

# China (Shanghai) Pilot Free Trade Zone: how does it benefit foreign investors in China

## Description

The China pilot free trade zone in Shanghai has just been launched at end of September, and a slew of regulations tailored for the FTZ have also been unveiled. In particular, the much expected “negative list” listing those industries that are restricted or prohibited from foreign investment is also issued.

Overall, the experimental FTZ in Shanghai has aroused positive sentiments in China and overseas. To say the very least from a micro-perspective, the policies and rules within the FTZ have improved and facilitated foreign investments substantially.

### 1. Removal of Pre-establishment approvals

Before introduction of new rules, a foreign investment in China may take three distinctly different stages: obtain approval from the department of local development and reform commission, and then obtain an approval from local foreign investment department and then get the company registered with local company registry. In each stage, investors need to get prepared certain required documents in order to obtain the approvals.

Now in the FTZ, such approvals are now basically removed except for those projects required by China cabinet where approval of development and reform commission shall still be required. Foreign investors may just apply to the governing body of FTZ for filing the investment project and then proceed with effecting other formalities such as land, environment, bank, accounting, taxation etc.. It shall be noted there that such filing does not have to prelude the registration of the company. In the past or outside of the FTZ, the approval, verification or filing of investment projects shall have to be obtained in place before investors can apply for registration of company with company registry.

This is a big change indeed, inuring to the benefits of foreign investors. One of the big obstacles for foreign investments has been the governmental approvals that may prove to be tricky and time-consuming.

But merger and acquisition within the FTZ shall still be subject to the same rules in terms of security and anti-trust scrutiny.

### 2. Further Opening up of Certain Industries

Designed only for the FTZ, certain industries are now further opened to foreign investors within the FTZ.

According to the Master Plan for the FTZ as approved by China cabinet, six sectors in service industries are now further opened to foreign investors, namely: (1) financial service; (2) maritime shipping service; (3) commerce and trade; (4) professional service; (5) cultural service, and (6) social service, each with concrete measure for further opening.

One of the area that intrigues me is the “education and training” listed under “(6) social service”. Just yesterday, I received a call from a foreigner who is interested in opening up a training school in Jiangsu province. However, English training has been categorized as a form of education subject to license of local education department. In most localities, this education license is not easy to obtain.

Now in the Master Plan, it is provided that “allow Sino-foreign cooperative joint ventures in for-profit education and training programs”. Foreign investments in language training programs have been on hold in Shanghai for many years after Wall Street English, English First and Disney English were approved. With this clear green light signal, I believe that there will be more language training business to be set up in the FTZ.

On the other hand, for-profit education and training business made its appearance on the “negative list” for foreign investment. Industries appearing on the Negative List are areas or sectors where foreign investments are minded and restricted, and won't be entitled to favorable treatment availed to off-list industries in the FTZ. In other words, foreign investors may still face the problem of obtaining education license before setting up its operation entity. The moderately good point is that FTZ governments may be more willing to issue such licenses than other local governments in China. Foreign investors may have to test the ground.

### 3. Capitalization Rule Further Relaxed

Before FTZ, a company in China shall have to be capitalized with a minimum registered capital of RMB 30,000, and usually a large registered capital shall have to be paid up over a period of two years (company limited by shares may be different if it is incorporated by way of public offering.)

Now in FTZ, a company can be capitalized in much the same way as in the west. Shareholders will subscribe to shares of the company and pay up the capital in accordance with provisions of the articles of association of the company. There will be no requirement on minimum capital and no requirement on cash contribution ratio and no requirement on time limit of paying up the subscribed capital.

However, it shall be noted that there are exceptions to the general rule above, namely, national laws or regulations (issued by Central government or higher legislature) provide for requirements on minimum registered capital for certain kinds of companies such as financial companies.

On the other hand, while people are hailing the landmark move in setting up the free trade zone in Shanghai, it remains to be seen how the whole picture will roll out in the end. As reported by South China Morning Post, foreign banks are mostly hesitant to open branches in the FTZ, uncertain about the rules that may take time to be clear and certain.

There are some other meaningful measures accorded to FTZ. If you want to know more, please let me

know.

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**Author**

admin

Shanghai Landing Law Offices