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Newsletter

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Legal Updates

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Legal Updates

1. New Trends in Overseas Investment Administration (Authors: Gloria XU, Claire XIAO)

On August 4, 2017, the *Guiding Opinions on Further Guiding and Regulating the Direction of Overseas Investment* (Guo Ban Fa [2017] No. 74) " (the "**Guiding Opinions**") was jointly promulgated, with the approval of the State Council, by the National Development and Reform Commission ("**NDRC**"), the Ministry of Commerce ("**MOFCOM**"), the People's Bank of China ("**PBOC**") and the Ministry of Foreign Affairs ("**MFA**"). The Guiding Opinions have drawn wide attention by further categorizing overseas direct investments as "encouraged," "restricted" or "prohibited" based upon the previous "negative list" for overseas direct investment. In this article, we will summarize the main content of the Guiding Opinions by comparing them to the existing principles governing overseas direct investment in light of recent trends related to the supervision of overseas direct investment.

Existing approval and filing system for overseas direct investment

On September 6, 2014, MOFCOM promulgated the *Measures for the Administration of Overseas Investment* (MOFCOM Order [2014] No. 3) ("**Administrative Measures**"), which enacted a "primary filing, supplemental approval" regulatory system for overseas direct investment, and provided that, based upon specific circumstances, overseas direct investment must be filed with or approved by the government. Under the Administrative Measures, overseas direct investment projects that are not referenced in the "negative list" need only to be filed with MOFCOM or its counterparts at the provincial level. This stipulation saw significant changes from the previous version of *Measures for the Administration of Overseas Investment* (MOFCOM Order [2009] No. 5), which set forth that all overseas direct investment projects were subject to MOFCOM approval. The Administrative Measures, for the first time, provided a "negative list" system for the administration of overseas direct investment, stipulating that overseas direct investment is negative listed and subject to approval where it involves "sensitive countries and regions (i.e., countries that have not established diplomatic relations with China, countries that are sanctioned by United Nations)" and "sensitive industries (industries related to products and technology restricted from export by the PRC government, industries that impact the interests of a country or a region."

In response to Administrative Measures, on December 27, 2014, NDRC promulgated an amendment to the *Measures for the Approval and Filing of Overseas Investment Projects* (NDRC Order [2014] No. 9) ("**Approval Measures**"), which stipulated that NDRC approval was required for overseas direct investment projects that "involve sensitive countries/regions and sensitive industries." The Approval Measures further explain the definition of "sensitive industry" by stipulating that these industries include basic telecoms operations, cross-border water resource

exploration and utilization, large-scale real property development, transmission lines, power grids, news media, etc., which is more specific than the definition under the Administrative Measures.

Trends in overseas direct investment supervision

Based upon the "filing-based approval plus negative list" system for overseas direct investment supervision, in late November 2016, NDRC, MOFCOM, PBOC and SAFE issued a joint statement("Joint Statement") which stipulated the following overseas direct investment projects would be prohibited in principle:

- a Overseas direct investments of USD \$10 billion or above;
- b The purchase or development by State-owned enterprises of large-sized real estate located outside China with Chinese investment exceeding USD \$1billion;
- c M&A and investment transactions with investment amounts of USD \$1billion or more while the target business is not among the domestic investor's main business;
- d Foreign direct investment by partnerships;
- e Overseas direct investment to acquire or subscribe less than 10% shares of an offshore public-listed company;
- f Overseas direct investment in an offshore entity whose assets value is substantially larger than the domestic investor;
- g Domestic capital participating in privatization transactions related to the delisting of China-based offshore public-listed company;
- h Overseas direct investment by recently-established entities.

On December 6, 2016, spokespersons for the NDRC, MOFCOM, PBOC and SAFE jointly held a press conference ("**Press Conference**") where they indicated that the regulatory departments will "pay close attention to irrational overseas direct investment in certain industries such as real estate, hotels, theaters, entertainment and sports clubs, as well as potential risks related to large-sized investments made by domestic entities to overseas target whose business is not among such domestic investor's main business, overseas direct investment made by limited partnerships and the phenomena of 'investments in overseas companies with substantially heavier assets than the Chinese investor' and 'quick-establishment, quick-investment.' We recommend the relevant enterprises to make investment decisions in a prudent manner."

The Guiding Opinions

The four ministries jointly promulgated the Guiding Opinions based upon the foregoing laws and regulations to further emphasize the principles for overseas direct investment supervision. These principles include:

- a With respect to the regulatory process, the Guiding Opinions continue to stipulate a filing system as the principal means of regulating overseas direct investment, and change to an “encouraged development plus negative list” standard to determine whether to require examination or filing for projects.
- b The Guiding Opinions further refines the “negative list” by re-categorizing “investments subject to approval” and “investments subject to filing” under the Administrative Measures and Approval Measures as “encouraged investments,” “restricted investments” and “prohibited investments.” According to the Guiding Opinions, enterprises undertaking encouraged investments will receive more preferential treatment with respect to tax, foreign exchange, insurance, customs and information; the regulatory departments will supervise enterprises that undertake restricted investments so as to encourage them to act in a prudent manner, and shall provide guidance and advice to them based upon actual circumstances; the regulatory departments will take effective measures to strictly control prohibited investments.
- c The Guiding Opinions divide overseas direct investments into the following categories:
 - i. Encouraged:
 - a) Overseas infrastructure investment that will facilitate the construction of the “Belt and Road” and connect surrounding infrastructure;
 - b) Overseas investment that will facilitate the export of superior production capacity, high quality equipment and technical standards;
 - c) Overseas direct investment that will help to strengthen cooperation with overseas high-tech enterprises and advanced manufacturing enterprises (such as the establishment of R&D centers);
 - d) Participate in offshore energy resource exploration and development, such as oil and gas, minerals, etc.
 - e) Mutually beneficial investment cooperation in the areas of farming, forestry, animal husbandry, fisheries, etc.;
 - f) Facilitate overseas direct investment in services sectors such as business trade, culture and logistics; support qualified financial institutions to establish branches and service networks abroad.
 - ii. Restricted: mainly refers to overseas investments that are not consistent with the national diplomatic policy, the win-win opening up strategy and state macro-control policies, including:
 - a) Overseas development investments in sensitive countries and regions that have not established diplomatic relations with China, or are unstable due to conflict or subject to investment restrictions in accordance with multilateral treaties or agreements concluded by China;

- b) Overseas direct investments in real estate, hotels, theaters, entertainment industry, sports clubs;
- c) Establishment of equity investment funds or investment platforms offshore without engaging in any specific operations;
- d) Overseas direct development investments that utilize outdated production equipment that does not meet the national technical standards required in the country of the investment target;
- e) Overseas direct investments that do not meet the local standards of the investment target with respect to environment protection, energy consumption and safety.

Overseas direct investments under the first three foregoing categories are subject to the approval of the competent supervisory authorities for overseas direct investment; it is not yet clearly specified whether investments under the latter two categories are required to be approved by or filed with the relevant departments.

iii. Prohibited: refers to overseas direct investment that will or may endanger national interests or national security, including:

- a) Overseas direct investment involving the export of core military technology and products without government approval;
- b) Overseas direct investment involving the use of technology, know-how or products that are prohibited for export by the PRC government;
- c) Overseas direct investment in the gambling or pornography industries;
- d) Overseas direct investments that are prohibited by international treaties concluded or acceded to by China;
- e) Other overseas direct investments that will or may endanger national interests or national security.

d Compared to the Administrative Measures and the Approval Measures, the Guiding Opinions:

- Expand the scope of encouraged overseas direct investment projects, and specify that the government will support overseas direct investments in this category;
- The scope of restricted overseas direct investments are expanded to include four new types of overseas direct investments (i.e., items (2) to (5) listed under the Restricted category above), which is a change from the previous rules that generally restricted overseas investments in “sensitive countries and regions” and “sensitive industries.” The Guiding Opinions clearly stipulate that overseas direct investment in real estate, hotels, theaters, entertainment and sports clubs (i.e. item (2)), and the establishment of overseas investment platforms (i.e. item (3)) is subject to prior examination and approval requirement. This requirement reflects the regulatory principles referenced in the Joint Statement and Press

Conference that the government will restrict overseas direct investment in the real estate industry, large-sized investments made by domestic entities to overseas target whose business is not among such investor's main business, overseas direct investments made by limited partnerships, transactions in which the acquired/invested overseas target is of heavier asset compared to the parent company and so-called "quick-establishment, quick-investment" transactions.

- Re-categorization of several "sensitive industries" involving investments subject to prior approval under the previous regulations as prohibited investments, and further refining of the list of prohibited investments.

Summary

The Guiding Opinions continue with the current principle that overseas direct investment is subject to filing administration, while also making adjustments to the existing "negative list." The Guiding Opinions further reflect the recent changes in overseas direct investment administration trends by clearly specifying the investment industries and business models that will be subject to close supervision and strengthen the supervision of establishment of offshore private equity fund. The Guiding Opinions will further affect domestic enterprises' decision as to their overseas investment targets and the design of investment structures.

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2. New Bike-sharing Rules: The Role of Government, Operators and Users (Authors: Gloria XU, Cheng CHEN, Qianfei WANG)

On August 1, 2017, the *Guiding Opinions on Encouraging and Regulating the Development of Internet Bicycle Rentals* (Jiao Yun Fa [2017] No. 109) (the "**Opinions**") was jointly promulgated with State Council approval by ten ministries and departments, including the Ministry of Transport, the Publicity Department of CPC, the Office of the Central Leading Group for Cyberspace Affairs, the National Development and Reform Commission, the Ministry of Industry and Information Technology, the Ministry of Public Security, the Ministry of Housing and Urban-Rural Development, the People's Bank of China, the General Administration of Quality Supervision, Inspection and Quarantine and the National Tourism Administration. Before the promulgation of the Opinions, which is the first national departmental rules specially aimed at the Internet bicycle rental (hereinafter referred to as "**bike-sharing**") industry, road traffic administration or other related departments in Beijing, Shanghai, Tianjin, Shenzhen, Guangzhou, Chengdu, Shijiazhuang and several other cities had successively released normative documents or drafts for comments of such documents related to bike-sharing industry.

According to the Opinions, **the municipal governments shall be responsible for administering the bike-sharing industry.** The Opinions grants a certain degree of autonomy to municipal governments to formulate their own specific local policies in light of their differences in urban planning and development level. In this article, we will summarize and comment on the Opinions around the three stakeholders in bike-sharing industry as put forward by the Opinions, i.e. governments, operators and users.

Role of Government

The Opinions requires governments to undertake more responsibilities related to administering bike-sharing operations, strengthen the administration and guidance in the bike-sharing industry and encourage bike-sharing industry to develop in an orderly and secure manner. Governments are to undertake the following duties in terms of administration of bike-sharing industry:

- Stick to giving priority to the development of public transportation. Government may promote the integrated development of public bicycle rentals and bike-sharing, while the development of Internet electric bicycle rentals is discouraged;
- Guide operators to put bicycles into operation in an orderly manner;
- Optimize bicycle transportation networks. Governments may render rational arrangement for slow traffic networks and bicycle parking facilities, actively promote the construction of bicycle paths and improve road signs and line markers;
- Promote the layout and construction of bicycle parking lots. Governments may draw up a negative list to exercise the no-parking policies in those areas and sections of road unfit for parking, plan and construct auxiliary bicycle parking lots in important urban commercial districts, public transport stations, transportation hubs and residential areas and the vicinity of tourist attractions etc.;
- Enhance standardized development of Internet bicycle rentals. Local governments are encouraged to establish local standards with respect to the operation, maintenance and disposal of bicycles in the bike-sharing industry, and to accelerate the establishment of basic and general national standards. Governments may adopt such means as certification and accreditation, supervision and spot-check etc. to ensure product quality and safety;
- Enhance credit management. Governments may accelerate the establishment of a credit record system in the bike-sharing industry, build basic enterprise and user credit databases, punctually share credit information with national credit information sharing platforms and enhance the evaluation of enterprise service quality and user credit ratings.

Since July of this year, municipal governments in Hangzhou, Zhengzhou, Fuzhou, Guangzhou, Nanjing and several other cities have proposed to control the quantity of shared bikes, and have required the suspension of newly increased bikes put into operation. However, as reflected in the

Opinions, it is still the major policy that the central government encourages orderly development of bike-sharing industry, and requires municipal governments to bring their role into active play when performing their administrative functions, and furnish public services of guiding, supporting and improving ancillary facilities to the bike-sharing industry. In the future, local governments are expected to formulate detailed requirements based on their administration of the industry of bike-sharing, including local policies and standards related to bike-sharing, which are likely to cause the reduction of damage rate, loss rate and accident rate of shared bikes.

Regulations on Operators

As mentioned above, the Opinions upholds the principle of encouraging the development of and administering in an orderly manner the bike-sharing industry. The Opinions further specifies responsibilities of and requirements for bike-sharing service operators, which sets higher requirements for compliance of operators on one hand, and serves as guidance for operators to observe when operating their bike-sharing business on the other hand. According to the Opinions, bike-sharing service operators need to observe the following operating principles:

- Fully utilize bicycle satellite positioning, big data and other information technologies to strengthen the operation and management of their bicycles;
- **The responsibility of operators regarding management of bicycles parking is specified.** Operators shall enhance the management of bicycle dispatching, parking and maintenance, promote the application of electronic fences and other technologies, timely dispose irregularly parked bicycles and bicycles with security threats or out of service and schedule bicycles in timely manner. **Operators that suffer from severe problems with respect to disorderly bicycles parking or placement and have poor offline operations and services, and fail to take effective measures upon being notified, will have those issues publicly disclosed and such operators will be restricted from placing bicycles into service;**
- Implement and use a real-name system for bike-sharing users;
- Enter into service agreements with users to define their respective rights and obligations, and to specify requirements on users' riding and parking;
- **Providing bike-sharing services to children under the age of 12 is prohibited;**
- Clearly display fee calculation methods and standards, make a public commitment to quality service, and establish a complaint handling mechanism;
- **Purchase personal injury insurance for users;**
- **Timely submit information on the quantity and distribution areas of bicycles that are placed into operation and other operating information to the local competent departments;**

- **Strengthen supervision on user fund. Operators are encouraged to adopt rental services to users without a deposit, and shall rigorously separate their own funds from users' funds of deposits and advances, open special accounts for user deposits and advances, implement earmarks for special purpose funds, and expedite the process of achieving “prompt deposits upon rental, prompt refunds upon return” of shared bikes;**
- Settlement services shall be provided by banks and non-bank payment institutions, and operators shall sign relevant agreements with such institutions;
- **Operators who undergo acquisitions, mergers, restructurings or cease operating shall protect the legitimate rights and interests of users and the security of their funds;**
- Comply with the Cyber Security Law. Operators shall place their servers within the territory of mainland China, implement graded protection to cyber security, data security management and personal information protection systems;
- The formation of credit information sharing alliances and the establishment a promise-keeping inspiring mechanism and a promise-breaking punishment mechanism are encouraged;
- The development of cross-enterprise and cross-brand **rental platform services is encouraged.**

In order to promote orderly management and ensure safe operations in bike-sharing industry, the Opinions clearly provides that it is operators who are responsible for bike parking management and purchase of personal injury insurance for users, and requires operators to accelerate the process of ensuring promptly paying deposits upon rental and refunding deposits upon return. Those aforesaid provisions subject operators to higher requirements in terms of operational modes and cost. In addition, the Opinions requires operators to promote satellite positioning, electronic fences, big data and other technologies, and encourage operators to provide Internet bike rental services on a deposit-free basis. In the future, municipal people's governments are likely to introduce detailed promotion and encouragement rules and regulations, which will encourage investment in technical improvement, implementation of deposit-free policy and users' credit data collection and evaluation etc. In addition, operators shall also upgrade the degree of network security and data security and standardize the collection and use of users' personal information.

Also, the aforementioned measures will promote the development of relevant technology application and credit services, facilitate technological development in operators, promote cooperation between operators and third-party technology providers, urban traffic data providers and credit service institutions, and establish an effective, safe and technology-based travel services network.

Regulations on Users

In order to further achieve the goal of travel safety, the Opinions also requires bike-sharing users

to voluntarily abide by the following norm of conduct:

- Observe laws, regulations and provisions regarding road traffic safety and urban administration and service agreements voluntarily, use bicycles in a civilized manner, ride bicycles safely and park bicycles normatively;
- **Check technical conditions of shared bicycles before riding** to ensure cycling safety;
- Do not carry passengers when riding bicycles in violation of the rules or mount child seats or other equipment in shared bicycles without authorization.

The Opinions specifies user’s duty of care with respect to the security status of shared bikes before riding. In the event of an accident, whether the user has exercised such duty of care shall be an important factor in division of responsibilities between operators and users. Also, the abovementioned requirement will encourage operators to work out relevant service agreements, which regulate and guide users to use shared bikes properly on one hand, and specify responsibilities borne by users in the event of accident due to misuse of bicycles by users on the other hand, and therefore are of instructive significance to division of responsibilities between users and operators when accidents occur.

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