CHINA PROMULGATES NEW REGULATIONS FOR OUTBOUND INVESTMENT

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Legal Briefings

On 26 December 2017, the National Development and Reform Commission (**NDRC**), one of China''s key regulators of outbound investment, issued new *Measures for the Administration of Outbound Investment by Enterprises* (**New Measures**). The New Measures will be effective on 1 March 2018, replacing the existing *Measures for the Administration of Approval and Filing of Outbound Investment Projects* issued by NDRC in 2014 (**Existing Measures**).

The New Measures follow the *Notice on Further Guiding and Regulating the Directions of Outbound Investment* (**Guidelines**) issued in August 2017. The Guidelines have clarified the regulatory approach to governing outbound investment and called for streamlining the approval and filing procedures for outbound investment. Please see our previous e-bulletin *China Has Released Guidelines on Outbound Investment* for a summary of the Guidelines.

HIGHLIGHTS OF THE NEW MEASURES

1. Expanding the scope of projects subject to NDRC scrutiny

The Existing Measures capture outbound investment which is made by a China-incorporated entity, or by an offshore entity but financed or guaranteed by a China-incorporated entity.

The New Measures expand the scope to cover outbound investment which is made by a China-incorporated entity, or by an offshore entity controlled by a China-incorporated entity, regardless of the source of funding or guarantee. “Control” is defined as direct or indirect ownership of the majority of voting rights of an entity, or the ability to direct important matters such as operations, finance, human resources and technology of the entity. “Outbound investment” is defined as investment to gain offshore ownership, controlling rights, operation and management rights and other interests through the contribution of assets or interests or the provision of finance or guarantee.

Notably, the New Measures specify that outbound investment covers establishing or participating in offshore equity investment funds and investment to gain control of overseas entities or assets through contractual or trust arrangements.

In respect of the entities making the outbound investment, the New Measures make it clear that both non-financial and financial entities are subject to the regime. This clarifies the existing uncertainty under the current regime as to whether outbound investment made by financial institutions should be subject to NDRC scrutiny.

The New Measures also provide that outbound investment made by offshore entities (including entities incorporated in Hong Kong, Taiwan and Macau) which are controlled by Chinese individuals will be subject to NDRC scrutiny.

2. Expanding the scope of sensitive countries/regions and sensitive sectors

Consistent with the current regime, outbound investment in sensitive countries/regions or sensitive sectors will continue to be subject to approvals as opposed to filings. However, the New Measures revise the scope of sensitive countries/regions and sensitive sectors as follows, which will potentially expand the scope of projects which will require approval:

- Sensitive countries/regions include countries and regions which have no diplomatic relations with China, or are in a state of war or civil disturbance, or in which investment is restricted under international treaties to which China is a party.

- Sensitive sectors include research, manufacturing and repair of weaponries, exploitation of cross-border water resources, news media and a newly added catch-all category of sectors in which outbound investment is restricted under China’s laws, regulations and macroeconomic policies. The reference to macroeconomic policies echoes the Guidelines which provide that outbound investment in a number of sectors (such as real estate, hotels, cinemas, and entertainment) is restricted and shall be subject to NDRC approval. NDRC is authorized under the New Measures to separately issue a catalogue of sensitive sectors.

3. Streamlining the approval and filing procedures

The New Measures make a number of changes which aim to streamline the approval and filing procedures. The approval and filing requirements and relevant timelines under the New Measures are summarized in the table below.

Action required	Authority	Type of outbound investment	Processing time
Approval	Central NDRC	Sensitive projects (i.e., investment in sensitive countries/regions or sensitive sectors) made by a China-incorporated entity, or by an offshore entity controlled by a China-incorporated entity	• Generally within 20 working days • May be extended to 30 working days in certain circumstances • This excludes the time for assessment by external experts (if needed)
Filing	Central NDRC	• Non-sensitive projects made directly by central SOEs • Non-sensitive projects made directly by local enterprises with an investment amount of USD300 million or more	Within 7 working days
	Local NDRC	Non-sensitive projects made directly by local enterprises with an investment amount of less than USD300 million	
Reporting – online prior to implementation of the project	Central NDRC	Non-sensitive projects made by offshore entities controlled by Chinese entities or individuals with an investment amount of USD300 million or more	Immediately if the information submitted is complete
No approval, filing or reporting required	N/A	Non-sensitive projects made by offshore entities controlled by Chinese entities or individuals with an investment amount less than USD300 million	N/A

Other highlights of the changes to the approval and filing procedures include:

- Abolishing the “road pass” regime

Under the Existing Measures, if an outbound investment is US$300 million or more and is carried out through a competitive bidding or acquisition process, the Chinese investor must first submit a “project information report” to NDRC before proceeding to execute any binding agreement, making any binding offer or submitting any formal bidding documents. NDRC will issue a confirmation letter if it considers that the relevant project is consistent with the national policies for outbound investment.

This information reporting requirement is sometimes referred to as the “road pass” regime and has historically given NDRC the discretion to determine which Chinese investor is best placed to pursue a particular transaction, as NDRC typically issues only one road pass for a particular transaction. The “road pass” regime brings unwanted uncertainty and government interference to a transaction and often disadvantages Chinese bidders participating in competitive bids. The New Measures have now abolished this regime.

- Simplifying the review process for local enterprises

Under the current regime, a local enterprise must first submit its application to the relevant local NDRC for review and then the local NDRC will forward the application to the central NDRC. In practice, this two-layer review can substantially prolong the approval or filing timeline. The New Measures now provide that where the central NDRC is the final decision making authority, a local enterprise may submit its application directly to the central NDRC for approval or filing without first going through the local NDRC.

Clarifying the deadline for obtaining approval or filing

The Existing Measures require that Chinese investors must obtain the necessary NDRC approval or fulfil the filing obligations before signing the definitive agreements, or must make obtaining such approval or completing the filing a “condition to effectiveness”. In practice, there has been uncertainty as to whether “condition to effectiveness” means a condition precedent to closing or a condition precedent to the effectiveness of the definitive agreement. The New Measures clarify that the deadline for obtaining the necessary approval or completing the required filing shall be before the implementation of the investment, i.e., before the investor actually contributes assets or interests or provides finance or guarantee to the project.

4. Enhancing post-approval and filing supervision

The New Measures introduce a number of measures to enhance the supervision by NDRC of outbound investment projects after approvals are granted or filings made. NDRC will work closely with other government bodies to set up new platforms to supervise outbound investment projects by way of online monitoring, conducting interviews, issuing written enquiries, spot checks and so forth. Chinese outbound investors are also required to report online on the completion of, and any material adverse changes to, the projects. A “name and shame” system will be established to publicize any non-compliance of the New Measures by outbound investors.

Impact on China outbound investment

China’s outbound investment has slumped by more than 40% in the past twelve months largely due to the government’s tightened control on capital outflow in an effort to stabilize the depreciation of the Renminbi and its crackdown on “irrational” and “non-genuine” outbound transactions.

The 19th National Congress of the Communist Party of China concluded in October last year with mixed signals: China will still be buying, but selectively, carefully and with due attention to long-term goals. This approach has been echoed by the Guidelines and now also reflected in the New Measures. The New Measures appear to strike a balance between encouraging outbound investment to support China’s Belt and Road Initiative and other macroeconomic policies on one hand, and restricting “irrational” and “non-genuine” outbound deals on the other.

Under the New Measures, the streamlining of the approval and filing procedures is welcomed by the market. However, the government is also increasing its scrutiny on “loopholes”, such as Chinese companies making outbound investment through offshore vehicles. In addition, depending on the catalogue of sensitive sectors promised by the New Measures, outbound transactions subject to approval rather than filing may be increased. Notwithstanding this, with more clarity and certainty in China’s regulatory approach to outbound investment, it is expected that there will be a cautious up-pick of outbound transitions from China in 2018.

KEY CONTACTS

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