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# China News Alert Issue 248

## Capital Markets

### China toughens forex receipts and export settlements

In order to step up the battle against "hot money" flowing into and out of China, three Chinese central governmental departments are to link their internal electronic systems from 14th July in a trial check of foreign exchange receipts and exports settlements, the State Administration of Foreign Exchange (SAFE) said recently.

These measures were interpreted by analysts as one of the latest efforts by the Chinese government to monitor capital flow and prevent more so-called "hot money" from flooding in and out of the country.

"Hot money" is usually defined as short-term global speculative funds moving among financial markets in search of the highest short-term returns.

SAFE said it would conduct the checks with two other departments: the Ministry of Commerce and the General Administration of Customs (GAC).

With the new online checking system in place, regulators will be able to compare enterprises' forex receipts and settlements with their exported goods at the GAC.

The new system will be put into formal operation from 4th August 2008.

In another action to help implement the new system, SAFE said it would ask mainland enterprises to report advance export receipts and deferred payments of imports.

SAFE said that by monitoring enterprises' advance export receipts and their later actual exports it would be able to prevent overseas funds entering the country for speculation under the guise of trade.

Whilst improving the monitoring of deferred payments for imports, SAFE could prevent a possible large capital loss in the future, said the administration.

The government does not release official figures about how much "hot money" there is in the system, it doesn't even use the term "hot money". But analysts estimate at least US$147.9 billion of "hot money" flowed into the country in the first five months of 2008, and as much as US$600 billion in "hot money" has entered the country in total, most of it after 2005.

Analysts also believe that over-invoiced exports, along with over-stating foreign direct investment and underground private banks, were three major channels for "hot money" to flow into China.

China had taken a series of increasingly aggressive measures in past months to blunt the impact of "hot money," amid the explosive growth of its foreign exchange reserves. The influx has been so massive as to raise alarms over the country's financial security.

According to SAFE, as of the end of May, forex reserves stood at US$1.797 trillion. SAFE figures show that during the first five months of 2008, forex reserves increased by 18.7 per cent year-on-year, or US$268.7 billion.

[Source：China Daily](http://www.chinadaily.com.cn/bizchina/2008-07/03/content_6817240.htm) ([see archive](China_toughens_forex_receipts_and_export_settlements.pdf))

### Unprecedented capital inflow tests Chinese regulators

China has taken a series of increasingly aggressive measures in past months to blunt the impact of so-called "hot money," amid the explosive growth of its foreign exchange reserves, which have soared beyond that which can be explained by trade and investment.

The inflow of capital has been so massive as to raise alarms over the country's financial security.

According to the State Administration of Foreign Exchange (SAFE), as of the end of May, forex reserves stood at US$1.797 trillion.

SAFE figures show that during the first five months of 2008, forex reserves increased by 18.7 per cent year-on-year, or US$268.7 billion.

What caught the attention of analysts was that forex reserves jumped at the same time as the current-account surplus and foreign direct investment (FDI) into the fixed-asset field declined.

Set against the increased forex reserves in the first five months of this year, there was US$78.02 billion represented by the trade surplus, which was down 8.6 per cent year-on-year.

Another US$42.78 billion was connected with FDI in the first five months of 2008, which increased by nearly 55 per cent year-on-year. But FDI going into fixed assets (longer-term investment), actually fell 3.5 per cent in the same period.

Jiang Zheng, a macro-economist at a Beijing-based securities firm, has closely tracked these figures and analysed the data.

After deducting the trade surplus and the FDI, there was an unexplained US$147.9 billion in the forex reserve increase figure, which Jiang and numerous other analysts consider to be "hot money", which is usually defined as short-term global speculative funds moving among financial markets in search of the highest short-term return.

The government does not release official figures on this category of funds; in fact, it doesn't even use the term "hot money", so analysts can only make estimates.

Jiang said the "hot money" figures deduced by analysts might even be underestimates. "There is a tricky decline among the FDI figures, i.e. the drop of fixed-asset investment," he explained.

"Foreign direct investment in the first five months of 2008 increased by about 55 per cent. But strangely, fixed-asset FDI in the first five months fell 3.5 per cent from last year's figure," Jiang said.

Jiang said it appeared that some speculative money had managed to move into China in the guise of FDI.

But there are many other channels for "hot money" to flow into China. These include falsified international trade with over-invoiced exports and underground private banks, according to Jiang.

Jiang and other analysts maintained that as much as US$600 billion in "hot money" had entered the country, most of it after 2005.

Jiang said he was somewhat surprised at the scale of "hot money" inflow in the first five months of this year. The monthly inflow of "hot money" from January to May 2008 was estimated at US$35 billion, more than double the US$15 billion figure for the same period last year, Jiang said.

In April alone, deduction showed that a record US$50.2 billion of "hot money" poured into China, he said.

[Source: Xinhua](http://news.xinhuanet.com/english/2008-07/01/content_8471103.htm) ([see archive](Unprecedented_capital_inflows_test_Chinese_regulators.pdf))

### Listed companies must meet environmental protection requirements for financing

China's Ministry of Environmental Protection has recently announced a new regulation stating that enterprises in fourteen industries, including power and steel, will not be allowed to apply for refinancing or listing if they fail to pass certain environmental protection standards.

The 'Directory of Classified Management on Industries of Listed Firms Subject to Environmental Protection Investigation' (Directory) lists the fourteen industries as: power, steel, cement, electrolysed aluminium, coal, metallurgy, construction materials, mining, chemistry, petrifaction, medicine, light industry, textiles and leather.

Enterprises applying for listing must ensure that they comply with the following stipulations: released pollutants meet national or local standards; pollutant emission permits are legally obtained, and that companies have satisfied the requirements of the permits; and that 100% of industrial solid waste and dangerous waste is safely disposed of.

[Source: Lexis Nexis](http://hk.lexiscn.com/latest_message.php?id=4276) ([see archive](Listed_Companies_Must_Meet_Environmental_Protection_Requirements_for_Financing.pdf))

### Financial advisers to be subject to qualification licensing regulations

On 4th July, the China Securities Regulatory Commission (CSRC) officially released 'Administrative Measures for Financial Advisers of Merger and Acquisition and Reorganisation of Listed Companies' (Measures), which will place financial advisers under qualification licensing regulations.

The Measures require securities companies acting as financial advisors for mergers and acquisitions (M&A) or the reorganisation of listed companies, to satisfy the following requirements: must meet the CSRC's requirements on net capital; be equipped with sound and well-working internal control mechanisms and management systems; strictly adhere to risk control and internal isolation systems; and have sound due diligence investigation systems, project risk appraisals and internal verification mechanisms.

Securities investment consulting institutions must obtain the securities investment consulting business qualification approved by the CSRC and have registered capital and net assets valuing no less than RMB 5 million. Their major shareholders and actual controllers must have remained unchanged for one year prior to the application, they must have a sound reputation and no record of serious violation of laws and regulations within the past three years. They must also have been engaged in the financial advising business for M&As and reorganisation of listed companies for more than two years with an annual income from the business of over RMB 1 million.

The Measures are scheduled to take effect as of 4th August 2008.

[Source: Lexis Nexis](http://hk.lexiscn.com/latest_message.php?id=4268) ([see archive](Financial_Advisers_to_be_Subject_to_Qualification_Licensing_Administration.pdf))

## Corporate & Commercial

### Hong Kong service firms set to receive more help

China's Ministry of Commerce and the government of Hong Kong will soon sign a document to help companies from the region's service sector operate on the mainland, Vice-President Xi Jinping said recently.

"I hope the arrangement will provide new opportunities for the development of the service sector in Hong Kong," he said.

"The central government will continue to support all initiatives and endeavours aimed at developing the economy and improving people's lives in Hong Kong."

Xi made the comments during a speech ahead of a banquet dinner held by the Hong Kong government in his honour at the Island Shangri-La Hotel.

"Focusing on developing the economy enables Hong Kong to grow more prosperous, play a more important part in the country's overall development and occupy a more favourable position in the global market," he said.

Xi was in Hong Kong for a three-day inspection tour of the city's preparations for the upcoming Olympic and Paralympic equestrian events.

In his speech, he praised the regional government and all parties involved for their dedication and hard work.

"The government has led the preparatory work with a great sense of commitment," he said.

"The whole country, and indeed the whole world, is deeply impressed by Hong Kong people's enthusiasm, their level of participation and their passion for the Olympics."

Xi also expressed his thanks to the government and people for their support in the aftermath of the Sichuan earthquake.

Reiterating the comments made by President Hu Jintao on 6th March, during a meeting with NPC deputies and CPPCC members from Hong Kong and Macao, Xi urged the Hong Kong government to continue developing the economy and enhancing social harmony.

"Since its return to the motherland, the future of Hong Kong has been in the hands of our Hong Kong compatriots and has been closely linked with the future of the motherland. We believe with the support of the motherland and the efforts of the SAR government, Hong Kong can overcome all challenges," he said.

[Source: China Daily](http://www.chinadaily.com.cn/china/2008-07/08/content_6826132.htm) ([see archive](Hong_Kong_service_firms_set_to_receive_more_help.pdf))

### Internal control systems still missing

Awareness of internal controls has increased among listed companies on the mainland in the past year but implementation is still weak, with only 44 per cent of companies establishing sound internal control systems, Deloitte reported recently.

In May 2008, Deloitte Touche Tohmatsu, one of the top global audit firms, surveyed 126 senior executives and board representatives from Chinese listed companies. This was the second survey by Deloitte aimed at tracking the awareness and readiness of mainland listed companies with regard to internal control systems. The first survey was conducted in June 2007, with 86 respondents.

Danny Lau, national leader of enterprise risk services of Deloitte China, said: "Our second survey indicates that Chinese companies are facing the internal control paradox: heightened awareness of regulatory requirements is not met by an increased level of commitment to implement an internal control system."

According to the survey, over half of the respondents (56 per cent) still have either no internal control system in place or their systems are not up to par.

When asked about the main obstacles for implementing internal control systems, four out of five respondents said the lack of a practical internal control framework or model was a big problem.

Chinese authorities have been working on this. On 28th June, the Ministry of Finance, China Securities Regulatory Commission, the National Audit Office, China Banking Regulatory Commission and China Insurance Regulatory Commission jointly announced the 'Basic Standard for Enterprise Internal Control', which requires the compliance of listed companies as from 1st July, 2009. Unlisted large and medium-sized Chinese companies are also being encouraged to adopt the standard.

"The standard is a major milestone in the development of internal control systems for Chinese companies. It's an important guideline and three detailed rules are on the way," said Allan Xie, partner of enterprise risk services of Deloitte China.

[Source: China Securities Jounal](http://www.cs.com.cn/english/ei/200807/t20080704_1515624.html) ([see archive](Internal_controls_still_missing.pdf))

### China's SOEs seek 16 executives from home and overseas

China's centrally-administered state-owned enterprises (SOEs) are seeking 16 senior executives from either home or abroad, according to the State-owned Assets Supervision and Administration Commission (SASAC).

The SASAC, the industry watchdog, said in a notice that the posts included three general managers, 10 deputy general managers and three chief accountants from various industries covering electricity, metallurgy, electronics, chemical engineering and trade enterprises.

Three Fortune 500 companies, including First Automobile Works, the most time-honoured Chinese automobile plant, Baosteel, the country's largest steel maker, and China Southern Power Grid were on the list.

Macao's Nam Kwong (Group) Company Limited will also launch a hunt for a general manager, making it the first centrally-administered SOE outside the Chinese mainland to look for such a senior position.

The SASAC has opened 103 senior management posts to domestic and overseas applicants since 2003 and selected 91 people out of 5,985 applicants for centrally-administered SOEs.

China currently has 150 central SOEs directly under the control of the SASAC, with total assets of 14.6 trillion yuan (US$2.12 trillion) as of November 2007.

[Source: People.com](http://english.people.com.cn/90001/90776/6443653.html) ([see archive](Chinas_SOEs_seek_16_executives_from_home_overseas.pdf))

### New rule puts end to easy online profits

People in Beijing who buy and sell online must apply for a business license and declare their earnings for tax purposes, the city government said recently.

The Beijing Administration for Industry and Commerce (BAIC) said all corporate entities and individuals who do business online must register with the administration and pay taxes on their earnings from 1st August.

Wang Jing, an official in charge of special trade with the BAIC, said such firms and individuals must provide the administration with their stores' names and IP addresses.

The BAIC will also hold website operators accountable for verifying the business licenses of online sellers, and business websites will be required to maintain transaction records for at least two years, he said.

Any firm or individual that fails to abide by the new regulations faces a fine of between 20,000 yuan (US$2,900) and 500,000 yuan, he said.

The rule does not apply to people who simply exchange personal items online, he said.

Online businesses, particularly those run by small-scale vendors and individuals, have long been exempted from business-related taxes, he said.

The aim of the new rule is to provide better regulation of operators' behaviour and to prevent illegal activities, not to kill the booming online trade, Wang said.

Last year, the BAIC received 323 complaints relating to e-commerce, up 29 per cent on 2006. Most of them were about late delivery, inferior quality products and fraud, he said.

One small online business owner in Beijing, known only as Doudou, said she will be forced to close down the T-shirt store she runs via Taobao.com, the country's biggest e-commerce site.

She said she will be unable to survive on the small profits she makes if she has to become an "official" business, and will instead try to sell off her stock before the 1st August deadline.

He Dayong, who operates an online business from Beijing's Dongcheng district, however, said he has been researching his market for months and welcomes the new rule, as it will help eliminate unscrupulous traders.

But Lu Bowang, an expert in e-commerce, said the rule will be hard to put into practice.

"How can you get tens of thousands of operators to register? They will simply move their businesses elsewhere."

A regional regulation cannot and should not be used to control the boundless online market, he said.

[Source: ce.cn](http://en.ce.cn/National/Politics/200807/04/t20080704_16049201.shtml) ([see archive](New_rule_puts_end_to_easy_online_profits.pdf))

## Other

### China to exempt earthquake regions from some government charges

China's Ministry of Finance announced recently it would exempt or cut down some government fund collecting from regions devastated by the 12th May earthquake over the next three years.

The grace period started on 1st July and runs to 30th June 2011, said the ministry in a notice circulated to earthquake-hit provinces such as Sichuan, Gansu and Shaanxi last week.

It said enterprises, institutions and individuals in the earthquake zone could temporarily stop paying into some key funds. These covered the Three Gorges Project construction and another supporting the relocation of residents for large- and medium-sized reservoirs. Both funds are collected by the central government for their electricity use.

In addition, companies in hard-hit regions would be exempt from extra charges for water and road transport. They could also stop paying into the cultural construction government fund and a special fund for movie development.

The ministry urged Sichuan, Gansu and Shaanxi provinces to follow suit for some local government funding and remove illegal funding projects.

The exemption move will add to a series of favourable taxation policies unveiled last week to help boost the economy in the earthquake zone.

[Source: China Daily](http://www.chinadaily.net/bizchina/2008-07/07/content_6825396.htm) ([see archive](China_to_exempt_quake_regions_from_some_govt_funding.pdf))

### Certain final judgments may be executed in either the mainland or Hong Kong

Beginning on 1st August, parties may apply to the people's court in mainland China or to the court in Hong Kong to recognise and execute a final enforceable judgment made by either court on funds to be paid.

On 3rd July the Supreme People's Court released the 'Arrangement on the Mutual Recognition and Execution of Judgments of Civil and Commercial Cases with Agreement Jurisdiction by Parties Involved' (Arrangement).

According to the Arrangement, final judgments for civil and commercial cases must be made with written jurisdiction agreements by the mainland people's court and the Hong Kong court.

For judgments on civil and commercial cases meeting conditions outlined in the Arrangement, applications may be filed to the intermediate people's courts where the respondents' domicile is located, where they regularly dwell, or where their property is located and to the senior courts of Hong Kong.

Courts may adopt, prior to or after the acceptance of judgment recognition and execution, preservation or mandatory measures on the respondent's property as applied by the applicants in line with local laws governing property preservation or the restriction of property transfer.

[Source: Lexis Nexis](http://hk.lexiscn.com/latest_message.php?id=4260) ([see archive](Certain_Final_Judgments_May_be_Applied_to_be_Executed_in_Either_Mainland_or_Hong_Kong.pdf))

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