

# Draft of the new foreign investment law in the PRC

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## Juan Calvo-Rubio

Lawyer Hong Kong office  
NET CRAMAN ABOGADOS

English Version ▲

**O**n 19 January 2015, the Ministry of Commerce of the People's Republic of China ("MOFCOM") published the Draft of the new Foreign Investment Law (FIE). Once the Draft is passed into Law, it will substitute the long-standing Three Laws on Foreign Investment –the Law on Chinese-Foreign Equity Joint Ventures, the Law on Wholly Foreign-Owned Enterprises and the Law on Chinese-Foreign Contractual Joint Ventures– (FIE Laws, promulgated in 1979). The obsolescence of the current Foreign Investment regime, scattered and inconsistent between national and local laws and regulations, together with China's effort to rationalize its foreign investment regulatory regime along with prevailing international standards, require this further legislative step.

The National People's Congress will probably provide with a timeline regarding its approval on its annual general Meeting (March 5th to 13th) but it's uncertain to date when it will be officially enacted.

The aim of the Draft is to adapt the Chinese foreign investment legal system to today's needs, reducing barriers to foreign investors whilst strengthening MOFCOM's scrutiny on foreigners who try to dodge the regulations on restricted industries.

The major prospective changes that the Draft would introduce can be set out as follows:

1. Implementation of a "negative list" and elimination/reduction of the current case-

by-case basis approval. Foreign investment Industries in China are currently categorized by the Industry Catalogue for the Guidance of Foreign Investments as "encouraged", "permitted", "restricted" and "prohibited". Upon the implementation of the new "negative list" (which has already been rehearsed in the Shanghai Pilot Free Trade Zone), those industries under the "encouraged" and "permitted" categories will no longer have to apply for approval, receiving pre-entry national treatment.

Thus, with the negative list, "prohibited" and "restricted" categories for foreign investment will be specifically listed in the new catalogue, and remaining industries will be fully open to foreign investment.

2. New concept of foreign investor. Under the existing Law, foreign investors are those who are incorporated outside the People's Republic of China (PRC), irrespective of their source of capital or of who does hold the effective control of the company. However, the Draft stipulates that only a domestic enterprise, established in China but controlled by a foreign investor, would be deemed to be a Foreign-Invested Enterprise. With the new Law, whether a company is foreign-invested or not will be determined by the nationality of the ultimate beneficiary (ies) rather than that of the direct shareholder. "Control" is understood

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in the Draft as: a) more than 50% of shares; b) voting power; c) significant influence over decision-making power; among others.

In resume, if the ultimate beneficiary (ies) is Chinese, the company will be treated as domestic.

3. Corporate governance structure. In order to comply with the new Draft, in case it is passed into law, many foreign-invested enterprises would have to amend their constitutional documents.
4. National Security Review. Article 48 FIL, establishes that “any foreign investment that harms or likely endanger the national security” will be likely to be reviewed.

Regarding the situation of Foreign Law Firms (FLF) in the Asian country, China’s accession to

the World Trade Organization (2001) brought a liberalization of the domestic legal services market, allowing foreign law firms to provide with legal services on matters relating to Chinese Law. However, with the new FIL, this activity is shifted from restricted to prohibited, what may hinder the Foreign Law Firm’s aim to settle down and carry out their professional practice in Mainland China (this rules will not be applied in the Shanghai Free Trade Zone). This measure is probably bound to take more control in the legal sector and force Foreign Law Firms to associate with local firms.

In conclusion, the Draft of the new Foreign Investment Law is an important first step in the global modernization process through Mainland China is going. It not only reflects China’s desire to adapts its Foreign Investor rules system to market needs but also further opens China to and advances foreign investment. ■

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