

## **Shanghai Municipality Issues Measures for the Launching of a Pilot Foreign-Invested Equity Investment Enterprise Project in Shanghai**

Implementing Measures for the Launching of a Pilot Program for Foreign-Invested Equity Investment Enterprise in Shanghai (the "Measures") were issued jointly by the Shanghai Municipal Financial Services Office, Shanghai Municipal Commission of Commerce and Shanghai Municipal Administration of Industry and Commerce on January 12<sup>th</sup>, 2011. The Measures will be effective on February 1<sup>st</sup>, 2011.

The main contents of the Measures are as follows:

### 1. Establishment of a Foreign-Invested Equity Investment Management Enterprise ("FEIME")

A FEIME is a foreign-invested management enterprise or a partnership mainly carrying out the following business:

- a. Sponsoring the Foreign-Invested Equity Investment Enterprises;
- b. Managing the investment of the Foreign-Invested Equity Investment Enterprise and providing related investment services; and
- c. Giving advice on the equity investment.

The requirements of the establishment of a FEIME are as follows:

- a. At least one investor who/which has the business scope relating to equity investment or equity investment management;
- b. At least two senior managers with more than 5 years' experience in equity investment or equity investment management, more than 2 years' experience in a senior manager position and relevant experience in China-related equity investments or Chinese financial institutions;
- c. The registered capital shall be at least USD 2 million and the contribution shall be in the form of cash.

### 2. Establishment of a Foreign-Invested Equity Investment Enterprise ("FEIE")

The FEIE is partnership enterprise with foreign investment primarily engaging in the following business:

- a. Investing with its own capital in private equity to the extent permitted by laws, including establishing new enterprises, investing in existing enterprises, etc.; and
- b. Providing management consulting services to the enterprises in which the FEIE invested.

The requirements of the establishment of a FEIE are as follows:

- a. The registered capital shall be at least USD 15 million and the contribution shall be in the

- form of cash;
- b. If the investors include the limited partners, each limited partner shall contribute at least USD 1 million.

Moreover, the FEIE shall not conduct the following activities:

- a. Investments in prohibited industries;
  - b. Investments in public stocks and corporate bonds in the secondary market;
  - c. Investments in futures and other financial derivative transactions;
  - d. Direct or indirect investments in the real estate for non self-use;
  - e. Investments by using capital other than its own capital; or
  - f. Loans or guarantees to third parties.
3. Qualification of a Pilot Enterprise (“Pilot Enterprise”)

A Pilot Enterprise is defined as a FEIME or FEIE (the “Applicant”) which have the corresponding qualification to receive special treatment for matters such as currency exchange, etc. This qualification is granted by a special joint committee led by the municipal finance office ("Joint Committee").

In order to be qualified as a Pilot Enterprise, the Applicant shall meet the following requirements:

- a. The proprietary assets of the Applicant shall be at least USD 500 million or assets under management of the Applicant shall be at least USD 1 billion during the past fiscal year before the application;
- b. The Applicant has the good corporate governance structure and internal control system;
- c. The foreign investor of the Applicant shall have at least 5 years’ experience of relevant investment;
- d. The Applicant hasn’t been subject to any judicial or regulatory penalties during the past two years.

Qualified as a Pilot Enterprise, a FEIME is entitled to convert the foreign currency capital into RMB, as the capital contribution to the newly established equity enterprise. The contribution of the FEIME can not be more than 5% of the equity of the invested enterprises. However, this part of the foreign investment will not change the nature of the new invested enterprises.

For a FEIE qualified as a Pilot Enterprise, the Measures do not provide for a quota system that permits the currency conversion of its capital between a foreign currency and RMB.

The capital contribution of the Pilot Enterprise shall be managed and supervised by the custodian bank according to the relevant regulations.

4. Comments

The implementation of the Measures will open the Chinese private equity market to foreign investors, especially the long term institutional investors. The Measures specify the substantial requirements and operational procedures of the establishment of a FEIE, FEIME and Pilot Enterprise, which will facilitate the foreign investment with respect to the private equity in China. Meanwhile, the Measures are expected to benefit foreign investors that invest in new strategic industry, high-technology area and other encouraged industries.

However, some outstanding issues are still needed to be further clarified in practice, such as currency conversion, fund repatriation, national treatment, etc. Furthermore, Shanghai Municipality indicates that it obtained US\$3 billion quota for the Measures. The allocation of the quota will also be an important element of the implementation of the Measures.