漢坤律師事務所
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Newsletter

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Legal Updates

Legal Updates

1. Shanghai Circulates Incentive Policy 2.0 for Foreign-Invested R&D Centers (Authors: David TANG, Jun LI, Serina WEI)

On October 16, 2017, Shanghai Municipal People's government circulated the *Several Opinions on Further Supporting Foreign-Invested Research and Development Centers to Participate in Shanghai's Construction of a Science and Technology Innovation Center with Global Influence* (Hu Fu Fa [2017] No. 79, hereinafter "**Opinions**"), which can be regarded as a policy 2.0 to promote the establishment and development of foreign-invested research and development centers ("R&D Centers") following the issuance in 2012 of the *Several Opinions of Shanghai Municipality on Encouraging the Establishment of Foreign-Invested Research and Development Centers* by the Shanghai Municipal Commission of Commerce, the Science and Technology Commission of Shanghai Municipality and the Shanghai Municipal Development and Reform Commission.

The Opinions contain 16 sections, and provide numerous and unprecedented support policies for R&D Centers, which focus on the following aspects:

I Providing Funding and Support to R&D Center Establishment and Innovation Technology Projects

The Opinions introduce detailed support funding policies for R&D Centers established in Shanghai, including funding for starting up and property leases for global R&D Centers or independent R&D Centers with more than 100 research personnel.[1] In response to multinationals' trend towards open innovation in recent years, the Opinions first provide support funding for property leases[2] for foreign-invested open innovation platforms, which are encouraged to join together the innovation resources of other multinationals, medium, small or micro enterprises and innovation teams to build "open innovation ecosystems." In addition, the Opinions also provide special funding amounting to RMB 3 million for enterprise technology platforms at the municipal level which will engage in improving innovation capability, upgrading core technologies and intelligent green manufacturing, and for major R&D projects in strategic emerging industries.

II Encouraging R&D Centers to Collaborate with Scientific Research Institutions, Government Platforms and Social Capital

[1] In Section 1 of the Opinions, for global R&D Centers or legally independent R&D Centers with more than 100 research personnel, they can receive 5 million RMB funding for starting up, and will receive a property lease funding amounting to 30% of the rent at the standard of no more than 1,000 square meters and no more than 8 RMB per sqm per day for a period of three years.

[2] In Section 2 of the Opinions, regarding open innovation platforms allows for property lease funds amounting to 30% of the rent at the standard of no more than 1,000 square meters and no more than 8 RMB per sqm per day from the government at the district level for a period of three years.

The Opinions encourage R&D Centers to collaborate with scientific research institutions, public service platforms, government projects and industry funds, domestic and overseas innovation service providers and social capital, to share innovation resources with those sources and platforms to promote the transformation of research innovations. The Opinions also encourage R&D Centers to utilize government scientific research platforms, such as the Shanghai public research service platform, the government-planned project experts database, the Shanghai municipal finance science and technology investment information management platform and the National Eastern Tech-Transfer Center. The Opinions further provide guidance and support policies for R&D Centers to utilize such platforms and channels, and also to direct social capital to support R&D Centers in order to apply innovations to production in Shanghai[3].

III Focusing on Protection and Realization of Intellectual Property for R&D Centers

One of the highlights in the Opinions is the focus on protecting and realizing the intellectual property of R&D Centers. The Opinions detail awards for each PCT patent or domestic invention patent applied for by an R&D Center.[4] To improve the multiple dispute settlement mechanism in the intellectual property area, the Opinions also attempt to combine administrative and judicial intellectual property protection approaches together to explore "integrated one-step services" that incorporate patent examinations, fast approvals and fast patent rights protections. Meanwhile, the Opinions encourage foreign investment in intellectual property services, and encourage internationally known intellectual property service institutions to develop their business in Shanghai to cultivate a better intellectual property service and protection environment.

IV Building an Environment Favorable for Talents, Simplifying Entry and Exit Policy

With respect to R&D Centers, Shanghai is competitive in human resources both domestically and in surrounding countries. The Opinions stipulate measures to assist R&D Centers to attract and gather research talents, including convenient measures for the entry and exit of Chinese talents, and for the entry and exit, work permits and residence permits for foreign talents. Foreign talents can also be listed in the government-planned project experts database. In particular, the Opinions allow foreign research personnel who are engaged by R&D Centers to directly apply for permits to work in China for the first time, which provides the most convenient working permit system ever for the foreign talents working in R&D Centers.

V Other Support Policies

Besides the above-mentioned policies, the Opinions also simplify the import and inspection formalities for samples and reagents for R&D Center operations and research. As for financial

[3] See Sections 5-8 of the Opinions.

[4] Section 10 of the Opinions provides that each successful PCT application may be awarded up to 250,000 RMB, with a subsidy of up to 50,000 RMB per country for up to 5 countries; each successful high-quality domestic invention patent may be awarded up to 15,000 RMB.

support policies, the Opinions expand the scope of free trade accounts so that R&D Centers can use these accounts to enjoy flexible cross-border financial service policies. The Opinions also encourage qualified R&D Centers to purchase insurances such as important technology equipment insurance, research and development equipment insurance, product liability insurance and product quality insurance.

Furthermore, the Opinions not only set out specific preferential policies for the establishment, development and operation of R&D Centers, but also specify the governmental departments responsible for the implementation of certain policies to make clear to these departments of their duties which is significant for guiding the practical operation of these policies. The new policies in the Opinions will promote R&D Centers to participate in the establishment of Shanghai as a scientific innovation center, while also helping R&D Centers to achieve better development in Shanghai.

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2. A Brief Overview of the Pilot Program for Foreign-funded Equity Investment Enterprises (Authors: James Yong WANG, Ally HU, Yi XU)

On September 22, 2017, the Shenzhen Municipal Finance Office, Shenzhen Municipal Government Financial Services Office, Market and Quality Supervision Commission of Shenzhen Municipality and Qianhai Administration Bureau jointly issued the *Pilot Program for Foreign-funded Equity Investment Enterprises in Shenzhen* ("**New QFLP Measures**"), based upon the *Interim Measures for the Launching of a Pilot Program for Foreign-funded Equity Investment Enterprises in Shenzhen* (Shen Fu Jin Fa [2012] No.12) (the "**Interim Measures**") and *Operating Procedures for the Pilot Program for Foreign-funded Equity Investment Enterprises in Shenzhen* (Shen Fu Jin Fa [2012] No.13) ("Operating Procedures"). The New QFLP Measures reflect improvements to the pilot program for qualified foreign limited partner ("**QFLP**") system in Shenzhen.

Foreign-invested equity investment pilot enterprises established under the QFLP system serve as an important channel for foreign investors to participate in investments in China. On December 24, 2010, the Shenzhen Municipal Finance Office, Shanghai Municipal Commerce Commission and Municipal Administration of Industry and Commerce jointly promulgated the *Implementing Measures for the Pilot Program for Foreign-funded Equity Investment Enterprises in Shanghai*, which marked the initial launch of the QFLP pilot program in Shanghai. Subsequently, the QFLP pilot program was also introduced successively in Beijing, Tianjin, Shenzhen, Chongqing and Qingdao. In 2012, Shenzhen officially launched the QFLP pilot program by promulgating the Interim Measures and Operating Procedures. Compared to these two earlier regulations, the New QFLP Measures see modifications mainly in the following aspects:

I. Expanded pilot enterprises and scope

According to the Interim Measures, foreign-funded equity investment management enterprises ("**FEIMEs**") may be established with investments from foreign enterprises or individuals (it is not expressly provided whether a FEIME can be established in the form of a Sino-foreign joint venture; in practice, however, we have found a small number of FEIMEs that exist in the form of Sino-foreign joint ventures), and are only permits "foreign investor management of foreign capital," meaning that FEIMEs are only permitted to manage foreign-funded equity investment funds. However, according to Article 8 of the New QFLP Measures, a FEIME cay be established either in the form of a wholly foreign-owned enterprise or in the form of a Sino-foreign joint venture. The New QFLP Measures also clearly specify the conditions to be met by domestic and foreign shareholders and partners:

- Foreign investors should meet either of the following conditions: (1) in the fiscal year prior to applying, hold proprietary assets (net assets) of not less than USD 100 million or its equivalent or hold assets under management of not less than USD 200 million or its equivalent; (2) hold an asset management license issued by the Hong Kong Securities and Futures Commission (or other offshore financial regulatory authority).
- Domestic investors should meet either of the following conditions: (1) be a licensed financial institution approved by the state financial regulatory department, such as a commercial bank, a securities exchange, an insurance company, a trust company, a financial leasing company or a public fund management company, or a be a direct 50% or greater held subsidiary thereof; (2) be a large-sized enterprise that was introduced by the municipal government, which in the year prior to applying held proprietary assets (net assets) of not less than RMB 500 million or assets under management of not less than RMB 1 billion yuan, have achieved profits for the most recent three consecutive years with total net profit not exceeding RMB 60 million and a cumulative total taxes paid of less than RMB 18 million.

The New QFLP Measures allow for "foreign investor management of domestic capital" on the basis of "foreign investor management of foreign capital," which means that FEIMEs are permitted to initiate the establishment of, or be entrusted to manage, domestic private equity and venture capital funds.

In addition, in accordance with the principle of "uniform standards for domestic-funded enterprises and foreign-funded enterprises," the New QFLP Measures also permit "domestic investor management of foreign capital," which means that qualified domestic private equity and venture capital fund management companies are permitted to initiate the establishment of, or be entrusted to manage, FEIMEs.

- A domestic private equity or venture capital fund management company must satisfy the following conditions to initiate the establishment of, or be entrusted to manage, a FEIME: (1) be a domestic enterprise incorporated in accordance with the laws of China; (2) be a domestic private equity or venture capital fund management company that has been registered with the

Asset Management Association of China ("**AMAC**") for more than six months; (3) in the year prior to applying, hold proprietary assets (net assets) of not less than RMB 500 million yuan or assets under management of not less than RMB 1 billion; (4) have a sound governance structure and solid internal control systems and not have received punishment from judiciary or relevant regulatory authorities in the last three years; (5) have a management company registered in Shenzhen.

Through the implementation of these three policies, "foreign investor management of foreign capital," "foreign investor management of domestic capital" and "domestic investor management of foreign capital," the Shenzhen QFLP pilot program further expands its targets and scope of application, which will help to encourage more domestic and foreign fund managers and investors to participate in the pilot program.

II. Clearly specifying the conditions for domestic and foreign FEIME investors

Based upon the criteria and conditions for qualified investors provided by AMAC, the New QFLP Measures specify appropriate entry thresholds for different types of investors in order to encourage various kinds of funds to participate in the pilot program:

- A domestic or foreign-funded enterprise must satisfy the following conditions to become a limited partner of a FEIME: (1) be an institution or individual which has corresponding risk identification ability and risk - taking ability; (2) in the case of an institutional investor, have a sound governance structure and solid internal control systems, and have not received punishment from judiciary or relevant regulatory authorities in its place of residence for last three years; if a foreign institutional investor, possess net assets of not less than USD 5 million or its equivalent, with a single investment of not less than USD 1 million or its equivalent; if a domestic institutional investor, hold net assets of not less than RMB 10 million, with a single investment of not less than RMB 1 million; (3) in case of individual investors, sign an equity investment enterprise (fund) risk disclosure letter; for both the domestic and foreign individual investors, hold financial assets of not less than RMB 3 million or achieve an average annual income of not less than RMB 500,000 for last three years, with a single investment of not less than RMB 1 million.

III. Clarifying FEIME investment limitations, and restricting the proportion of investments from the same controller

Consistent with the principle upheld by the central government of promoting investment in industry sectors and discouraging virtual investments, the New QFLP Methods require FEIMEs to be guided by the Catalogue for Foreign Investment Industries to invest directly in industry sectors and prohibit the establishment of FEIMEs in the form of fund of funds (in our understanding, this means that it is not possible to establish an FEIME for fund of funds management purposes, even though an investment made by the fund of funds through its ultimate equity investment and venture capital funds could also directed to industry sectors. In addition, it remains to be confirmed in practice whether

QFLP funds making portfolio investments through a subordinate SPV is subject to this restriction). Besides this restriction, if the general partner and the limited partner of a FEIME are controlled by the same controller, the total capital contribution ratio of that controller cannot exceed 50%.

IV. Clearly specifying requirements for fund manager registrations and fund filings; FEIMEs failing to complete such registrations and filings are disqualified from participating in the pilot program

In order to eliminate the existence of so-called "empty shell FEIMEs," which refers to FEIMEs that have not issued products for several years and which have not exited from the pilot program due to the absence of an exit mechanism, the New QFLP Measures require FEIMEs to complete registration with AMAC within 12 months of obtaining approval to conduct FEIME operations and to establish an initial FEIME and the first domestic private equity or venture capital fund within this 12-month period. FEIMEs and domestic private equity or venture capital funds so established should be filed with AMAC within 6 months from their establishment (it remains to be confirmed how to determine the time of establishment, whether by the date of establishment, the time of initial closing or the time of final closing; we understand that it may be the time of initial closing or final closing). A FEIME failing to complete fund manager registrations and fund filings in a timely manner will be disqualified from participating in the pilot program and be publicly notified.

V. Clearly specifying procedures for amending FEIME registration items

Because the Interim Measures are ambiguous about the procedures for amending FEIME registration items, in practice some FEIME directly conduct relevant AIC registration amendments without approval. According to the New QFLP Measures, if a FEIME applies to amend its registration items (including the change of company name, business scope, shareholders or partners, to increase or decrease subscribed or paid-in contributions, to change the contributions payment schedule, change company form, senior officers, or the division or merger, dissolution, liquidation or bankruptcy of the company) , the Market and Quality Supervision Commission of Shenzhen Municipality will seek the opinion of the Shenzhen Municipal Finance Office. Where an FEIME intends to amend its registration items, the FEIME should submit application materials to the Shenzhen Municipal Finance Office, which should make a decision within 15 business days after initially reviewing the materials and consulting the opinion of the pilot program leading group.

VI. Specifying post-supervision responsibilities of trust banks

The New QFLP Measures clearly specify the responsibilities of custodial banks. Specifically, FEIMEs should entrust a commercial banking institution authorized by the state financial supervision department, above the branch level, which has the capital escrow capacity and qualifications to take custody of principal funds. The FEIME and FEIME-managed domestic RMB funds should entrust a commercial banking institution authorized by the state financial supervision department, above the branch level, which has the capital trust capacity and qualifications to take custody of project funds.

Banks in charge of both principal capital and project capital escrow accounts will supervise the use of capital within such accounts to ensure the authenticity and compliance of the use of such funds. The banks will supervise the FEIMEs to use the funds within the escrow accounts within their business scopes, in accordance with the law and in a legitimate manner, shall conduct anti-fraud and anti-money laundering inspections upon project settlement, and will urge the FEIMEs to pay the relevant taxes and fees. Specifically, the bank in charge of the principal capital escrow accounts is responsible for supervising the income or profit of all the projects managed by the FEIMEs, while the banks in charge of the project capital escrow accounts are responsible for supervising the movement of capital for specific projects.

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Important Announcement

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