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**CIRC REMOVES SOME LIMITS ON FOREIGN INSURERS**

**Key Points:**

- **Geographical restriction removed**
- **Foreign insurers may own 51% of the shares of a Sino-foreign insurance brokerage company**

On December 11, 2004, the China Insurance Regulatory Commission (“CIRC”) announced that pursuant to China’s WTO commitment, effective immediately, foreign-invested life insurance companies are permitted to engage in health insurance, group insurance and pension fund management business. All geographical restrictions previously imposed on establishment of foreign-invested insurance companies were removed on the

same date. In addition, foreign insurers are now allowed to own 51% of a Sino-foreign insurance brokerage company, up from the previous limit of 50%. The above announcement was made on CIRC’s official Web site. – *Jennifer Liu*

**SAFE ISSUES NEW RULE TO REINFORCE MANAGEMENT OF BAD ASSETS DISPOSAL TO FOREIGN INVESTORS**

**Key Points:**

- **Requires approval from SAFE**
- **Requires registration with SAFE**

The State Administration of Foreign Exchange of the People’s Republic of China (“SAFE”) recently issued

a new circular, *Notice on the Administration of Foreign Exchange Regarding Assets Management of Companies Utilizing Foreign Investment to Dispose Bad Assets* ("Notice"). The Notice, which became effective on January 1, 2005, provides guidance on the approval procedures for the sale of bad assets to foreign investors. The Notice is also applicable to situations in which a PRC Asset Management Company ("AMC") sells or transfers bad assets to an entity or individual in the Hong Kong SAR, Macao SAR or Taiwan Area, or to foreign nationals, or to other Chinese financial entities who utilize foreign investment to deal with bad assets upon the approval of the relevant authorities.

SAFE has been involved in the approval of the transfers and disposals of bad assets to foreign investors regarding the foreign input and output and the foreign exchange.

The foreign investor shall provide details of the transaction to the appropriate SAFE office when a transaction consummates, remits any profit out of China, or it no longer owns the bad assets.

The foreign investor is allowed to resell the bad assets. A tax clearance certificate is required to remit proceeds from any such sale out of China.

The AMC must also comply with the registration requirements of SAFE when it uses the bad assets as contributions to a foreign investment enterprise.

– Carole Fan

## UPDATE ON JUDICIAL INTERPRETATION OF IPR CRIMES

### Key Points:

- ***Importer/exporter of counterfeit goods may be deemed accomplice in IPR crime***

- ***Distributing infringing works on the Internet for profit may be punished***

The Judicial Interpretation by the Supreme People's Court and the Supreme People's Procuratorate on Several Issues Concerning Application of Laws in Handling Criminal Cases Involving the Infringement of Intellectual Property (the "Judicial Interpretation") became effective on December 22, 2004. The Judicial Interpretation reduces the monetary threshold for criminal offenses involving intellectual property infringement. For both copyright and trademark infringements, the initial threshold to warrant a jail sentence has been lowered, from 200,000 yuan in illegal operating income previously to 50,000 yuan.

Under Article 16 of the Judicial Interpretation, anyone who knowingly provides assistance, including import-export agency services, in the crime of infringing on intellectual property will be deemed an accomplice. An exporter or importer of counterfeit goods can be charged independently even if the principal is at large. However, an exporter or importer is responsible only for the amount of counterfeit products for which such exporter or importer provides his or her services.

The Judicial Interpretation does not address the criminal liabilities of end users, as use by end users of infringing products does not satisfy the definition of an IPR crime under the Criminal Law. However, an end user can be held criminally liable if he or she, without permission of the copyright owner, distributes a written work, musical work, motion picture, television program or other visual works, computer software or other works to the public by an information network for the purpose of making profits.

The Judicial Interpretation represents a positive development in strengthening China's anti-piracy laws. However, its practical effect on reducing intellectual property violations in China remains to be seen. – *Wang Liang*

## AMENDING THE CATALOGUE GUIDING FOREIGN INVESTMENT IN INDUSTRY (2004 REVISION)

### Key Points:

- *Revisions to encouraged and restricted categories*

One of China's most important and widely consulted documents for foreign investors is the *Catalogue Guiding Foreign Investment in Industry*. First issued in the mid-1990s, the catalogue classifies hundreds of multifarious investment sectors – both manufacturing and service sectors – into “encouraged,” “restricted” and “prohibited” categories for foreign investment. The restrictions and transitional market access commitments detailed in the catalogue reflect those contained in China's Protocol of Accession upon joining the WTO. For example, the “restricted” category details the restrictions on foreign investment in transportation shipping, logistics, telecommunications, finance, banking, insurance and distribution, among others. Effective November 30, 2004, the revised catalogue fine-tunes China's market access restrictions by both adding and removing sectors from the “encouraged” category. For example, the “manufacture of alumina (production in excess of 300,000 tons)” is removed from the category, while the “production of differentiated chemical fibers” is added to the category. The “restricted” category is revised through the addition of three sub-sectors, viz., (i) the

construction and management of theme parks, (ii) market research (restricted to joint ventures only) and (iii) the production and distribution of radio and TV programs and the production of movies (the Chinese investor must retain majority interest). Foreign investors are therefore encouraged to review the amendments carefully to assess the potential impact of the revised catalogue on their existing or planned business operations. – *Diarmuid O'Brien*

## MOFCOM RELEASES NEW RULES ON AUTOMATIC IMPORT LICENSES FOR AUTO PRODUCTS

### Key Points:

- *Auto import licenses required for importation of auto products*
- *Authorizations from manufacturers required for importation of auto products for brand sales*

The Ministry of Commerce (“MOFCOM”) has issued implementing rules on procedures and documentation requirements that auto importers in China must complete to obtain automatic import licenses (“Rules”). The Rules are effective from January 1, 2005.

The Rules set forth detailed rules for the implementation of *Administrative Measures on Import of Mechanical and Electrical Products, Measures for the Administration of Automatic Import Licenses for Goods*, as well as the *Auto Industry Development Policy and Regulations on the Import and Export of Goods*.

Auto products subject to the Rules are listed in the annually renewable Catalogue on Commodities under Automatic Import Licenses (“Catalogue”). The

latest edition of the Catalogue for 2005, issued by MOFCOM on January 4, 2005, for the first time covers imported motor vehicles, auto spare parts and assemblies (including SKD and CKD) of the integrity, as well as any key components that “constitute the characters of completed motor vehicles.”

MOFCOM and its local offices in charge of electronic and machinery product import and export are responsible for the automatic import licensing of auto products (“Licensing Authority”).

Under this new licensing system, all auto importers must register for import of products that fall under the Catalogue to obtain the Automatic Import Licenses prior to taking any procedure at customs.

When applying for the license, in addition to the materials required under the *Measures for the Administration of Automatic Import Licenses for Goods*, an auto dealer that intends to sell imported cars in China must also provide the import contract and foreign car manufacturer’s authorization for distribution of cars under its brand(s). An importer of cars for self-use must provide its business license, and an auto manufacturer applying for import of motor assemblies and spare parts for production of auto products must provide the relevant *Category of Motor Vehicles Manufacturing Enterprises and Products* that identifies the type of car(s) it produces.

The Licensing Authorities will register and issue licenses automatically within no more than 13 days for import of auto products that fall under MOFCOM’s direct administration, or within 10 days for those under the direct administration by

MOFCOM’s branches. An Automatic Import License will be valid for six (6) months only within the calendar year of its issuance.

To facilitate the initiation of the new licensing system, MOFCOM also released an *Announcement on Conversion of Quota-Based Import Licenses to Automatic Import Licenses for Import of Auto Products* on December 28, 2004. By presenting to Licensing Authorities the relevant auto purchase contracts signed before December 31, 2004, the Electronic & Machinery Product Import Quota Certificates, the original Import Licenses and certain other documents required under the Announcement, auto importers can then convert their expired quota-based licenses to Automatic Import Licenses, so that they can complete import of any auto products that were ordered before the end of 2004 but remained undeliverable within the valid term of the original licenses. The valid term of such new converted license will last for only half a year without further extension. – Maureen Meng

## CSRC UNVEILS NEW IPO PRICING REGULATIONS

### Key Points:

- **New pricing system**
- **Greater market orientation**

On January 1, 2005, the Trial Pricing Quoting System for Initial Public Offers in China was established through the promulgations of the Notice on Issues Concerning the Trial Price System for Initial Public Offers (“IPO”) (“Notice”) and Memorandum No.18 Concerning the Standards for Approval on Issuance of Shares (“Memorandum”) on December 7, 2004 by China Securities Regulatory Commission (“CSRC”).

Under this new pricing system, the IPO pricing in China is independently determined by the market instead of the examination and approval of CSRC, while the CSRC's approval of the IPO and supervision on the process of pricing are still necessary. The Notice regulates the general procedures and methods for IPO pricing and the Memorandum provides for specific supervision requirements on the institutional investors who are qualified to advise on pricing.

According to the Notice, such institutional investors include the following six types: (1) securities investment fund companies; (2) securities companies; (3) trust investment companies; (4) finance companies; (5) insurance companies; (6) qualified foreign institutional investors ("QFII") and other institutional investors approved by CSRC.

In order to standardize information disclosure practices, the prospectus will be classified as the Letter of Intent to Issue Shares and not include information on price.

After the issuer proclaims a Letter of Intent to Issue Shares, the process for the price quoting will start and proceed in two stages: the primary quoting, during which the price range will be determined, and the accumulative bid quoting, during which the price will be finalized. The issuer must obtain, through its sponsor, price quotes from not fewer than 20 (or 50 if the IPO involves the issue of more than 400 million shares) institutional investors who satisfy CSRC requirements.

The issuer may then allot up to 20% of the shares (or 50% if the IPO involves the issue of more than 400 million shares) to be issued in the IPO to the

institutional investors who have provided price quotes. The institutional investors who are allotted shares must agree not to sell their shares within three months after the IPO shares are first listed for trading. The remaining IPO shares will be allotted to the public.

Further, the Notice allows the underwriting agreement to be signed only after the price has been determined by the pricing quoting system.

In addition, the Notice sets forth requirements applicable to sponsors and relevant intermediary institutions for the IPO process, including accounting firms and law firms, and applicable penalties in case of violations of relevant provisions. – *Zhang Wei*

## CSRC PROMULGATES RULES PROTECTING STOCK MARKET INVESTORS

### **Key Points:**

- **Holders of listed shares granted the right to approve new offers**
- **Listed companies required to provide voting platform on the Internet for shareholders**

The China Securities Regulatory Commission ("CSRC") issued the *Several Rules for Strengthening Protection of Interests of Holders of Shares Offered to the Public* on December 7, 2004. The new rules mark a significant step toward protecting the interests of minority shareholders in China's stock markets, where most of China's listed companies are controlled by majority shareholders holding "legal person shares" not listed on the stock market who are known to engage in practices harmful to the minority shareholders.

Notably, under the new rules a listed company must

obtain the approval of a simple majority of *listed shares* voting in order to (i) offer new shares or convertible bonds to the public, or place new shares among existing shareholders (except where the controlling shareholder commits full subscription to all the new shares); (ii) acquire material assets at a price 20% or more over the net book value of the assets; (iii) accept repayment of debt by any shareholder with its shares in the company; or (iv) cause a material subsidiary to go IPO overseas. These requirements are in addition to those under existing regulations.

To facilitate shareholders' voting, the new rules also require the listed company to provide a voting platform on the Internet when voting is conducted on a proposal to issue or place new shares.

The rules also specify certain rights and duties of the independent directors. For example, material connected party transactions and the hiring of accounting firms are now subject to the approval of the independent directors; independent directors are also entitled to independently hire outside auditors to conduct audits at the expense of the listed company.

– Zhao Yong

## CSRC AMENDS ANNUAL REPORTING FORMAT FOR LISTED COMPANIES

### **Key Points:**

- ***Profitable listed companies must provide explanations if they do not distribute cash dividends***

On December 13, 2004, the China Securities Regulatory Commission (“CSRC”) released the Notice re Amending No.2 Guidelines for the Content and Format of Disclosure of Information by

Companies with Publicly Issued Shares (“Notice re Amending No.2 Guidelines”). The Notice re Amending No.2 Guidelines aims to make information disclosure in the annual report of a listed company (“Company”) more transparent and thorough.

The original No.2 Guidelines for the Content and Format of Disclosure of Information by Companies with Publicly Issued Shares (amended in December 24, 2003, “No.2 Guidelines”) require the Company to disclose information related to the controlling shareholder or control person of the Company’s controlling shareholder. Among other things, the Notice regarding Amending No.2 Guidelines now requires the Company to identify with diagrams the equity-holding structure and control relationship between the Company and control person.

If there is affiliation among the top 10 shareholders of the Company’s floating shares, the original No.2 Guidelines require the Company to provide explanations for such affiliation. The Notice re Amending No.2 Guidelines takes the disclosure requirement a step further and requires explanations for affiliation between any of the top 10 shareholders of floating shares and any of the top 10 shareholders of the Company.

The Notice re Amending No.2 Guidelines also specifically requires disclosure of any objection raised by any outside director of the Company, while the original No.2 Guidelines only generally ask the Company to “introduce the performance of responsibilities by the outside director(s)”.

One of the most important revisions in the Notice re Amending No.2 Guidelines is that the Company will be asked to provide explanations if it does not pay

cash dividends when the Company is profitable. The Company also needs to explain how the undistributed profits are going to be expended, and provide plan(s) for such expenditure.

The scope of material information for the Company is also expanded in the Notice re Amending No.2 Guidelines. Any material information related to a subsidiary controlled by the Company will be deemed as material information of the Company, and shall be disclosed accordingly.

In addition, The Notice re Amending No.2 Guidelines sets out detailed revisions to the format of the Summary of Annual Report of the Company.

– Shawn Tai

## MOFCOM IMPLEMENTS REGULATIONS ON STORAGE AND DISTRIBUTION OF REFINED OIL PRODUCTS

### Key Points:

- *New regulatory system in operation*
- *Application of strict qualifying criteria*

Effective from January 1, 2005, are the Ministry of Commerce (“MOFCOM”)’s *Provisions on the Administration of the Market for Refined Oil Products*, designed to provide a comprehensive regulatory regime for the efficient operation of China’s ever expanding wholesale, retail and storage markets for refined oil products (gasoline, kerosene and diesel oil). More particularly, the provisions detail the qualifying criteria required of enterprises wishing to enter these markets, the examining procedures and time limits pertinent to processing applications, the functions of MOFCOM as the supervising authority and, finally, provision for the imposition of legal liability (administrative punishment) for certain

listed breaches. We see, for example, that enterprises applying for a refined oil wholesale business license must be qualified as follows:

1. Possess a fixed “refined oil” supplying channel, transmission channel, dedicated railway/waterway dock or other infrastructural facilities to load/unload refined oil;
2. Possess a refined oil warehouse in excess of 4,000m<sup>3</sup> that is wholly owned by the applicant or of which the applicant is the majority shareholder. The warehouse must be built in accordance with the *PRC Design Standard for Oil Warehousing* (GBJ74-84). All warehousing and other infrastructural facilities must satisfy national regulations on production safety and environmental protection;
3. Possess professional staff qualified in measuring, storage and fire prevention relating to the “refined oil sector” and satisfactory management rules;
4. Meet the requirements of the refined oil wholesale network development plan.

The provisions provide for a relatively quick processing time for applications – at the local level, COFCOM must grant/reject preliminary approval within 20 days; if approved, the application is reviewed by the ministry for final approval within a further 20 days. In compliance with international transparency standards, all rejected applications must be accompanied by a written notice giving the reasons therefore. These provisions are a long-outstanding and welcome addition to China’s regulatory framework, particularly as, for the first time, they introduce national regulatory standards

and procedures that supersede the existing body of local and municipal regulations. They also mark a

further step in the maturity and development of China's regulatory framework. – *Diarmuid O'Brien*

## Other articles and publications

*Please let us know if you would like copies of any of the following:*

**James Zimmerman and Diarmuid O'Brien**, "CIETAC Financial Dispute Arbitration Rules: Practice and Problems," *Asian Dispute Review* (November 2004)

**James Zimmerman**, *China Law Deskbook, Second Edition (2005): A Legal Guide for Foreign-Invested Enterprises*. More information is available on ABA's Web site:

<http://www.abanet.org/abastore/index.cfm?section=main&fm=Product.AddToCart&pid=5210139>.

## Squire Sanders Contacts:

<p><b>BEIJING</b></p> <p>Daniel F. Roules Sungbo Shim James M. Zimmerman Squire, Sanders &amp; Dempsey L.L.P. Suite 2501, 25<sup>th</sup> Floor, North Tower Beijing Kerry Centre 1 Guanghai Road, Chaoyang District Beijing 100020, China +86.10.8529.6998 Email: <a href="mailto:droules@ssd.com">droules@ssd.com</a> <a href="mailto:sshim@ssd.com">sshim@ssd.com</a> <a href="mailto:jzimmerman@ssd.com">jzimmerman@ssd.com</a></p>	<p><b>SHANGHAI</b></p> <p>Daniel F. Roules Amy L. Sommers Squire, Sanders &amp; Dempsey L.L.P. Room 30-31, 39/F, Plaza 66 1266 Nan Jing West Road Shanghai 200040, China +86.21.6288.0060 Email: <a href="mailto:droules@ssd.com">droules@ssd.com</a> <a href="mailto:asommers@ssd.com">asommers@ssd.com</a></p>
<p><b>HONG KONG</b></p> <p>Mao Tong Squire, Sanders &amp; Dempsey Room 4008 Gloucester Tower The Landmark, 11 Pedder Street Central, Hong Kong +852.2509.9732 Email: <a href="mailto:tmao@ssd.com">tmao@ssd.com</a></p>	<p><b>TOKYO</b></p> <p>Ken Kurosu Steven S. Doi Squire, Sanders &amp; Dempsey L.L.P. Ebisu Prime Square Tower, 16/F 1-1-39 Hiroo Shibuya-ku, Tokyo 150-0012 Japan +81.3.5774.1800 Email: <a href="mailto:kkurosu@ssd.com">kkurosu@ssd.com</a> <a href="mailto:sdoi@ssd.com">sdoi@ssd.com</a></p>

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February 2005

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