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## RSM Tax Advisory (Hong Kong) Limited

羅申美稅務諮詢有限公司

Welcome to Tax Flash – RSM Tax Advisory (Hong Kong) Limited’s Newsletter Covering Technical Development in Taxation

### PRC FOREIGN INVESTMENT LAW

*On 15 March 2019, the PRC National People’s Congress passed the new Foreign Investment Law. The new Law will be effective on 1 January 2020 and the prevailing three Laws (i.e. Wholly Foreign Owned Enterprise Law, Sino-Foreign Cooperative Joint Venture Law and Sino-Foreign Equity Joint Venture Law) governing the legal framework of foreign investment enterprise (“FIE”) will be repealed on the same day. For those FIEs which are established before the implementation of the new Foreign Investment Law, they will have a five-year transitional period to maintain their legal organization structure.*

*In this Tax Flash, we will provide you the salient points of the new Foreign Investment Law.*

#### 1. DEFINITION OF “FOREIGN INVESTMENT”

Pursuant to Art. 2 of the Foreign Investment Law, “foreign investment” refers to the following investing activities within the PRC directly or indirectly conducted by foreign natural persons, enterprises, and other organizations (hereinafter referred to as “foreign investors”):

- Establishment of a FIE in the PRC (solely or jointly with other investors)
- Acquisition of shares, equities, portion of property, or other similar interest in a PRC enterprise
- Investment in a new project in the PRC (solely or jointly with other investors)
- Investment in any other way as specified by laws, administrative regulations or the State Council

#### 2. “PRE-INVESTMENT NATIONAL TREATMENT AND NEGATIVE LIST” MANAGEMENT SYSTEM

Art. 4 of the Foreign Investment Law states that foreign investment would be granted “pre-investment national treatment” and subject to “negative-list administration” i.e. if foreign investment is in a sector not on the “negative list” for market access, treatment given to the foreign investor(s) and their investment during the investment access stage shall no less favourable than that given to local investor(s) and their investment.

### 3. INVESTMENT FACILITATION

To encourage foreign investments, the Foreign Investment Law contains provisions that put foreign investors on equal footing with domestic investors:

- All State policies on supporting the development of enterprises shall equally apply to FIEs (Art. 9)
- Comments and suggestions from FIEs shall be sought when formulating laws and regulations relating to foreign investment (Art. 10)
- FIEs can equally participate in setting standards in accordance with the law and enhance information disclosure and social supervision on standards setting (Art. 15)
- The compulsory standards formulated by the State shall equally apply to FIEs (Art. 15)
- FIEs can equally participate in government procurement activities (Art. 16)
- The products and services provided by FIE shall be treated equally by the PRC government (Art. 16)
- FIEs may raise funding through public offering of shares, corporate debenture and other ways in accordance to the law (Art. 17)

### 4. INVESTMENT PROTECTION

The Foreign Investment Law also contains provisions to protect the lawful rights of foreign investors and FIEs:

- The PRC government would not expropriate FIEs. In cases where the PRC government need to expropriate FIEs for public interest under special circumstances in accordance to the relevant laws and regulations, the foreign investment would be compensated fairly and reasonably (Art. 20)
- Foreign Investors may, in accordance with the law, freely transfer in and out of the PRC their contributions, profits, capital gains, income from asset disposal, royalties of intellectual property rights, compensation or indemnity obtained, income from liquidation, etc. within the PRC in RMB or a foreign currency (Art. 21)
- The PRC government shall protect the intellectual property rights of foreign investors and FIEs, and the legitimate rights and interests of holders of intellectual property rights and relevant right holders. In case of any infringement of intellectual property right, legal liability shall be investigated strictly in accordance with the law (Art. 22)
- The PRC government shall encourage technology cooperation based on free will and business rules. Conditions for technology cooperation shall be determined by all investment parties upon mutual and fair negotiation. No administrative department shall force any transfer of technology (Art. 22)
- Administrative departments shall keep confidential any trade secret of foreign investors or FIEs which are obtained during the performance of their duties (Art. 23)
- Where the relevant laws and regulations are not available, the government shall not impair the legitimate rights and interests of or impose any additional obligation to FIEs; set condition for market access and withdrawal, or intervene the normal production and operation activity of FIEs (Art. 24)

- Local governments at all levels shall strictly keep their policy commitments made to foreign investors and FIEs. For changes due to national or public interests, the statutory authority and procedures shall be followed and the foreign investor or FIE concerned shall be compensated for losses incurred (Art.25)
- A complaint mechanism will be established. FIEs or their investors can apply for administrative review or file administrative lawsuits when their rights and interests are infringed (Art. 26)
- FIEs may establish and / or voluntarily join any chamber of commerce or association, which shall carry out relevant activities in accordance with laws, regulations to safeguard the rights and interests of its member (Art. 27)

## **5. INVESTMENT ADMINISTRATION**

- Unless otherwise specified, relevant competent department shall review the application for license (if required) filed by the foreign investor in accordance with the relevant laws and regulations same as domestic investors (Art. 30)
- The organization form, institutional framework, permitted activities, administrative requirements etc. of a FIE will be governed by the PRC Company Law, PRC Partnership Enterprise Law, etc. (Art. 31)
- A foreign investment information reporting system will be established. Foreign investors or FIEs should report their investment information to competent departments for commerce through the enterprise registration system and the enterprise credit information publicity system (Art 34)
- Safety review may be conducted for any foreign investment affecting or having the possibility to affect national security, and the decision made in accordance with the law shall be final (Art. 35)
- For FIEs formed prior to the adoption of the Foreign Investment Law, they will have a five-year transition period maintain their legal organization structure (Art 42)

## **POINTS TO NOTE**

The new Foreign Investment Law establishes a unified legal framework for all types of foreign investment into China. It sets forth regulations on the access, facilitation and protection, etc., of foreign investment which emphasizes equal national treatment to level the playing-field for all investors and provides stronger legal protection on foreign investors' legitimate rights and interests.

It is no doubt that foreign investors would welcome the measures introduced by the new Law. However, please note that the Law only provides principle-based provisions. It is expected that the State Council will issue implementation measures to provide clarifications on how to enforce the Foreign Investment Law in the near future. Some of the practical issues and grey areas that need to be addressed include:

- the applicability of prevailing administrative measures and requirements related to foreign investment (e.g. debt equity ratios)
- Variable Interest Entity (“VIE”) structure arrangement
- how will information disclosure obligations work
- for existing FIEs, what should be done to follow the corporate governance rules under the PRC Company Law

Foreign investors should closely monitor the regulatory and practice developments and seek professional assistance where necessary.

## RSM Tax Advisory (Hong Kong) Limited

RSM Hong Kong's dedicated and experienced tax specialists can:

- Advise on tax efficient holding and operational structures for new cross-border investment, including the formation of Hong Kong and Chinese business entities
- Review existing cross-border investment structures, advise on identified deficiencies, quantify any potential exposure from such deficiencies, and further advise on restructuring approach and procedures
- Assist clients to discuss and clarify matters with tax officials, including transfer pricing and advance rulings
- Act as client representative in tax audits and tax investigations
- Provide transaction support services on mergers and acquisitions, including tax due diligence, deal structure advice, tax health checks, related human resources arrangements and other tax compliance and consultation services
- Advise on human resources and structuring employment arrangements in a tax-efficient manner
- Advise on tax equalization schemes
- Provide tax compliance services for individual and corporate clients in Hong Kong and China

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