies concerned rather than the turnover directly affected by the sanctioned conduct. Through various newly-issued implementation rules, and the procedural rules which consolidate and unify the settled view and practice, the authority is better positioned and equipped for more robust enforcement after the recent institutional reshuffle.
In April, the Hong Kong Government and the Mainland Supreme People’s Court signed the Arrangement Concerning Mutual Assistance in Court-ordered Interim Measures in Aid of Arbitral Proceedings by the courts of the two territories (the “Arrangement”). The Arrangement, which became effective in October, allows parties to arbitral proceedings seated in Hong Kong SAR to apply, at any time before an arbitral award is made, to Mainland courts for interim measures including property preservation, evidence preservation and conduct preservation. Equally, any party to arbitral proceedings in Mainland may apply to the Hong Kong SAR courts for interim measures pursuant to Hong Kong law — a remedy that is already available to parties to foreign-seated arbitral proceedings.

Hong Kong SAR-Mainland mutual enforcement

In February, the Hong Kong Government and the Mainland Supreme People’s Court signed an agreement for reciprocal enforcement of civil and commercial judgments under both PRC and Hong Kong law. The agreement, which became effective in October, extends the pre-existing reciprocal enforcement mechanism to include injunctions and specific performance and does away with the requirement of the parties’ advance agreement to submit to the exclusive jurisdiction of a Mainland or Hong Kong SAR court. Certain matters, including personal bankruptcy and corporate insolvency, are not covered by the agreement.

(R)QFII investors no longer subject to SAFE-determined quotas

In September, the State Administration of Foreign Exchange (“SAFE”) announced that it would be revising the relevant regulations of the QFII programme to remove individually assigned quotas and total overall caps on institutional investors. Similar restrictions under the Renminbi QFII programme will be removed at the same time.

Investments by foreign invested enterprises

In October, SAFE released reforms that will facilitate foreign invested enterprises in non-investment sectors in making equity investments with their registered capital. Such FIEs will no longer be required to have the word “investment” in their business scope, which was in practice very difficult to obtain, in order to be eligible to make equity investments.

Relaxation of restrictions in banking and insurance sectors

In September, the China Banking and Insurance Regulatory Commission relaxed several key restrictions on the operations of foreign-funded banks and foreign bank branches, including business scope restrictions, track record, prudential and capital requirements. Another set of reforms makes it possible for a broader range of insurance and financial institutions to invest in foreign-funded insurance companies.

Shanghai-London Stock Connect

June saw the official launch of the Stock Connect scheme between the Shanghai and London stock exchanges, which allows eligible companies listed on both exchanges to issue depositary receipts in each other’s market. A-share listed Huatai Securities is the first issuer to list global depositary receipts (GDRs) under the scheme, raising US$1.69bn in what was London’s largest GDR offering since 2012.

Reducing procedural burdens of inbound debt

In October, SAFE announced various measures to reduce the procedural burden for enterprises borrowing offshore. For example, it expanded, to a total of 18 free trade zones and the entire city of Shanghai, a pilot programme which allows qualifying enterprises to convert foreign exchange capital raised offshore (including loans and market-based funding) into RMB, without SAFE verifying the use of proceeds upon conversion. It also removed the requirement for borrowers to apply to SAFE to deregister the foreign debt upon repayment of the loan. Instead, borrowers can do this through the domestic banks.

Merger control review process streamlined

2019 saw continued progress in streamlining and expediting the merger review process. Cases reviewed under the simplified procedure are generally cleared within one or two months and clearance of offshore deals with no mainland China nexus take an even shorter time to obtain. Meanwhile, complex cases with potential competition concerns still receive close scrutiny with “pull and refile” to buy more review time not uncommon. The proposed joint venture between Zhejiang Garden Biochemical and Royal DSM took 552 days to obtain clearance the most prolonged review period thus far.

Interest rate reform

In August, the central bank unveiled interest rate reforms intended to allow for more effective transmission of monetary policy and lower costs of funding for the real economy. Its new loan prime rate is set at an average of the rates 18 designated commercial banks charge their best corporate clients. The central bank hopes that this will better reflect market dynamics than the previous mechanism, under which the one-year lending rate stood still at 4.35% for the last four years. This reform was followed by a 5-basis point cut in the one-year medium-term lending facility rate (a key reference rate used by banks to price their loans) in early November.

More flexibility for backdoor listings

In October, the rules on material asset restructurings by A-share listed companies were revised, reducing the look-back period from 60 months to 36 months and removing the profit test as one of the trigger thresholds for requiring CSRC approval of a backdoor listing. Amid the slowing economy, the revisions should make it easier for A-share listed companies to raise finance and undergo transformations by acquiring high quality assets and businesses from their controlling shareholders.

Foreign investment catalogue

The foreign investment authorities updated the negative list in July, with the goal of eliminating, by the end of 2019, all market-entry restrictions on foreign investment outside the negative list. Previous restrictions in the list in oil and gas, cinemas, infrastructure and freight forwarding were among those to be removed in this revision. The government also significantly expanded the list of industries eligible for preferential policy treatment, with a focus on high-end manufacturing, advanced services and labour-intensive industries.
In 2020, mainland China is expected to continue with market-based reform and eliminating procedural intervention in a broad range of regulatory areas. These reforms, together with the new Foreign Investment Law, aim to improve the process of doing business.

**Whistleblower rules on the way**

The State Council issued a guiding opinion on 12 September 2019 kicking off the establishment of the whistleblower regime with the aim of enforcing supervision on enterprises. The guiding opinion called for rewards and protection for whistleblowers. Currently, there are no specific rules protecting workplace whistleblowers. While further details are awaited, employers should fully prepare for the possibility that future corporate governance will further prevent or mitigate regulatory risks.

**Social credit system to be fully live in 2020**

A series of policies was released this year to further the establishment of the social credit system (“SCS”). Before the SCS is expected to go fully live in 2020 (which is the ultimate goal set out in a general plan in 2014), there is already a huge amount of data being gathered by and for the government in place and this pool of information will continue to grow with a central database and information sharing platform, called “Internet + Monitoring”, which is currently being developed. The authority is still working on granular details about the SCS, whilst multinational companies are particularly concerned about whether they would be targets for the SCS and what impacts they would be subject to if they were blacklisted.

**New law to expand resources tax base**

Mainland China’s first resources tax law will come into effect in September 2020. The new law lists all 164 types of taxable resources covering all currently discovered minerals and salts. In general, local governments are given the flexibility to set the tax rate for different resources within a range on the basis of price or output, subject to approval of the local people’s congress. The law will also standardise tax reductions and exemptions.

**PRC Securities Law to be amended**

As the State Council moves closer to finalising the new registration-based IPO system, 2020 may see an amended Securities Law passed to update the regulatory regime to cover depositary receipts, stock issuance conditions, new information disclosure requirements and exemption of employee share options from restrictions on public offerings. Additional rights to compensation for investors against listed companies, securities companies and directors are expected to be another key focus of the new law.

**Orderly exits by controlling shareholders**

Preventing the onset of market chaos as a result of large stake sales in listed companies has been a longstanding concern of the mainland Chinese stock market. It has been reported that a plan has been submitted by the regulators for approval, which will regulate the disposal of stakes in listed companies after the post-IPO lock-up period expires. This follows the introduction of restrictions earlier this year against share sales by controlling shareholders when the listed company is buying back its shares.

**First stage rollout of China VI emission standards**

In 2020, the first stage of the mainland’s China VI emission standard will be applied to all buses, postal and sanitation vehicles, after having first been introduced in gasoline fuelled vehicles in 2019. The second stage rollout, which incorporates particle number and remote emissions control, will not be completed until 2023.

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**2020 highlights**

Foreign investors to be promised a level playing field alongside improvements in the business environment

More extensive regulatory scrutiny of business and investment activities, both online and offline

Financial sectors to be further opened up to foreign investors – abolition of ownership caps in three key sub-sectors and wide-ranging reform in other niche areas
Antitrust scrutiny of online platforms
With the State Administration for Market Regulation completing the consolidation of antitrust enforcement powers in 2019, antitrust enforcement is expected to enter a new era from 2020. It is anticipated that antitrust scrutiny of internet platforms will increase in 2020 together with impositions of sanctions.

Merger control and national security amid geopolitical tensions
Merger control and national security reviews of cross border M&A transactions will continue to be streamlined amid ongoing geopolitical issues, such as the Sino-US trade dispute. More broadly, with the coming into effect of new rules on monopolistic agreements in 2019, more clarity on legal rules and heightened penalties on infringements are on the rise.

Foreign investment law and related implementing rules
With the new Foreign Investment Law, 2020 will enshrine, for the first time, the concepts of a level playing field for foreign investors and protection of their rights as a principle of national law. Foreign investors will be busy complying with the five-year transition period for revision of their existing foreign invested entity structures in accordance with the PRC Company Law. At the same time, the new law sets the scene for additional fundraising opportunities. Implementing rules are being prepared, which may provide some clarity on the new rights and obligations and on the regulatory status of Chinese-controlled foreign direct investment into mainland China.

Liberalisation of caps and restrictions in financial services
At various points in 2020, the caps on foreign investment in securities, mutual fund management and life insurance companies will be completely removed, making 100% foreign-owned presences in these sectors possible. We can also expect the further opening up of niche financial services such as pensions, wealth management, money broking, commercial factoring and insurance asset management to foreign investment.

Outbound investment regulation
2020 is likely to see the further development of the outbound investment regime to include a comprehensive set of quantitative and qualitative information to be submitted online to MOFCOM on a monthly and half-yearly basis following the closing of an outbound investment project. Additional requirements apply to projects that are above a certain value or located in specially designated regions. The new system is also expected to cover crisis reporting.

Foreign arbitral institutions in mainland China
Come 2020, eligible international arbitral institutions from countries and territories outside mainland China, including Hong Kong SAR, Macau SAR and Taiwan, will be entitled to apply to establish offices in Lingang in the Shanghai Free Trade Zone to administer foreign-related arbitration proceedings in the international commercial, maritime and investment sectors. Prior to this, the enforceability of such internationally-administered arbitration proceedings had already been recognised in ad hoc judicial decisions. The market anticipates that the new rules, which are stated to have a term of three years, will spark a new era of international arbitration.

Reducing the procedural burden of inbound debt
SAFE has announced plans to introduce reforms permitting domestic borrowers in some areas to utilise and repay cross-border loans without needing to register each individual fund flow. The loan would still need to be registered with SAFE up-front and fall within the borrower’s foreign debt quota (currently set at two x net assets). This move would continue the trend towards lifting procedural barriers to cross-border financing arrangements and could potentially be accompanied by other similar measures.

Attracting foreign investment in distressed debt
During 2019, PRC regulators have been concerned about systemic risks resulting from increasing volumes of bad debt. It has been reported that domestic financial asset management companies, which deal in non-performing loans, may now be suffering liquidity pressures themselves. In 2020, we could see regulators taking further measures to address these concerns - for example, by expanding pilot schemes to facilitate the direct transfer of non-performing loans offshore.

Revisions to QFII-related rules
In early 2020, SAFE’s foreign exchange rules will be revised, and the bank account classifications updated, to implement (i) the removal of the QFII quota system for institutional investors, and (ii) the consolidation of the QFII programme with its RMB-denominated counterpart. The rules may also be amended to provide for tighter supervision of QFII investors and the trading activities in their client accounts, including distinguishing proprietary from client investments and reporting on overseas hedging activities.

Collective land and farmland reform
The amended Land Administration Law comes into effect from 1 January 2020. It will no longer be mandatory for construction to be undertaken on state-owned land or on collective land that has been acquired by the state. The new law will improve the marketability of collective land, as such land, if zoned for industrial, commercial or other business purposes and duly registered, will be capable of being directly transferred or leased by the owner. The new law also aims to protect the rural environment by conferring permanent status on certain farmland.
What now?
Your contacts

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