



Client Alert

昊理文法律动态

December 2009

[Corporate and M&A/公司与并购]

Opportunities in RMB Funds Market for Foreign-invested Private Equity

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On 2 December 2009, the State Council of the PRC issued the Administrative Measures on Establishment of Domestic Partnership Enterprises by Foreign Enterprises or Individuals (“Partnership Measures”), effective as of 1 March 2010. The removal on some aspects of the restriction on the RMB Private Equity Funds encourages more foreign enterprises or individuals which are willing to invest in China.

I. Practice under Two Different Modes of RMB Funds by Foreign Investors

1. Pure RMB Private Equity Funds

Previously, foreign enterprises or individuals are strictly constraint to establish domestic partnership enterprises in accordance with the Partnership Enterprise Law of the PRC. At present, the situation has obviously changed due to the Partnership Measures resulting in some positive consequences which may inspire foreign investors devoting in RMB Private Equity Funds market. The partnership enterprises established by foreign enterprises or individuals may fully consist of foreign investors or in the form of a combination of foreign and domestic investors.

Theoretically, foreign enterprises or individuals could act as the General Partner (“GP”) or Limited Partner (“LP”) to engage in the investment, particularly the pure RMB Private Equity Funds.

Pursuant to Article 4 of the Partnership Measures, the contributed capital of the enterprises to be established may be made in freely convertible foreign currency or legally obtained RMB. In Article 5 Clause 3, it stipulates that the Administration of Industry and Commerce (“AIC”) is required to notify an equivalent level local authority of Ministry of Commerce (“MOFCOM”) the registration information of partnership enterprise that AIC has registered. However, some confused questions have not disappeared in such ambiguous provisions. Does it indicate that the foreign investors still need to get approval from MOFCOM or its provincial authority for investment, or just filing for record when applying for establishment? It remains silent on this issue. No further detailed guide could be found in the Partnership Measures. The relevant regulations shall be consequently facilitated to be more practical for foreign investors attempting to establish domestic partnership enterprises. In additionally, another issue is whether the proposed investment on restricted industry made by the foreign-invested pure RMB Private Equity Funds is still required to be approved? The definite answer can not be found in the provision.

2. RMB Funds Operated by Cooperative Joint Venture (“CJV”)

According to the Administrative Measures on Foreign-invested Venture Investment Enterprises (“Venture Measures”) dated 1 March 2003, RMB Funds could be managed and operated by CJV. Due to the strict requirements are set out in the Venture Measure, very few CJV

RMB Funds are approved and operated in China. More importantly, the investments on domestic restrict industry made by CJV Funds is required to be approved. Practically speaking, it is not so efficient compared with domestic pure RMB Private Equity Funds.

Comparing with the Venture Measures, the Partnership Measures prescribe many principled provisions apparently. In compliance with Article 14 of the Partnership Measures, it may be overridden by the Venture Measures to some extent.

II. Conflict of Interest between RMB and Foreign Currency Funds

Providing that a GP manages both RMB and foreign currency funds simultaneously, he confronts with the challenges on keeping the balance of investment fields and interest distributions among the domestic LP and the oversea LP. The immature market and imperfect legal system also make a deep influence on the decision-making for foreign investors. It’s necessary to build a series of mechanism adjusting the interests between LP and GP. In most case, RMB Funds may be used in the restricted industry by foreign-funded capital.

III. Conclusions

It’s clearly a good opportunity for foreign investors to consider establishing domestic partnership enterprises under the Partnership Measures as the limited liability partnership is common in private equity.

In conclusion, the Partnership Measures provide a legal framework on foreign investor’s participation in partnership in China and refer to other existing laws and regulations currently. More detailed guidelines are expected to execute the said measures.

Should you have any questions about this Client Alert, please contact the partner of HaoLiWen Corporate and M&A Practice Group:

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