

NEW CHANGES INTRODUCED BY THE IMPLEMENTING RULES OF NATIONAL SECURITY REVIEW FOR FOREIGN MERGERS AND ACQUISITIONS

On August 25, 2011, the Ministry of Commerce (“MOFCOM”) promulgated the long-awaited Implementing Rules on National Security Review for Foreign Merger and Acquisition of Domestic Enterprises (“Implementing Rules”). The Implementing Rules took effect as of September 1, 2011 and replaced the Interim Measures on Implementation of the National Security Review System for Mergers and Acquisitions of Domestic Enterprises by Foreign Investors (“Measures”).

Although they do not differ significantly from the Measures, the Implementing Rules introduce some substantive changes to the Measures. The main changes are as follows:

(1) FIVE WORKING-DAY TIMEFRAME FOR NOTIFICATION BY THE LOCAL MOFCOM

In assessing applications for foreign merger and acquisition (“M&A”) transactions, a local MOFCOM may decide that the transaction falls within the ambit of a national security review. In case such national security review application has not been lodged with MOFCOM, the local MOFCOM will issue a written notification to the relevant applicant for submission of an additional application for national security review within five working days from the acceptance of the application and withhold processing the foreign M&A application in the meantime.

(2) PRE-CONSULTATION IS AVAILABLE BUT NOT A MANDATORY PROCEDURE FOR THE NATIONAL SECURITY REVIEW

The Implementing Rules confirm that pre-consultation is not a mandatory procedure for national security review. It does not have a binding effect and cannot be used as the basis for the national security review application. However, it is confirmed that such verbal pre-consultation is available. This clarification is helpful in that potential applicants may consult MOFCOM in advance on any particular requirements of intended M&A transactions.

(3) SCOPE OF NATIONAL SECURITY REVIEW

Unlike other implementing rules to a law or regulation in China, the Implementing Rules have not specifically listed the industries and enterprises that may be subject to the national security review. Instead, it states that whether a transaction falls within the national security review shall be determined by the substance of the transaction and the actual influence of same. It also stresses that a foreign investor may not evade the national security review regime, whether by nominee equity holding, trust, multi-level reinvestments, lease, loan, control mechanisms through contractual arrangement, overseas transactions. This rule may discourage foreign investors from using traditional methods to get around these rules. However, the Implementing Rules have not set forth the legal liabilities for such breach.



(4) CONTINUAL POST-TRANSACTION REVIEW

Even if M&A transactions were approved or were not subject to the national security regime initially, any subsequent post-transactional changes may still render the transaction subject to the national security review regime. The Implementing Rules specifically include the change of ultimate foreign ownership or control as one of the situations requiring such review.

It is noted from the above that MOFCOM has tried to strengthen the national security review regime by determining a transaction from its substance and actual influence, thereby further preventing possible evasion of the national security laws and regulations. However, there remains uncertainty as to the scope of the sectors subject to national security review. In practice, it is reported that MOFCOM and its local counterparts have circulated an internal checklist which lists in detail 60 industries which may be subject to security review.

Such list has been installed in the internal system of national and local bureaus of commerce for internal scrutiny as to whether a transaction falls within the list and thus subject to national security review. As the list is not published, it is unclear whether industries apparently not related to national security will be caught under the list.

It remains to be seen how the Implementing Rules are implemented in practice and whether the review will constitute another serious obstacle for foreign companies doing business in China.

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