

Client Alert

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China's MIIT Issues Long-Awaited New Telecoms Catalogue

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More than twelve years after the promulgation in 2003 of the *Catalogue of Telecommunications Services* (《电信业务分类目录(2003版)》); the “**2003 Catalogue**”) China's Ministry of Industry and Information Technology (“**MIIT**”) finally promulgated the amended *Catalogue of Telecommunications Services* on December 25, 2015 (《电信业务分类目录(2015年版)》); the “**2015 Catalogue**”), which will take effect from March 1, 2016. On December 28, 2014, MIIT also released on its website an Interpretation of the 2015 Catalogue of Telecommunications Services by Relevant Responsible Persons of the Ministry of Industry and Information Technology (工业和信息化部相关负责人解读《电信业务分类目录(2015年版)》); the “**Interpretation**”), which provides helpful guidance on the policy goals informing the drafting of the 2015 Catalogue.

The Telecommunications Catalogue is a critical element of China's telecommunications regulatory system. It identifies and categorizes telecommunications services for the purposes of the licensing regime and operating rules set out in the underlying Telecommunications Regulations. A first version was issued in 2000, followed relatively shortly by the 2003 Catalogue. The intervening 12 years has seen significant changes in both technology and business models and a revamping of the 2003 Catalogue was greatly overdue. As we discussed in our June 13, 2013 alert, the MIIT released in 2013 for public comment of a draft revised Catalogue of Telecommunications Services (《电信业务分类目录(2013版)》(征求意见稿)); the “**2013 Draft**”). The 2015 Catalogue is heavily based on the 2013 Draft but also involves some significant refinements in the categorization of telecommunications services. The 2015 Catalogue clarifies significantly the regulatory treatment of a host of cloud-based and other on-line services that were previously in a grey area under the 2003 Catalogue. We outline below some of the more significant provisions of the 2015 Catalogue and discuss its likely implications for foreign investors in China's telecommunications sector.

GENERAL STRUCTURE

The 2015 Catalogue tracks the basic structure laid down in the Telecommunications Regulations and adopted in the 2003 Catalogue, dividing telecommunications services into two key categories: basic telecommunications services (“**BTS**”) and value-added telecommunications services (“**VATS**”). BTS essentially relate to underlying infrastructure such as voice and data transmission and VATS are services delivered via that infrastructure such as call centers and Internet-related services.

CHANGES TO BTS

The 2015 Catalogue includes the following new classes of BTS which were also proposed in the 2013 Draft:

- LTE (4G) digital cellular mobile communication services;

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- wire access infrastructure services; and
- satellite-based fixed communication services.

The 2013 Draft had also proposed including mobile telecommunications resale services as a new class of BTS. The 2015 Catalogue drops this new class of BTS and instead includes a notation that mobile telecommunications resale services are to be administered following the rules for VATS. This reflects the approach taken on a trial basis in the *Trial Plan for Mobile Telecommunications Resale Services* (移动通信转售业务试点方案), implemented by the MIIT during the period from May 17, 2013 to December 31, 2015, with a view to opening mobile telecommunications services businesses to private companies.

The 2015 Catalogue also removed the following obsolete classes of BTS:

- public telegraph and user telegraph services;
- analog trunking communication services; and
- wireless data transmission services.

The 2013 Draft contemplated removal of wireless paging services from the list of BTS, but these have been preserved in the 2015 Catalogue.

No new BTS licenses will be issued after March 1 for those services dropped from the 2015 Catalogue, but existing license-holders may continue to provide them within the term of validity of their existing BTS licenses (which generally have ten year terms).

CHANGES TO VATS

The 2003 Catalogue proved to be a blunt instrument for the MIIT and its local counterparts in recent years as they sought to regulate a host of new cloud-based and other on-line services. The VATS class, 'Internet Information Services' ("IIS"), has often been used as a "catch-all" licensing category for many services, including software-as-a-service, that did not fit neatly into any other class in the 2003 Catalogue.

Following the overall approach proposed in the 2013 Draft, the 2015 Catalogue addresses some of the shortcomings of the 2003 Catalogue in the following key ways:

- **By introducing new types of VATS**

The 2015 Catalogue introduces three new types of VATS:

- **Internet resource collaboration services ("IRCS")**. This appears to cover 'cloud' services utilizing remote datacenters such as storage, grid computing, platform-as-a-service ("PaaS"), infrastructure-as-a-service ("IaaS"), and potentially some forms of software-as-a-service ("SaaS").

The 2013 Draft had contemplated designating IRCS as a discrete class of VATS. A key modification under the 2015 Catalogue is to treat IRCS instead as a sub-set of Internet Data Center Services ("IDCS"). Companies wishing to engage in IRCS will therefore now need to apply for an IDCS license. Treating IRCS as within the scope of IDCS may subject IRCS operators to the additional onerous technical requirements applicable to IDCS operators, including the requirement to provide machine room and relevant support facilities and to implement security-safeguarding measures. This is consistent with the

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trend demonstrated in other recent PRC legislation (such as the National Security Law and the draft Network Security Law) to enhance regulatory control and standards of security and control over businesses which handle Chinese data.

- **Content distribution network services.** This class covers edge-caching and other distributed network data distribution management services intended to promote availability and minimize latency.
- **Internet domain name resolution services.** This class covers the provision of authoritative and recursive DNS hosting and resolution services. More broadly, the definition also covers other “code and protocol conversion” between user identifying codes (such as telephone numbers, domain names, and Internet service numbers) between other networks and the Internet, or within the Internet.
- **By clarifying the scope of IIS**

The 2015 Catalogue recasts its description of IIS in a way that is likely to have far-reaching consequences. As a general matter, the description has been made far more technology-neutral. We note below (in “Implications”) how this might lay the foundation for more effectively regulating information services provided via mobile applications, as well as via websites.

The 2015 Catalogue lists the following on-line services as IIS and provides detailed definitions of each:

- information release platform and transmission services;
- information search services;
- social network platform services;
- instant information exchange services (including instant messaging and real time voice/video call services); and
- information protection and processing services (including anti-virus and spam filtering services).

The wording of the 2015 Catalogue makes clear that the sub-classes are illustrative and not exhaustive. It seems likely therefore that IIS will continue to be utilized for novel Internet services as the market evolves.

Interestingly, some interpretative language proposed in the 2013 Draft has been omitted from the 2015 Catalogue.

For example, in providing a definition of information publication services, the 2013 Draft had provided as specific examples news websites, BBS, client applications, mobile newspapers, and App stores, and in providing a definition of social network platform services had provided as specific examples social networks, blogs, podcasts, microblogs, virtual communities, chat rooms, and on-line games. These two sets of examples have both been omitted from the 2015 Catalogue.

The 2013 Draft had also included definitions of “transactions processing services”, “network/electronic equipment data processing services”, and “electronic data exchange (EDI) services” within its explanation of the scope of the on-line data-processing and transaction-processing services category. These definitions have likewise been omitted from the 2015 Catalogue.

These omissions may not be that meaningful. Some commentators have sensibly suggested that MIIT officials excluded certain interpretive guidance merely to avoid unintentionally limiting the scope of related VATS

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categories as technology and business models continue to evolve, and that the interpretative guidance in the 2013 Draft remains useful in applying the 2015 Catalogue to today's technology and business models.

- **By clarifying the distinction between Category One and Category Two VATS**

The 2003 Catalogue divides VATS into two categories (a division not contemplated in the Telecommunications Regulations themselves). However, it did not make express the basis for the distinction between the two categories.

The 2015 Catalogue maintains the distinction between the two, but moves "Internet access services" from Category Two to Category One VATS and "on-line data-processing and transaction-processing services" (which covers, among other things, the operation of e-commerce marketplaces) from Category One to Category Two VATS. The Interpretation in turn offers an explanation for the distinction between the two categories and these moves, stating that Category One VATS comprise services "based on infrastructure and resources" and that Category Two VATS comprise services "based on public application platforms". While the language used in the Interpretation is somewhat opaque, market understanding is that the distinction being drawn is between 'telecoms' services that require dedicated infrastructure and other resources (which fall under Category One) and those that can be provided on a 'virtual basis' without requiring dedicated infrastructure (which fall under Category Two).

Implications for Foreign Investors

The 2015 Catalogue does not materially liberalize access to China's telecommunications market for foreign investors. Indeed, in some respects such access may be effectively diminished under the 2015 Catalogue.

The most immediate impact of the 2015 Catalogue is likely to be the clarity and consistency that it will impart to the regulatory treatment of a wide range of Internet-based services that were not addressed in the 2003 Catalogue and therefore fell into a regulatory grey area often being treated inconsistently by different local branches of MIIT. Some of these services (such as cloud computing and app-based information services) have proven to be very lucrative and foreign interest in participation has been high. In the absence of clear and consistent regulations, such participation has taken many forms, including, amongst others, direct provision of services by a wholly-foreign owned enterprise ("WFOE") that does not hold a VATS license, complex contractual arrangements with Chinese partners, and traditional 'VIE' structures. By expressly bringing such services into the telecommunications licensing regime, the 2015 Catalogue effectively rules out the possibility of using a WFOE to provide such services, and going forward, in almost all cases, foreign companies will need to identify and work with domestic Chinese partners and obtain a VAT license.

Foreign investors should also take particular note of the following specific ramifications of the 2015 Catalogue:

IIS via Mobile Applications

The description of IIS in the 2003 Catalogue focused on the type of network technology deployed in providing the service more than on the nature of the underlying services. This was reflected in the MIIT's regulatory policies and procedures, which implicitly assumed a website-to-browser operational model. In consequence, the regulatory regime has been ill-adapted to address the growth in app-based information services (i.e. those in which information is served over the Internet from a server to a dedicated mobile application rather than to a web browser) ("**App-Based Information Services**"). Local MIIT offices have often taken inconsistent stances on whether App-Based Information Services constitute IIS. As a result, many businesses have been running

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App-Based Information Services without an IIS license. Some operators have faced the invidious position of being informed that their App-Based Information Service constitutes IIS and then discovering that the application for an IIS licence assumes a website-to-browser operational model.

Implementing the approach proposed in the 2013 Draft, the 2015 Catalogue eschews this website model assumption and instead focuses on the underlying service in more technology-neutral terms. As a result, from March 1, businesses will generally require an IIS in order to operate App-Based Information Services. It is important to note that it is normally the operator of the server that will require the IIS license rather than the publisher of the relevant app (although in many cases both of these functions may be performed by the same entity). Thus, it seems unlikely that an entity which develops an app that uses published APIs to display information served from another company will require an IIS license.

Classification of Cloud Services as a form of IDCS

Treating IRCS as within the scope of IDCS may further complicate the ability of FIEs to participate in IRCS. China did not undertake to open foreign investment in IDCS in its accession to the World Trade Organization and MIIT has in practice not issued IDCS licenses to foreign invested companies other than to joint ventures with qualifying Hong Kong and Macau companies under the terms of the Closer Economic Partnership Agreement with Hong Kong. If MIIT continues this policy with IRCS having being included within the scope of IDCS, only joint ventures with qualifying Hong Kong and Macau companies and not other foreign invested companies may be able to engage in IRCS business.

The Status of SaaS

The 2015 Catalogue still leaves some important uncertainties. In particular, while PaaS and IaaS clearly fall within the newly-broadened definition of IRCS (and hence IDCS), the status of SaaS is less clear. Arguably, the core concept of SaaS, i.e. remotely using vendor-operated application software via a thin client interface under a subscription model, should constitute "Internet application deployment" under the IRCS definition. However, the universality of this conclusion has been doubted by some commentators, and it is possible that some forms of SaaS may fall outside of the scope of IDCS. Some SaaS offerings may also include functionality that falls within one or more of the new sub-classes of IIS (for example, information search functionality or anti-virus services). As a result, it will generally be necessary to examine in detail both the functionality within and the technical facilities underpinning a proposed SaaS offering in order to ascertain whether its provision will amount to IDCS and/or IIS. Software companies around the world are increasingly adopting SaaS as a replacement for traditional licensing and distribution models. Notwithstanding the uncertainties, it is highly likely that from March 1, most if not all SaaS will require some form of VATS license for which most forms of FIE will not be eligible to apply. In order to proceed with SaaS models after that date, foreign software companies will need to team up with local partners.

The 2015 Catalogue is couched in rather high-level language, and much will depend upon how that language is interpreted and enforced by the MIIT (and its local offices, which have not always seen eye-to-eye on matters of interpretation of the 2003 Catalogue). The MIIT is expected to issue further implementing rules in due course (particularly with respect to the new classes of BTS and VATS), which may help clarify the remaining uncertainties.

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