



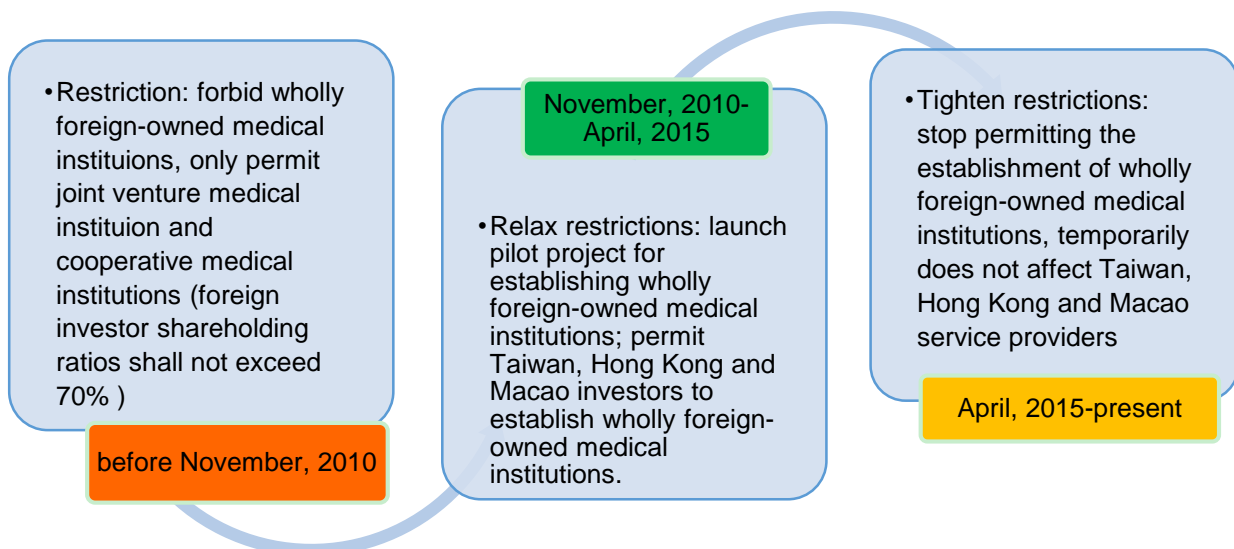
## Foreign Direct Investment Law

### Study on Foreign-Invested Medical Institutions (I): Policy Analysis

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Can foreign investors set up wholly-owned medical institutions in China? This is a question that clients constantly ask when entering the Chinese healthcare industry, and this question is even more complicated when it comes to specific cases. We therefore intend to analyze this issue in terms of regulatory policy and practice by drawing on our experience in assisting multiple foreign institutions to make investments in the domestic healthcare industry. This article is the first of two and will focus on policy analysis.

The PRC government's policies for foreign investment in domestic medical institutions have consistently changed over time. Initially, the PRC government tended to restrict foreign capital from entering the domestic medical industry. At the end of 2010, these restrictions had begun to be relaxed. In 2015, however, the government again tightened its control over foreign investment in domestic medical institutions. These three stages of the PRC government's position towards foreign investment are roughly shown in the following chart:



“Foreign investors” includes investors outside of China and also investors in Taiwan, Hong Kong and Macao. PRC laws and regulations related to the admission of foreign investment ordinarily apply to foreign investors and then cite applicability to Taiwan, Hong Kong, and Macao. In this case, however, policies related to foreign investment in the healthcare industry not only contain general rules applicable to foreign investors, but also some special rules that are only applicable to Taiwan, Hong Kong and Macao investors.

### **Foreign Investors – Bad News, Good News and Bad News Again**

Foreign capital began entering PRC medical institutions in the late 1980s. As the reform and opening up deepened, domestic medical and healthcare services become inadequate to meet the growing needs of foreigners. On February 10, 1989, the former Ministry of Health and former Ministry of Foreign Trade and Economic Cooperation jointly promulgated the *Several Provisions on the Establishment of Hospitals or Clinics by Foreigners or Overseas Chinese and the Medical Practice in China by Foreign Doctors (expired)*, which stipulated that overseas Chinese were permitted to establish one or two wholly-owned non-profit pilot hospitals or clinics and foreigners and overseas Chinese were permitted to establish one or two pilot Sino-foreign joint ventures or contractual hospitals or clinics. In each case, approvals should be obtained from the Ministry of Health and Ministry of Foreign Trade and Economic Cooperation. This is a prologue to establishing foreign-invested medical institutions in China.

Following these policies, the government expressly prohibited the establishment of wholly foreign-owned medical institutions for a significant period. The *Interim Measures for the Administration of Chinese-foreign Equity Joint and Cooperative Joint Medical Institutions* (order of Ministry of Health and Ministry of Foreign Trade and Economic Cooperation, [2000] No. 11, hereinafter referred to as “**Interim Measures**”), effective as of July 1, 2000, set forth that foreign investors were only permitted to establish medical institutions in the form of a joint venture or contractual business, and required the domestic shareholding in such investments to be no less than 30%. *Catalogue for the Guidance of Foreign Investment Industries (revised in 1997)* categorized medical institutions as restricted industry and expressly stipulated that domestic shareholders should have control over such institutions. *Catalogue for the Guidance of Foreign Investment Industries (revised in 2002)* still categorized medical institutions as restricted industry but deleted the domestic shareholder control requirement so as to avoid conflicting with the Interim Measures.

In November 2010, *Circular of the General Office of the State Council on Forwarding the Opinions of the National Development and Reform Commission, the Ministry of Health and Other Departments on Further Encouraging and Guiding Non-government Funding for Medical Institutions* (Guo Ban Fa [2010] No. 58) proposed the opening up of medical institutions and categorizing medical institutions as permitted industry. The circular stipulated the phasing out

of foreign investor shareholding restrictions in medical institutions and to launch a pilot project for qualified foreign investors to establish wholly foreign-owned medical institutions in China. Subsequently, on January 30, 2012, the *Catalogue for the Guidance of Foreign Investment Industries (Revised in 2011)* was promulgated, which also categorized medical institutions as permitted to foreign investment. On November 13, 2013, *Provisional Measures on the Administration of Wholly Foreign-Owned Medical Institutions in the China (Shanghai) Pilot Free Trade Zone* was entered into force, which expressly stipulated that foreign investors were permitted to establish wholly foreign-owned medical institutions in Shanghai pilot free trade zone. Subsequently, on July 25, 2014, the National Health and Family Planning Commission (“**NHFPA**”) and the Ministry of Commerce (“**MOFCOM**”) jointly promulgated the *Circular on Carrying out the Pilot Program for the Establishment of Wholly Foreign-Owned Hospitals* (Guo Wei Yi Han [2014] No. 244, hereinafter referred to as “**Circular 244**”), expressly stipulating that foreign investors may establish wholly foreign-owned hospitals through greenfield investment, merger or acquisition in Beijing, Tianjin, Shanghai, Jiangsu, Fujian, Guangdong and Hainan (“**Seven Pilot Provinces/Municipalities**”).

This period of opening up, however, did not last long. On April 10, 2015, *Catalogue for the Guidance of Foreign Investment Industries (Revised in 2015)* was implemented, and again categorized medical institutions as restricted industry and stipulated that foreign-invested medical institutions may only operate in the form of a joint venture or cooperative. On April 8, 2015, the General Office of the State Council promulgated the *Circular on Issuing the Special Administrative Measures (Negative List) for Foreign Investment Access to Pilot Free Trade Zones*, effective since May 8, 2015, which also categorizes medical institutions as restricted industry. Since the negative list is applicable to the free trade zones in Shanghai, Guangdong, Tianjin and Fujian, this meant the end of the policy permitting the establishment of wholly foreign-owned medical institutions in the Shanghai free trade zone.

Since Circular 244 has not yet been formally abolished, does this mean wholly foreign-owned hospitals are still allowed to be established in the Seven Pilot Provinces/Municipalities? We are afraid that the answer should be no.

- First of all, in terms of legal provisions, Circular 244 was promulgated based upon the *Catalogue for the Guidance of Foreign Investment Industries (Revised in 2011)*, which categorized medical institutions as permitted industry. Since the Catalogue has been further revised and the updated version has been approved by the State Council, the Circular 244 pilot program has lost its policy and legislative foundation.
- Secondly, in terms of practical operations, we consulted with certain competent provincial and municipal healthcare and commercial administrations who also believe the new policy supersedes the Circular 244 pilot program.

- Of course, strictly speaking, there should be no direct conflict between the old and new laws. We recommend that the government resolve this conflict as soon as possible.

Considering that the *Catalogue for the Guidance of Foreign Investment Industries (Revised in 2015)* significantly reduces restricted categories and relaxes restrictions on the foreign investor shareholding ratio in multiple industries, the categorization of medical institutions as restricted industry again causes us to believe that the authorities are unlikely to permit foreign investors to establish wholly foreign-owned medical institutions in China in the near future.

On September 3, 2016, the Standing Committee amended the *Law of the People's Republic of China on Wholly Foreign-owned Enterprises* and other three laws, stipulating that the establishment of foreign-invested enterprises that are not subject to special State admission management rules shall be subject to a filing rather than approval process. The State Council is to formulate or approve the special admission management rules, and the decision will become effective October 1, 2016. It remains to be seen whether the special rules will repeat the relevant provisions in the *Catalogue for the Guidance of Foreign Investment Industries* or instead provide a new national negative list based upon the existing free trade zone list.

Long-term Restriction	Relax Restriction	Tighten Restriction
<ul style="list-style-type: none"> <li>• Several Provisions on the Establishment of Hospitals or Clinics by Foreigners or Overseas Chinese and the Medical Practice in China by Foreign Doctors</li> <li>• Interim Measures for the Administration of Sino-foreign Equity Joint and Cooperative Joint Medical Institutions</li> </ul>	<ul style="list-style-type: none"> <li>• <i>Circular on Further Encouraging and Guiding Non-government Funding for Medical Institutions</i></li> <li>• <i>Catalogue for the Guidance of Foreign Investment Industries (Revised in 2011)</i></li> <li>• <i>Provisional Measures on the Administration of Wholly Foreign-Owned Medical Institutions in the China (Shanghai) Pilot Free Trade Zone</i></li> <li>• <i>Circular on Launching Pilot Project for Establishing wholly foreign-owned Hospitals</i></li> </ul>	<ul style="list-style-type: none"> <li>• <i>Catalogue for the Guidance of Foreign Investment Industries (Revised in 2015)</i></li> <li>• <i>Special Administrative Measures (Negative List) for Foreign Investment Access to Pilot Free Trade Zones</i></li> </ul>

### Special Treatment for Taiwan, Hong Kong and Macao Investors

Compared with foreign investors, Taiwan, Hong Kong and Macao investors appear to enjoy more preferential policies in relation to investing or establishing medical institutions in mainland China:

- On January 1, 2009, [Supplementary Provisions II to the Interim Measures for the Administration of Sino-foreign Equity Joint Venture Medical Institutions and Sino-foreign Contractual Joint Venture Medical Institutions \(Order of Ministry of Health and Ministry of Commerce No. 61\)](#) was put into force, which expressly stipulated that Hong Kong and Macao service providers were permitted to set up wholly foreign-owned clinics in Guangdong without restrictions as to the total investment amount.
- According to *Mainland-Hong Kong Closer Economic Partnership Arrangement* and *Mainland-Macao Closer Economic Partnership Arrangement* (“**CEPA**”), NHFPA and MOFCOM jointly promulgated the *Tentative Measures for Administration of Foundation of Wholly-Controlled Hospitals in Mainland China by Hong Kong and Macao Service Providers (Wei Yi Zheng Fa [2010] No. 109, the “Circular 109”)*, stipulating that Hong Kong and Macao service providers may set up wholly foreign-owned hospitals in Shanghai, Fujian, Guangdong, Hainan and Chongqing. The permitted regions shall expand to all municipalities directly under the Central Government and provincial capital cities since April 1, 2012.
- According to the *Cross-strait Economic Cooperation Framework Agreement* (“**ECFA**”), NHFPA and MOFCOM also jointly promulgated *Tentative Measures for Administration of Foundation of Wholly-Controlled Hospitals in Mainland China by Taiwan Service Providers (Wei Yi Zheng Fa [2010] No. 110, the “Circular 110”)*, stipulating that Taiwan service providers may set up wholly foreign-owned hospitals in Shanghai, Jiangsu, Fujian, Guangdong and Hainan beginning on January 1, 2011.
- On December 30, 2013, NHFPA and State Administration of Traditional Chinese Medicine jointly promulgated the *Several Opinions on Accelerating the Operations of Medical Institutions with Social Capital (Guo Wei Ti Gai Fa [2013] No.54)*, which stipulated that Taiwan, Hong Kong and Macao service providers may establish wholly foreign-owned hospitals and expand to all cities at or above the prefectural level in China, provided that the approvals of the provincial health departments are obtained. The application of the regulation is also subject to local restrictions.

Pursuant to above policies, on December 13, 2011, the first wholly Taiwan-owned hospital, Landseed International Hospital, was founded in Shanghai. On January 1, 2013, the first wholly Hong Kong-owned hospital, C-MER (Shenzhen) Dennis Lam Eye Hospital, was founded in Shenzhen, Guangdong.

Unlike the situation in the Seven Pilot Provinces/Municipalities, the *Catalogue for the Guidance of Foreign Investment Industries (Revised in 2015)* expressly stipulates that “if there are other provisions in the CEPA, ECFA and the supplementary agreements, and the free trade zone agreements or investment agreements concluded and signed by and between China and other

relevant countries, such provisions shall prevail.” Therefore, we can infer that the establishment of wholly foreign-owned medical institutions by Taiwan, Hong Kong and Macao investors will not be affected by the new policies.

### Summary of Policies related to Foreign-invested Medical Institutions

In summary, except for Taiwan, Hong Kong and Macao investors, foreign investors are currently prohibited from establishing wholly foreign-owned hospitals nationwide (including in free trade zones and the Seven Pilot Provinces/Municipalities). The new policies related to foreign-invested medical institutions are summarized in the following chart:



### Different Foreign Investor Qualification Review Standards - Another Interesting Difference

Both Circular 109 and Circular 110 expressly stipulate that Taiwan, Hong Kong and Macao service providers applying to establish wholly foreign-owned hospitals in mainland China must “have direct or indirect experience in medical care investment and management and satisfy either of the following requirements: (1) they are able to provide any advanced hospital management experience, management model and service model; or (2) they are able to provide internationally leading medical technologies.” Besides this, the Interim Measures also provide that “the Chinese and foreign parties to a joint venture medical institution or a cooperative medical institution shall have direct or indirect experience in medical and healthcare investment and management, and shall meet one of the following requirements: (1) they are able to provide internationally advanced managerial experience in managing medical institutions, modes of management and modes of services; (2) they are able to provide internationally cutting-edge medical technologies and equipment; or (3) they can complement or make up for the inadequacy of local medical service capacity, medical treatment technologies, funds and medical facilities.”

We can see that, aside from the flexible “complement” condition that was added to the Interim Measures, all three laws require foreign investors to have direct or indirect experience in

healthcare investment and management. However, although the requirement equally applies to joint-venture medical institutions, cooperative medical institutions and wholly foreign-owned medical institutions, review procedures for establishing these three forms of medical institutions are not the same. With respect to establishing joint venture medical institutions and cooperative medical institutions, it is not mandatory for foreign investors to submit materials evidencing they have direct or indirect experience in healthcare investment and management. However, with respect to wholly foreign-owned medical institutions, such materials are required to be submitted and will be strictly examined. Thus, foreign investors that do not have direct or indirect experience in medical care investment and management cannot establish wholly foreign-owned medical institutions in the name of Taiwan, Hong Kong and Macao investors. Such investors may, however, be able to set up joint venture medical institutions or contractual hospitals so long as their shareholding ratios do not exceeding 70%.

In addition to the differences in review standards among Circular 109, Circular 110 and the Interim Measures as mentioned above, different local authorities may in practice also have different requirements for the three different forms of medical institutions:

Application materials		Joint venture medical institutions and cooperative medical institutions	Wholly foreign-owned medical institutions established by Taiwan, Hong Kong and Macao investors
1.	Application for Establishing Medical Institutions	√	√
2.	Project Proposal	√	√
3.	Feasibility Study Report	√	√
4.	Incorporation Certificate, Certificate of Legal Representative Identity, Proof of Bank Credit	√	√
5.	Project Site Report, Lease Certificate for Project Use Land, Project Construction Plan	√	√
6.	Appraisal report confirmation documents for proposal to invest in state-owned assets by the State-owned Assets Management Department	√ (if applicable)	N/A
7.	Certificate of the service provider	×	√
8.	Documents evidencing that service providers are able to provide advanced hospital management experience, management methods and service methods or internationally leading medical technologies.	×	√

In addition to the basic review materials listed in the above table, local examination and approval authorities may require Taiwan, Hong Kong and Macao investors to provide additional documents to prove that they are service providers who engage in substantial business operations, such as the Profits Tax Returns and Notices of Assessment and Demand for Tax Payment for the last three years and Tax Returns for Salary and Pension of Employees in Hong Kong. With respect to qualifications for service providers, please refer to the CEPA and ECFA.

Regulations and policies related to foreign-invested medical institutions are still under development and are subject to the influence of the economic environment and macro policies. We will continually observe this issue. As the laws and regulations change, we also note some notable cases have arisen in judicial practice which we will discuss further in the next article.



## ● **Important Announcement**

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