

## Review Restart Reform of SEZ – A Brief Analysis of Hainan FTP’s Investment and Financing Facilitation Policies

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Hainan is China’s largest special economic zone by area. On June 1, 2020, the Central Committee of the Communist Party of China and the State Council issued the *Overall Plan for the Construction of Hainan Free Trade Port* (the “**FTP Plan**”) to provide for implementing the Hainan Free Trade Port system **throughout Hainan Island**. The FTP Plan is the cornerstone of China’s support for Hainan to **gradually explore** and **steadily promote** the construction of **a free trade port with Chinese characteristics**, and to incrementally establish free trade port policies and systems. The FTP Plan also demonstrates China’s determination and efforts to take to a new level of the promotion and development of an open economy.

The FTP Plan sends several significant signals for opening-up. Key words such as “trade liberation and facilitation,” “investment liberation and facilitation,” “zero tariffs,” “low tax rates,” “reduced tax regimes,” “strengthened rule of law,” and “front line being opened up, second line being controlled” instill hope in the market for deepening reform and future development for Hainan, China’s largest special economic zone.

In this article, we focus on introducing and summarizing the new measures and systems under the FTP Plan for investing in Hainan enterprises and overseas financing of Hainan enterprises.

### New access policies of Hainan market

#### I Implement the market access upon commitment system

The FTP Plan requires: (1) strict implementation of “access when not prohibited,” whereby, under the premise of “effective control,” **permits and approvals are cancelled in principle** for areas **subject to mandatory standards** and **replaced by a sound record-filing system**, and market participants can begin investment and business activities by committing to satisfying related requirements and submitting relevant materials for record-filing; (2) **foreign investment to be subject to the pre-access national treatment plus negative list system**, which significantly reduces prohibited and restricted items.

To implement the market access upon commitment system, the FTP Plan sets forth the following key tasks to be completed before 2025 and 2035:

1. The key tasks before 2025 are: to implement a **“minimal approval”** investment system and to formulate a series of regulatory provisions, including:
  - A. Formulating a **special list for relaxed market access and a negative list for foreign investment market access in the Hainan Free Trade Port**;
  - B. Clarifying the geographical scope covered by the business operations for foreign-invested enterprises established in specified service industries that are to first open up;
  - C. Establishing and improving **national security reviews system, industry access environmental standards, and social credit system**, etc., and fully implementing the “minimal approval” system;
  - D. Deepening the reform of “separating permits from business licenses”;
  - E. Establishing and improving a process supervision system based on credit supervision and compatible with negative list management.
2. **The key tasks before 2035 are: to further improve the opening-up policies and related systems and arrangements, including:**
  - A. **Fully liberalizing investment access management**, except for areas involving **national security, social stability, ecological protection red lines, major public interests, and other areas for which China implements access management**;
  - B. In areas with mandatory standards, establishing an investment regime of **“standards system plus commitments system,”** whereby market entities can engage in investment and business activities by committing to meet relevant requirements.

The core of the “market access upon commitment system” is the “access when not prohibited” system and the “access upon making commitments” system, both of which were introduced before the release of the FTP Plan.

“Access when not prohibited system”. The promulgation of the *Negative List for Market Access (2018 Version)* by the National Development and Reform Commission (“**NDRC**”) and the Ministry of Commerce on December 21, 2018 indicated that China had fully implemented the negative list for market access system which, in essence, **prohibited market access approval items and ensured equal market access by all entities in accordance with law, except for the entry into negative-listed industries, fields, and businesses, etc.** The FTP Plan reiterates “access when not prohibited” and proposes clearly the establishment of a special list for relaxed market access in the Hainan Free Trade Port. We expect to see a special list for market access in the Hainan Free Trade Port that is less restrictive than in other regions of the country, which conforms to Hainan’s strategic positioning for building itself as a pilot zone for comprehensively deepening reform and opening up, a national pilot zone for promoting ecological progress, an international tourism consumption center, and a national critical strategic service guarantee zone.

“Access upon making commitments” system. The State Council promulgated on November 6, 2019 the *Circular on Carrying out Full Coverage Pilot Programs for the Reform of “Separating Permits from*

*Business Licenses” in Pilot Free Trade Zones*, which stipulates that beginning from December 1, 2019, full-coverage list management would be implemented for all business-related permits in pilot free trade zones. The reform is to be promoted in four ways: **direct cancellation of approvals, conversion approvals into record-filings, implementation of notification and commitment system, and optimization of approval services.**

Subsequently, in February 2020, Haikou City took a leading role by formulating the *Trial Implementation Plan of Haikou City on Full Coverage for the Reform of “Separating Permits from Business Licenses”*, the focus and highlight of which is to subject more matters to notification and commitment management. Specifically, **where enterprise-related business licensing matters need to be retained, notification and commitment management will apply if enterprises commit to meet the business licensing conditions after being notified by government departments of the foregoing conditions, and the relevant government departments can correct behaviors that do not meet the business license conditions through in-process and ex-post supervision<sup>1</sup>.**

The FTP Plan further indicates that in areas with mandatory standards, **permits and approvals system should in principle be cancelled and replaced by a sound record-filing system.** To engage in investment and operations, market players only need to commit to comply with the relevant requirements and submit relevant materials for record-filing.

As part of the “market access upon commitment”, items restricted and prohibited from foreign investment are significantly reduced under the pre-access national treatment plus negative list management system. These provisions are consistent with the foreign investment supervision principles under the Foreign Investment Law. However, compared with other regions in China, it is believed that in the future, the negative list for foreign investment access to Hainan Free Trade Port will be more streamlined, and the prohibited and restricted items will be greatly reduced. We look forward to further exploration of the Hainan Free Trade Port in respect of the “market access upon commitment”.

## **II Innovate and improve investment freedom systems and promote changes in governmental functions**

The FTP Plan proposes facilitation for the supervision of establishment, operation, deregistration, and bankruptcy of enterprises:

1. To facilitate establishment of enterprises: mainly by issuing electronic licenses;
2. To facilitate operations of enterprises: mainly by “ready to respond to all requests from enterprises” and “not to intervene enterprises’ operation unless problems arise”;
3. To facilitate bankruptcy: mainly by fulfilling duties and responsibilities.
4. To facilitate bankruptcy: mainly by fulfilling duties and responsibilities.

In addition, the FTP Plan also proposes the government, with respect to cross-border direct investment

<sup>1</sup> <http://www.hnzhengfa.gov.cn/shixiandongtai/show-7935.html>.

transactions, to simplify management in accordance with the pre-access national treatment plus negative list model, improve the convenience of registration and exchange, and explore new forms to adapt to market demand for cross-border investment management.

These proposals for facilitation will inevitably require the transformation of government functions. The FTP Plan requires government departments to insist on inclusive and prudential supervision of emerging business models, and stipulates that the commitments governments make must be fulfilled. Government departments should promptly indemnify or compensate those who suffer losses caused by their failure to fulfill commitments or inadequate implementation.

### III Further expand the industry opening-up

The FTP Plan provides for vigorously developing tourism, modern service industries, and high-tech industries, and will further lift restrictions on foreign investment in such industries. It is noted that NDRC and the Ministry of Commerce promulgated Decree No. 32 and Decree No. 33 on June 23, 2020, issuing the *Special Administrative Measures (Negative List) for the Access of Foreign Investment (2020)* (the “**Negative List 2020**”) and *Special Administrative Measures (Negative List) for the Access of the Foreign Investment to Pilot Free Trade Zones (2020)* (the “**FTZ Negative List 2020**”), which will be effective on July 23, 2020<sup>2</sup>. We also set forth for comparison provisions of the FTP Plan, the Negative List 2020, and the FTZ Negative List 2020:

Industry	FTP Plan	Negative List 2020	FTZ Negative List 2020
Telecommunications services	<ul style="list-style-type: none"> <li>■ Open up value-added telecommunications services and <b>gradually remove restrictions on foreign shareholding ratios</b>.</li> <li>■ Enterprises which are physically registered and have service infrastructure within Hainan Free Trade Port are allowed to conduct online data processing and transaction processing services across the entire territory of Hainan Free Trade Port and internationally, and gradually to conduct business across China under the premise of safety and effective control.</li> <li>■ Open basic telecommunications services safely and</li> </ul>	<ul style="list-style-type: none"> <li>■ Limited to investment in telecommunications services opened in accordance with China's WTO accession commitments; the proportion of foreign investment in a value-added telecommunications service shall not exceed 50 percent (excluding e-commerce, domestic multi-party telecommunications, store-and-forward business, and call centers);</li> <li>■ Basic telecommunications business must be controlled by the Chinese party.</li> </ul>	<ul style="list-style-type: none"> <li>■ Limited to investment in telecommunications services opened in accordance with China's WTO accession commitments; the proportion of foreign investment in a value-added telecommunications service shall not exceed 50 percent (excluding e-commerce, domestic multi-party telecommunications, store-and-forward business, and call centers);</li> <li>■ Basic telecommunications services must be controlled by the Chinese party (the operator must be a legally established company specializing in basic telecommunications business).</li> </ul>

<sup>2</sup> Upon effectiveness, the Negative List 2020 and the FTZ Negative List 2020 will respectively supersede the *Special Administrative Measures (Negative List) for the Access of Foreign Investment (2019)* and the *Special Administrative Measures (Negative List) for the Access of the Foreign Investment to Pilot Free Trade Zones (2019)*.

Industry	FTP Plan	Negative List 2020	FTZ Negative List 2020
	<p>orderly</p> <ul style="list-style-type: none"> <li>■ Undertake international Internet data exchange pilots, build international submarine optical cables and landing points, and set up international telecommunications gateway exchanges.</li> </ul>		
<p><b>Healthcare</b></p>	<ul style="list-style-type: none"> <li>■ To support Hainan to vigorously introduce foreign premium medical resources. Summarize the pilot construction experience of regional medical centers, and conduct research and support Hainan to build a regional medical center.</li> </ul>	<ul style="list-style-type: none"> <li>■ Medical institutions are limited to joint ventures.</li> </ul>	<ul style="list-style-type: none"> <li>■ Medical institutions are limited to joint ventures.</li> </ul>
<p><b>Education</b></p>	<ul style="list-style-type: none"> <li>■ Overseas <b>high-level universities and vocational colleges</b> of science, technology, agriculture and medicine are allowed to <b>independently run schools</b> in Hainan Free Trade Port and to <b>establish international schools</b>.</li> <li>■ Promote key domestic universities to introduce well-known foreign universities to set up Chinese-foreign cooperative education institutions with independent legal personality in Hainan Free Trade Port.</li> </ul>	<ul style="list-style-type: none"> <li>■ Pre-school, regular senior middle schools and higher educational institutions are <b>limited to Chinese-foreign cooperative schools and must be led by the Chinese side</b> (the principal or principal administrative person should be of Chinese national, and the Chinese members of the administrative committee, board of directors or joint management committee must be no less than one half of the total number).</li> </ul>	<ul style="list-style-type: none"> <li>■ Pre-school, regular senior middle and higher educational institutions are <b>limited to Chinese-foreign cooperative schools and must be led by the Chinese side</b> [the principal or principal administrative person should be of Chinese national (and settle in China), and the Chinese members of the administrative committee, the board of directors or joint management committee must not be less than one half of the total number.] <b>[Foreign educational institutions, organizations or individuals may not set up schools and other educational institutions (excluding vocational training institutions beyond the educational system and vocational training institutions within the educational system) mainly intended for recruiting Chinese citizens as their students, but foreign educational institutions may cooperate with Chinese educational institutions in the establishment of educational institutions that mainly recruit Chinese citizens as their students.]</b></li> </ul>
<p><b>Finance</b></p>	<ul style="list-style-type: none"> <li>■ Support qualified <b>overseas securities fund futures</b></li> </ul>	<ul style="list-style-type: none"> <li>■ No explicit restriction (Have removed the following provision of</li> </ul>	<ul style="list-style-type: none"> <li>■ No explicit restriction (Have removed the following provision of the <i>Special Administrative</i></li> </ul>

Industry	FTP Plan	Negative List 2020	FTZ Negative List 2020
	<p><b>institutions to set up wholly-owned or joint venture</b> financial institutions in Hainan Free Trade Port.</p>	<p>the <i>Special Administrative Measures (Negative List) for the Access of Foreign Investment (2019)</i>: “the foreign shareholding ratio of securities companies, securities investment fund management companies, futures companies and life insurance companies shall not exceed 51% (restriction on foreign shareholding ratio to be lifted in 2021).”</p>	<p><i>Measures (Negative List) for the Access of the Foreign Investment to Pilot Free Trade Zones (2019)</i>:                      “The foreign shareholding ratio of securities companies, securities investment fund management companies, futures companies and life insurance companies shall not exceed 51% (restriction on foreign shareholding ratio to be lifted in 2021).”</p>

It is observable in the table above that the FTP Plan introduces blueprints for opening-up several industries. Compared with the provisions of the Negative List 2020 and the FTZ Negative List 2020, the FTP Plan points out the direction of opening-up in Hainan at this stage, while the negative list for the Hainan Free Trade Port’s and its supporting rules are yet to be issued based on the foregoing provisions of the FTP Plan.

### Overseas financing of Hainan enterprises

For overseas financing of Hainan enterprises, the FTP Plan provides facilitation policies from the aspects of overseas share and bond issuances, including:

#### Key tasks before 2025 are:

- **To support** domestic enterprises registered in Hainan Free Trade Port to **issue stocks overseas** based on their domestic and overseas financing plans, **to prioritize the support to enterprises’ financing through overseas debt issuances, and to delegate the authority to manage the foreign debt issuance registration to the Hainan Provincial Development and Reform Department.**
- To provide that **banks will directly conduct foreign exchange registration for overseas listings** of enterprises in Hainan Free Trade Port on a pilot basis.

#### Key tasks before 2035 are:

- To allow **non-financial enterprises** that meet certain conditions to **borrow foreign debt at their own discretion** based on actual financing needs, **and to ultimately realize full convertibility of the foreign debt of non-financial enterprises in Hainan Free Trade Port.**

Under the current regulations, NDRC registration and record-filing formalities are required when domestic enterprises and their controlled foreign enterprises or branches borrow funds from abroad, whether denominated in local currency or foreign currency, with a maturity of more than one year and the repayment

of principal and interest as agreed, including overseas debt issuances, medium- and long-term international business loans, etc. The FTP Plan devolves enterprise foreign debt registration and record-filing formalities to the Hainan Provincial Development and Reform Department, which will improve efficiency. Explicitly stipulating banks to handle foreign exchange registration for overseas listings and full convertibility of the foreign debts of non-financial enterprises are breakthroughs compared to the current management of foreign exchange under the capital account.

### **Future legislative prospects for the Hainan Free Trade Port**

The Standing Committee of the National People's Congress has included the Hainan Free Trade Port Law on the legislative agenda. In addition to the Hainan Free Trade Port Law, the construction of the Hainan Free Trade Port also requires the refinement and supplementation of local regulations and commercial dispute resolution mechanisms. The FTP Plan has specifically given Hainan full legal authorization to promulgate free trade port commercial regulations on business deregistration, bankruptcy, fair competition, and expropriation. Any reform policies and measures proposed in the FTP Plan involve adjustments to existing laws and administrative regulations shall be implemented upon unified authorization by the National People's Congress and its Standing Committee or the State Council. We will continue to monitor and analyze the legislation of the Hainan Free Trade Port, and provide further information for reference for investment and financing of Hainan enterprises.

***Important Announcement***

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