



The end of the WFOE & JV in PRC: January 1, 2020

CCI FRANCE CHINE JULY 16, 2020



SMALL REMINDER



FOREIGN INVESTMENT LAW

KEYWORDS

Equal Treatment – Confidentiality Principles

Information Reporting

IPR Protection

THE END OF WFOE & JV

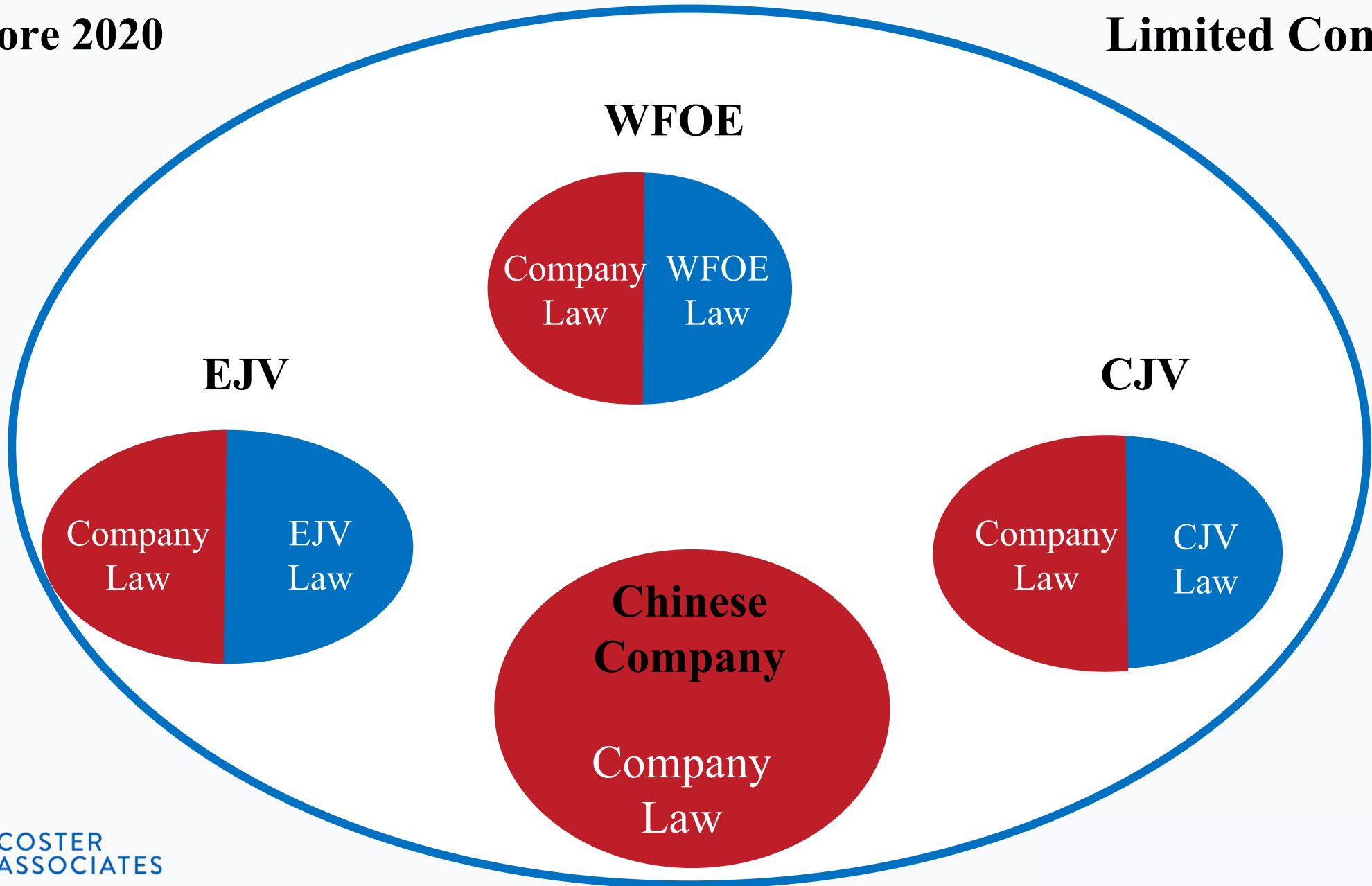
- **From January 1, 2020 - Repelled by New Foreign Investment Law**
 - *Law on Sino-foreign Equity JV*
 - *Law on WFOE*
 - *Law of on Sino-foreign Cooperative JV*
- Foreigners can no longer set up a new WFOE or JV after December 31, 2019

« *PRC Company Law will rule them all* »



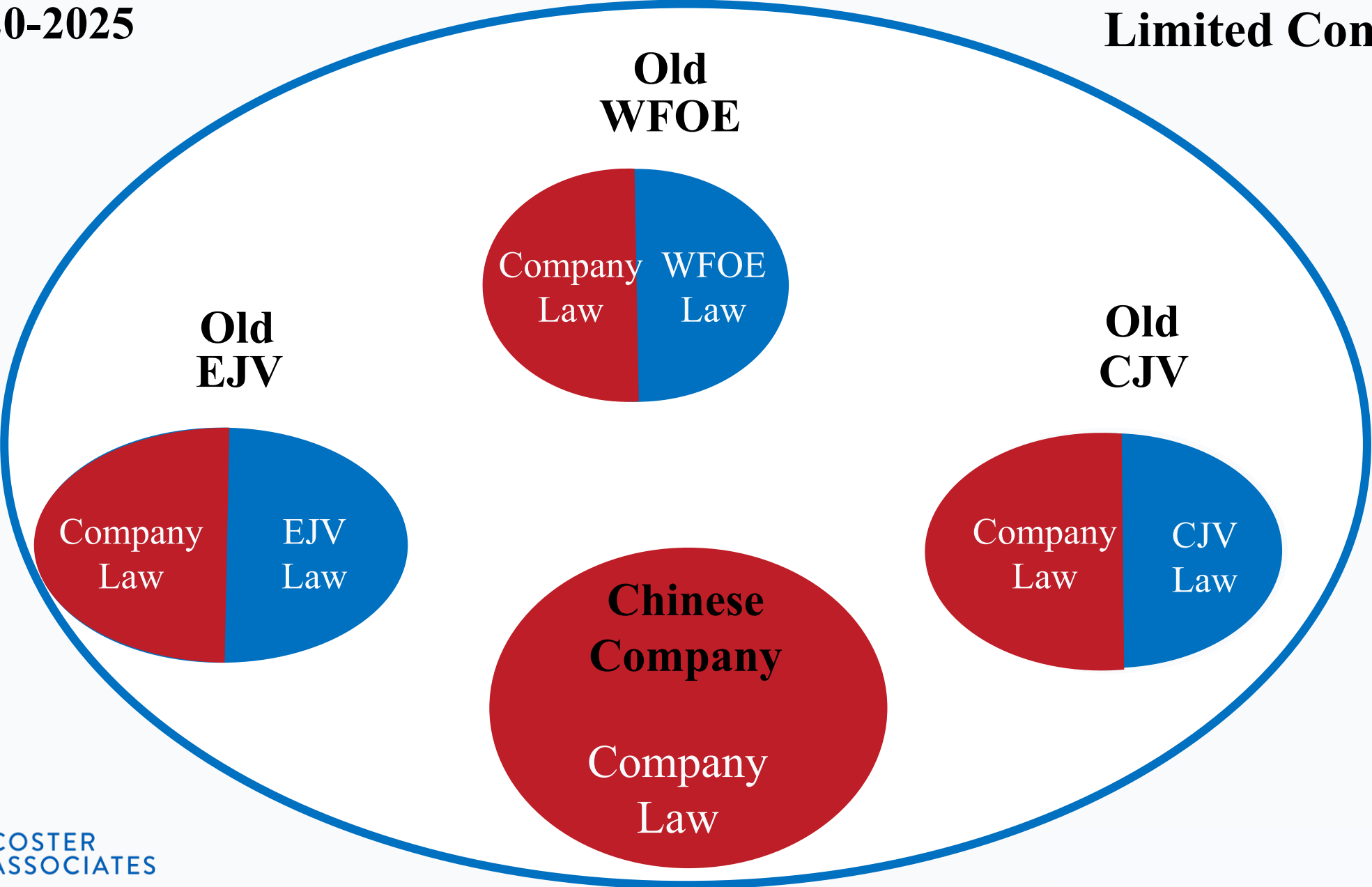
Before 2020

Limited Company



2020-2025

Limited Company



After 2025

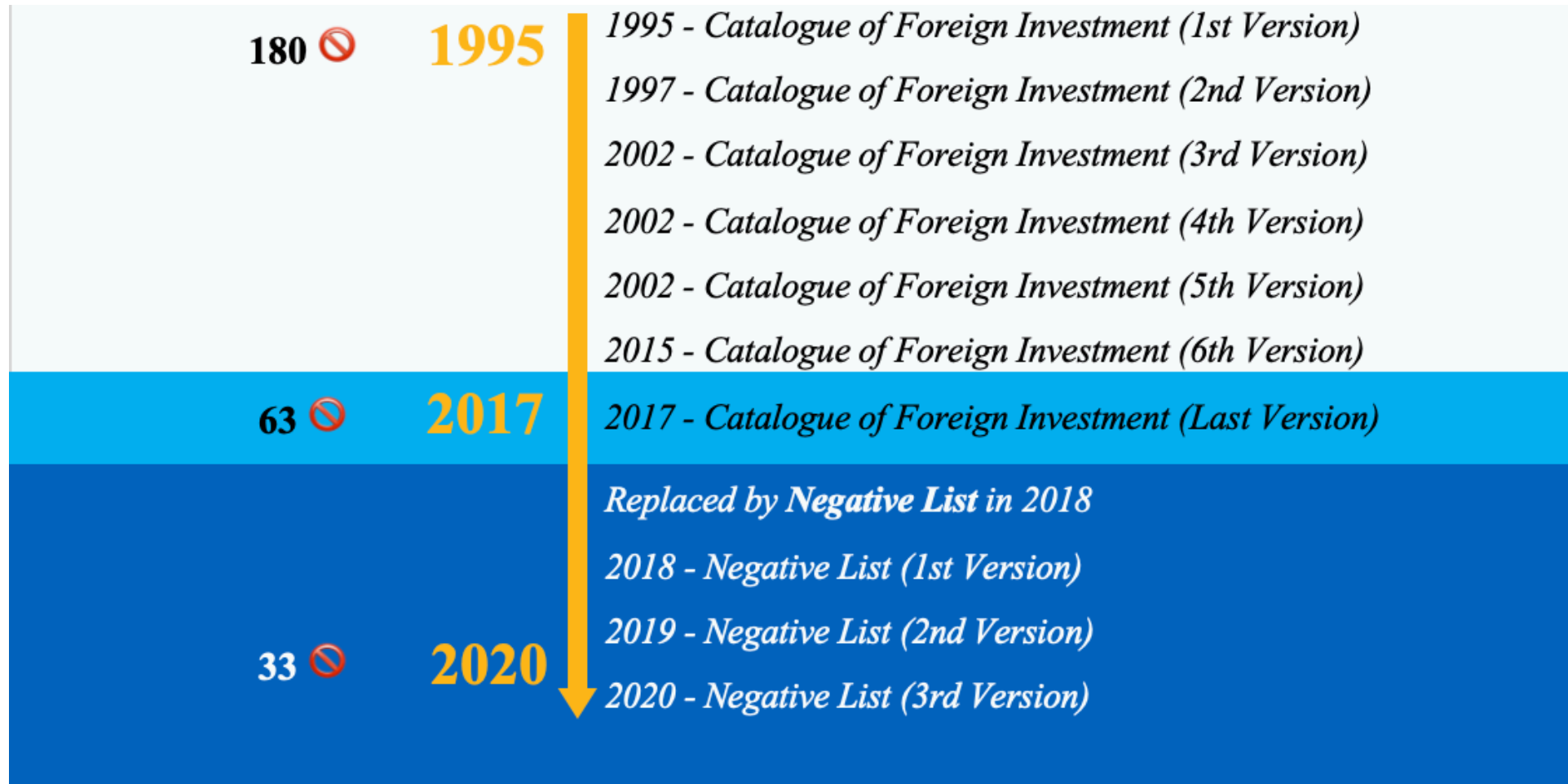
Limited Company



**Chinese Company with or
without Foreign Investment**

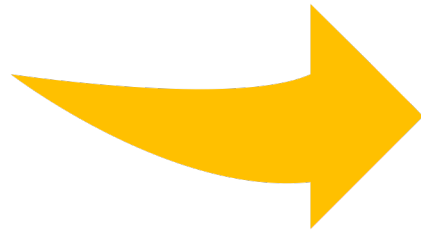
Company
Law

NEGATIVE LIST(S) REMAINS



IMPACT much wider than corporate structures !

- Direct or indirect investments in PRC
- Foreign natural persons, foreign enterprises or other foreign organizations
- Contracts for establishment of FIE, share transfer contracts, equity transfer contracts, assets transfer contracts or other similar interests, contract for newly-built projects, etc.
- But also: gift, division of assets, merger, split-off, etc.



- For investment contract not in the Negative List but need to be registered:
VALID- SHADOW AGREEMENT IS LEGAL
- If in NEGATIVE list:
ILLEGAL BUT POSSIBLE TO CURE IT before the judgement
- If in NEGATIVE list but after not anymore:
VALID

NEWS / METRO

First case related to new Foreign Investment Law: American shareholder wins shares back



By Ke Jiayun

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An American shareholder won his shares back in a company dispute following the new Foreign Investment Law taking effect on January 1. It provides foreign investors with the same rights as Chinese people, the Pudong New Area People's Court said on Wednesday.

The case was the first related to new law to be heard by the court.

The court said, the plaintiff, a Chinese American called Carson, and two Chinese men, surnamed Zhang and Cheng, had decided to set up a trading company in Shanghai in November 2009. Cheng is the plaintiff's brother.

Carson invested 510,000 yuan (US\$72,867) in the company while the other two put in 250,000 yuan and 240,000 yuan, respectively. The three signed a shares agreement on November 10. Since Carson was not allowed to establish a company with Chinese natural persons, the company was put under the names of Zhang and Cheng with his shares assigned to them. Zhang was registered as the company's owner. Although he couldn't hold shares, Carson participated in management and making decisions.

Later, Zhang's friendship with the brothers broke down and Carson decided to get back his shares from Zhang and give them to Cheng. However, Zhang rejected his request.

Carson filed a lawsuit demanding the return of his shares.

During the hearing, Zhang denied that Carson had invested in the company and said his money had just been for deals or debts.

He said even if Carson had made an investment, it should be considered invalid because Carson was an American and his setting up the company with Chinese natural persons violated the Sino-Foreign Equity Joint Ventures Law.

However, that legislation had been replaced by the Foreign Investment Law on January 1, which sets no such restriction on foreign investment. Accordingly, the court found in Carson's favor.

Source: SHINE Editor: Shen Ke



CHINESE FOREIGN INVESTMENT

New Foreign Investment Law protection extended to:

- Chinese citizens settled overseas
- Investors from HK, Macao and Taiwan



 Chinese citizens living in Mainland China but investing through HK, Macao or Taiwan ?

Chinese citizens or other Chinese investors (excluding FIE) wholly-owned enterprises established overseas investing in PRC?



5 YEARS REDEMPTION TERM



WFOE and JV established before January 1, 2020, may keep their original organizational forms for **5 years**:

- Possible to change it
- Possible to wait



AFTER 2025?

- Chinese company registry shall not process the application(s) for any other registration matter(s)
- Public announcement: social credit ?

WFOE - JV - CHINESE COMPANY

Subjects	Under EJV Law	Under CJV Law	<u>Chinese Company</u> WFOE
Highest authority	Board of <u>Directors</u>	Board of directors /Joint Management Committee	Shareholders
Powers and duties of highest authority	All major issues such as change of AOA, increase and decrease of registered capital ,merger or spin-off and dissolution	All major issues such as change of AOA, increase and decrease of registered capital, merger or spin-off and dissolution	More detailed than those under the JV Laws
Voting rules for major issues	Unanimous consent of the present	Unanimous consent the present	Favorable votes of shareholders holding 2/3 or more of the voting rights
<u>Number of members</u>	3 directors minimum	3 minimum	3-13 or <u>Executive Director</u>
Quorum	2/3 of all directors	2/3 of all directors or members of the Joint Management Committee	Free to be agreed by shareholders
Term of director	4 years	No more than 3 years	No more than 3 years
Legal representative	Chairman of the Board	Chairman of the Board or <u>Director</u> of the Joint Management Committee	Chairman of the Board, <u>Executive Director</u> or <u>General Manager</u>

WFOE - JV - CHINESE COMPANY

Impact on corporate governance?

➤ WFOE: limited because of 2006 – update opportunity – 3 funds

➤ JV: huge - in favor of majority shareholder

• *Art. 46 Implementation Regulations for the FIL*

*Upon adjustment of organization form or organization structure of an existing foreign investment enterprise pursuant to the law, the equity or interests transfer method, gains distribution method, residual assets distribution method etc. agreed in the contract between the EJV or CJV parties **may continue to be handled in accordance with the agreement.***

SOME JV'S IMPACTS

- **Highest authority:** from the BoD to the Shareholders Meeting
- **Directors appointment:** for JV the number of directors to be appointed by each shareholder is determined in % to each shareholder's capital contribution / number of directors to be appointed can be stipulated in the AoA.
- **AoA amendment:** important decisions require unanimous approval of the present directors / approval of 2/3 of the shareholders holding voting power.
- **Chinese employee can become a partner**

Dividend: in % to the capital contribution / same under the Company Law but shareholders may decide on a different scheme by unanimity.

Shares transfer: consent of all shareholders + pre-emptive rights of others shareholders / No consent for internal transfer - external transfers consent of more than half of the other shareholders.

If refused, the dissenting shareholders have an obligation to purchase the shares.

If refused to purchase will however be deemed as consenting to the transfer. Pre-emptive right to purchase the shares on the same terms. Possible to agree on a different scheme for transfer of share.



HOW TO BE READY?

1. To review AOA : MSA withdrawing («市场监督管理局变更登记»)
2. To review your AOA, JV contract or shareholder agreement (deadlock, call option, etc.)
 - a) highest authority;
 - b) voting rules for major issues;
 - c) quorum;
 - d) share transfer mechanism...

HOW TO BE READY?

3. Bargaining power assessment and core interests identification before to start the negotiation

For majority shareholders:

- a) to reduce the restrictions of unanimous consents mechanism;
- b) to take the advantage of voting rights.

For minority shareholder:

- a) to keep the unanimous consents mechanism;
- b) to negotiate exit options

HOW TO BE READY?

Jam risk in 2025

Social credit risk in
case of deadlock

Plan ahead the
negotiation, do
not wait for
2025



MANY NEW OPPORTUNITIES

- Merger- Acquisition
- Shadow equity investment
- Funding options: shares swap
- Public issue of stock, bonds,
other securities



STILL SOME UNCERTAINTIES

- DEADLOCK 2025
- National security review
- Total Investment Rule
- Company Social Credit
- Communist party





THANK YOU

