

Provisional Rules on the Acquisition of Domestic Enterprises by Foreign Investors

(Promulgated by the Ministry of Foreign Trade and Economic Co-operation, the State General Administration of Taxation, the State General Administration of Industry and Commerce, and the State Administration of Foreign Exchange on March 7, 2003.)

Article 1. This set of Rules, formulated in accordance with laws and administrative regulations on foreign invested enterprises and other related laws and administrative regulations, aims to promote and standardize foreign investment in China, introduce foreign advanced technologies and managerial experience, improve the level of foreign investment absorption, realize rational allocation of resources, safeguard employment, and maintain fair competition and national economic safety.

Article 2. Acquisition of domestic enterprises by foreign investors mentioned in this set of Rules refers to a foreign investor's purchase of the shareholders' right of, or increased investment in domestic enterprises not funded by foreign investors according to contractual agreement (hereinafter referred to as domestic firms) which results in the domestic firm changing into a foreign invested enterprise (hereinafter referred to as share right acquisition), or when a foreign investor sets up a foreign invested enterprise to purchase and operate assets from domestic enterprises according to contractual agreement through the venture formed, or when a foreign investor purchases assets from domestic enterprises according to contractual agreement and establishes a foreign invested enterprise based on the assets purchased to operate the assets (hereinafter referred to as assets acquisition).

Article 3. Foreign investors shall abide by Chinese laws, administrative regulations and departmental rules, follow the principles of being fair and reasonable, equivalent and paid, honest and faithful, not cause over-concentration, exclusiveness or restriction towards competition, nor shall they disturb social economic order or harm social public benefits in acquiring domestic enterprises in China.

Article 4. Foreign investor's acquisition of domestic enterprises shall conform to the requirements imposed by Chinese laws, administrative regulations and departmental rules on the qualifications of investors and industrial policies.

In industries where foreign investors are not allowed to set up solely foreign owned firms according to the Catalogue of Industries for Foreign Investment, acquisition shall not result in entire foreign ownership. For sectors where it is required that the Chinese side should have the majority share, either absolutely or comparatively, the acquisition in the sectors shall not introduce changes to the controlling position of the Chinese partners. Foreign investors are not allowed to acquire enterprises within a sector not opened to foreign investment.

Article 5. A foreign investor acquiring a domestic enterprise to establish a foreign invested enterprise shall obtain approval from the examination and approval authority in line with the provisions of this set of Rules, and handle the modification of registration or establishment registration formalities with the competent registration administration. The capital contribution from a foreign investor in the registered capital of the foreign invested enterprise established after the acquisition shall normally be no less than 25% in the total.

Where the ratio is below 25%, it shall go through the examination and approval and registration procedures as currently governing the establishment of foreign invested enterprises, unless otherwise specified by laws and administrative regulations. The examination and approval authority shall specify on the approval certificate of foreign invested enterprise, the remark "with foreign capital contribution of less than 25%" The registration authority shall put the same on the business license of the foreign invested enterprise accordingly.

Article 6. The examination and approval authority mentioned in this set of Rules refers to the Ministry of Foreign Trade and Economic Co-operation of the People's Republic of China (hereinafter referred to as MOFTEC) or provincial level department in charge of foreign trade and economic co-operation (hereinafter referred to as the provincial level examination and approval authority), the registration authority, refers to the State General Administration of Industry and Commerce or local administration of industry and commerce delegated by the State General Administration of Industry and Commerce.

In cases where a foreign invested enterprise established after acquisition falls within the scope of foreign invested enterprises of special type or industry that needs to be examined and approved by MOFTEC in accordance with the provisions of laws, administrative regulations and departmental rules, the provincial level examination and approval authority shall submit the application documents to MOFTEC for examination and approval, which will decide whether or not to approve according to laws.

Article 7. In cases of share right acquisition by foreign investors, the foreign invested enterprise established after acquisition shall bear the creditor's rights and debts of the domestic firms acquired.

In cases of assets acquisition by foreign investors, the domestic enterprise selling assets shall continue to bear its existing creditor's rights and debts.

Foreign investors, domestic firms being acquired, creditors and other parties concerned may reach agreement among themselves on the disposal of creditor's rights and debts of the domestic firms being purchased, however, the agreement thus reached shall not harm the benefits of a third party and social public benefits. Agreement to dispose of the creditor's rights and debts shall be submitted to the examination and approval authority.

A domestic firm selling its assets shall issue notice to its creditors within 10 days upon adopting the resolution to sell the assets and publish in provincial level or above newspapers that have a nationwide circulation. Creditors are entitled, within 10 days upon receiving the notice or upon the publication of the notice, to the right of asking the domestic enterprise selling assets to provide corresponding guarantee.

Article 8. Parties to the acquisition shall base their trading price on the evaluation made by assets evaluation institutions with regard to the value of share right to be transferred or the value of assets to be sold. Parties to the acquisition may agree among themselves to set-up assets evaluation institutions according to the law. Assets evaluation shall be conducted according to the method of evaluation commonly used internationally.

In cases where foreign investor's acquisition of domestic enterprises results in the changes in share right formed by investment of state assets or transfer of the property right of state assets, evaluation shall be conducted in line with the related provisions governing the management of state owned assets to identify trading price.

It is not allowed to transfer share rights or sell assets at prices significantly lower than the evaluation result and transfer assets abroad in disguised form.

Article 9. In cases where a foreign investor acquires a domestic enterprise to establish a foreign invested enterprise, the foreign investor shall pay all the money required in the acquisition to the shareholders

transferring their share right or the domestic enterprise selling its assets within three months upon the issuance of the business license of foreign invested enterprise.

In cases where the period is to be extended due to extraordinary circumstances, the foreign investor may, upon approval from the examination and approval authority, pay 60% of the total money requested within six months upon the issuance of the business license of foreign invested enterprise and pay the remainder within a year. The investor shall be entitled to the distribution of earnings according to the actual ratio of capital contribution.

In cases where there is a share right acquisition by a foreign investor and the foreign invested enterprise formed after the acquisition increases investment, the investor shall specify within the contract and articles of association of the foreign invested enterprise to be established, the period of capital contribution. In cases where the full amount of payment is requested, the investor shall pay the capital within six months starting from the day of issuance of business license of foreign invested enterprise. If payment in instalments is allowed, the first instalment paid by the investor shall be no less than 15% of its ratio of capital contribution and shall be made within three months, starting from the day of issuance of business license of foreign invested enterprise.

In the case of assets acquisition by a foreign investor, the investor shall specify within the contract and articles of association of the foreign invested enterprise to be set up, the period of capital contribution. In cases of establishing a foreign invested enterprise and contractually purchasing assets from a domestic enterprise and operating the assets through the enterprise set-up, the investor shall contribute the capital within the period of money payment specified in paragraph 1 of this article in cases where the capital is an equivalent amount to the assets. Payment of the remainder shall be made according to the period of payment specified in line with the modality stipulated in paragraph 2 of this article.

In cases where a foreign investor acquires a domestic enterprise and establishes a foreign invested enterprise, the investor shall pay, in cases of contributing cash, the committed capital within three months, starting from the day of issuance of business license of foreign invested enterprise, if the capital contributed by the foreign investor is below 25%. If the investor contributes capital in the form of kind, industrial property right and others, it shall pay within six months, starting from the day of issuance of the business license of foreign invested enterprise.

Means of payment shall conform to the provisions of related Chinese laws and administrative regulations. Foreign investors using stocks over which they have disposal right or RMB assets owned lawfully to pay the money involved in acquisition shall undergo verification by the foreign exchange administration first.

Article 10. In cases of contractual purchase of share right of a domestic enterprise by a foreign investor and the domestic enterprise is changed into a foreign invested enterprise, the registered capital of the foreign invested enterprise shall be the same as that of the original domestic enterprise, with the capital contribution ratio of the foreign investor the same as the percentage accounted for, by the share right it has purchased in the original registered capital. In cases where the domestic enterprise, whose share right is purchased by a foreign investor, increases its investment at the same time, the registered capital of the foreign invested enterprise established after acquisition shall be the total of the registered capital of the original domestic enterprise and the increased investment. The foreign investor and other investors to the domestic enterprise being acquired shall identify their respective capital contribution ratios in the registered capital of the foreign invested enterprise on the basis of assets evaluation of the domestic enterprise.

In cases where a foreign investor subscribes increased investment in a domestic enterprise and the domestic enterprise is changed into a foreign invested one, the registered capital of the foreign invested enterprise shall be the total of the registered capital of the original domestic enterprise and the increased investment.

The foreign investor and other investors to the domestic enterprise being acquired shall identify their respective capital contribution ratios in the registered capital of the foreign invested enterprise on the basis of assets evaluation of the domestic enterprise.

Chinese natural person share holders of the domestic enterprise whose share right is being purchased may, upon approval, continue to serve as Chinese investors to the foreign invested enterprise formed after acquisition, provided the natural person share holders have enjoyed share holder status in the original company for over a year.

Article 11. In cases of share right acquisition by a foreign investor, the ceiling of total investment of the foreign invested enterprise to be formed after acquisition shall be agreed upon according to the following percentage:

1. Total investment not exceeding 10/7 the registered capital in cases where the registered capital is below US\$2.1 million;
2. Total investment not exceeding twice the registered capital in cases where the registered capital is between US\$2.1 million and US\$5 million;
3. Total investment not exceeding 2.5 times the registered capital in cases where the registered capital is between US\$5 million and US\$12 million;
4. Total investment not exceeding 3 times the registered capital in cases where the registered capital is over US\$12 million.

Article 12. In cases of share right acquisition by a foreign investor, the investor shall submit the following documents to the examination and approval authority with the corresponding examination and approval power according to the total investment of the foreign invested enterprise formed after acquisition:

1. Resolution specifying unanimous agreement from shareholders of the domestic limited liability company being acquired for share right acquisition by the foreign investor or resolution adopted by the general meeting of shareholders of the domestic limited liability company being acquired, giving consent to share right acquisition by a foreign investor;
2. Application for changing the domestic enterprise being acquired into or establishing a foreign invested enterprise according to law;
3. Contract and articles of association of the foreign invested enterprise formed after acquisition;
4. Agreement specifying purchase of the share right of a domestic enterprise or subscription of increased investment of the domestic enterprise by a foreign investor;
5. Financial auditing report for the latest fiscal year of the domestic enterprise being acquired;
6. Identification proof or business opening proof or credit proof of the investor;
7. Explanation to the enterprises invested by the domestic enterprise being acquired;
8. Business license (copy) of the domestic enterprise being acquired and enterprises invested by it;
9. Employee arrangement plan of the domestic enterprise being acquired;

10. Documents requested in articles 7 and 19 of this set of Rules.

In cases where the business scope, scale and land use right of the foreign invested enterprise formed after acquisition involve permits from other related governmental bodies, the related approval documents shall be submitted at the same time.

The business scope of enterprises invested in by the domestic enterprise being acquired shall conform to the requirements of industrial policies governing foreign investment. Adjustment is required in the case of non-compliance.

Article 13. Share right purchase contract specified in article 12 of this set of Rules shall be subject to Chinese laws and include the following contents:

1. Status of various parties, including name, address, name of legal representative, title, nationality;
2. Percentage and price of share right purchased or increased investment subscribed;
3. Period and way of implementation of the contract;
4. Rights and obligations of parties to the contract;
5. Breach of liabilities and dispute settlement;
6. Time and location of the signing of the contract.

Article 14. In cases of assets acquisition by a foreign investor, the trading price of the assets and the actual production and operational scale shall be the basis on which to calculate the total investment of the foreign invested enterprise to be established. The ratio between registered capital to total investment of the foreign invested enterprise to be established shall conform to relevant provisions.

Article 15. In cases of assets acquisition by a foreign investor, the investor shall submit the following documents to the examination and approval authority with corresponding examination and approval right according to the total investment of the foreign invested enterprise to be established, the type of enterprises, and sectors within which the enterprise is to be established and in line with the provisions of laws, administrative regulations and departmental rules on the establishment of foreign invested enterprises:

1. Resolution specifying agreement from the holder of the property right of the domestic enterprise or from the authoritative authority for selling assets;
2. Application for establishment of a foreign invested enterprise;
3. Contract and articles of association of the foreign invested enterprise to be established
4. Assets purchase agreement signed between the domestic enterprise and the foreign invested enterprise to be set up, or assets purchase agreement signed between foreign investor and domestic enterprise;
5. Articles of association and business license (copy) of the domestic enterprise being acquired;
6. Proof of notice and publication from the domestic enterprise being acquired to its creditors;
7. Identification proof or business opening proof and related credit proof of the investor;
8. Employee arrangement plan of the domestic enterprise being acquired;

9. Documents requested in articles 7 and 19 of this set of Rules.

In cases where the purchase and operation of assets of domestic enterprises according to the provisions of the previous paragraph involves permits from other related governmental bodies, the related approval documents shall be submitted at the same time.

In cases where a foreign investor purchases assets of a domestic enterprise according to contractual agreement and launches a foreign invested enterprise with the assets, the investor is not allowed to conduct operational activities with the assets before the establishment of the foreign invested enterprise.

Article 16. Assets purchase contract specified in article 15 of this set of Rules shall be subject to Chinese laws and include the following contents:

1. Natural status of various parties, including name, address, name of legal representative, title, nationality;
2. List and price of assets to purchase;
3. Period and way of implementation of the contract;
4. Rights and obligations of parties to the contract;
5. Breach of liabilities and dispute settlement;
6. Time and location of the signing of the contract.

Article 17. In cases where a foreign investor acquires a domestic enterprise to establish a foreign invested enterprise, with the exception of the terms specified in article 20 of this set of Rules, the examination and approval authority shall, within 30 days upon receiving the complete set of documents requested, decide whether or not to approve the application according to laws. An approval certificate of foreign invested enterprise will be granted to those passing the examination and approval.

In cases where a foreign investor purchases a share right of a domestic enterprise on the basis of contractual agreement and the examination and approval authority decides to approve the purchase, the examination and approval authority shall send copies of the approval documents to the transferor of the share right and the foreign exchange authority at the place where the domestic enterprise is located at the same time. The foreign exchange authority at the place where the transferor of the share right is located shall handle, for the transferor, registration formalities of foreign capital acceptance and issue a foreign capital registration certificate specifying that the foreign investor has paid the money for the share right acquisition.

Article 18. In cases of assets acquisition by foreign investors, investors shall, within 30 days upon receiving the approval certificate of foreign invested enterprise, go to the registration authority to apply for establishment registration and obtain a business license of foreign invested enterprise.

In cases of share right acquisition by foreign investors, the domestic enterprise being acquired shall apply to the original registration authority for modification of registration in line with this set of Rules and obtain a business license of foreign invested enterprise. In cases where the original registration authority has no jurisdiction over the registration, the authority shall transfer the application documents to another registration authority that is qualified within 10 days, starting from the day of receiving the documents, together with the registration files of the domestic enterprise. The domestic enterprise being acquired shall submit the following documents and is held liable for the authenticity and effectiveness of the documents when applying for modification of registration:

1. Application for modification of registration;
2. Resolution adopted by the shareholders' meeting of the domestic enterprise being acquired concerning the transfer of share right or increasing investment according to the Corporate Law of the People's Republic of China and the articles of association of the company;
3. Contract specifying foreign investor's purchase of the share rights of the domestic enterprise or subscribing increased investment in the domestic enterprise;
4. Revised articles of association of the company or amendment to the original articles of association and contract of foreign invested enterprises to be submitted according to the law;
5. Approval certificate of foreign invested enterprise;
6. Identification documents or proof of business opening, credit proof of foreign investors;
7. Revised name list of board of directors and documents specifying name and address of newly added directors and document of post appointment of newly added directors;
8. Other documents and certificates requested by the State General Administration of Industry and Commerce.

In the case of transferring state owned share right and foreign investor's subscribing increased investment in companies with state owned share right, the approval document issued by the department in charge of foreign trade and economic co-operation shall also be submitted.

Investors shall, within 30 days upon receiving the business license of foreign invested enterprise, go to the taxation, customs, land, and foreign exchange administrations to handle the related registration formalities

Article 19. In cases where any of the following circumstances apply to a foreign investor acquiring a domestic enterprise, the investor shall report the situation to MOFTEC and the State General Administration of Industry and Commerce:

1. One of the parties to the acquisition has a business turnover of over RMB1.5 billion in China during the year of application;
2. Having acquired more than 10 enterprises in accumulation from the associated sectors in China within a year;
3. Acquisition has caused one of the parties to the acquisition to have a market share of 20% in China;
4. Acquisition leads to the market share of one of the parties to the acquisition in China reaching 25%.

In cases where none of the circumstances mentioned in the above paragraphs apply, but MOFTEC and the State General Administration of Industry and Commerce consider, upon the request from domestic enterprises who are in competition with the parties to the acquisition, related functional department or industrial associations, that the foreign related acquisition involves a significant market share or other important factors exist that have a significant influence on market competition or the national economy and People's livelihood and national economic safety, the two authorities may request the foreign investors involved to report to them information concerning the acquisition.

Parties to the acquisition, as mentioned above, include enterprises associated with the foreign investors.

Article 20. In cases where any of the circumstances stipulated in article 19 of this set of Rules applies to the acquisition of domestic enterprises by a foreign investor, and MOFTEC and the State General Administration of Industry and Commerce consider that the acquisition might lead to over-concentration, hindering of fair competition, harming consumer benefits, the two authorities shall, within 90 days upon receiving the complete set of documents requested, call jointly or individually after consulting each other, a hearing for the related departments, institutions, enterprises and other interested parties, and decide whether or not to approve the application according to law.

Article 21. In cases where any of the following circumstances apply to the overseas acquisition, the parties to the acquisition shall, before publishing the acquisition plan or at the same time as reporting to their host country/region competent authorities, submit the acquisition plan to MOFTEC and the State General Administration of Industry and Commerce, which shall check to see whether any circumstances exist which would cause an over-concentrated domestic market, hinder domestic fair competition, harm the interests of domestic consumers, and make a decision of whether or not to approve the plan:

1. One of the parties to the overseas acquisition has assets of over RMB3 billion inside China;
2. One of the parties to the overseas acquisition has a business turnover of over RMB1.5 billion in the Chinese market during the year of application;
3. One of the parties to the overseas acquisition and its associated enterprises has a market share of 20% in the Chinese market;
4. The market share of one of the parties to the overseas acquisition and its associated enterprises reaches 25% in China due to the overseas acquisition;
5. One of the parties to the overseas acquisition participates either directly or indirectly in more than 15 foreign invested enterprises in the related sectors in China due to the overseas acquisition.

Article 22. In cases of acquisition under any of the following circumstances, a party to the acquisition may apply to MOFTEC and the State General Administration of Industry and Commerce for exemption from examination:

1. Capable of improving fair market competitive conditions;
2. Regrouping loss-making enterprises and securing employment;
3. Introducing advanced technology and managerial personnel and capable of enhancing enterprises' international competitiveness;
4. Capable of improving the environment.

Article 23. When submitting documents, investors shall classify the documents as requested and attach a table of contents of the documents. All documents submitted shall be written in Chinese.

Article 24. Investment companies established by foreign investors inside China, according to the law, shall apply this set of Rules in the acquisition of domestic enterprises.

Share right acquisition of foreign invested enterprises by foreign investors shall abide by the provisions of existing laws and administrative regulations on foreign invested enterprises and A Number of Regulations on Share Right Change of Foreign Invested Enterprises. In cases where there are no competent provisions, this set of Rules shall prevail.

Article 25. This set of Rules shall be referred to in cases of acquisition of enterprises in Mainland China by investors from Hong Kong SAR, Macao SAR, and Taiwan Region.

Article 26. This set of Rules shall enter into force as of April 12, 2003.