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END OF AN ERA: MOFCOM REMOVES REGISTERED CAPITAL AND ANNUAL INSPECTION OBLIGATIONS FOR FIES

On 28 October 2015, the PRC Ministry of Commerce ("MOFCOM") issued new rules that remove significant obligations related to companies' registered capital and annual inspections.

The Decision on Revising Certain Rules and Regulatory Documents ("Decision") follows the State Council's plan, published in early 2014, to reform company registration and the capital registration system ("Plan"). The objective of the State Council's Plan (which applies to both domestic and foreign-invested enterprises, "FIEs") is to (i) replace the "paid-in capital" registration system with a "subscribed capital" registration system and (ii) replace the annual inspection procedure with an annual online reporting procedure.

MAIN CHANGES

The Decision impacts 29 rules or regulatory documents. The main changes for FIEs in the PRC are the following:

1. Minimum Registered Capital

The following types of FIEs are no longer subject to minimum registered capital requirements for establishment:

- Companies limited by shares;
- Venture capital firms;
- Investment companies; and
- Financial lease companies.

2. Registered Capital Contribution

The Decision also cancels all requirements on the minimum amount of initial capital contribution, the minimum amount of cash contribution (as opposed to non-cash contribution), and the contribution schedule. Shareholders of an FIE may determine these matters at their discretion and record them in the joint venture contracts or articles of association of the FIE. Some examples of the repealed rules are set out below:

- For companies limited by shares, the requirement that the registered capital must be paid up and that the sponsors must pay up all subscribed shares in a single instalment within 90 days of the date of issuance of the approval certificate is removed.
- For unincorporated venture capital firms, the requirement to pay up all subscribed capital within five years is removed.

- For investment companies, the requirement to pay up all the registered capital within five years from the date of issuance of the business licence is removed.
- For companies with non-cash contributions, the upper limit of 70% non-cash contributions is removed.

Unfortunately the Decision has not removed the registered capital to total investment ratio requirements, which restrict an FIE's ability to use cross-border debt financing (commercial or shareholder loans) to finance its activities in the PRC. Because these measures remain in place, the repeal of the above rules may have only a limited impact for the time being.

Following the shift to the subscribed capital registration system, MOFCOM and its local counterparts will no longer review registered capital contributions. Accordingly, the widely existing requirement that the registered capital must be paid up (as evidenced by a capital verification report) when conducting various corporate and business transactions is also abolished. Such transactions include:

- FIE investment into other companies in China;
- Merger or division of FIEs;
- Opening of new stores by commercial FIEs; and
- Contribution of a company's equity into another company's capital.

3. Joint Annual Inspection

As part of the plan to modernise the regulatory oversight of companies, the annual inspection of FIEs, which used to be jointly conducted by the commerce, tax, finance, foreign exchange and statistics authorities, was replaced with an online joint reporting procedure in 2014. In accordance with this change, the Decision cleaned up various annual inspection-related provisions and removed "the passing of the joint annual inspection" as a condition precedent to several corporate and business transactions of FIEs, including:

- Opening of new stores by commercial FIEs;
- Contribution of a company's equity into another company's capital; and
- Foreign exchange settlement and sale under capital account for real estate FIEs.

COMMENTS

Legally speaking, the State Council's Plan applies to all legal entities established in China, including FIEs. In addition, as it was issued by the State Council, the Plan supersedes all inconsistent provisions promulgated by MOFCOM. Nevertheless, in practice, local authorities are usually reluctant to take the initiative to apply a regulation that does not emanate from their direct supervising entity.

In this context, the Decision further harmonises MOFCOM's foreign investment rules with the State Council's reform plan by listing each provision to be revised. The Decision should remove uncertainty in many transactions by streamlining the foreign investment approval formalities and unifying local practices.

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