

# China Client Alert

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## Foreign-Invested Partnership - An Opportunity for Private Equity Funds in China?

On March 1, 2010, a new form of foreign-invested enterprise under Chinese law will be introduced: the foreign-invested partnership. This type of entity is created by the Administrative Measures on Establishment of Partnership Enterprises by Foreign Enterprises or Individuals (the "Measures"), which were promulgated by the State Council on November 25, 2009 and will come into effect on March 1, 2010. The Measures are one of the implementing rules of the 2007 Partnership Enterprise Law and thus enable foreign investors to create the types of partnerships (limited and unlimited) and management arrangements for those partnership available under the Partnership Enterprise Law. According to the Measures, two or more foreign investors, or foreign investors together with Chinese individuals, legal persons or other entities can establish partnerships in China. Moreover, foreign investors can also join an existing domestic partnership by making new contributions or acquiring partnership interests. The Measures provide that contributions may be made in foreign currency, but do not clarify whether and how foreign investors can make contributions in kind or through services, which is expressly permitted under the Partnership Enterprise Law.

The Measures break new ground in another respect as well: apart from representative offices, foreign-invested partnerships will be the only foreign-invested entity that can be established without prior approval by the Ministry of Commerce (the "MOFCOM") or its local counterparts or any other regulatory authority. The representative or agent of the partners can directly apply to the administration bureau of industry and commerce (the "AIC") for registration. In addition to the documents required for the registration of all partnerships, the partners applying to register a foreign-invested partnership must also submit an explanation of its compliance with foreign investment industrial policies. If regulatory approval is required for the proposed business of the partnership, this approval must be obtained before AIC registration. Thus, not surprisingly, foreign-invested partnerships will likely be subject to the same sectoral approval requirements as other foreign-invested enterprises.

By promulgating the Measures, the State Council provides a simple and clear avenue for foreign investment under the existing framework of the Partnership Enterprise Law. Other authorities now have to clarify how this novel entity fits

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into regulations governing tax, foreign exchange and other aspects of its business.

It remains unclear whether foreign-invested private equity funds may be established under the Measures. According to the official announcement of the Measures made by the State Council, the relevant ministries still have different views on the regulatory approach to foreign investments in private equity funds in China. Therefore, the Measures are not clear on whether the foreign investors can use this mechanism to establish private equity funds in China. The Measures only provide that special rules on foreign invested partnerships mainly conducting investment business shall be complied with. This provision may be simply a placeholder for future regulations or a reference to the Administrative Provisions on Foreign-Invested Venture Capital Enterprises, which provide a form of non-legal person venture capital fund similar to a partnership. The regime will have to be clarified before private equity funds can be established under the Measures.

As often in China, local authorities may be allowed to experiment first in this area before a nationwide rule is adopted. There have been news reports recently that the Beijing Municipal Government is going to issue local rules, explicitly permitting establishment of foreign-invested private equity funds in the form of a limited partnership pursuant to the Partnership Enterprise Law and the Measures. We may therefore expect clarification before the Measures come into effect on March 1, 2010.

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