

Foreign Investment

“Grand Unification” Era of China’s Administration on Foreign Investment – A Brief Commentary on the New Foreign Investment Law

On December 26, 2018, the National People’s Congress published the *Foreign Investment Law of the People’s Republic of China (Draft)* (the “**Draft**”) in order to solicit public opinion. Based on a wide variety of opinions received and several rounds of reviews, on March 15, 2019, the *Foreign Investment Law of the People’s Republic of China* (the “**FIL**”) was adopted at the second session of the 13th National People’s Congress. Scheduled to come into force on **January 1, 2020**, the FIL provides a unified rule on the **access, promotion, protection, administration** and other aspects of foreign investment, thereby becoming the **new fundamental law** in respect of foreign investment in China. Meanwhile, once FIL takes effect, *the Law on Sino-Foreign Equity Joint Ventures*, *the Law on Sino-Foreign Cooperative Joint Ventures* and *the Law on Wholly Foreign Owned Enterprises* (collectively, the “**FIE Laws**”) will be repealed simultaneously. The FIE Laws have played a significant role in China’s attraction and utilization of foreign investment, but now they’re

about to step down from the historical stage.

This article provides a brief introduction of the main content of the FIL, the major changes since the Draft, FIL’s highlights and impact on foreign-invested enterprises, and provides comments and suggestions on issues to be further clarified in the implementing regulations of the FIL.

I. Main Content of the FIL

The FIL comprises 6 chapters (**General Provisions, Investment Promotion, Investment Protection, Investment Administration, Legal Liability and Supplementary Provisions**) and 42 articles in total, which is 3 articles more than the 39 articles that made up the Draft. The following table provides a summary of the main content of the FIL.

	Main Content	Major Differences
	FIL	from the Draft
Definition	<p>The FIL defines foreign investment (Article 2) as “any investment activity directly or indirectly carried out by foreign natural persons, enterprises or other organizations (“foreign investors”) within the territory of China”.</p> <p>Specifically, the FIL describes four types of investment activities that represent foreign investment:</p> <ul style="list-style-type: none"> (i) Foreign investors, separately or jointly, establishing foreign-invested enterprises in mainland China; (ii) Foreign investors acquiring shares, equity interests, shares of property or other similar interest in enterprises in mainland China; (iii) Foreign investors, separately or jointly, investing in new construction projects in mainland China; (iv) Foreign investors making investments through other means as provided by laws, administrative regulations or State Council provisions. 	No substantial changes compared to the Draft.
Investment Promotion	<p>The FIL explicitly provides for the following means of promoting foreign investment:</p> <p>Market Environment : FIL emphasizes the aim of creating a stable, transparent, foreseeable and level-playing market</p>	<p>Compared to the Draft, the FIL contains the following major changes:</p> <p>Market Environment: The “investment environment” in the Draft is replaced by “market environment”. In addition, the FIL</p>

	Main Content	Major Differences
	FIL	from the Draft
	<p>environment (Article 3);</p> <p><u>National Treatment:</u> The FIL makes it clear that all national policies in supporting of the development of enterprises shall equally apply to foreign-invested enterprises in accordance with the laws (Article 9); foreign-invested enterprises can equally participate in setting standards in accordance with the laws, and the compulsory standards formulated by the State shall equally apply to foreign-invested enterprises (Article 15); the State shall guarantee that foreign-invested enterprises can participate in government procurement activities through fair competition in accordance with the laws. Products produced and services provided by foreign-invested enterprises within the territory of China shall be treated equally in accordance with the laws in a government procurement (Article 16);</p> <p><u>Preferential Treatments:</u> The State may encourage and guide foreign investors to invest in specific industries, fields and areas. Foreign investors and foreign-invested enterprises may enjoy preferential treatments in accordance with laws, administrative regulations or provisions of the State Council (Article 14);</p>	<p>emphasizes the need to create a “level-playing” market environment;</p> <p><u>National Treatment:</u> The exception to the consistent application of national policies in support of the development of enterprises on foreign-invested enterprises, i.e. “except as otherwise provided in laws and regulations”, is replaced by “equally apply to foreign-invested enterprises in accordance with the laws”. The phrase “foreign-invested enterprises can fairly participate in government procurement activities” in the Draft is changed into “foreign-invested enterprises can participate in government procurement activities through fair competition in accordance with the laws”, emphasizing that the FIL only protects lawful activities, and the fairness mainly refers to the process of competition. It is further specified that not only the products, but also the “services” shall be treated equally;</p> <p><u>Preferential Treatments:</u> The preferential treatments offered to the foreign investors in the Draft is limited to those explicitly stipulated by laws, administrative regulations or State Council provisions. This can be understood as meaning that none of the national ministries and commissions, local legislature or government may, without a legal</p>

	Main Content	Major Differences
	FIL	from the Draft
		ground provided by upper laws, offer any preferential treatments to foreign investors in specific industries, fields or areas through department rules, local laws or regulations;
Investment Protection	<p>The FIL explicitly provides the following protection for the foreign investment made by foreign investors:</p> <p><u>National Expropriation:</u> The state shall not expropriate foreign investments. Under special circumstances, the State may expropriate or requisite an investment made by foreign investors for public interests in accordance with the laws. Such expropriation or requisition shall be conducted in accordance with legal procedures and fair and reasonable compensation shall be given in a timely manner (Article 20);</p> <p><u>Profit Remittance:</u> Foreign investors' capital contributions, profits, capital gains, proceeds from assets deposition, intellectual property rights royalties, lawfully obtained compensation or indemnity, proceeds from liquidation may be freely remitted inward or outward of China in RMB or foreign currency (Article 21);</p> <p><u>Intellectual Property Rights:</u> The State shall protect the intellectual property rights of foreign investors and foreign-invested enterprises. The terms for any technology</p>	<p>Compared to the Draft, the FIL contains the following major changes:</p> <p><u>National Expropriation:</u> The FIL specifically requires that the expropriation and requisition shall only be conducted in accordance with law, and that compensation shall be given in a timely manner;</p> <p><u>Profit Remittance:</u> “proceeds from assets deposition” and “proceeds from liquidation” have been included in the scope of remittance in this article, and free remittance “inward” has been added on top of “outward”;</p> <p><u>Intellectual Property Rights:</u> The terms for technology cooperation are required to be determined through “fair negotiation under the principle of equity”;</p> <p><u>Duty of Confidentiality:</u> The duty of confidentiality and the legal liability for a breach were not contained in the Draft, but a newly added content in the FIL;</p> <p><u>Administrative Intervention:</u></p> <p>Government intervention (such as impairment of rights, imposition of additional obligations, market</p>

	Main Content	Major Differences
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	<p>cooperation shall be determined through fair negotiation between the parties to the investment under the principle of equity. Administrative means shall not be used to compel the transfer of technology (Article 22);</p> <p><u>Duty of Confidentiality:</u> Administrative departments and their staff members shall keep confidential in accordance with the laws any business secret of foreign investors or foreign-invested enterprises they are aware of during the performance of their duties, and shall not divulge or illegally provide the same to others (Article 23). A penalty will be imposed in accordance with the laws in case of any violation; if a crime occurs, such staff will be held criminally liable (Article 39);</p> <p><u>Administrative Intervention:</u> Foreign investment rules formulated by the State shall be in compliance with laws and regulations, and shall not illegally (i) impair the legitimate rights of or impose additional obligations on foreign-invested enterprises; (ii) set any conditions for market access or exit, or (iii) intervene or influence normal production and operation activities of foreign-invested enterprises without provisions of laws and administrative regulations (Article 24);</p> <p><u>Government Commitment:</u> Governments shall strictly abide by all policy commitments made to, and</p>	<p>assess or exist conditions) is limited to the extent that it is “in compliance with laws and administrative regulations”. This can be understood as meaning that none of the national ministries and commissions, local legislature or government may, without the legal ground provided by upper laws, intervene or restrict foreign investment through department rules, local laws or regulations;</p> <p><u>Government Commitment:</u> No substantial changes compared to the Draft.</p> <p><u>Foreign Investors’ Complaints:</u> Compared to the Draft, the FIL specifically provides that in case that the mechanism fails to resolve the complaint, foreign investors may apply for administrative review, or institute administrative litigation in accordance with the laws.</p>

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	<p>contracts concluded with the foreign investors and foreign-invested enterprises in accordance with the laws (Article 25).</p> <p><u>Foreign Investors' Complaints:</u> The State shall establish and improve a complaint mechanism for foreign-invested enterprises. In case that the mechanism fails to resolve a complaint, foreign investors may apply for administrative review, or institute administrative litigation in accordance with the laws (Article 26).</p>	
Investment Administration	<p>The FIL specifies the following three investment administrative systems for foreign investment:</p> <p>(i) Pre-establishment National Treatment and Negative List administrative system (Article 28);</p> <p>(ii) Information Reporting system (Article 34); and</p> <p>(iii) National Security Review system (Article 35).</p>	<p>On the basis of the definition of the Negative List given in the Draft, the FIL adds the definition of “Pre-establishment National Treatment”, which means “the treatment given to foreign investors and their investments at the investment access stage shall not be less favorable than those given to the investors of the host country”.</p> <p>The FIL also adds a new article (Article 33) providing that foreign investors that acquire companies within the territory of China through mergers and acquisitions or participate in the concentration of undertakings by other means shall be subject to the scrutiny of merger control as stipulated by the Anti-Monopoly Law of the People's Republic of China.</p>
Legal Liability	The FIL stipulates the following legal consequences for any violation of the negative list, information reporting	Compared to the Draft, the FIL adds “ corresponding legal liability in accordance with the law ” as the legal liability for the

	Main Content FIL	Major Differences from the Draft
	<p>system or laws and regulations:</p> <p>(i) <u>Violation of the Negative List:</u> Foreign investors shall be ordered to rectify or stop investment activities, or dispose of shares and assets within the prescribed time limit, or take other necessary measures to restore to the original state prior to investment. If there have been any gains derived from such investment, such gains shall be considered illegal and confiscated by the government, and the foreign investors shall bear corresponding legal liability in accordance the laws (Article 36).</p> <p>(ii) <u>Violation of the Information Reporting System:</u> Foreign investors shall be ordered to rectify within a prescribed time limit by competent department of commerce; if rectification is not made in time, a penalty of between CNY100,000 and CNY500,000 shall be imposed (Article 37).</p> <p>(iii) <u>Violation of laws and regulations:</u> Foreign investors shall be subject to investigation in accordance with laws and blacklisted in credit information systems (Article 38).</p>	<p>violation of negative list on top of administrative sanctions. Further, FIL also adds the legal liability for the violation of information reporting system, and deletes “sanctions jointly taken by relevant authorities” as the legal liability for the violation of laws and regulations.</p>
Exceptions	<p>(i) <u>Exception of Pre-establishment National Treatment and Negative List Administrative System:</u> If more preferential treatment</p>	<p>Compared to the Draft, the applicable international convention or treaty only refers to the one with “more preferential treatment”, and the State shall have the</p>

	Main Content	Major Differences
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	<p>concerning investment access is offered to a foreign investor under any international convention or treaty that the People's Republic of China concludes or joins in, relevant provisions in such convention or treaty may be applied. (Article 4);</p> <p>(ii) <u>Exception of Special Industries:</u> For foreign investment administration in financial industries such as banking, securities and insurance, or in financial markets such as securities market and foreign exchange market within the territory of China, where the State has special regulations, such regulations shall be applied for foreign investment in those industries (Article 41).</p>	<p>discretion to decide whether to apply such more preferential treatment, which means the more preferential treatment "may", but not "shall", be applied.</p>
Transition Period	<p>Foreign-invested enterprises, which were established in accordance with the FIE Laws before the implementation of the FIL, may keep their existing organization forms and other aspects for five years upon the implementation of the FIL. Specific implementation measures shall be formulated by the State Council (Article 42).</p>	<p>No substantial changes compared to the Draft.</p>

II. Highlights of the FIL

Among the highlights of the FIL are the clear responses to various long-held concerns from foreign investors and foreign-invested enterprises, which should go some way to improving the

environment for foreign investment and shoring up foreign investors' confidence in investing in China. They include:

2.1 National treatment: all national policies in supporting of the development of enterprises shall equally apply to foreign-invested

enterprises in accordance with the laws (Article 9); foreign-invested enterprises can equally participate in setting standards in accordance with the laws, and the compulsory standards formulated by the State shall equally apply to foreign-invested enterprises (Article 15); the State shall ensure that foreign-invested enterprises can participate in government procurement activities through fair competition in accordance with the laws. Products produced and services provided by foreign-invested enterprises within the territory of China shall be treated equally in a government procurement in accordance with the laws (Article 16);

- 2.2 Prevention of compulsory technology transfer:
The terms for any technology cooperation shall be determined through fair negotiation between the parties to the investment under the principle of equity. Administrative means shall not be used by administrative departments or their staff members to compel the transfer of technology (Article 22); and

2.3 Governmental commitment: Local governments and their relevant departments shall strictly abide by all policy commitments made to, and contracts concluded with the foreign investors and foreign-invested enterprises in accordance with the laws (Article 25).

III. Impact of the FIL on FIEs

Upon the FIL coming into effect, the FIE Laws will be repealed simultaneously. This will have a different impact on the legal form of the Sino-Foreign Equity Joint Ventures, Sino-Foreign Cooperative Joint Ventures and Wholly Foreign Owned Enterprises (collectively, the “Foreign-invested Enterprises” or “FIEs”). Article 31 of the FIL provides that “the legal form, organization structure and code of conduct of a foreign-invested enterprise shall be governed by the provisions of the Company Law of the People’s Republic of China, the Partnership Enterprise Law of the People’s Republic of China, and other applicable laws.” Based on this provision, we have summarized the major impact of the FIL on the FIEs in the following table:

	Existing Enterprises	New Enterprises
Sino-Foreign Cooperative Joint Ventures	<ul style="list-style-type: none"> Existing enterprises that have been established as legal persons shall, during the 5-year transition period, be transformed to limited liability companies or joint-stock companies in accordance with the <i>Company Law</i>; Existing enterprises that have been established without legal person status may, during the 5-year transition period, be transformed to partnerships in accordance with the <i>Partnership Enterprise Law</i>, or limited liability companies or joint-stock companies in accordance 	<ul style="list-style-type: none"> The legal form of the Sino-Foreign Cooperative Joint Ventures shall not exist anymore following the implementation of the FIL.

	Existing Enterprises	New Enterprises
	with the <i>Company Law</i> .	
Wholly Foreign Owned Enterprises	<ul style="list-style-type: none"> No substantial impact since such enterprises are basically limited liability companies incorporated in accordance with the <i>Company Law</i>. 	<ul style="list-style-type: none"> To be established as a limited liability company or joint-stock company (applicable for a company with at least two foreign investors) in accordance with the <i>Company Law</i>; As for an enterprise invested in by a foreign natural person investor, such enterprise can be in the form of individual proprietorship enterprise provided that the <i>Law on Individual Proprietorship Enterprise</i> will be amended to be applied to foreign natural persons¹.
Sino-Foreign Equity Joint Ventures	<ul style="list-style-type: none"> Although the legal form of Sino-Foreign Equity Joint Ventures is already a limited liability company, their articles of association need to be revised within the 5-year transition period in order to comply with the requirements of the <i>Company Law</i> in respect of organization structure and corporate governance. 	<ul style="list-style-type: none"> To be established as a limited liability company or joint-stock company in accordance with the <i>Company Law</i>.

Since the Sino-Foreign Equity Joint Venture is an important type of entity among the FIEs, and its corporate governance structure will be significantly affected by the FIL, we hereby set out

the major impact that the FIL may impose on Sino-Foreign Equity Joint Ventures taking the form of limited liability companies.

	Sino-Foreign Equity Joint Ventures	Before the FIL	After the FIL
1	Restriction on	Chinese natural persons	No restriction

¹ Article 31 of the FIL provides that the legal form of a foreign-invested enterprise shall be governed by the provisions of the *Company Law*, the *Partnership Enterprise Law*, and other applicable laws. Compared to the Draft submitted for second review on January 29, 2019, the FIL has added "other applicable laws" in this article, which can be understood that foreign-invested enterprises are theoretically able to take a legal form other than those stipulated in the *Company Law* or *Partnership Enterprise Law*. For example, foreign natural persons should be able to set up individual proprietorship enterprises in accordance with the *Law on Individual Proprietorship Enterprises*. In order to show the national treatment and consistent treatment established by the FIL, we understand that the provision "This law shall not apply to wholly foreign owned enterprises" under Article 64 of the *Law on Individual Proprietorship Enterprises* shall be removed.

	Sino-Foreign Equity Joint Ventures	Before the FIL	After the FIL
	Chinese Shareholder	cannot be the shareholder of newly incorporated joint ventures ² .	
2	Investment Percentage of Foreign Shareholder	Generally no less than 25%	No restriction
3	Highest Authority	Board of Directors	Shareholders' meeting
4	Appointment of the Directors	Directors shall be appointed or removed by respective shareholders of the joint ventures.	Directors who are not employee representatives shall be elected and replaced by the shareholders' meeting
5	Chairman and Vice Chairman of the Board	Chairman and Vice Chairman of the Board shall be appointed by the Chinese shareholder and the foreign shareholder respectively	No restriction
6	Legal Representative	Chairman of the Board	Chairman of the Board, Executive Director or General Manager
7	Voting Requirement for the Highest Authority to Approve Important Matters	Matters mandatorily subject to unanimous approval of all Directors presenting at the meeting of the Board: <ul style="list-style-type: none"> – Amendment of articles of associations; – Increase or reduction of registered capital; – Suspension or dissolution of the company; 	Matters mandatorily subject to approval of shareholders holding more than 2/3 of the voting rights: <ul style="list-style-type: none"> – Amendment of articles of associations; – Increase or reduction of registered capital; – Dissolution or change of company form;

² Article 54 of the *Provisions on Merger and Acquisition of Domestic Enterprises by Foreign Investors* (Decree 6 of the Ministry of Commerce 2009) provides that "A Chinese natural person shareholder of a domestic company whose equity is acquired by a foreign investor may, upon approval, continue to be the Chinese investor of the foreign-invested enterprise after the conversion." However, this provision does not apply to newly incorporated Sino-Foreign Equity Joint Ventures.

	Sino-Foreign Equity Joint Ventures	Before the FIL	After the FIL
		– Split-up or merger of the company.	– Split-up or merger of the company.
8	Appointment of Senior Management Personnel	General/Deputy General Manager (or Factory Head/Deputy Factory Head) shall be appointed by the Chinese shareholder and the foreign shareholder respectively	No restriction
9	Foreign Partner's Contribution in Form of Industrial Property Rights or Know-how	Industrial Property Rights or Know-how used for capital contribution must meet either of the following conditions: <ul style="list-style-type: none"> – The technology that can significantly improve the performance, quality or production efficiency of the current product; or – The technology that can significantly save raw materials, fuels or power. 	No specific restriction, as long as it does not fall into properties that cannot be used as capital contribution according to the laws and administrative regulations.
10	Restriction on Equity Transfer	The transfer of any shareholder's equity interest is subject to the consent of all other shareholders.	Unless otherwise provided in the articles of association, a shareholder may freely transfer part or all of its equity interest to another shareholder. Transfer to third parties shall require consent from more than half of all other shareholders. Other shareholders failing to reply within 30 days from receipt of the written notice shall be deemed to have consented to the proposed transfer. Where more than half of the other shareholders do not consent to the proposed transfer, the

	Sino-Foreign Equity Joint Ventures	Before the FIL	After the FIL
			non-consenting shareholders shall purchase such equity interests, failing which they shall be deemed to have consented to the proposed transfer. Where the consent has been given to the proposed transfer, the non-transferring shareholders shall have right of first refusal to purchase such equity interests on the same conditions.
11	Profit Sharing Rules	All parties to the joint venture shall share the profit in proportion to their respective contribution to the registered capital.	Shareholders shall be entitled to the profit in proportion to their respective paid-in capital in the registered capital, unless all the shareholders agreed otherwise.
12	Mandatory Fund Allocation and Percentage	<ul style="list-style-type: none"> – Reserve Funds – Employee Bonus and Welfare Reserve – Enterprise Development Reserve Ratio of the above reserves shall be determined by the Board	<ul style="list-style-type: none"> - Statutory Reserve - Discretionary Reserve <p>Contribution of statutory reserve shall be 10% of the post-tax profit, but such contribution is not required if the aggregate sum of the statutory reserve reaches 50% of the registered capital.</p>
13	Governing Law of Joint Ventures Contract	<ul style="list-style-type: none"> – Chinese law (Article 12 of the <i>Implementing Regulation of the Law of the People's Republic of China on Sino-Foreign Equity Joint Ventures</i>, Article 126 of the <i>Contract Law</i>) 	Chinese law (Article 126 of the <i>Contract Law</i>)

IV. Comments and Suggestions on FIL's Implementing Regulations

As a fundamental law, the FIL has provided several principles on the promotion, protection

and administration of the foreign investment, thus it must require implementing rules or other ancillary regulations (the "Implementing Regulations") to facilitate its implementation. Our article are to be clarified in the Implementing

Regulations are as follows:

<p>1. Definition of “Foreign Investor” and “Foreign Investment” (Article 2, Paragraph 2)</p>	<p><i>“For the purpose of this law, foreign investment refers to any investment activity directly or indirectly carried out by foreign natural persons, enterprises or other organizations (“foreign investors”) within the territory of China”, including...”</i></p>
<p>Comments/Suggestions</p> <p>We suggest that the Implementing Regulations should further clarify the definition of “Foreign Investor” and “Foreign Investment” in the following aspects:</p> <ul style="list-style-type: none"> (i) Whether “foreign investors” may include foreign or regional governments, and international organizations. (ii) Since, in addition to direct investment, the definition of investment includes “indirect investment”, it is not clear whether for an investment in China, the identity of its foreign investor shall be determined by such investor’s ultimate controlling shareholder. (iii) It needs to be clarified whether an investment made in China by an overseas company that is controlled by a Chinese company will be classified as “foreign investment”. <p>We believe that it is necessary to clarify in the Implementing Regulations whether the identity of a “foreign investor” will be determined by the place of registration of the foreign investor that directly holds shares, equity or interest of the invested enterprise in China, or by the place of registration of the ultimate controller of such foreign investor. If it is the latter, a definition of “control” is also required.</p> <p>Given the increasing number of overseas investments emanating from China, a lack of such criteria may lead to severe confusion regarding whether investment in China conducted by overseas companies directly or indirectly controlled or wholly-owned by Chinese enterprises or natural persons will be governed by the FIL.</p> <p>Moreover, with increasing numbers of Chinese citizens migrating overseas and foreign citizens becoming resident in China, we suggest that there is a need for clarification as to whether an enterprise invested in China by foreign individuals that acquire Chinese nationality or by Chinese citizens that obtain foreign nationality shall be governed by the FIL.</p>	
<p>2. National Security Review (Article 35)</p>	<p><i>“China shall establish a foreign investment national security review system to perform security reviews on foreign investment that affects or may affect national security. National security decisions made according to the law shall be final.”</i></p>
<p>Comments/Suggestions</p> <p>The FIL provides that there shall be a foreign investment national security review system, without further specifying any detailed rules, such as in terms of the scope and content of the review, requirements of application documents, procedure or time limit of the review, etc.</p>	

<p>Currently, the only rules that regulate a national security review of foreign investments are the <i>Notice of the General Office of State Council on the Establishment of a Security Review System Pertaining to Mergers and Acquisitions of Domestic Enterprises by Foreign Investors</i>³ and the <i>Notice of the General Office of State Council on the Promulgation of the Trial Measures on National Security Review for Foreign Investments in Pilot Free Trade Zones</i>⁴. There is no clear legal basis for a national security review of foreign-invested enterprises that will be set up outside free trade zones. We suggest that the Implementing Regulations shall provide for the scope, content and procedures of the national security review for all kinds of foreign investment.</p>	
<p>3. Transition Period of Existing Foreign-invested Enterprises (Article 42)</p>	<p><i>“Foreign-invested enterprises, which were established in accordance with the FIE Laws before the implementation of the FIL, may keep their legal forms and other aspects for five years upon the implementation hereof. Specific implementation measures shall be formulated by the State Council”</i></p>
<p>Comments/Suggestions</p> <p>After the FIL comes into force, the Sino-Foreign Cooperative Joint Ventures as a legal form for enterprises shall not exist anymore. Article 21 of the <i>Law on Sino-Foreign Cooperative Joint Ventures</i> provides that <i>“when the Chinese and foreign partners agree in the co-operative enterprise contract that, on the expiry of the term of co-operation, all the fixed assets of the co-operative enterprise shall be owned by the Chinese partner, methods to allow the foreign partner to recover its investment in advance within the term of co-operation may be stipulated in the co-operative enterprise contract.”</i></p> <p>As for a Sino-foreign Cooperative Joint Venture adopting the above provision, when it is transformed to a limited liability company in accordance with the <i>Company Law</i> during the 5-year transition period, the investment recovery issue can be resolved by an agreement based on Article 34 of the <i>Company Law</i>, pursuant to which the shareholders may agree that the profit will not be distributed in proportion to their respective contributions to the company’s registered capital.</p> <p>However, the <i>Company Law</i> does not provide a legal basis pursuant to which all the fixed assets of the company can be owned by the Chinese partner only on the expiry of the term of co-operation. Paragraph 2 of Article 186 of the <i>Company Law</i> provides that the residual assets of a company after liquidation <i>“shall be distributed to shareholders in accordance with the ratio of capital contribution”</i>, without any exceptions. Therefore, we suggest that the Implementing Regulations provide clear guidance on such issue in relation to the transition period.</p>	
<p>4. Governing Law of Partnership Agreement</p>	<p>/</p>

³ Guo Ban Fa [2011] No. 6

⁴ Guo Ban Fa [2015] No. 24

Comments/Suggestions

Article 126 of the *Contract Law* provides that “parties to a contract with a foreign element may choose the law to be applied in the handling of contractual disputes, except where laws provide otherwise. Where the parties to a contract with a foreign element fail to choose the governing law of the contract, the law of the country with the closest connection to the contract shall be applied.

Sino-foreign equity joint venture contracts, Sino-foreign cooperative enterprise contracts and Sino-foreign contracts for the cooperative exploitation and development of natural resources which are to be performed within the territory of the People's Republic of China shall be governed by the law of the People's Republic of China.”

Hence, after the repeal of the FIE Laws, joint venture contracts of Sino-Foreign Equity Joint Ventures that are incorporated in accordance with the *Company Law* shall still be governed by the Chinese laws. However, in the absence of any rules in the *Contract Law* requiring the partnership agreement of Sino-Foreign Partnership under the *Partnership Enterprise Law* to be governed by the Chinese law, **whether the parties to the Sino-foreign partnership agreement will be free to choose a foreign governing law, pursuant to the PRC Contract Law?**

We suggest that the Implementing Regulations should further clarify this issue. Theoretically, the restriction in Article 126 of the *Contract Law* on the choice of law **refers only to restriction made by laws**, thus neither administrative regulations nor department rules may formulate provisions that are not in compliance with the *Contract Law*.

1. Applicability of FIL to Investors from Hong Kong, Macau and Taiwan

Comments/Suggestions

The definition of “foreign investor” in the FIL does not cover investors from Hong Kong, Macau or Taiwan, whose investments in mainland China were previously considered to be “foreign investment”. Therefore, **we suggest that the Implementing Regulations clarify whether the FIL shall apply, by reference, to investment in mainland China made by investors from Hong Kong, Macau and Taiwan.**

V. Outlook

If the Law on Sino-Foreign Equity Joint Ventures promulgated in 1979 is considered the first window left ajar by a less-developed China to attract foreign investment, the FIL promulgated in 2019 can be seen as a large door opened by a striding forward China with a more open mind and

more positive attitude to attract foreign investment. By stepping through this door, China’s administration on foreign investment has entered a stage of grand unification, which will significantly increase the efficiency of foreign investment while reducing the investment cost. Except for industries in the negative list, all foreign investment will not be subject to any prior approval or filing, and the

national treatment is fully assured by law. In this regard, the FIL is no doubt a good news for foreign investors who come to invest in China, and a signal of a more mature, open and confident foreign investment administration of China.

In addition, the FIL is not just a good news for foreign investors. Almost forty years has passed since the establishment of the first Sino-Foreign Equity Joint Ventures in China. Upon the repeal of

the FIE Laws, the era in which there is no legal basis for a Chinese natural person to be a shareholder of a Sino-foreign equity joint venture or cooperative joint venture has gone for good. As such, the promulgation of FIL serves not only a milestone of the development of foreign investment in China, but also exhilarating news for Chinese individuals who have increasing financial capability and wish to participate more in the international economic exchange and cooperation.

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