Wholly Foreign-Owned Medical Institutes No Longer Prohibited in China

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The People's Republic of China recently eased its restrictions on foreign capital investment in the health care industry to promote private medical institutes and the establishment of wholly foreign-owned medical institutes.

The People's Republic of China National Development and Reform Commission, Ministry of Health (MOH), Ministry of Finance, Ministry of Commerce (MOC) and Ministry of Human Resource and Social Security jointly issued the Notice Regarding Further Promotion and Guidance for Private Capital to Invest in Medical Institutes (Notice) on 26 November 2010.

According to the Notice, restrictions on foreign capital investment into the medical arena have been eased to promote private investment. There are several notable changes:

- Foreign capital may now establish wholly foreign-owned medical institutes through pilot programs.
- The approval procedures for foreign-invested medical institutes have been simplified.
- Private medical institutes will be entitled to certain tax incentives.
- Government-owned social medical insurance will apply to certain eligible private medical institutes.

Pilot Programs

Prior to the issuance of the Notice, investment in medical institutes was under the "restricted category" in the Catalogue of Industries for Guiding Foreign Investment. Foreign investment in medical institutes was also limited to a maximum stake of 70 per cent in a medical institute.

The Notice, for the first time, adjusts the investment in medical institutes from the "restricted category" to an "allowed category". Moreover, the Notice provides there will be pilot programs for eligible foreign investors to establish wholly foreign-owned medical institutes, and with the success of such programs, limitations on wholly foreign-owned medical institutes will gradually be removed in the future.

Adjusting medical institutes from the limitation of a restricted category to an allowed category and establishing wholly foreign-owned medical institute through pilot programs are strong signs the China government wants to attract foreign investment capital into the health care industry. However, although China has given the green light to wholly foreign-owned medical institutes, the PRC government will likely move cautiously. It is likely that only a few foreign investors with strong capabilities will be approved to establish wholly foreign-owned medical institutesat the pilot program stage.

In addition, because each city or province has its own planned quota for the numbers of medical institutes within the city or province, if the planned quota has been met, it will be difficult for subsequent foreign investors to establish additional medical institutions in that city or province. As such, the number of wholly foreign-owned medical institutes would be limited. Interested foreign investors should seize this new window of opportunity as soon as possible and take immediate action to establish wholly foreign-owned medical institutions through the pilot program.

Simplified Approval Procedures

Approvals for the establishment for foreign-invested medical institutes were complicated and time consuming in the past. For example, during the establishment of the United Family Hospital (UFH) Group, one of the top Sino-foreign health care service providers in China, the Beijing UFH first needed approval by the competent MOH at the district level in Beijing, then at the municipal level and finally at the state level. The Beijing UFH then needed to obtain approval from the competent MOC. As a result, official approval for the Beijing UFH alone took 18 months.

In order to encourage foreign investment in medical institutes, such time consuming approval procedures needed to be changed. Therefore, the Notice provides that the approval procedures for establishing foreign-invested medical institutes will be simplified. According to the Notice, foreign-invested medical institutions in the form of joint ventures shall be approved by the MOH and MOC at the provincial/municipal level, whereas, wholly foreign-owned medical institutes shall be approved by the MOH and MOC at the state level.

Because the Notice only provides high-level guidance, deference is given to the relevant government department, *e.g.*, MOH and MOC, for further detailed rules for implementation. Hence, it is expected that current laws and regulations regarding foreign-invested medical institutes will be amended, and further detailed implementation rules will be issued in the near future. Foreign investors need to stay tuned; future newsletters will provide any new updates in a timely manner.

Tax Incentives for Private Medical Institutes

In the past, “non-profit medical institutes”, which can only use income for the sustainable development of the medical institutes (shareholders cannot receive dividends), were entitled to tax incentives of exemption from corporate income tax at the rate of 25 per cent and the business tax at the rate of 5 per cent on their medical income. On the other hand, "for-profit medical institutes", which attempt to garner profits for shareholders, needed to pay both corporate income tax and business tax on their medical income. Because foreign-invested medical institutes were generally deemed "for-profit medical institutes", they were subject to heavy tax burdens, which deterred many foreign capital from investing in medical institutes in China.

Now the Notice allows foreign-invested medical institutes to be either "non-profit medical institutes" or "for-profit medical institutes". In other words, if the foreign investor chooses to invest in "non-profit medical institutes", the "non-profit medical institutes" can be exempt from corporate income tax and business tax. Furthermore even if the foreign investor chooses to invest in "for-profit medical institutes", the "for-profit medical institutes" can be exempt from business tax, and only need to pay corporate income tax on the medical income.

Reimbursement From Social Medical Insurance

Previously, foreign-invested medical institutes generally could not be reimbursed by the government-sponsored social medical insurance mainly because they decided the price of their medical service and medicine on their own and did not follow the government-designated medical service and medicine price.

However, the Notice expands the scope of social medical insurance so that if medical institutes accept the designated medical service and medicine price by the government, they can be eligible for and get reimbursed from the government social medical insurance. The Notice further denotes that the nature of the shareholders of the medical institutes (*i.e.*, state-owned, privately owned or foreign owned, etc.) should not be used as criteria to select the medical institutes to be covered by government social medical insurance.

Nevertheless, at present, the reimbursement levels from the government are extremely low for many services. If the government remains as the only source of insurance, it will be hard-pressed to support a health care system in which improved medical services and medicines cost more. For the ability to provide higher coverage, the government still needs to encourage the development of private insurance options.

Apart from the above points, the Notice also provides guidance to promote and encourage private capital to invest in the health care sector, and to uniform the treatment between state-owned and privately owned medical institutes. As health care reform evolves in China, the health care sector will become more and more open to foreign investors.