TaylorWessing

A More Structured World - The Birth of FIE Negative List

On December 7, 2016, the National Development and Reform Commission ("**NDRC**") and the Ministry of Commerce ("**MOFCOM**") jointly issued a draft revision to the Catalogue for Guidance of Foreign Invested Industries ("**Draft**", 《外商投资产业指导目录》（修订稿）) for public comment (deadline January 6, 2017). This will be the seventh amendment to the Catalogue for Guidance of Foreign Invested Industries ("**Catalogue**") since it was issued in 1995.

Q1: What is the Catalogue?

A: It is the key document regulating foreign investment access.

The Catalogue has always been one of the very first key PRC rules any foreign investor may need to look into – by separating industries into "encouraged", "permitted (if not listed in the Catalogue), "restricted" and "prohibited" to foreign investment, the Catalogue answers the very first question of any (potential) foreign investor – can I invest in China at all, and which industry is open to me?

Q2: What is the key change of the Draft?

A: Restructuring to "Encouraged + FIE Negative List"

The Catalogue is composed of three categories of "encouraged", "restricted" and "prohibited" industries.

Now the Draft is composed of the "encouraged" category and a long-waited Negative List of Foreign Investment Assessment ("**FIE Negative List**", also known as "special administration measures on assessment").

The FIE Negative List is formed by collecting/consolidating the industries subject to foreign investment approval mechanism (see our previous comment relating to foreign investment approval/filing). Such industries used to be scattered in all three categories of the Catalogue, i.e. restricted, prohibited and although encouraged however with management or equity ratio restrictions.

Components of the FIE Negative List include the following:

1. the "restricted" category (i.e. being the original restricted category plus repeating of the encouraged industries which are subject to management or share ratio restrictions);
2. the original "prohibited" category; and
3. a general guidance/principle of the FIE Negative List. For example:
   - FIE Negative List only includes the restrictions/prohibitions exclusively applicable to foreign investment. For this purpose, according to the authorities, 11 industries (e.g. casino/gambling; villa construction) have been removed from the FIE Negative List, since the related restrictions/prohibitions are applicable to both foreign and pure domestic investment.
   - If one industry is subject to any share ratio requirement under the FIE Negative List, then Sino-foreign joint venture in form of a foreign invested partnership will not be allowed.

Q3: Other routine changes?

A: NDRC/MOFCOM claimed to have reduced the restricted industries from 93 to 62.

Similar to other 6 times of amendments, this Draft also adjusts the industrial policies/attitude towards some specific industries. According to the joint statement of NDRC and MOFCOM, in general, the Draft keeps the "encouraged" category stable without many changes, while it reduces the number of industries with restrictions by 31 - from 93 (including 19 encouraged items with share ratio requirement, 38 restricted items and 36 prohibited items) to 62.

Some of such removals of restrictions may really open gate to foreign investment (e.g. the credit investigation and rating services is deleted from "restricted" (item 29), and it is also mentioned by MOFCOM and NDRC as a focus of opening up). However it is yet to be clarified in detail whether the said 31 also include the 11 items removed from the Draft simply because they are caught by restrictions/prohibitions applicable to both foreign and pure domestic investment (see section 3 under Q2).

Please feel free to reach out to us if you would like to know the impact indicated by the Draft on any specific industry.

Q4: What do I need to check in future to determine foreign investment access?

A: In general for restrictive access policies (with descending prevailing sequences): (1) relevant treaties or bilateral agreements, (2) FIE Negative List, and (3) Master Negative List

According to the Opinions of the State Council on Implementing of the System of Negative List for Market Access (in Chinese 国务院关于实行市场准入负面清单制度的意见, "**Opinion**") effective as of December 1, 2015 and other similar rules, the State plans, starting from 2018, to roll out nationwide the unified market access negative list mechanism with a Pre-establishment National Treatment (前国民待遇) for foreign investment (jointly as "**Negative List Mechanism**").

To be specific, according to the Opinion and other rules, foreign investment access (particularly the restrictions/prohibitions) shall mainly be consolidated and regulated in the following three perspectives:

1. Negative List for Market Access applicable to both foreign and pure domestic investment ("**Master Negative List**". A trial version has been issued by NDRC and MOFCOM in March 2016 to be implemented in Tianjin, Shanghai, Fujian and Guangdong provinces/cities (note: not FTZ zones!));
2. FIE Negative List; and
3. Any relevant signed treaties or bilateral agreements ("**Treaties**").

Treaties shall prevail in case of any discrepancy according to the Opinion. Between FIE Negative List and the Master Negative List, since the FIE Negative List would be the more special measure in terms of foreign investment, we understand that it shall prevail in case of any discrepancy to the more general Master Negative List.

Q5: What is the relationship with other several market access related lists, such as Free Trade Zone (FTZ) Negative List?

A (1): Likely FTZ Negative List remains applicable in FTZ.

So far there is no specific or official explanation publicly available in this regard. However considering the nature of FTZ (i.e. R&D center, pilot region before rolling out new policies to other regions or the whole State, in Chinese "试验田" "先行先试" as called by the State Council), it seems more sensible for the FTZ Negative List to remain in use to test/pilot certain/other industrial policies, which may later on be introduced to the Draft or the Master Negative List. In such context, Shanghai FTZ today confirmed that the Shanghai FTZ Negative List remains in use in Shanghai FTZ.

A (2): Negative List Mechanism should have partly absorbed several other lists.

Although the Catalogue used to be the key document deciding foreign investment access, there are other several lists or rules which in nature also contain industrial-policy-like administrative measures applicable to foreign investment. According to the Opinion, we understand that such rules shall remain in place. However the Master Negative List and the FIE Negative List are expressly required to collect, consolidate and synchronize with relevant parts from the following lists/rules:

1. The Catalogue for Guidance of Restructuring Industries/《产业结构调整指导目录》 (i.e. it is the general industrial policy applicable to both pure domestic and foreign investment, containing "encouraged" and "prohibited" (named as "Restricted" and "To-be-eliminated") industries.
2. Relevant Treaties;
3. The Catalogue of Investment Subject to Verification of the Government / 《政府核准的投资项目目录》 (i.e. the catalogue of fixed asset projects subject to verification of competent NDRC, which is applicable to both pure domestic and foreign investment);
4. The Collective List of Items Subject to Administrative Approval of Each Department of the State Council / 《国务院各部门行政审批事项汇总清单》 (i.e. the list of all matters which requires administrative approval from the mentioned authorities, including the foreign access related matters. Applicable to both pure domestic and foreign investment); and
5. Other market access administrative matters which are established according to law, administrative regulations or decisions of the State Council / 依据法律、行政法规、国务院决定设定的市场准入管理事项 (i.e. we understand that it is a catch-all clause to include any scattered market access restrictions. Application depends on specific situation).

Q6: What can we expect as the next steps?

A: Pilot ends by end of 2017; to be expanded to the whole nation as of 2018.

Likely during the pilot phase before 2018, one may expect to see: expansion of pilot regions; different treatment for "negative" industries; adjustment to the State security review and foreign exchange rules.

1. **Timeline**: according to the Opinion, the pilot of the Negative List Mechanism ends by December 31, 2017. Starting from 2018, it shall be officially rolled out nationwide.
2. **More pilot regions:** during the pilot phase, the pilot regions could be expanded from current four cities/provinces of Tianjin, Shanghai, Fujian and Guangdong to other regions. Among others, Heilongjiang, Jilin and Liaoning provinces may be the very next regions joining the pilot scheme according to recent opinions issued by the State Council; interviews of NDRC/MOFCOM officials also indicate that some middle or western cities/provinces may join the pilot scheme.
3. **Different treatments for "negative" industries:** according to the Opinion, Negative List Mechanism may further explore different ways to deal with different industries caught by the Master Negative List and FIE Negative List. For example, some less critical industry may be open to (foreign) investment if the investor undertakes to perform certain obligations. It is called "access upon undertaking / 承诺式准入" according to the Opinion.

No timeline is specified yet, however one may assume that such task is likely to be done still within the pilot phase.

4. **Adjustment of State security review and foreign exchange rules**: State security review and foreign exchange related rules are supposed to be adjusted to fit into the Negative List Mechanism according to the Several Opinions regarding Establishing An Open and New Economic System jointly issued by the State Council and the Central Committee of the Communist Party of China on May 5, 2015. Again no timeline is specified yet, however one may expect that such task is also likely to be done still within the pilot phase.

   Whether the pilot State security review rules as applicable to the four FTZs since May 8, 2015 can successfully "graduate" from FTZ and be expanded to further pilot regions or even the whole nation will need to be seen.

Q7: What can generally be stated as regards the intended change?

A: Unprecedented structure change to the Catalogue itself; it positively synchronized with other foreign investment access control rules; however it is only one (small) fraction under the general scheme of the Negative List Mechanism.

- From the perspective of the Catalogue itself: comparing to the earlier 6 amendments the Draft is unprecedented in substantially changing the structure of the Catalogue.
- From the perspective of foreign investment access control (see Q4), the Draft positively adjusts the original Catalogue to synchronize with the Master Negative List/applicable treaties, and together with the Master Negative List/applicable treaties, to synchronize with other market access lists/rules.
- From the general scheme of shifting market access control of domestic and foreign investment to the Negative List Mechanism, the Draft of course is only one part and solely from foreign investment and from industry perspectives. The Negative List Mechanism concept as such is much more comprehensive and will need to include also the domestic investment perspective, procedures related arrangements (e.g. from approval to filing, as we analyzed in above link) and other supporting mechanisms (e.g. State security review and foreign exchange rules).

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